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# CPSE ETF further fund offer may give short-term gains, but should you invest?

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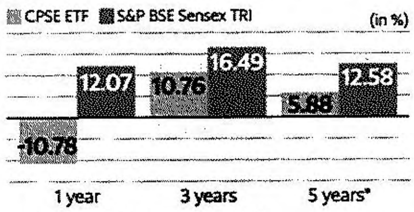
## Muted returns

The CPSE ETF has underperformed the broader Sensex over almost all time periods




*From 28 March 2014 to 12 March 2019

Source: Value Research, Data as on 12 March 2019

## How investors at different entry points fared

The discount has greatly cushioned the relatively modest returns of the ETF

**CPSE Exchange Traded Fund**

| Listing date | Period | Returns (in %) | Discount (in %) |
|---|---|---|---|
| NFO | 04.04.2014-13.03.2019 | 5.61 | 5* |
| 1st FFO | 31.01.2017-13.03.2019 | -2.76 | 5 |
| 2nd FFO | 28.03.2017-13.03.2019 | -4.44 | 3.50 |
| 3rd FFO | 10.12.2018-13.03.2019 | 13.96 | 4.50 |

*Bonus of one unit for every 15 units was also provided to investors who held their units for at least one year

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The government's further fund offer (FFO) of CPSE ETF will open to retail investors today and will be open till 22 March. The FFO was opened to anchor investors on 19 March and seeks to raise ₹3,500 crore with an option to retain up to ₹5,000 crore in case of oversubscription. The exchange-traded fund (ETF) is managed by Reliance Nippon AMC. Investors are being offered a 4% discount on the 'reference market price' of the underlying ETF shares. The reference market price is the average of the full day volume weighted average price of the constituents of the Nifty CPSE Index on the NSE over 20 and 22 March.

The CPSE ETF was launched in 2014 and has seen three FFOs since then. The current offering is the fourth FFO. Investors who bought the ETF at its initial launch were offered a 5% discount and bonus units if they held the ETF for more than one year. Investors in the subsequent three offers were also offered discounts of 5%, 3.5% and 4.5%, respectively. The CPSE ETF has 11 public sector companies. Just four companies in the power, coal and oil sectors make up as much as 77% of the ETF—ONGC, NTPC, Coal India and IOC. These are not the same PSUs as the original composition of the CPSE ETF in 2014. A few PSUs such as GAIL India, NTPC, Container Corporation of India and Engineers India have been dropped while others like NLC India, SJVN and NBCC India have been added. "The CPSE ETF is trading at very attractive valuations. As of 28 February, the dividend yield of the index was as high as 5.52% compared to 1.25% for the Nifty 50. The PE ratio was 8.43 compared to 26.32 on the Nifty. In addition, the government is also giving a 4% discount to investors," said Vishal Jain, head, ETFs, and fund manager, Reliance Nippon AMC.

### SHOULD YOU INVEST?

Experts are divided on this question. Shyam Sekhar, chief ideator and founder, iThought, came out in support of the ETF on valuation and macroeconomic grounds. "PSUs are extremely under-owned and have a lot of short-term negatives priced in. Overall, the economic growth has been muted in the last five years as there was no investment cycle revival. This is likely to change in the next five years regardless of who wins the election. CPSEs in the energy sector will benefit from this revival and an ETF is a good way to access them," he said.

Samant Sikka, founder, Sqrrl, an online mutual fund platform, also favoured the investment due to its ability to give low-cost exposure to multiple public sector firms. "Investors in the CPSE ETF are well served by the basket of companies, which spares them the time and effort needed to buy individual companies. The product is also highly transparent, liquid and low-cost," he said.

**A discount of 4% in the CPSE ETF can offer short term gains to investors who exit immediately after the listing**

However, some believe that the CPSE ETF may not be a good idea from a long-term perspective. Deepak Khemani, a Mumbai-based wealth manager recommends the ETF only as a short-term play due to the discount. "Ideally, people should invest in ETFs for the long term. However, in PSU-dominated ETFs like CPSE, investors usually enter only for the discount and exit soon after listing. I would not recommend it as a long-term investment. However, someone who wants to capture the discount can do so," he said.

### MINT'S TAKE

The CPSE ETF consists wholly of the government-owned companies and this comes with certain risks. Government companies are often managed from a welfare or political point of view rather than the profit motive. For example, in January 2018, ONGC was forced to buy HPCL from the central government to help meet the government's disinvestment target. The CPSE ETF has also delivered poor returns in the past. Its returns since launch stand at 6.62% CAGR (as on 19 March 2019). Valuations of the ETF are indeed attractive compared to the broader market but this may just be a reflection of the poor performance of the ETF constituents and the lack of market confidence in them. The discount can offer short-term gains to investors who exit immediately after listing. However, short-term market plays are not a tactic that we recommend.