Debt funds' exposure to banks' certificates of deposit doubles

CHIRAG MADIA
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The exposure of debt mutual fund (MF) schemes towards certificate of deposits (CDs) issued by banks has more than doubled in the past one year. Meanwhile, exposure to commercial paper (CP) issued by non-banking financial companies (NBFCs) and government securities (G-Secs) has increased 17.5 per cent and 7.6 per cent, respectively.

A large part of investments into the G-Secs have been made in low-duration bonds on the fear of rising interest rates, said industry players.

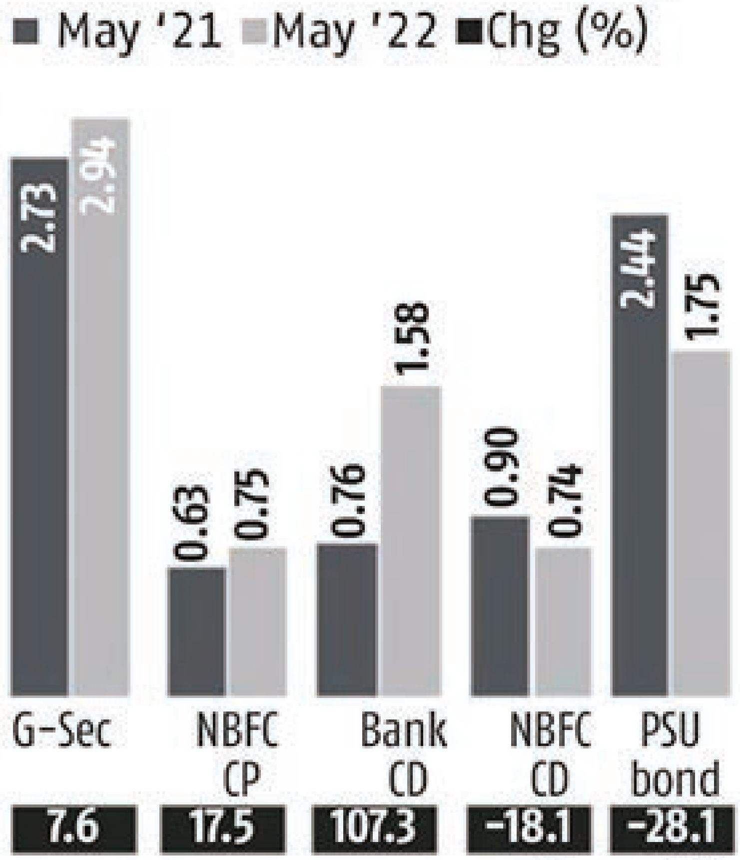
The exposure to G-Secs stood at ₹2.93 trillion in May 2022 compared to ₹2.73 trillion a year ago, shows Securities and Exchange Board of India (Sebi) data. While deployment into Bank CDs surged to ₹1.58 trillion in May 2022.

"Most debt schemes have statutory liquidity requirements, wherein funds have to invest in G-Secs/treasury bills for maintaining liquidity. This could explain the high G-Sec's holdings," said Sandeep Bagla, CEO, TRUST Mutual Fund

He added the carry in short-tenure G-Secs is quite attractive. In the last few months, debt MFs have reduced the average maturity for several debt schemes in anticipation of interest rate increases.

SHIFTING PREFERENCES

How deployment by debt MFs towards various debt instruments has changed



Typically, the prices of fixed-income securities are determined by prevailing interest rates and interest rates and prices are inversely proportional. In the last few months, the Reserve Bank of India (RBI) has hiked the interest rates by 90 basis points to control the rising inflation.

The sharp increase in the investments of Bank CDs is on the back of pickup in credit offtake. The expectations of lower deposits growth and increased credit costs amid inflationary pressures has prompted banks to issue these instruments over the last few months, said the officials in the MF industry.

According to the rating agency Care, bank credit witnessed a strong growth of 12.1 per cent year-on-year (y-o-y), expanding by a significant 611 basis points (bps) for the fortnight ended May 20, up from 6 per cent in the year-ago period (May 21, 2021).

"After a modest credit growth in recent years, the outlook for bank credit growth is expected to remain positive due to economic expansion, rise in government and private capital expenditure, rising commodity prices, implementation of production linked incentive Scheme, extension of emergency credit lines for MSME and retail credit push," said the rating agency in its note. Meanwhile, debt fund managers cut down their exposure into CDs issued by NBFCs and bonds issued by public sector undertakings (PSU) by 18 per cent and 28 per cent (year-on-year), respectively.

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