

Notice - Cum - Addendum No. 32 of 2018
Addendum to the Scheme Information Document and Key Information Memorandum of
IDFC Cash Fund

Change in features of the Scheme:

NOTICE is hereby given that pursuant to SEBI circular dated October 6, 2017 on categorization and rationalization of mutual fund schemes, the features of IDFC Cash Fund, an open ended liquid fund, shall stand modified as follows with effect from **Monday, May 28, 2018** ("Effective Date"):

Investment Objectives

Existing	Proposed
To generate optimal returns with high liquidity by investing in high quality money market and debt instruments.	The Scheme seeks to offer an investment avenue for short term savings by looking to generate returns commensurate with a low risk strategy and with high liquidity, from a portfolio that is invested in debt and money market securities with maturity up to 91 days.

Asset Allocation Pattern (existing)

Instruments	Indicative Allocation (as % of total assets)	
	Maximum	Minimum
Money Market Instruments and debt instruments with maturity up to 91 days	100	0

Investment in Securitised Debt upto 50%

Gross Exposure to Repo of Corporate Debt Securities – upto 10% of the net assets of the Scheme

Investment in Foreign Debt Instruments upto 50%

The Scheme will invest in those Debt/Money Market Instruments of maturity of upto 91 days.

In case of securities where the principal is to be repaid in a single payout the maturity of the securities shall mean residual maturity. In case the principal is to be repaid in more than one payout then the maturity of the securities shall be calculated on the basis of weighted average maturity of security. In case of securities with put and call options (daily or otherwise) the residual maturity of the securities shall not be greater than 91 days. In case the maturity of the security falls on a non-business day then settlement of securities will take place on the next business day.

On introduction of cheque writing facility by RBI / such other authority, the AMC may introduce the same under the scheme.

On introduction of the said facility, the Scheme will comply with guidelines, procedures issued and as required, a minimum percentage of the net assets or such other minimum asset allocation, as may be prescribed by the concerned authority from time to time, will be adhered to. The Fund in normal circumstances would invest in short dated instruments. Investments would predominantly be in the call market, repos, commercial papers (CPs), certificates of deposits (CDs), short dated bonds, bills rediscounted (BRDS) and MIBOR linked instruments etc. that may become available from time to time. The primary investment strategy is to minimize interest rate risk and ensure liquidity at all times.

Cheque writing facility

The Reserve Bank of India (RBI) had announced in its mid-term Review of Monetary and Credit Policy for 1999-2000 that it would permit scheduled commercial banks to offer 'cheque writing' facility to Gilt Funds and to those Liquid Income schemes of mutual funds which predominantly invest in money market instrument (not less than 80% of their corpus). In accordance with this announcement and the guidelines issued by RBI and any amendments to the Guidelines thereof, the Scheme may offer Cheque Writing Facility to its Unitholders.

Asset Allocation Pattern (proposed/ revised)

Asset Class	Indicative allocation (as % of total assets)
Debt Securities (including G-Sec and securitised debt) and Money Market Instruments with maturity* up to 91 days	0% - 100%

*In case of securities where the principal is to be repaid in a single payout the maturity of the securities shall mean residual maturity. In case the principal is to be repaid in more than one payout then the maturity of the securities shall be calculated on the basis of weighted average maturity of security. In case of securities with put and call options (daily or otherwise) the residual maturity of the securities shall not be greater than 91 days. In case the maturity of the security falls on a non-business day then settlement of securities will take place on the next business day.

Investment in Securitised Debt - up to 50% of the total assets.

Exposure in Derivatives - up to 100% of total assets.

Gross Exposure to Repo of Corporate Debt Securities - up to the extent permitted by the Regulations (currently up to 10% of total assets, subject to change in line with the regulations from time to time).

Investment in Foreign securities - up to 50% of total assets.

Investment in Securities lending - up to 20% of the total assets with maximum single party exposure restricted to 5% of the total assets.

The Scheme may engage in short selling of securities in accordance with the applicable guidelines / regulations. The scheme may invest in Credit Default Swaps (CDS) in accordance with the applicable regulations as and when permitted by SEBI/RBI up to the extent permitted by the regulations.

The cumulative gross exposure through derivatives and debt & money market instruments along with repo transactions in corporate debt securities and credit default swaps shall not exceed 100% of the net assets of the Scheme.

Investment Strategy

Existing	Proposed
The domestic debt markets are maturing rapidly with liquidity emerging in various debt segments through the introduction of new instruments and investors. The aim of the Investment Manager will be to allocate the assets of the Scheme between various money market and fixed income securities with the objective of achieving stable returns with a highly liquid portfolio. The actual percentage of investment in various fixed income securities will be decided after considering the prevailing political conditions, the economic environment (including interest rates and inflation), the performance of the corporate sector and general liquidity and other considerations in the economy and markets.	The Scheme proposes to invest in fixed income securities and money market instruments with the aim of generating returns commensurate with a low risk strategy. The Scheme will invest in Debt securities and money market instruments with maturity up to 91 days. The aim of the Investment Manager will be to allocate the assets of the Scheme amongst various fixed income instruments (debt / money market) with the objective of optimizing returns with a highly liquid portfolio. The actual percentage of investment in various fixed income instruments from time to time will be decided basis the prevailing macro-economic environment (including interest rates and inflation), market conditions, general liquidity, and fund manager views.

Further, the following disclosures are being inserted in the Scheme Information Document:

Risks associated with Investing in Derivatives (inserted under the section "Risk Factors"):

Derivative products are leveraged instruments and can provide disproportionate gains as well as disproportionate losses to the investor. Execution of such strategies depends upon the ability of the fund manager to identify such opportunities. Identification and execution of the strategies to be pursued by the fund manager involve uncertainty and decision of fund manager may not always be profitable. No assurance can be given that the fund manager will be able to identify or execute such strategies. The risks associated with the use of derivatives are different from or possibly greater than, the risks associated with investing directly in securities and other traditional investments. As and when the Scheme trade in the derivatives market there are risk factors and issues concerning the use of derivatives that investors should understand. Derivative products are specialized instruments that require investment techniques and risk analyses different from those associated with Money Market Instruments bonds. The use of a derivative requires an understanding not only of the underlying instrument but of the derivative itself. Derivatives require the maintenance of adequate controls to monitor the transactions entered into, the ability to assess the risk that a derivative adds to the portfolio and the ability to forecast price or interest rate movements correctly. There is the possibility that a loss may be sustained by the portfolio as a result of the failure of another party (usually referred to as the "counter party") to comply with the terms of the derivatives contract. Other risks in using derivatives include the risk of mispricing or improper valuation of derivatives and the inability of derivatives to correlate perfectly with underlying assets, rates and indices.

Derivatives are highly leveraged instruments. Even a small price movement in the underlying security could have a large impact on their value. Also, the market for derivative instruments is nascent in India.

The risks associated with the use of derivatives are different from or possibly greater than the risks associated with investing directly in securities and other traditional investments.

The specific risk factors arising out of a derivative strategy used by the Fund Manager may be as below:

- Lack of opportunity available in the market.
- The risk of mispricing or improper valuation and the inability of derivatives to correlate perfectly with underlying assets, rates and indices.

Risk associated with Interest Rate Future

- Market Risk - Derivatives carry the risk of adverse changes in the market price.
- Liquidity Risk - This occurs where the derivatives cannot be sold (unwound) at prices that reflect the underlying assets, rates and indices.
- Model Risk - The risk of mispricing or improper valuation of derivatives.
- Basis Risk - This risk arises when the instrument used as a hedge does not match the movement in the instrument/ underlying asset being hedged. The risks may be inter-related also; for e.g. interest rate movements can affect equity prices, which could influence specific issuer/industry assets.
- Risk associated with imperfect hedge due to use of IRF are - 'Basis Risk' is the risk that arises when the instrument used as a hedge does not match the movement in the instrument/ underlying asset being hedged. This could result into potential gains or losses from the strategy.

Risk Management Strategies

Risk Description	Risk Management
As and when the Scheme trades in the derivatives market there are risk factors and issues concerning the use of derivatives that Investors should understand. Derivative products are specialized instruments that require investment techniques and risk analyses different from those associated with stocks and bonds. The use of a derivative requires an understanding not only of the underlying instrument but also of the derivative itself. Derivatives require the maintenance of adequate controls to monitor the transactions entered into, the ability to assess the risk that a derivative adds to the portfolio and the ability to forecast price or interest rate movements correctly. There is the possibility that a loss may be sustained by the portfolio as a result of the failure of another party (usually referred to as the "counter party") to comply with the terms of the derivatives contract. Other risks in using derivatives include the risk of mispricing or improper valuation of derivatives and the inability of derivatives to correlate perfectly with underlying assets, rates and indices.	The fund has provision for using derivative instruments in the manner permitted by SEBI from time to time. Interest Rate Swaps will be done with approved counter parties under pre-approved ISDA agreements. Mark to Market of swaps, netting off of cash flow and default provision clauses will be provided as per international best practice on a reciprocal basis. Interest rate swaps and other derivative instruments will be used as per local (RBI and SEBI) regulatory guidelines.

Note on investment in Derivatives (inserted under the Section "Information about the scheme")

The following information provides a basic idea as to the nature of the derivative instruments proposed to be used by the Scheme and the risks attached there with.

Advantages of Derivatives:

The volatility in Indian markets both in debt and equity has increased over last few months. Derivatives provide unique flexibility to the Scheme to hedge part of its portfolio. Some of the advantages of specific derivatives are as under:

Derivatives Strategy:

The Scheme may use derivatives instruments like Interest Rate Swaps, Forward Rate Agreements, Interest Rate Futures or such other derivative instruments as may be introduced from time to time and in the manner permitted by SEBI/RBI from time to time.

Interest Rate Swaps (IRS)

An IRS is an agreement between two parties to exchange stated interest obligations for an agreed period in respect of a notional principal amount. The most common form is a fixed to floating rate swap where one party receives a fixed (pre-determined) rate of interest while the other receives a floating (variable) rate of interest.

In terms of SEBI circular no. Cir/IMD/DF/11/2010 dated August 18, 2010, Mutual Funds may enter into plain vanilla interest rate swaps for hedging purposes. The counter party in such transactions has to be an entity recognized as a market maker by RBI. Further, the value of the notional principal in such cases must not exceed the value of respective existing assets being hedged by the scheme. Exposure to a single counterparty in such transactions should not exceed 10% of the net assets of the scheme.

Basic Structure of a Swap:

Bank A has a 6 month Rs 10 crore liability, currently being deployed in call. Bank B has a Rs 10 crore 6 month asset, being funded through call. Both banks are running an interest rate risk.

To hedge this interest rate risk, they can enter into a 6 month MIBOR (Mumbai Inter Bank Offered Rate) swap. Through this swap, A will receive a fixed pre-agreed rate (say 7%) and pay "call" on the NSE MIBOR ("the benchmark rate"). Bank A's paying at "call" on the benchmark rate will neutralise the interest rate risk of lending in call. B will pay 7% and receive interest at the benchmark rate. Bank A's receiving of "call" on the benchmark rate will neutralise his interest rate risk arising from his call borrowing.

The mechanism is as follows:

- Assume the swap is for Rs. 10 crore from March 1, 2017 to September 1, 2017. A is a fixed rate receiver at 7% and B is a floating rate receiver at the overnight compounded rate.
- On March 1, 2017 A and B will exchange only an agreement of having entered this swap. This documentation would be as per International Swaps and Derivatives Association (ISDA).
- On a daily basis, the benchmark rate fixed by NSE will be tracked by them.

On September 01, 2017 they will calculate the following:

- A is entitled to receive interest on Rs. 10 crore at 7% for 184 days i.e. Rs. 35.28 lakh, (this amount is known at the time the swap was concluded) and will pay the compounded benchmark rate.
- B is entitled to receive daily compounded call rate for 184 days & pay 7% fixed.
- On September 1, 2017, if the total interest on the daily overnight compounded benchmark rate is higher than Rs. 35.28 lakhs, A will pay B the difference. If the daily compounded benchmark rate is lower, then B will pay A the difference.
- Effectively Bank A earns interest at the rate of 7% p.a. for six months without lending money for 6 months fixed, while Bank B pays interest @ 7% p.a. for 6 months on Rs. 10 crore, without borrowing for 6 months fixed.
- The AMC retains the right to enter into such derivative transactions as may be permitted by the applicable regulations from time to time.

Forward Rate Agreement (FRA)

A FRA is basically a forward starting IRS. It is an agreement between two parties to pay or receive the difference between an agreed fixed rate (the FRA rate) and the interest rate (reference rate) prevailing on a stipulated future date, based on a notional principal amount for an agreed period. The only cash flow is the difference between the FRA rate and the reference rate. As is the case with IRS, the notional amounts are not exchanged in FRAs.

Interest Rate Future (IRF)

Interest Rate Futures means a standardized interest rate derivative contract traded on a recognized stock exchange to buy or sell a notional security or any other interest bearing instrument or an index of such instruments or interest rates at a specified future date, at a price determined at the time of the contract.

Exchange traded IRFs are standardized contracts based on a notional coupon bearing Government of India (GOI) security.

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As there is an inverse relationship between interest rate movement and underlying bond prices and the futures price also moves in tandem with the underlying bond prices. If the Fund Manager has a view that interest rates will rise in the near future and intends to hedge the risk from rise in interest rates; the Fund Manager can do so by selling the IRF contracts to hedge the interest rate risk on the underlying portfolio.

If the Fund Manager is of the view that the interest rates will go down the Fund Manager will buy IRF to participate in appreciation.

Example:

The scheme holds cash & cash equivalent and expects that the interest rate will go down and intends to take directional position. Accordingly, the fund manager shall buy IRF –

- Trade Date - January 1, 2018
- Futures Delivery date - April 1, 2018
- Current Futures Price - Rs. 102.00
- Futures Bond Yield- 8.85%
- Trader buys 200 contracts of the April 2017 10 Year futures contract of face value of Rs.1000 on NSE on January 1, 2018 at Rs. 102.00

Closing out the Position

- Date: January 7, 2018
- Futures market Price - Rs. 105.00
- Trader sells 200 contracts of April 2018 10 year futures contract of face value of Rs.1000 at Rs. 105 and squares off his position
- Therefore total profit for trader $200 * 1000 * (105 - 102)$ is Rs.6,00,000

Pursuant to SEBI circular no. CIR/MRD/DRMNP/11/2015 dated June 12, 2015, the following position limits shall be applicable to mutual funds in for IRF contracts:

- a) Scheme of Mutual Fund Level - The gross open positions across all contracts within the respective maturity bucket shall not exceed 3% of the total open interest in the respective maturity bucket or INR 200 crore, whichever is higher.
- b) Mutual Fund Level - The gross open positions across all contracts within the respective maturity bucket shall not exceed 10% of the total open interest in the respective maturity bucket or INR 600 crore, whichever is higher.

Hedging

Debt securities are exposed to the risk of rising interest rates, which in turn results in the reduction in the value and such impact can be seen in the value of the portfolio of the scheme. Under such circumstances, in order to hedge the fall in the value of the portfolio of the scheme due to falling bond prices, the fund manager may sell IRF contracts.

Example:

Date: January 01, 2018
 Spot price of Security: Rs 101.80
 Futures price of IRF Contract: Rs 102.00

On January 01, 2018, the Fund Manager bought 2000 GOI securities from spot market at Rs 101.80. The Fund Manager anticipates that the interest rate will rise in near future, therefore to hedge the exposure in underlying security the Fund Manager sells March 2018, Interest Rate Futures contracts at Rs 102.00.

On March 01, 2018 due to increase in interest rate:

Spot price of Security: Rs 100.80
 Futures Price of IRF Contract: Rs 101.10

Loss in underlying market will be $(101.80 - 100.80) * 2000 = \text{Rs } 2000$
 Profit in the Futures market will be $(101.10 - 102.00) * 2000 = \text{Rs } 1800$

Imperfect Hedging

The Scheme may use Interest Rate Futures (IRF) in accordance with SEBI guidelines and may imperfectly hedge its portfolio or part of its portfolio using IRFs. Use of IRF may result in imperfect hedging when the IRF used for hedging the interest rate risk has different underlying security(s) than the existing position being hedged.

Example of imperfect hedge due to use of IRF:

Date: January 1, 2018
 Spot price of 8 year GOI Security: Rs.101.80
 Futures price of IRF Contract (underlying is 10 year GOI): Rs.102.00

On January 1, 2018, the Fund Manager bought 2000 GOI securities from spot market at Rs.101.80. The Fund Manager anticipates that the interest rate will rise in near future, therefore to hedge the exposure in underlying security the Fund Manager sells March 2018, Interest Rate Futures contracts at Rs.102.00.

On March 1, 2018 due to increase in interest rate:

Spot price of 8 year GOI Security: Rs.100.80
 Futures Price of IRF Contract (underlying is 10 year GOI): Rs.101.10

Loss in underlying market will be $(101.80 - 100.80) * 2000 = \text{Rs } 2000$
 Profit in the Futures market will be $(101.10 - 102.00) * 2000 = \text{Rs } 1800$

Because of imperfect hedging strategy, the profit in futures market is Rs.1800 while the loss in the cash market is Rs.2000, resulting in a net loss of Rs. 200.

The above change in the scheme features has been approved by the Board of Directors of the AMC and the Trustee Company.

The above changes in scheme features being a change in the fundamental attributes of the Scheme, in terms of regulation 18(15A) of SEBI (Mutual Funds) Regulations, investors in the Scheme are given an option to exit (redeem / switch-out) at the prevailing Net Asset Value without any exit load, in case they do not wish to continue in the Scheme in view of the proposed change in the Scheme's features. The period of this no load exit offer is valid for a period of 30 days from **Wednesday, April 25, 2018 to Friday, May 25, 2018** (both days inclusive). The normal redemption / switch request form may be used for this purpose and submitted at any of the IDFC AMC / CAMS ISCs. The no load exit option will be available only to those investments in the Scheme made prior to **Wednesday, April 25, 2018**.

Such exit option will not be available to unitholders whose units have been pledged or encumbered their units in the Scheme and Mutual Fund has been instructed to mark a pledge/lien on such units, unless the release of the pledge/lien is obtained and appropriately communicated to AMC / Mutual Fund prior to applying for redemption/switch-out.

Unitholders who do not exercise the exit option on or before **Friday, May 25, 2018** would be deemed to have consented to the proposed change. It may be noted that the offer to exit is merely an option and is not compulsory.

All other features, terms and conditions of the Scheme, as stated in the Scheme Information Document (SID) & the Key Information Memorandum (KIM) of the Scheme, read with the addenda issued from time to time, remain unchanged.

As regards the unitholders who redeem their investments during the Exit Option Period, the tax consequences as set forth in the Statement of Additional Information of IDFC Mutual Fund and Scheme Information Document of the Scheme would apply. In view of individual nature of tax consequences, unitholders are advised to consult your financial / tax advisor for detailed tax advice.

The Notice - Cum - Addendum forms an integral part of the SID and KIM of the Scheme, read with the addenda.

Date: April 23, 2018