INTERVIEW: ANSHU KAPOOR, head, Edelweiss Private Wealth Management

'First time bond issuers gained from govt stimulus'

Borrowers who have not been able to tap the bond market via normal issuances, have been resorting to different mechanisms like down-selling of assets and securitising loan pools, says **Anshu Kapoor***, head of Edelweiss Private Wealth Management. In an interview with* **Bhavik Nair***, he said he expects yields of AAA-rated bonds to stabilise at current levels while yields of AA-rated bonds may experience some tightening amid surplus liquidity, improvement in investor sentiment and hunt for yields. Edited excerpts:*

How much have corporate bond spreads widened in recent times?

In March 2020, credit spreads had widened significantly compared to their lows in February, amid a sharp increase in FPI outflows and Covid-19 induced volatility. FPIs sold around ₹60,000 crore worth of Indian bonds in March leading to a sharp rise in yields of corporate bonds maturing in the 2-4 year segment. For example, yields of a 3-year Nabard bond hardened from around 6.35% in February to a peak level of around 7.75% in March 2020, before easing to around 5.50% as in early June after the RBI stepped in with a series of measures to ease pressure and improve sentiment. The RBI's timely actions in form of unscheduled rate cuts and introduction of 3-year LTRO and TLTRO programmes have succeeded in arresting the sentiment and reversing the trajectory of corporate bond yields, to a significant extent. This led to a significant increase in demand for corporate bonds, with residual maturity of 3-4 years in April and May. This has resulted in tightening in credit spread of the 1-year Nabard to around 110 bps as on June 5, from around 170 bps in early April, while credit spreads of 2-3year AAA-rated credits have remained stable even while their absolute levels have declined.

With the government credit guarantees in its fiscal package, have you seen any positive response from lenders?

Yes, government credit guarantees have had an immensely positive impact on the Indian bond market. The total fundraising in the first two months of FY21 far exceeds the amount raised during the same time in FY19 and FY18. Since April, 11 companies have tapped the bond markets for the first time, raising a total of about ₹1,500 crore. Without the government stimulus, these first-time issuers may have found it difficult to raise funds in a risk-averse market environment.

What is happening to firms that are unable to tap the bond market due to risk aversion by lenders? Where are they turning for funds?

Liquidity has not been freely available to all as lenders/investors, including banks, have been selective. Risk aversion definitely has a large part to play. As a result, those who are the worst hit by the current crisis are facing a shortage of liquidity. Borrowers who have not been able to tap the bond market via normal issuances, have been resorting to different mechanisms like down-selling of assets, securitising loan pools, tying up with PSBs for partial credit guarantee schemes and seeking borrowing lines, etc. Eventually, the RBI/government may realise that to channelise funds to these borrowers, they will have to resort to direct measures such as directly buying papers in a special purpose vehicle (SPV).

Who are the major lenders in the corporate bond market in these times? Are banks shying away from participating?

Banks continue to make excess investments over and above their SLR requirements while non-SLR investments are showing a drop. However, reverse repo parking by banks has eased off from the peak of about ₹8.5 lakh crore. In terms of corporate bonds, funds are flowing largely to AAA and AA categories but others are still facing difficulties in raising additional capital from the market.

How are FPIs treating Indian bonds? Do you see them coming back any time soon?

FPIs have been net sellers in debt, withdrawing about ₹23,000 crore in May, whereas in equity, there has been an inflow of ₹15,000 crore. Clearly, the outlook on India's debt is cautious, especially with expectations of high government borrowing. Having said that, India has the most attractive yields among major emerging markets. This, coupled with low currency volatility, should attract FPIs in debt.

Where do you see SDL yields from here on?

Our overall hypothesis is that interest rates have more room for coming down. Even the recent RBI minutes point to the fact that India still has traditional ammunition left. With interest rates falling, borrowing costs will fall. Though there was an expectation of rise in SDL yields as supply increased, it was abated by easing off of the Ways and Means advances limit for the states by the RBI. Overall, we expect G-sec to fall to 5.50% levels and the spread between G-sec and SDLs should correct to about 50-60 bps, depending on the credit profile of the states.