

Rich turn risk-averse, eye debt for big returns

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MUMBAI: The steady decline in returns on fixed income products has forced wealth managers to evolve newer [investment strategies](#) to service affluent but conservative investors. Investment product designers are now being given the mandate to write structures that provide the safety cushion of a fixed income instrument but deliver higher returns.



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With bank deposits yielding around 5.75% (pre-tax return) returns and liquid funds giving 4%, conservative [investors](#) are squarely missing a debt product that can give decent returns, say wealth managers. While income funds give out around 6% yields, the segment is fraught with volatility and mark-to-market risk, making it unattractive for conservative investors.

This is forcing wealth managers to prescribe large debt, small equity structures to risk-averse clients. The focus of these structures is to generate maximum returns on the debt portion. The small equity component, which receives just around 10-15% of the [investment](#) corpus, will act as the high return kicker.

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Conservative investors do not have any profitable option to invest on the debt side. To counter this problem, we have created structures that invest a major portion of the corpus into debt instruments, while keeping a small portion invested in equities, said Akhilesh Singh, wealth management head, Emkay Global [Financial Services](#).

The returns from the equities portion increase the value of the portfolio, which is skewed heavily towards debt instruments, he says.

The equity-debt allocation mix of large debt, small equity structures will be in 15:85 ratio, favouring debt instruments. The structure is designed to generate about 5.5% each on debt and [equity](#) portion, which will assure an overall portfolio return of around 10.5%.

Another facet of the structure is when the fund manager buys options to the level of equity exposure, which will give the portfolio up to 100% exposure in market. Such a treatment will ensure both capital protection and equity market participation to the maximum level possible. Even after charging long-term capital gains tax on returns generated, the portfolio is back-tested to yield a post-tax return of 9%.

The scheme works very much like a reverse of equity-linked notes, say wealth managers. In equity-linked notes (ELNs), returns are mainly derived from investments in equities. The role of the debt portion in ELNs is primarily to ensure capital protection. In large debt, small equity structures, the debt portion is equally responsible for providing returns.

In effect, a limited participation into equities will yield higher coupons on these portfolios. These structures will do well when interest rates firm up, said [Maneesh Kumar](#) of Burgeon Wealth Advisors.

According to experts, the underlying debentures (debt portion) in these structures are issued off the balance sheets of the issuer (mainly a NBFC). Investors should not invest with issuers having high NPAs.