HSBC Asset Management

# FOCUS FUND

# HSBC Corporate Bond Fund (HCBF)

An open ended debt scheme predominantly investing in AA+ and above corporate bonds. Please refer Page no. 9 of the SID for explanation on Macaulay^ duration. Moderate interest rate risk and relatively low credit risk.

**January 2022**

## View on Corporate Bond segment

**Accommodative but cautious RBI**

- Unanimous decision by MPC (Monetary Policy Committee) in December maintaining Status quo on rates and 5-1 vote in favor of retaining accommodative stance. However, RBI announced that it would increase fortnightly 14-day variable rate reverse repo (VRRR) in a gradual manner to up to INR 7.5 lakh crores by end December 2021 (from current INR 6 lakh crores). However, the window has not been fully utilized by banks as banks have preferred to park surpluses in shorter tenor VRRRs.

**Long bonds are likely to be volatile given supply concerns, lack of RBI OMO support and global macro-environment; supply lower in the short to medium part of the curve**

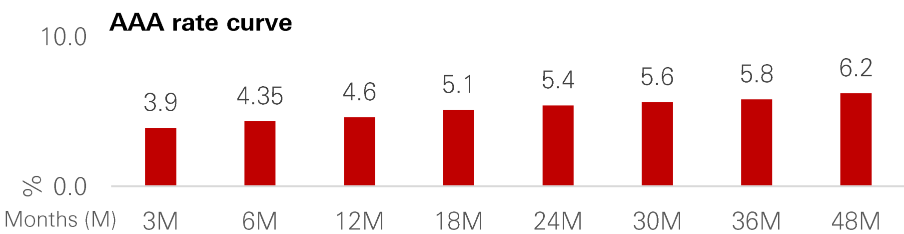
- Global bond yields such as US Treasury yields have inched up sharply in the past one month given expectations of central banks tightening liquidity and interest rates faster than was earlier discounted.
- After announcing INR 1tn in Q1 and INR 1.2 tn in Q2, RBI discontinued GSAP in October policy. RBI has not announced any OMO post October and has sold small quantum of G-Sec in secondary markets on a periodic basis. As a result, demand- supply dynamics for G-Sec remains a concern. Also, the extent of supply in the near term from G-sec and SDL front is largely towards the duration segment, with H2 borrowing in the 2-5 year segment being lower.
- These are likely to make G-Sec in the belly of the curve and long bonds more volatile.

**Steepness in G-Sec and Corporate yield curve offers attractive carry and roll down**

- The short and medium part of the corporate curve still remains attractive from carry play point of view and have to a reasonable extent, discounted RBI's calibration in liquidity. We also like the short-medium part of Government securities curve as current three years point over one year and five-seven years point over one/three year offers attractive risk-return tradeoffs.

**Corporate spreads expected to be largely well behaved**

- Supply in corporate bonds in the short to medium segment remains reasonable. While spreads are tight v/s Government securities, we may not see much expansion in spreads given the supply demand dynamics. While some volatility cannot be ruled out towards end of the fiscal, ample liquidity and demand for bonds in the short to medium duration segment, we expect spreads to be well behaved over the medium term.




- With overnight rates between 3.5%-4% and ultra-short end of the curve between 4% and 4.50%, the 24m - 48m segment currently at 5.30% - 6.2% discount likelihood of 20-25 bps hardening at ultra-short end. This is due to VRRR and RBI action over next 6 months. And any excess hardening of say up to 30bps can still be able to generate return at par with Ultra short / low duration funds over next 6 - 12m holding period given the steepness of 130-150 bps over 1 to 4 year part of the curve

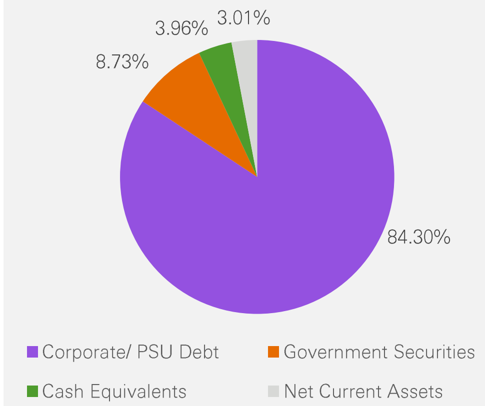
^ The Macaulay duration is the weighted average term to maturity of the cash flows from a bond. The weight of each cash flow is determined by dividing the present value of the cash flow by the price. Please refer to the page number 9 of the Offer Document on which the concept of Macaulay's Duration has been explained. Source: HSBC Asset Management, India, Data as of 31 December 2021

## Portfolio

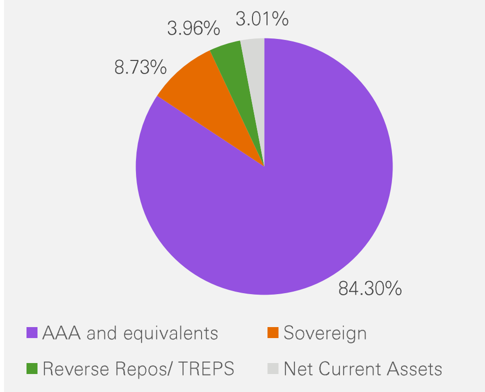
| Issuer | Rating | % to Net Assets |
|---|---|---|
| **Corporate/ PSU Debt** | | |
| **Corporate Bonds / Debentures** | | **84.30%** |
| REC Top 10 | CRISIL AAA | 11.48% |
| Reliance Industries Top 10 | CRISIL AAA | 11.38% |
| Indian Oil Corporation Top 10 | [ICRA]AAA | 11.08% |
| Indian Railway Finance Corporation Top 10 | CRISIL AAA | 11.03% |
| LIC Housing Finance Top 10 | CRISIL AAA | 10.94% |
| Small Industries Development Bk of India Top 10 | [ICRA]AAA | 10.84% |
| HDB Financial Services Top 10 | CRISIL AAA | 8.90% |
| National Bk for Agriculture & Rural Dev. Top 10 | [ICRA]AAA | 8.65% |
| **Government Securities** | | **8.73%** |
| 5.15% GOVT OF INDIA RED 09-11-2025 Top 10 | SOVEREIGN | 6.40% |
| 8.21% HARYANA SDL RED 31-03-2026 Top 10 | SOVEREIGN | 2.33% |
| **Cash Equivalent** | | **6.97%** |
| **TREPS*** | | **1.31%** |
| **Reverse Repos** | | **2.65%** |
| **Net Current Assets** | | **3.01%** |
| **Total Net Assets as on 31-Dec-2021** | | **100.00%** |

*TREPS : Tri-Party Repo

## Asset Allocation




## Rating Portfolio




## Current Portfolio Strategy

- From medium term perspective, HSBC Corporate Bond Fund is expected to benefit from attractive carry at short and medium part of the curve.
- It offers value for investors at current short-term yields over funding cost in terms of spread.
- In recent months, we have witnessed some volatility in the short to medium segment as yields have inched upwards given the increasing absorption of liquidity through VRRR auctions.
- However, the short and medium part of the curve still remains attractive from carry play point of view and have to a reasonable extent, discounted RBI's calibration in liquidity.
- The current steepness in the 2-3 year segment will most likely benefit despite firming up of rates at the ultra-short end of the curve given the steepness in the curve currently.
- We also like the short-medium part of Government securities curve as current three years point over one year and five-seven years point over one/three year offers attractive risk-return tradeoffs.
- The extent of supply in H2 and going into FY 23 from G-sec and SDL front is largely towards the 10-14yr and 30yr segments and this should keep the pressure contained in the medium part of the segment.
- Overall, the pick-up versus overnight rate is quite attractive in the short-medium segment on the G-sec curve and alongside on the corporate curve. As such we intend to maintain a neutral duration versus the index in near term.

Source: HSBC Asset Management, India, Data as of 31 December 2021

## Rationale on existing credit exposures* (Top 5)

1. **Rural Electrification Corporation:** REC is a public financial institution under the administrative control of Ministry of Power. Until 2003, REC's primary objective was to provide financial assistance on concession to SPUs for rural electrification. RECs mandate was broadened in 2003 to include financing of all segments of the power sector. It provides financial assistance to state electricity boards (SEBs) for financing transmission, distribution and generation projects. REC's credit profile derives strength from government ownership and support it receives from it. The credit profile is also supported by its good resource profile and adequate capitalization and profitability. Entity's asset quality issues are likely to have bottomed out, similar to case of PFC. Post-acquisition of REC by PFC, rating agencies have reaffirmed both agencies at AAA, taking into account mainly the strategic importance of the company. PFC and REC are expected to continue to be strategically important to the Government of India and will continue to play an important role in funding of power projects, especially those of the state government owned electricity companies. Recent policy actions in terms of liquidity support to discoms which have been have been undertaken through REC and PFC, reiterate its strategic importance.
2. **Reliance Industries:** The company's large size and established presence in the crude oil refining and leadership position in the domestic petrochemical industries, huge cash and liquid investments and being net cash at a consolidated level, lends a strong financial profile to the name. In addition, the entity has industry leading refining margins, comfortable gearing, low working capital intensity are some of the additional factors which give comfort on the name. Further, the company's capex cycle in-non telecom businesses is nearing its end which gives visibility on free cash flows going forward. Entity has cemented a strong Leadership position in the domestic petrochemical industry and integrated operations across E&P, refining, and petrochemical businesses. It is the industry leading margins in the refining business, healthy profitability of the petchem business which is expected to further improve going forward. It has healthy debt metrics which is expected to improve further with generation of free cash flow post completion of capex cycle. Recent stake sales in Jio, trending the company to a net debt free status is another over-riding comfort on the name. Recently announced demerger is unlikely to have a credit impact as it only strengthens the standalone profile and makes it more attractive for strategic investors in future which should enhance the company's financial standing.
3. **Indian Oil Corporation:** IOC is the largest oil refining and marketing company. with approx. one third refining market share. IOC also has the largest network of crude oil and petroleum product pipelines in India. In terms of oil marketing and sales, IOCL is again the leader with ~45% petroleum market share with over 42,900 touch points. IOC also meets majority of the requirement of GOI owned organizations such as the Indian Railway and defense forces. Overall, majority GOI ownership, strategic importance, robust liquidity profile and strong balance sheet are the key credit strengths.
4. **Indian Railway Finance Corporation:** IRFC is is wholly owned by Government of India (GoI) through Ministry of Railways (MoR). The company was set up with the objective of borrowing funds from the market to provide rolling stock to Indian Railways (IR). IRFC leases rolling stock to Indian Railways, which reimburses the company through lease rentals, paid on a half yearly basis in advance. The lease agreement between IR and IRFC is structured in such a way that IRFC's expenses are reimbursed, allowing it to earn an adequate margin. The credit profile of IRFC derives significant comfort from the support it receives from GoI and its strategic importance to IR; IRFC provides market funding to about 25% of IR's rolling stock requirements. Given the large capex requirements of IR, IRFC will continue to play a critical role in mobilizing funds for IR at competitive rates and therefore remain strategically important over long term. The company's importance to IR is further evident from the fact that it also raises market borrowings required by Rail Vikas Nigam Ltd. for execution of projects relating to upgrading railway infrastructure. The underlying risk on this exposure is borne by MoR.
5. **LIC Housing Finance:** LICHF is the second largest housing finance company in India after HDFC/Individual loan portfolio. Credit strength is derived from the support of the parent (LIC), sound capitalization and healthy resource profile. Asset quality has remained strong and stable in the past few years and given that the book is largely retail and to salaried customers; it is likely that these levels are maintained as the portfolio continues to grow. Company has started to expand the non-housing segment in a calibrated way, which helps improve the yields, and at the same time has been able to maintain low level of overall delinquencies. Retail housing is ~85% of the total book. A large number of LIC Housing's senior management personnel are on deputation from LIC. LIC has also committed to not allowing its stake to fall below 33% which gives a strong support to its rating. Expect continued support over long term in terms of ownership, common branding and managerial inputs.

Source: HSBC Asset Management, India, Data as of 31 December 2021

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## Investment Objective:

To seek to generate reasonable income and provide risk-adjusted returns by investing primarily in AA+ and above rated corporate debt securities. However, there can be no assurance or guarantee that the investment objective of the scheme would be achieved.

## Fund Details

**Fund Manager** [3]
Ritesh Jain

**AUM** (as on 31.12.21)
230.37 Cr

| | |
|---|---|
| **Average Maturity** | 2.38 years |
| **Modified Duration** | 2.08 years |
| **Macaulay Duration** | 2.19 years |
| **Yield to Maturity** [1] | 5.34% |

**Benchmark**
NIFTY Corporate Bond Index 2

**Inception Date**
30 September 20

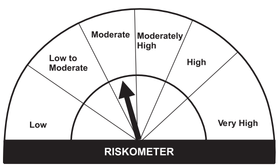
**Exit Load**
NIL

1 YTM Based on invested Amount

2 SEBI vide its circular no. SEBI/HO/IMD/IMD-II DF3/P/CIR/2021/652 dated October 27, 2021, on 'Guiding Principles for bringing uniformity in Benchmarks of Mutual Fund Schemes' has introduced two-tiered structure for benchmarking of certain categories of schemes. Accordingly, the benchmark has been classified as Tier 1 benchmark. Furthermore , the same is effective from 01 December 2021

### HSBC Corporate Bond Fund Riskometer

HSBC Corporate Bond Fund




Investors understand that their principal will be at Moderate risk

**Corporate Bond Fund** - An open ended debt scheme predominantly investing in AA+ and above rated corporate bonds. Please refer Page no. 9 of the SID for explanation on Macaulay duration. Moderate interest rate risk and relatively low credit risk.

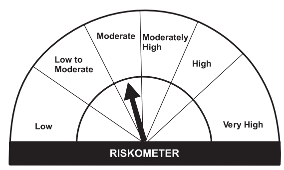
**This product is suitable for investors who are seeking##:**

- Income over medium term.
- Investment predominantly in corporate bond securities rated AA+ and above.

**##Investors should consult their financial advisers if in doubt about whether the product is suitable for them.**

Please note that the above risk-o-meter is as per the product labelling of the Scheme available as on the date of this communication/ disclosure. As per SEBI circular dated October 5, 2020 on product labelling (as amended from time to time), risk-o-meter will be calculated on a monthly basis based on the risk value of the scheme portfolio based on the methodology specified by SEBI in the above stated circular. The AMC shall disclose the risk-o-meter along with portfolio disclosure for all their schemes on their respective website and on AMFI website within 10 days from the close of each month. Any change in risk-o-meter shall be communicated by way of Notice cum Addendum and by way of an e-mail or SMS to unitholders of that particular Scheme.

**Benchmark: NIFTY Corporate Bond Index**




### Potential Risk Class (HSBC Corporate Bond Fund)

| **Credit Risk →** / **Interest Rate Risk ↓** | Relatively Low (Class A) | Moderate (Class B) | Relatively High (Class C) |
|---|---|---|---|
| **Relatively Low (Class I)** | | | |
| **Moderate (Class II)** | **AII** | | |
| **Relatively High (Class III)** | | | |

"Potential Risk Class ('PRC') matrix indicates the maximum interest rate risk (measured by Macaulay Duration of the scheme) and maximum credit risk (measured by Credit Risk Value of the scheme) the fund manager can take in the scheme. PRC matrix classification is done in accordance with and subject to the methodology/guidelines prescribed by SEBI to help investors take informed decision based on the maximum interest rate risk and maximum credit risk the fund manager can take in the scheme, as depicted in the PRC matrix."

Source: HSBC Asset Management, India, (HSBC AMC), Bloomberg. Data as of 31 December 2021

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**Mutual fund investments are subject to market risks, read all scheme related documents carefully.**