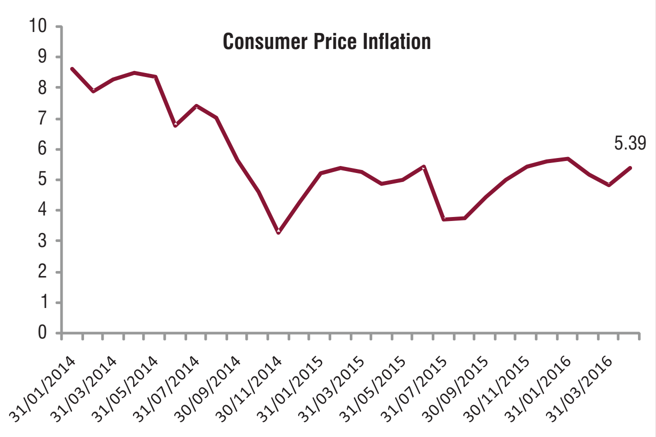
Monthly Fixed Income Update & Commentary on Focus Funds

June 2016

Birla Sun Life Mutual Fund

Key Rates & Market Yields	May-16	Apr-16
Repo Rate	6.50%	6.50%
Reverse Repo Rate	6%	6%
CRR	4%	4%
Overnight Rates		
CBLO	6.45%	5.37%
Short Term Debt		
3 months CP	8.07%	8.44%
6 Months CP	8.36%	8.5%
3 Months CD	7.17%	7.35%
6 months CD	7.29%	7.38%
91 days T-Bill	6.78%	6.73%
182 days T-Bill	6.91%	6.84%
364 days T-Bill	6.95%	6.88%
Long Term Debt		
3 yr G-Sec	7.22%	7.27%
5 Yr G-Sec	7.44%	7.46%
10 Yr G-Sec	7.47%	7.44%
Corporate Bond Yields (AAA)		
6 months	7.61%	7.62%
1 year	7.68%	7.73%
3 year	7.87%	7.86%

Macro Economic Parameters	Current Update	Last Update
CPI	5.39%	4.83%
WPI	0.34%	-0.85%
IIP	0.1	2
Trade Deficit	$4.8bn	$5.1bn
Current Account Deficit (CAD)	1.3% of GDP (Sep- Dec15)	1.27% of GDP (Jun- Sep15)
Fiscal Deficit	3.50%	3.92%
GDP Growth Rate	7.90%	7.20%
Exchange Rate Rs vs $	67.26	66.34



Data as on May 31, 2016. Source: Bloomberg, BSL AMC Internal Research

Fixed Income Market Update

- Global financial markets have been unsettled since the start of 2016. Increased concerns about global economic recovery have dominated the global risk sentiment.
- On domestic front, the incremental lead indicators released reflect a gradual and uneven improvement in growth.
- Going forward, India's economic recovery is expected to gain traction as benign inflation, increase in disposable incomes following 7th CPC implementation, an above-normal monsoon, and continued monetary policy accommodation are expected to bring about both urban and rural demand, which in turn are expected to strengthen profitability of Indian companies, kick-starting a virtuous cycle of growth.
- Credit off-take in the industrial sector has been tepid primarily due to slow pace of pick up in private sector investment, stressed balance sheets of banks, and modest global demand.
- Low gold imports and decline in non-oil non gold imports resulted in moderation in the trade deficit in April, declined to 4.8bn$ (from 5.1bn$ in Mar'16).

Event Update

- The recent monetary policy announcement was largely in line with expectations. RBI maintained an accommodative policy stance in its policy review today while keeping the key policy rates unchanged.
- The policy highlighted an upside risk to CPI but it remains confident on the achievement of the 5% target for this fiscal. RBI states that a strong monsoon, continued astute food management, as well as steady expansion in supply capacity, especially in services, could help offset these upward pressures.
- Since the announcement of liquidity measures in the last policy statement, the liquidity conditions remained under pressure in May. In order to mitigate these pressures, the Reserve Bank injected liquidity through purchases under open market operations (OMOs) of 700 billion during April-May. Additionally, liquidity was injected through variable rate repos of various tenors, in addition to the regular 14-day term repos and overnight fixed rate repo and MSF.
- Positive domestic macros, especially revival in consumption demand conditions would be of utmost importance. Further, easing interest rate cycle is expected to provide a gradual traction to domestic investment, which would be crucial to revive manufacturing activity.

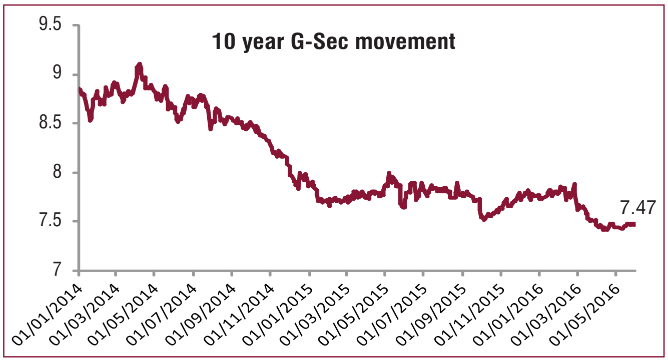
Portfolio Positioning & Strategy

- The movement in Govt securities market was rather tepid in the month of May with the 10y benchmark trading in a narrow range of 4 bps. From the portfolios standpoint, we remain biased towards duration.
- Duration is built primarily through Govt bonds as we have been averse to corporate bonds because of the low spreads at which they were trading(~30-35 bps). Though the corporate bond spreads(AAA-GSec for 3-10 yr segment) have widened in the last few months to ~50-55 bps, yet we remain cautious about adding duration through corporate bonds (unless any part of the yield curve looks unusually attractive).

Portfolio Action & Strategy

BSL Dynamic Bond Fund

The fund has been running a duration strategy for over a year now which has benefited the fund. Rally in certain tenors of sovereign bonds of upto 50 bps over past couple of months has benefited the fund by generating capital gains and helping it be amongst the top performing bond funds. We believe that the G-Sec demand-supply scenario will continue to favour a high duration strategy since long term HTM investors like Insurance companies, Pension funds etc will remain in high demand for these bonds. The potential for capital gains from these bonds is quite high.

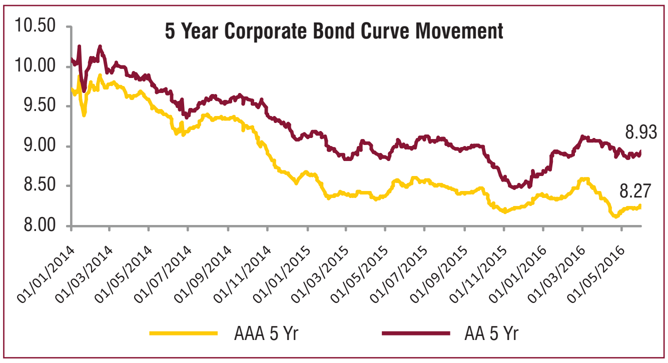


Going forward, depending on markets & data from high frequency indicators, we may steadily start increasing exposure to corporate bonds as the spreads come up from their existing low levels.

BSL Medium Term Plan

BSL Medium Term Fund has been one of the superior performing funds on account of its foresight in risk reward evaluation and steering away from exposures that could attract downgrades or defaults. Instead, in a stressed credit environment the fund could've liquidated ~1/3rd of the portfolio as the same was deployed in sovereign bonds. Moreover, a rally in certain tenors of sovereign bonds of upto 50 bps has benefited the fund by generating capital gains.

After benefiting from the GSec holding in the portfolio, the duration has been brought down from 3.2 years in April 16 to 2.5 years in May 2016. We believe that the G-Sec demand-supply scenario continues to be favourable and hence, we still continue have ~25% exposure to G-Secs. Moreover, with corporate bond spreads expanding reasonably across segments (specifically in A-AAA 3 yr segment) and improving credit environment, we intend to build fresh exposure to corporate bonds and credit structures at this juncture which will add to the carry of the overall portfolio. Currently, the YTM of the portfolio is 9.38%.



BSL Short Term Opportunities Fund

The scheme had been running a reasonable exposure to sovereign bonds (~35%) in the last couple of months. Going forward, we intend to bring down the exposure to sovereign bonds and increase exposure to corporate bonds. After remaining at ultra low levels for several months, Corporate bond spreads have moved up to median levels (50- 55 bps for AAA-Gsec). The fund is currently positioned in such a way that ~50% - 65% of the portfolio is invested in AAA/sovereign bonds and ~35% -50% of the portfolio is invested in AA centric corporate bonds. For the last few months we were constructive on duration and were underweight on corporate bonds. With expansion in corporate bond spreads & softening interest rate environment, we intend to build higher exposure to corporate bonds in our portfolio going forward. The YTM of the portfolio has inched up 8.37% to 8.50%. The fund continues to focus on an accrual strategy with a high credit quality bias.

BSL Cash Manager Fund

In this fund we have been running a modified duration in the range of ~1 year for the last couple of months. In the 1-2 year bonds space the spreads and carry currently look attractive to us owing to the liquidity position of the economy now & as expected to be in future with RBI's efforts towards moving to a neutral liquidity position from a the current deficit one. We believe that the RBI's efforts on infusing liquidity into the system to move it from deficit liquidity to neutral liquidity is going to ease short term rates going forward. Hence, it is only justified to benefit by investing in 1-2 year segment now and benefit going forward when the yields come down.

Owing to this strategy, the fund is at the higher end of its duration band (0.5 – 1.25 yrs) and hence, the credit risk taken in the fund at this time is limited.

Data as on May 31, 2016. Source: Bloomberg, BSL AMC Internal Research