Growing Preference for Corporate Debt Markets

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The financial sector in India has been continuously evolving and has witnessed remarkable progress, matching global standards in certain segments. There is a strong linkage between economic performance and the financial sector given that the latter provides the key tools for economic growth and development.

The corporate debt market has been an integral part of India's financial economic system as it plays a key role in financial investment and funding. The corporate debt market has been an integral part of India's financial economic system as it plays a key role in financial investment and funding.

Banks have traditionally been the main source of finance for companies in India. However, in recent times, with banks and corporates facing the "twin balance sheet" problem, funding from banks has been adversely impacted, taking bank credit growth to multi year lows. The constraints in the banking sphere have pulled down the private capital formation or investments over the last few years. These challenges and constraints have resulted in a change in mindsets for lenders and borrowers to explore alternative sustainable source of finance.

Regulators too have been working towards developing and promoting alternate sources of funding. To this end they have been focusing on developing the corporate bond market and are trying to move corporates towards the corporate bond market to source their funding requirements. Having a blend of instruments such as bonds, non-convertible debentures (NCDs), securitised instruments and commercial paper issued by private corporates, public sector undertakings and financial institutions, the corporate bond market has been the go-to option for corporates in the recent years. The growing preference for corporate bond markets can be seen from the increase in total issuances in recent years. Corporate bond issuances have jumped from Rs. 3.70 lakh crores in FY13 to Rs. 6.44 lakh crs in FY18, a 74% increase in 5 years. Commercial paper issuances too have witnessed robust growth. Issuances here have risen from Rs. 6.10 lakh crs in FY13 to Rs.22.92 lakh crs in FY18, a growth of 275%.

Recently SEBI has released a draft report on deepening the corporate bond market in line with what was announced by the Finance Minister in the Union Budget 2018-19. There is a recommendation that post March 2019 all large corporates defined as those with above Rs 100 crore of long term borrowing (which excludes ECBs and inter corporate borrowing) will have to borrow 25% of incremental funding requirements from the corporate bond market. This will hold for AA rated companies to begin with and will be extended to A rated companies at a later date. This is a progressive step taken which when implemented will increase supply of high quality paper in the market.

As the economy grows, the corporate debt market garners interest and with it credit rating. The state of the financial sector viz. the corporate debt market and banking industry which in turn is dependent on the state of the economy and prevailing and potential investment climate is critical for the credit rating industry. The growth in the corporate debt market and banking industry chalks the growth for the credit rating industry.

The Indian Economy has weathered two structural breaks in the form of demonetization and implementation of Goods and Service Tax (GST) in FY17 and FY18 respectively and is now emerging on the path of higher growth. With this the demand for funds is slated to increase and the corporate bond markets are looked upon as being equipped to meet the growing fund requirements.