Brokers' Borrowing Boom Is Remodeling India's Short-Term Debt Market

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Summary:

Brokers now account for about 21% of commercial paper issued this year, up from 4% in 2021.

Prominent brokerages have raised roughly 3.2 trillion rupees ($33 billion) via commercial paper to fund client leverage.

Leveraged equity positions neared a record 1.6 trillion rupees by Sept. 30, while margin loans remain under 0.5% of India's $4.8 trillion market.

What happened

India's brokerages are tapping short-term debt at scale to keep pace with clients' margin trades. Data from primedatabase.com show brokers' share of commercial paper issuance has jumped to about 21% this year from 4% in 2021, with prominent firms raising around 3.2 trillion rupees, or $33 billion, via commercial paper. Among the top issuers of short-term paper are heavyweight bank-owned outfits such as HDFC Securities Ltd., ICICI Securities Ltd., and Kotak Securities. The margin-trading boom is spilling into debt funding even as Indian stocks have come under pressure from higher oil prices and elevated global yields.

Why brokers are borrowing more

Leverage demand is the driver. According to IndiaMTF.com, margin-based equity holdings had risen to almost the 1.6 trillion-rupee record as of Sept. 30. As Kotak Securities Ltd. chief operating officer Sandeep Chordia put it, "The rise in CP issuance by brokers is closely aligned with the growth in their

margin trade facility books." He added, "We expect this linkage to continue as MTF scales up." Policy shifts are also nudging the market: In February, the Reserve Bank of India tightened banks' lending to proprietary trading firms, sending brokers in search of other funding. Then in June, the securities regulator proposed letting brokers issue bonds to finance these trades, expanding options beyond bank loans and commercial paper.

Short-term funding markets rarely make headlines until something breaks in them. Market Briefs watches that plumbing free every weekday.

How the math pencils out

Based on Bloomberg-compiled data, last week three-month paper from nonbank financiers delivered a yield of 7.18%, while brokerages typically charge about 9% to 20% for margin loans depending on terms. That spread helps explain the rush into CP.

What it means for your money

Compared with the overall market, margin balances remain tiny - under 0.5% of India's $4.8 trillion equity market. Still, the pace is drawing attention. In August, Nithin Kamath, who founded Zerodha Broking Ltd., the country's second-largest stock broker, cautioned that a sharp drop could put the firm's fast-growing margin-loan business at risk, even while the product is turning into a more significant revenue source.

Appetite remains strong: "The size of the industry's funding book has more than tripled in three years and there remains huge appetite for leverage trading," said Dharmesh Vala, who is the chief executive at Nayan M. Vala Securities Pvt. in Mumbai. Translation to your day-to-day: more leverage can add extra oomph to rallies and extra sting to selloffs, so volatility may feel choppier than it used to.

A borrowing boom among brokers changes the risk profile of an entire market. Join Market Briefs free and keep an eye on it.