Need for a Vibrant Corporate Bond Market

What is the issue?

As India's corporate bond market is expected to boom and with the vacuum created by erstwhile development finance institutions (DFIs), the time is ripe for developing a deep, liquid and vibrant corporate bond market.

What is the status of Indian corporate bond market?

- Since 2008, corporate bond market has been witnessing higher investment flows.
- It was mainly due to
    - Simplification of procedures
    - Sophisticated clearing and settlement of trades
    - Focus on better disclosure standards
    - Issue of exotic bonds (Masala bonds, Green Bonds, etc.)
    - Raising the quantitative limits for foreign institutional investors
- While primary corporate bond issuances were of ₹7.8 lakh crore during FY2020-21, outstanding corporate debt stood at ₹35.1 lakh crore (18.2 % of India's GDP).
- The Indian bond market has been dominated by sovereign bonds and the corporate bond market has a meagre share of 27% during the last decade.

What are the problems in Indian corporate bond market?

- Crowding out by issuance of G-Secs
- Private placement
- Persistent inflation coupled with higher interest rates
- Information asymmetry
- Limited diversified basket of instruments
- Illiquid secondary market
- Non-availability of repo options
- Absence of broad investor base
- Lack of credit default swaps/insurance

What measures can be suggested to overcome this issue?

- **Financial literacy and education -** Since over 76 % of adults in India do not even understand the basic financial concepts, audio-visual contents/booklets may be developed as part of the digital literacy drive.
- **Incentives for retail investors -** Indian corporate bond market is dominated by a few institutional investors and professional fund managers, mainly concentrated in financial services sector (72.1 %).
- The government may provide tax incentives to channelise household savings into financial assets such as corporate bonds from real estate and gold.
- **ESG framework -** Corporates following the ESG (Environmental, Social, Governance) framework may have greater strategic freedom and will be the primary choice of market-savvy investors.
- **Credit guarantee enhancement:** At present, credit guarantee fund scheme exists for MSMEs to extend collateral-free credit.
- Similar one can be provided for enhancement of corporate bonds through creation of an earmarked fund by collecting cess from the cash-rich companies.
- **Maintaining price stability -** The government's public debt needs to be gradually downsized for effective transmission of monetary policy in order to crowd in private investment.
- **Enhancing liquidity -** Tri-party repo market may be developed for corporate bonds to provide liquidity for the participants in the market.
- The regulators may act together to allow 'A' rated corporate bonds as collateral to expand the issuers and the investor base.
- **Functional autonomy -** Independent directors and credit rating agencies should have functional independence to improve corporate governance and to boost the investors' confidence.
- **Corporate bond index** - A dedicated corporate bond index enables real time monitoring of the market and fosters price discovery, thereby increasing investor's buoyancy.

Reference

1. https://www.thehindubusinessline.com/opinion/we-need-a-vibrant-corporate-bond-market/article37403478.ece

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