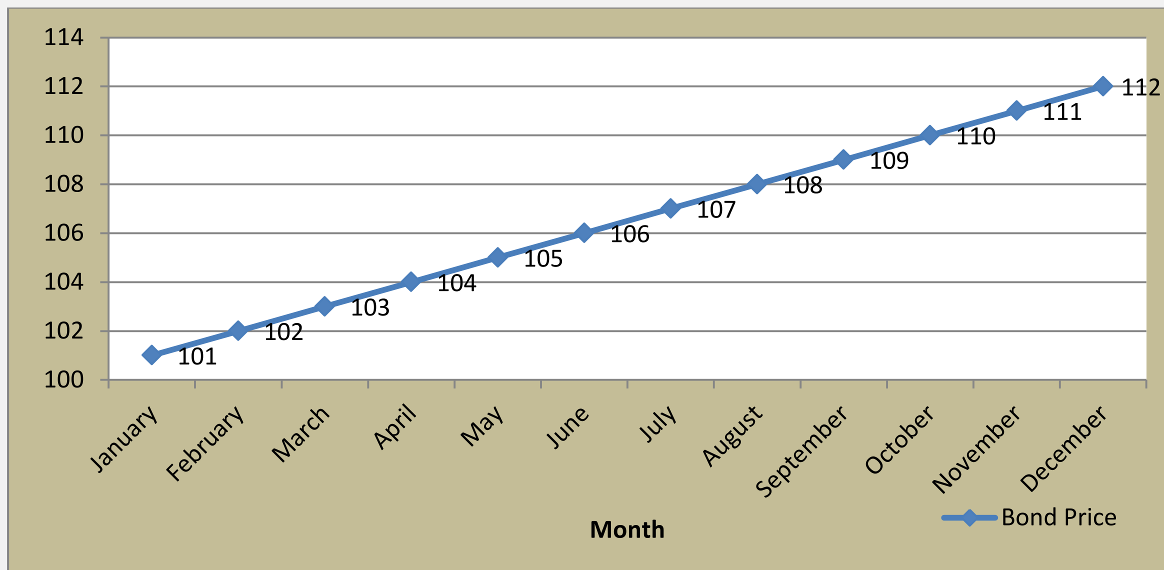
“Why RBI action will not have a lasting affect on Debt Funds”

Pebble Silk Monthly Advisory Communiqué *August ’13*

Hi,

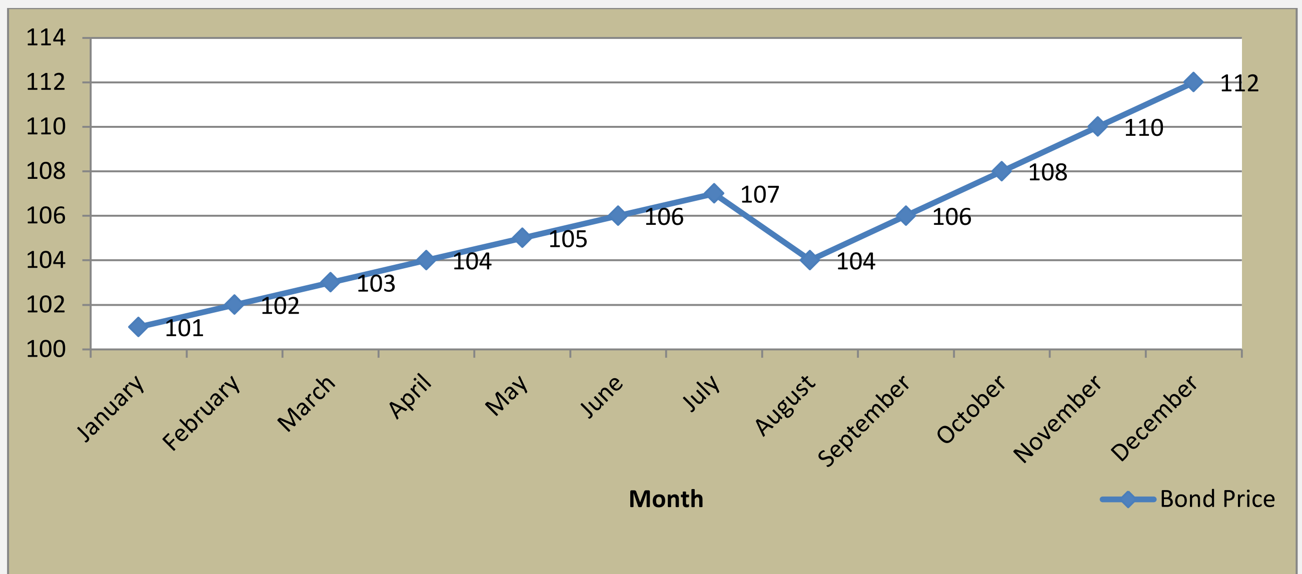
In the current turbulence in the debt funds, it is important to understand the working of bond market with a simple example.



Assumptions:

- *In a normal scenario (no change in interest rate), the bond price increases from 100 to 112 in 12 months.*
- *This is an increase of Re.1 every month*
- *Please note – You started with 100 and ended at 112*

Impact post RBI Action



- *Assume RBI raises interest rate in August end*

- *The bond value falls from 107 to 104*

Now, in the remaining 4 months, let us note the bond price start gaining by Rs.2 every month (instead of Re1). This is so because the maturity value of the bond is fixed at 112 in any case. So the bond prices have to rise at a speed so that they can reach 112 in remaining months.

- ***In the end we get the same maturity i.e. Rs.112 on both the cases***

- *Thus, it is important for us to stay invested to gain from faster accruals and reaching the returns similar to pre- RBI action.*

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