Govt seeks proposals for debt exchange traded fund by May 16

ETF structure to be decided by advisor in conjunction with government

The government plans to launch its first debt exchange traded fund (ETF) early in the second half of 2018-19. The ETF's basket is expected to contain debt offerings from 12-15 state-owned companies, including banks and central public sector enterprises (CPSE), Business Standard has learnt.

The Centre will also discuss how to attract more retail investors into corporate bond markets, with market regulator Securities and Exchange Board of India (Sebi), starting with the planned debt ETF.Bonds of NTPC, Power Finance Corporation, Rural Electrification Corporation, LIC Housing Finance, Indian Railway Finance Corporation, National Highways Authority of India and others could be included in the basket. These would be fresh issuances.

All these public sector undertakings (PSUs) are active in the corporate bond markets. "The ETF will comprise PSUs, which are already raising money through the corporate debt market route. The advantage this platform will provide them is reducing the costs of borrowing," said an official.Though the government, the central bank and the market regulator have made efforts towards developing a thriving corporate debt market, it is yet to take off

The main aim of the ETF, therefore, is to develop the corporate debt market further and attract more retail investors to bond markets, the official said. "Right now, it is dominated by larger players like pension funds and institutional investors," he said.

"In India, the corporate bond market constitutes a relatively small size around 13 per cent in terms of gross domestic product as compared with government debt market which is 30.4 per cent of GDP," states the request for proposal (RFP) to hire a financial advisor which will create and launch the debt ETF. The RFP was issued earlier this month.

The pre-bid meeting for prospective advisors was held on April 27 and proposals are to be submitted by May 16. How the debt ETF will be structured will finally be decided by the selected financial advisor in conjunction with the government. The advisor will examine all options of raising funds through bonds, credit-linked notes and promissory notes by PSUs and PSBs through the debt-ETF platform, and whether such an ETF can be created with or without underlying bonds or notes.

As reported earlier, the government will not get any proceeds from the debt ETF. "We thought it would be prudent to come out with an instrument which will help PSUs access financing from the debt markets in a more efficient manner," outgoing DIPAM (Department of Investment and Public Asset Management) secretary Neeraj Gupta had told Business Standard in February.

"Nearly 15 PSUs have raised Rs 3 trillion through bonds in last three years. Individually they are neither very liquid, nor do they offer ease of transactions to investors who sometimes find it difficult to buy into individual bond products. What we are trying to do is leverage their strengths and requirements, and bring some sort of index whereby they can raise money in a regular manner," he had said

The government had divested part of its equity stake in some PSUs through two ETF issuances — the CPSE ETF and the Bharat-22 ETF. Both ETFs saw strong demand from investors.

According to the National Stock Exchange website, debt ETFs are simple investment products that allow investors to take an exposure to fixed income securities. These debt ETFs combine the benefits of debt investments with the flexibility of stock investment and the simplicity of mutual funds. While there are several equity ETFs listed on exchanges, there are two ETFs with the underlying being government securities, and a liquid fund which makes ultra short-term investments in collateralised lending and borrowing obligation/repo and reverse repo.

(Business Standard)