Short term rates hit 8% on tight liquidity

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Yields on short term money market instruments are beginning to inch up again with rates on one-year commercial paper (CP) touching a high of 8%.

Liquidity deficit, non-banking finance companies looking to raise short term money post the Reserve Bank's decision to increase risk weights on loans to these companies are some of the factors behind the increase in CP yields.

"There is a a general upward movement in money market yields. But more pronounced in NBFC spreads over T-bill rates after the recent action by the RBI," said Dhawal Dalal, Edelweiss Asset Management. "Additional risk weights should result in 20-30 bps increase in cost of funds and thereby lending rate. But mutual funds may offer at slightly better levels depending on the credit, tenor and other considerations," he said.

Yield on 12-month CP jumped by 13 basis points to 8.1% as on 5 December as compared to 7.97% as on 15 November, a day after which RBI increased risk weights on loans against NBFCs by 25 basis points. Similarly yields on 2-3 month CPs issued by NBFCs jumped by 20 basis points to 7.87% during the same period.

"CPs rate may be better than NCD rates. But NBFCs will be looking to issue more non-convertible debentures instead of CPs. Short term rates going up. Rates are going to remain higher for a longer period of time," said Ajay Manglunia, managing director and head of the investment grade group, JM Financial.

Yield on 12-month CP jumped by 13 basis points to 8.1% as on 5 December. ISTOCKPHOTO

Banking liquidity has been in a deficit mode for most of November with the RBI injecting liquidity at an average of ₹1.4 trillion during the past week. This tight liquidity has been due to rising cash demand during the festive season, higher credit demand and foreign fund outflows.

According to data compiled by Prime Database, commercial paper issuances stood at ₹8.85 trillion during April to November this year compared to ₹9.23 trillion during the corresponding period last year.

Besides the larger ones, other NBFCs are not looking to tap the money market to raise funds. Despite the increase in lending rates, these NBFCs feel that they would prefer bank funding.