Bond market woos firms with lower interest rates

Indian companies are cutting reliance on banks for their borrowing needs

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MUMBAI: Top-rated companies are selectively shifting to the bond market for their borrowing needs, cutting their reliance on banks, as the bond market offers lower interest rates and easier terms.

While these are still early days, bankers said that large corporates are increasingly locking in funds by selling bonds instead of opting for floating rate loans amid a rising interest rate scenario.

For an AAA-rated corporate, a 2-3 year bond is now available at 7.15-7.45%, whereas a three-year bank rate is at 7.3-7.5%.

Most of the funds being raised by these companies mature in 2-3 years.

AAA-rated non-bank lenders and state-run companies have been tapping the bond market over the past few months. Many infrastructure companies, especially those in the road and telecom sectors and the National Investment and Infrastructure Fund (NIIF), are also selling bonds."Manufacturing companies, who were relying on bank borrowing, have started doing fixed rate bond issuances. Public sector units (PSUs) have started coming to the market. With more issuances coming to the market in the short tenure, there is short supply in the longer tenure," said Ajay Manglunia, managing director of JM Financial.

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According to data compiled by Prime Database, ₹1.45 trillion worth of debt has been raised by selling bonds since June. That is 15% more than the amount raised through bonds and non-convertible debentures last year.

Banks have also been borrowing from the bond market by raising perpetual, tier-II and infrastructure bonds.

Punjab National Bank, Bank of Baroda and Canara Bank raised funds through additional tier-I or AT1 bonds.

Issuances of certificates of deposits (CDs) have also seen a spike as banks raise these short-term funds to meet the credit demand, which continues to outpace deposit growth.

"Only AAA corporates are selectively looking at the bond market. Non-AAA-rated companies still prefer the loan market. Credit spreads have become very tight, and yields on AAA-rated bonds are not moving higher. While credit spread on 10-year AAA corporate bond was around 25 basis points (bps) earlier, it has narrowed to around 10 bps over G-Sec on an annualized basis," said Dhawal Dala, chief investment officer, Edelweiss AMC.

While borrowing from the bond market can often be cheaper, it can also be fraught with risks. Bond investors can be fickle and move out quickly when things turn bad. In contrast, banks tend to develop long-term relationships with their clients and often support them during bad times.

That said, banking sector credit growth continues to be strong, expanding 15.8% from a year earlier as of 12 August, led by demand from retail and small and medium businesses, while working capital demand remains healthy among corporates.