Concept Note

HSBC Corporate Bond Fund

An open ended debt scheme predominantly investing in AA+ and above rated corporate bonds

22 December 2020

Summary

The fund is constructed with an orientation towards high liquidity and credit conservatism in the moderate duration segment (3-5 year).

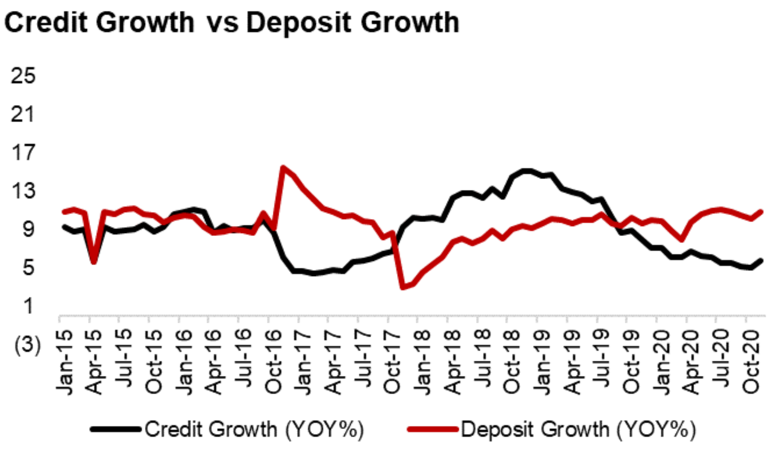
Corporate Bond Fund – What is the nature of this fund category?

As per SEBI directive, a corporate bond fund should invest at least 80%^ of its assets in highest rated instruments (i.e. AA+ and above). This category is meant to appeal to those investors who do not want to take in undue credit risk and look for stability with NAV appreciation predominantly from accrual and marginal capital gains.

^ In accordance with the SEBI letters dated May 18, 2020 and August 17, 2020, The Investment Committee of the AMC, Board of AMC and Trustees of HSBC Mutual Fund have approved an additional investment of upto 15% of the AUM of HCBF in Government Securities or T-Bills till December 31, 2020 or any other time as may be permitted by SEBI. Consequent to this, HCBF may invest a minimum of 65% of total assets in AA+ and above corporate bonds.

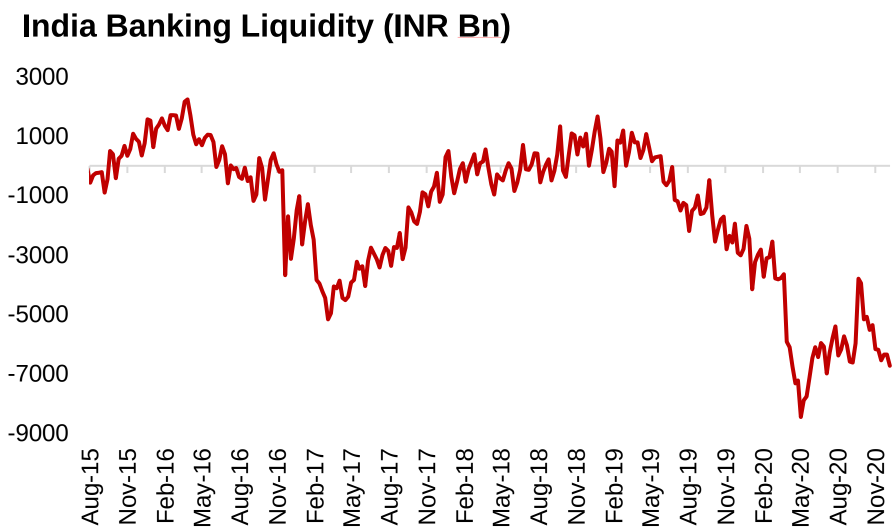
Few of the drivers for Short Duration Funds are:

A. Credit & deposit growth: Over the last year and half, weak economic growth coupled with a significant risk aversion has led to a deceleration in banking credit growth. Consequent to the risk aversion, there has been a surge in deposits as well.



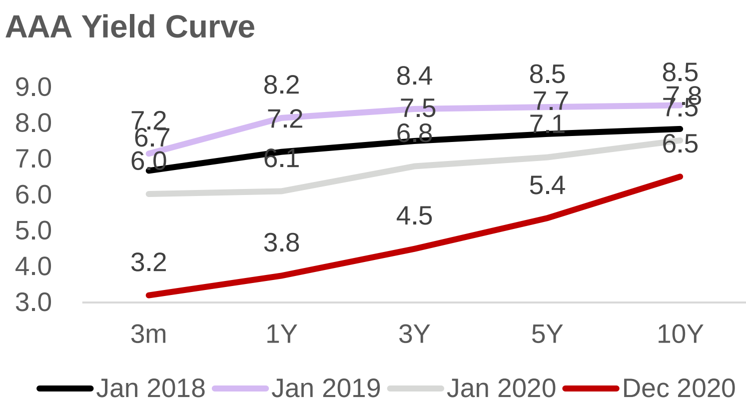
B. System Liquidity: RBI actions has resulted in significant surplus liquidity in the system driving a steep fall in rates in the shorter end of the curve. Strong FX flows led to aggressive sterilization in turn leading to significant surplus liquidity condition in the market. Open Market Operations (to stabilize yields) have in tandem aided to the significant surplus liquidity.

HSBC Global Asset Management



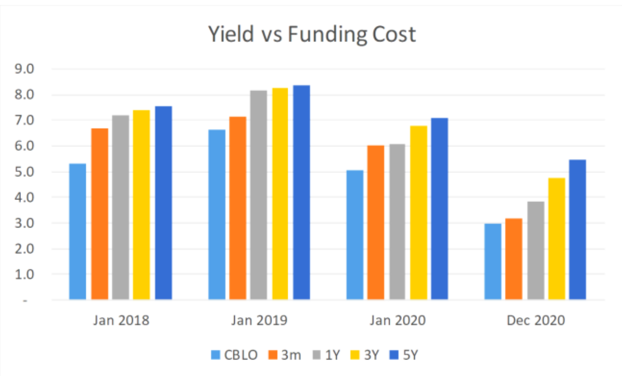
Lower credit offtake/risk aversion coupled with high system liquidity has resulted in chase for high quality assets.

C. Liquidity driven steepness / spreads between tenors: The liquidity as well as RBI support has led to significant term spread and steepness in the curve. The divergence between 1 and 3year point and between 3 and 5year point are at all-time highs thereby making the medium part (3-5year) of the curve relatively attractive.



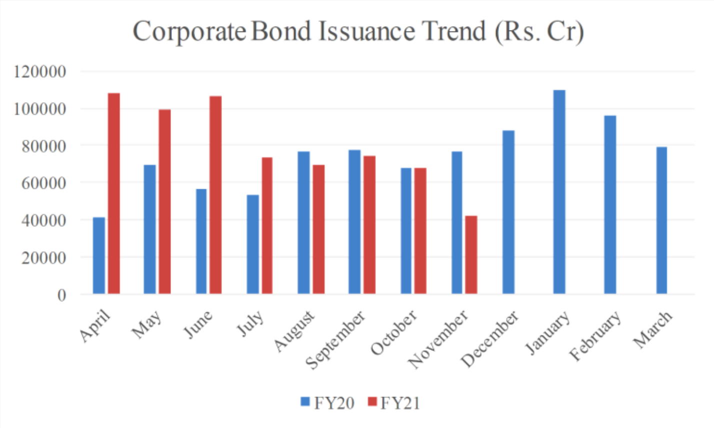
(In Bp)	Jan 2018	Jan 2019	Jan 2020	Dec 2020
3y vs 1y	30	25	70	75
5y vs 1y	50	30	95	160
10y vs 1y	64	35	142	276

D. Relative attractiveness of the corporate curve versus funding cost



With the funding cost, closer to reverse repo (rather than repo) driven by surplus liquidity, the yields in the money market segment have compressed sharply, raising the relative attractiveness of the medium term segment.

E. Overall Supply of corporate bonds: With initial round of rate cuts, and pandemic driven uncertainty supported by liquidity, the decline in bond yields have prompted corporates to borrow more to refinance and create a buffer in their balance sheet. With the pandemic related uncertainty easing, corporate borrowing has also slowed down. Also with subdued capex requirement and surplus liquidity condition s banks are more than willing to finance higher rated borrowers, we expect supply to remain muted in the near term. For the remainder of the year, we do not expect to see a seasonal spurt in borrowing towards the end of the year as bulk of the borrowing has already been undertaken. As such the supply curve in the bond space not likely to be very aggressive.



Going forward, fresh borrowing will depend on revival of capex in FY22. Some refinancing needs may also prompt borrowers to tap the market if rates remain conducive.

Overall, given the backdrop of current economic environment the prominent variable driving the corporate bond market continue to remain positive.

How does HSBC Corporate Bond Fund's (HCBF) portfolio construct looks like?

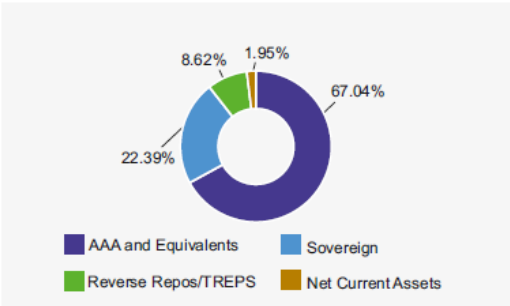
Security Name	Per NAV	Rating	Maturity In Years
Corporate Bonds / Debentures			
8.10% RURAL ELEC CORP NCD RED 25-06-24	3.47%	CRISIL AAA	3.57
6.39% INDIAN OIL CORP NCD RED 06-03-2025	3.34%	CRISIL AAA	4.27
7.40% RELIANCE INDUS NCD 25-04-2025	6.87%	CRISIL AAA	4.40
6.19% IRFC NCD RED 28-04-2023	3.32%	CRISIL AAA	2.41
7.25% LARSEN & TOUBRO NCD RED 24-04-2023	3.39%	CRISIL AAA	2.40
5.47% NABARD NCD RED 11-04-2025	3.21%	ICRA AAA	4.36
6.88% NHB LTD NCD RED 21-01-2025	6.82%	CRISIL AAA	4.15
5.85% EXIM BANK NCD RED 12-09-2025	3.26%	CRISIL AAA	4.79
6.50% POWER FIN CORP NCD RED 17-09-2025	3.97%	CRISIL AAA	4.80
6.43% HDFC LTD NCD RED 29-09-2025	3.29%	CRISIL AAA	4.83
7.30% HDB FIN SERV LTD NCD 29-06-2023	4.06%	CRISIL AAA	2.58
6.19% LIC HSG FIN NCD RED 25-11-2024	4.59%	CRISIL AAA	3.99
5.45% NTPC LTD NCD RED 15-10-2025	5.80%	CRISIL AAA	4.88
5.1121% HDB FIN SERV LTD NCD 26-07-2022	0.65%	CRISIL AAA	1.65
5.5% INDIAN OIL CORP NCD 20-10-2025	1.29%	CRISIL AAA	4.89
5.85% REC LTD NCD RED 20-12-2025	3.22%	CRISIL AAA	5.06
5.50% KOTAK MAH PRIME NCD RED 12-10-2023	6.49%	CRISIL AAA	2.87
	67.04%		
Government Bonds			
6.18% GOVT OF INDIA RED 04-11-2024	6.71%	SOVEREIGN SOV	3.87
	6.71%		
REPO ISSUE DATE 27.11.2020 2.85%	5.23%		0.00
	5.23%		
State Development Loans			
8.21% Haryana SDL RED 31-03-2026	0.70%	SOVEREIGN SOV	5.26
8.45% PUNJAB SDL RED 31-03-2024	1.41%	SOVEREIGN SOV	3.29
8.88% WEST BENGAL SDL RED 24-02-2026	0.73%	SOVEREIGN SOV	5.16
8.36% MAHARASHTRA SDL RED 27-01-2026	3.55%	SOVEREIGN SOV	5.09

8.53% UTTAR PRADESH SDL 10-02-2026	9.29%	SOVEREIGN SOV	5.12
	15.68%		
TREPS			
TREPS_RED_01.12.2020	3.39%		0.00
	3.39%		
	98.05%		
Cash & Other Receivables :	**1.95%**		
Total	**100.00%**		

Quantitative Data

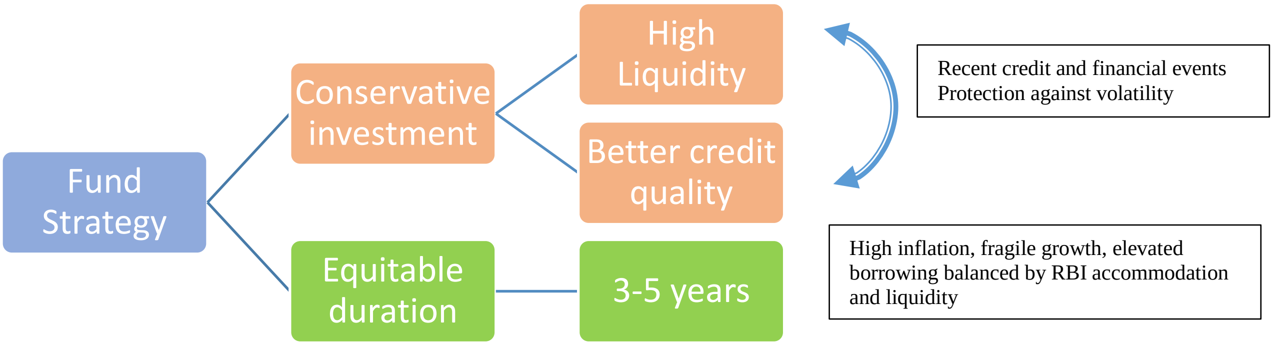
YTM[4]	5.10%
Average Maturity	3.84 year
Modified Duration	3.19 year
Macaulay Duration	3.32 year

Rating Profile



Data as on 30 November 2020

What are the benefits of investing in HSBS Corporate Bond Fund?



A. Moderate Duration positioning

HCBF aims to maintain a duration of 3-5 years in an actively managed strategy. The duration positioning is derived from the following factors:

- The high term premium in the 3-5year space against historical trends makes that part of the curve relatively very attractive. Also the current prevailing ~200bps of spreads between overnight funding cost and the 3-5year segment seems to be adequately compensating for the duration risk in the segment. In terms of spreads, we are at historical highs and we foresee these spreads to normalize over a period of time.

B. Strong Asset Quality

The strategy of HCBF is to maintain a high credit quality. 100% of the investments of the scheme are in Government securities and AAA rated names with bulk of the investment in Government or Government sponsored entities. The objective of such a portfolio construct is predominantly three fold:

a) Over the last two years, we have witnessed significant volatility in the credit environment spanning several sectors and financial entities. We believe that the credit environment continues to remain fragile as banking credit growth is yet to pick up.

b) Additionally, spreads between AAA and AA names which may have shed bulk of the COVID related scare, are still far from the pre-IL&FS levels suggest that market sentiment towards credit is very weak.

c) Recent events have proven that liquidity is paramount in a fund construct. Keeping overall investor interest in mind (to give investors exit options at low impact cost), we believe that high credit profile is important as it lends strong liquidity to the underlying portfolio.

C. High Liquidity with exit options at all points in time

The fund emphasizes on liquidity, and has invested only in Sovereign - and liquid AAA bonds The segment is having the highest degree of liquidity in market.

D. Post tax returns

Compared to traditional fixed income products, HCBF offers attractive post tax returns due to benefit of indexation.

What is the Outlook on the market?

At the current juncture the four key scenarios macro that may play out are as follows:

(High)--------------Inflation ------------(Low)		
(Low)	RBI can stay accomodative and cut rates, but fiscal pressures will keep rates elevated/ range bound	RBI can cut rates and remain accomodative to support growth; rates can go down
(High)	RBI can remain accommodative but no scope for rate actions – RBI (at best) will use unconventional measures to keep rates from going up as fiscal pressures will be very high; curve will be very steep	RBI can reverse its accomodative stance; borrowing may not go down meaningfully --> rates will go up
	(Low)--------------------------Growth ------------------------(High)	

With credit environment remaining uncertain, we would endeavor to maintain the current credit and duration profile over the medium term.

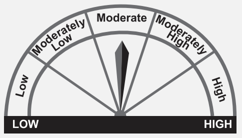
In summary, Corporate Bond Fund provides a degree of stability with significantly low degree of volatility versus Long duration products and has the potential to offer a better risk-adjusted post-tax return with a quality portfolio. It is suitable for investors with an investment horizon of ~1-3 years,

Summary of Investment Thesis:

The fund is constructed with an orientation towards high liquidity and credit conservatism in the moderate duration segment (3-5 year). Alpha generation is directed from curve movements and G-sec vs corporate play rather than credit. We believe that current market environment is not opportune to play the credit strategy as it may be fraught with volatility in the near to medium term.

HSBC Corporate Bond Fund

Riskometer



Investors understand that their principal will be at Moderate risk

This product is suitable for investors who are seeking*:

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

^ 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

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

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HSBC Asset Management (India) Private Limited, 16, V.N. Road, Fort, Mumbai-400001
Email: hsbcmf@camsonline.com | Website: www.assetmanagement.hsbc.com/in

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