Innovative Bonds and Securitisation Summit, 2015

Key Takeaways

Session 1

- Regulators are trying to facilitate the growth of the bond markets including creating secondary market liquidity
- Bond markets have come a long way over the last 10 years or so and the growth over the last year has been particularly very impressive
- However there are multiple regulators and their approach to regulation is quite often not consistent
  - There is constant cross regulators interaction to align the interest of the markets with that of the regulators
- Daily turnover ratios in corporate bond markets are still a small fraction of similar ratios in case of government bonds, and mostly it is on-the-run bonds that are traded
  - Mostly the corporate bond investors may be hold-to-maturity investors

Regulatory clarity required

- Withholding tax rate for FPI investments in corporate bonds needs long term clarity
  - Currently, the TDS provisions talk about a 5% withholding tax rate only upto 2017
- Companies Act deposit rules are superfluous in case of bonds
  - Bonds are not deposits; it is only because of regulatory definition
  - Regulators must exempt bonds regulated by SEBI (say listed bonds) from requirements of Companies Act
- Unsecured bonds must be allowed to be listed and traded

Session 2

- Globally, securitisation markets slow but certainly seem to be rebounding
  - Newer asset classes are being tried
  - Percentage share of non-traditional jurisdictions has also increased
- In India, the distribution tax has completely killed the securitisation market
  - What is surviving is direct assignments of priority sector loans
  - The market is so heavily dependent on priority sector
    - Therefore, with the PSL requirements for banks coming down, the demand for PSL securitisations may also get reduced
- The market is also lapping up lot of non-priority sector asset classes
- The market is trying several new/ innovative bonds structured instruments
  - CBOs
  - Multi-originator structures

Session 3

- Interest in covered bonds both from investors and issuers remains alive however legal challenges continue to hinder the maiden issuance in the country
  - Regulators views on coming out with a Covered Bonds regulation seems positive, however the lingering legal issues on bankruptcy remoteness, stacking order of priorities on receivables and claw back of creditors continue to be lurking issues delaying the issuance of the regulations
- Legal counsel presenting in the session was of the view that the bankruptcy remoteness is a matter of contract
  - Contract being clear, it possible to do isolation

Session 4

- There are several new debt instruments investors are keenly investing in, whether the bonds are influenced by
  - Tier IA requirements of banks under Basle III
  - Guilt linked bonds
  - Base rate linked bonds
  - CMBS
  - Equity kickers annexed to bonds, and more

Session 5

- The draft guidelines on rupee-denominated bonds will open up a whole new avenue for corporates to raise funds
- It may be game changer
- However the end-use restrictions have equated the option with ECBs
  - This may have to be deleted soonest
- Withholding tax clarity is also an issue
- Currently there seems to be less interest on longer maturities but we will have to wait for the market to mature

Mr Verma's address

- PFRDA has opened up investment avenues which include securitised paper, AIFs, REITs etc
  - This opens up tapping of long term funds from Pension Funds, provident funds etc which had largely been not available so far
- EPFO may also agree on the same lines
- However, the supply side has to improve

Session 6

- There seems to be strong interest from investors to invest in alternative products such as structured bonds, loans against shares, CMBS, etc
- There is also a diverse range of investors willing to invest in such products

Session 7

- Partial credit guarantees and mortgage guarantees may reduce the cost of capital market instruments
- CDS market has been a complete non starter
  - Hopefully the regulators remove the regulatory obstacles
  - Mutual funds should be permitted to act as protection sellers as well
  - Currently the capital requirement in case of protection sold is higher than in case of direct long position on the bond itself
    - Therefore, it is inefficient to sell protection than to invest in the bonds
    - This needs to be corrected

Session 8

- Proponents of Islamic finance are not different from conventional funding
  - It imbibes the moral/ ethical consequences of financial transactions
- Islamic finance has a history in India, however there is very little traction
  - There are ethical funds/ NBFCs/ shariah compliant mutual funds and venture capital funds in India
  - While the opportunities of growth are humungous, the challenges towards growth of Islamic finance include
    - lack of financial literacy
    - Political sensitivity
    - Absence of financial products
- Several of Islamic structures and bonds could be relevant alternatives for the Indian market