

US-64: A bailout postponed?

Prior to making US-64 NAV-based, the government has added some more sweeteners to prevent large scale redemptions. However, there is an overriding feeling that the government has only managed to postpone the inevitable. Three informed views:

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TEMPORARILY, UTI has postponed its liquidity crisis for a later date if not till 2003, in the expectation that market sentiments would improve, NAV would go up from its present level and, UTI would be able to clear the mess created in mid-2001.

US-64 is a flagship scheme existing for over 35 years with highly satisfied investors till the scheme was wrongly closed for redemption in July 2001 to avert payment crisis resulting into loss of trust on the part of investors and causing panic in the market. It was alleged that there was leakage of information and heavy redemption by some large investors — a case of blatant insider trading.

UTI was expecting the central government to bail it out of the mess it has created but ultimately borrowed Rs 6,500 crore including Rs 2,500 crore from some banks. It is unfortunate that these banks were also involved in redemption of their own units taking small investors for a ride. The panic in US-64 was due to the large fish eating small fish: i.e., some of the major investors got redemption prior to the closure of redemption leaving small investors at the mercy of UTI management. Even the government turned a Nelson's eye to what was happening in May and June 2001 in UTI. Now the small fish are being protected.

The dismal performance of US-64 is due to the both systematic risk and mismanagement due to the nexus between UTI and large investors. However, how can the largest mutual fund with a market share of about 90 per cent fare well when the stock markets have been abnormally down and there has been large scale mismanagement using discretionary powers?

The last year has witnessed several financial and economic shocks: Ketan Parekh scam in the stock market; insolvency of Ketan Parekh dragged down Madhavpura Cooperative Bank; jail for UTI chairman; payment crisis in Calcutta Stock Exchange; alleged involvement of BSE top management in a scam and resultant change in top management;

global economic slowdown; earthquake in Gujarat; cyclone in Orissa; attack on World Trade Center; and India's Parliament and J&K Assembly.

What are the options available to investors (particularly small investors) who have remained loyal, though helpless, and enjoying good returns from the UTI's US-64 for the last 35 years?

Investors need to hold their units as NAV is logically expected to improve once the Sensex starts going up. US-64 equity exposure is substantially along Tarapore Committee Recommendations.

Investors should hold their portfolio till at least May 2003 instead of redeeming at administered prices of Rs 10.50 in January 2001. They would gain a tax free 14.3 per cent return in 17 months. No other investment can offer such attractive returns, in today's context. Moreover, if NAV goes up due to market boom, investors may gain more by selling at NAV

administered price in 2003. Alternatively, small investors holding less than 5,000 units can sell their units back to the fund at administered price of Rs 10.50 in January, and buy fresh units at about 6.09 at lower NAV linked prices, claim loss in their income tax calculations, have a realised profit of 4.41 maintaining their portfolio.

It is felt in some quarters that the NAV declared by UTI is on a higher side because the valuation of many US-64 holdings is implausibly high. In my opinion, this is not the right time to fix up the NAV. It has only created some sort of panic. The UTI should have declared NAV when Sensex was between 3,600 and 4,200: the normal range. Anything below it or above it is abnormal and therefore would get reflected in the NAV. However, this should not be a cause of too much worry. NAVs of 24 mutual funds both in private sector as well as public sector are less than that of US-64. Moreover, 84 per cent of US-64 debt portfolio is in government securities and investments with ratings between AAA and BBB.

Presently, investors have got the best bet with market driven NAV and UTI (government) administered price for redemption. Crisis is temporarily averted and UTI has bailed itself out for the time being.

