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LIC MUTUAL FUND

LIC MF Short Duration Fund

Abstract

India's evolving financial landscape has increased demand for investment products that balance stability, liquidity and moderate returns in volatile macroeconomic environments. Traditional fixed-income instruments often expose investors to either excessive interest-rate sensitivity or inadequate liquidity, creating challenges for retail and institutional investors seeking short-to medium-term financial planning solutions. LIC Mutual Fund addressed this market requirement through the *LIC MF Short Duration Fund*, an open-ended short-term debt scheme investing in debt and money market instruments with a Macaulay duration maintained between one and three years. Operational since 1 February 2019, the fund was designed to deliver risk-adjusted returns while maintaining moderate interest rate risk and moderate credit risk exposure. The fund follows an actively managed investment strategy combining top-down macroeconomic analysis, selective credit exposure, disciplined duration management and liquidity optimisation.

Introduction

LIC Mutual Fund launched the *LIC MF Short Duration Fund* as an open-ended debt scheme investing primarily in debt securities and money market instruments while continuing a Macaulay duration between one and three years. Operational since 1 February 2019, the fund was conceptualised as a stable, fixed-income solution for investors seeking reasonable returns over short-to medium-term horizons with moderate risk exposure.

The initiative appeared during a period of variable interest rates and volatile macroeconomic conditions, when investors increasingly sought low-volatility investment options that could balance liquidity, stability and yield optimisation.

The fund adopted an actively managed strategy focused on high-quality debt instruments, tactical duration management, selective credit exposure and macroeconomic

responsiveness. The portfolio management process incorporated in-house credit research and top-down analysis of interest rates, liquidity circumstances, inflationary expectations, RBI policy stance, fiscal deficits, global interest rates and exchange rate movements.

The scheme also introduced investor-centric features such as daily SIP options, zero exit load structures, multiple IDCW frequencies and transparent risk classification employing the PRC Matrix framework. The product has successfully strengthened investor confidence in short-duration debt investing while maintaining liquidity and portfolio stability across changing market conditions.

The Problem Statement India's fixed-income investment environment has consistently faced structural challenges, including volatility, liquidity, accessibility and interest rate sensitivity. Retail and institutional investors seeking short- to medium-term investment avenues commonly face a difficult trade-off among stability, yield optimisation and liquidity management.

Traditional debt products frequently expose investors either to high duration risk during interest rate fluctuations or to low-yield structures incapable of generating meaningful returns. This became particularly significant over volatile macroeconomic cycles characterised by changing RBI monetary policies, inflationary forces, fiscal deficit concerns and global interest rate uncertainty.

Investors also required investment products capable of supporting short-term financial planning objectives such as emergency funds, education expenses, travel planning and institutional liquidity management without exposing capital to excessive market volatility.

Another important challenge involved balancing portfolio duration and credit quality. Many debt schemes that aim to improve returns have increased exposure to longer-duration securities or lower-credit-quality instruments, thereby increasing risk for conservative investors.

The fixed-income market additionally faced concerns regarding transparency, portfolio quality and access to retail participants. Many traditional fixed-income instruments lacked active risk control frameworks and flexible structures for investor participation. LIC Mutual Fund, therefore, identified the need for a professionally managed short-duration debt solution capable of delivering moderate, risk-adjusted returns through disciplined duration management, selective credit exposure, liquidity optimisation and macroeconomic responsiveness.

Solutions Stack The *LIC MF Short Duration Fund* was designed as a comprehensive short-duration fixed-income solution integrating active duration management, selective credit exposure, macroeconomic analysis and investor-centric flexibility.

The first component involved maintaining Macaulay duration between 1 and 3 years, consequently reducing interest rate sensitivity compared to longer-duration debt products. This duration framework enabled the fund to effectively balance liquidity and yield optimisation.

The second component focused on portfolio diversification across debt and money market instruments. The scheme invested in investment-grade debt securities, money market instruments, mutual fund units and instruments of the Corporate Debt Market Development Fund (CDMDF).

The third major component involved active investment management. The portfolio followed a top-down investment process evaluating factors such as interest rate outlook, term structure, systemic liquidity, RBI policy stance, inflationary expectations, government borrowing programmes, fiscal deficit trends, global interest rates and foreign exchange movements. In-house credit research formed an additional crucial pillar of the solutions stack. The investment management team emphasised rigorous credit analysis while investing primarily in investment-grade securities rated by recognised credit rating agencies.

The fourth component involved tactical allocation shifts. Portfolio duration and asset allocation were dynamically adjusted in response to evolving macroeconomic conditions and liquidity environments to optimise returns while protecting capital.

The fund also introduced investor-friendly operational features, including daily SIP options, zero exit load structures and multiple IDCW frequencies, to improve accessibility and investment flexibility.

Strategic Vision and Institutional Philosophy

LIC Mutual Fund approached the *LIC MF Short Duration Fund* initiative with the strategic objective of creating a transparent, actively managed and investor-friendly debt solution that balances stability, liquidity and moderate return generation.

The institution recognised that modern investors increasingly require low-volatility investment options aligned with short to medium-term financial planning objectives. The fund was therefore positioned as a disciplined fixed-income solution suitable for conservative and moderately risk-sensitive investors.

The strategic philosophy underlying the initiative rested on four pillars. The first involved duration optimisation by maintaining Macaulay duration within the SEBI-defined one-to-three-year framework.

The second pillar focused on high portfolio quality through investment-grade debt instruments and strong in-house credit analysis. The third involved dynamic responsiveness to changing interest rate cycles, liquidity status and macroeconomic developments. The fourth emphasised accessibility and transparency through SIP flexibility, risk disclosures and investor-centric operational features.

The fund also aligns with LIC Mutual Fund's broader institutional philosophy of prudent portfolio management, disciplined risk governance and long-term investor assurance, confidence-building within India's debt capital markets.

Implementation Journey

The first implementation phase focused on designing a portfolio structure capable of balancing moderate returns with controlled interest rate and credit risk exposure. The scheme adopted the SEBI-defined short-duration category framework, with Macaulay duration ranging from 1 to 3 years.

The second phase consisted of establishing the active portfolio management process. The investment team developed a top-down macroeconomic assessment framework merging interest rate analysis, liquidity monitoring, inflation forecasting and fiscal assessment into portfolio construction decisions.

Subsequent implementation efforts concentrated on optimising portfolio quality. Exposure to high-quality corporate bonds was increased while allocations to

instruments with elevated duration or credit risk were selectively moderated.

A major milestone occurred on 29 July 2023, when IDBI Short Term Bond Fund merged with *LIC MF Short Duration Fund*, creating a blended performance structure based on a weighted-average approach as per SEBI guidelines. Throughout implementation, the fund maintained continuous responsiveness to changing liquidity situations, interest rate cycles and macroeconomic developments.

Implementation Challenges

The implementation process encountered a number of challenges in market and portfolio management. One of the primary challenges involved navigating volatile interest rate environments while maintaining portfolio stability and optimal duration exposure. Frequent changes in RBI monetary policy and global rate conditions required continuous practical adjustments.

Another challenge involved balancing liquidity, yield optimisation and credit quality simultaneously. Higher-yield opportunities often entail greater credit or duration risk, requiring disciplined investment selection and risk governance. The fund also underwent challenges related to investor expectations during periods of lower short-term yields. Conservative investors often seek higher returns without proportionate risk, requiring transparent communication of realistic fixed-income performance expectations.

Operationally, identifying high-quality issuers within the limited short-duration investment universe remained challenging, particularly during periods of market stress and liquidity tightening. The fund also remained sensitive to sudden interest rate hikes despite its short-duration orientation, reflecting broader macroeconomic factors in debt markets.

Highlights

- LIC Mutual Fund launched the *LIC MF Short Duration Fund* in February 2019 as an actively managed short-term debt scheme designed to provide stable, risk-adjusted returns with moderate interest-rate and credit risk exposure.
- The fund addressed challenges in India's fixed-income market such as volatility, liquidity constraints and excessive duration risk by maintaining a Macaulay duration between one and three years and focusing on high-quality debt instruments.
- The investment strategy combined active duration management, selective credit exposure, top-down macroeconomic analysis and rigorous in-house credit research to optimise liquidity, portfolio quality and returns across changing market conditions.
- Investor-centric features such as daily SIPs, zero exit loads, multiple IDCW frequencies and transparent risk disclosures improved accessibility, flexibility and confidence among retail and institutional investors.
- The initiative benefited around 9.6 lakh investors, strengthened LIC Mutual Fund's position in the short-duration debt category and demonstrated how professionally managed debt products can support stable, low-volatility financial planning solutions.

Outcomes LIC MF Short Duration Fund generated significant investor-centric and institutional outcomes through its disciplined portfolio management strategy. The fund successfully established itself as a stable, transparent short-duration debt solution capable of delivering consistent, risk-adjusted returns even in volatile interest rate environments. The initiative strengthened investor confidence in short-term debt investing by maintaining portfolio quality, liquidity and capital preservation across varying market cycles.

The scheme currently benefits approximately 960,000 external beneficiaries, demonstrating significant market participation and institutional scale. Operationally, the fund maintained active responsiveness to changing liquidity conditions and macroeconomic developments through tactical duration management and selective credit allocation. The introduction of investor-friendly features, such as daily SIPs, zero exit loads and multiple IDCW frequencies, improved accessibility and flexibility in participation for retail investors.

Institutionally, the initiative strengthened LIC Mutual Fund's positioning in the short-duration debt category while demonstrating disciplined fixed-income portfolio management. The merger with IDBI Short Term Bond Fund in July 2023 additionally enhanced portfolio scale and operational integration within the fixed-income ecosystem.

Conclusion LIC MF Short Duration Fund demonstrates that actively managed short-duration debt schemes can provide stable, investor-friendly fixed-income solutions in volatile macroeconomic environments. By maintaining disciplined Macaulay duration management, selective credit exposure, active macroeconomic responsiveness and strong portfolio quality controls, LIC Mutual Fund successfully created a balanced investment vehicle for investors seeking moderate returns with controlled risk.

The initiative also highlights the growing importance of professionally managed debt products within India's evolving financial ecosystem. As investors increasingly seek transparent, liquid and low-volatility alternatives to traditional fixed-income instruments, short-duration debt schemes are becoming critical components of household and institutional financial planning.

Importantly, the fund illustrates that successful debt portfolio management requires not only yield optimisation but also the continuous balancing of liquidity, credit quality, duration risk and investor faith.



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