Secondary Market for Corporate Loans - Manoharan Committee

Why in news?

The task force set up by the RBI to examine the possibilities of a secondary market for corporate loans in India submitted its report recently.

What is a secondary market?

- When a company issues its securities for the first time, it does it in the primary market.
- After the IPO (Initial Public Offering), those securities get available for trade in the secondary market.
- A secondary market is thus a marketplace where already issued securities (both shares and debt) can be bought and sold by the investors.
- It is a market where investors buy securities from other investors, and not from the issuing company.
- Equity shares, bonds, preference shares, treasury bills, debentures, etc. are some of the key products available in a secondary market.
- SEBI functions as the regulator for the secondary market.

What are the key suggestions?

- The task force was led by Canara Bank Chairman T N Manoharan.
- It suggested creating a self-regulatory body (SRB) to manage the secondary market.
- This would develop appropriate benchmark rates for secondary market purchase and sale of corporate loans.
- The SRB is expected to also finalise detailed modalities and formulate guidelines.
- It would -
    i. standardise the paperwork associated with loans, making them easier to trade
    ii. maintain the standards and examine documentation
    iii. maintain a central registry, and so on
- Aside from the creation of this quasi-regulator, the committee also suggested that existing requirements be changed.
- It said the secondary market for corporate loans, currently dominated by

banks, be thrown open to mutual funds, pension funds, and insurance companies.
- To start with, it was recommended that term loans be prioritized for sale in the secondary market.
- Subsequently, depending upon the experience gained, other categories of loans like revolving credit facilities should follow suit.
- These include cash credit, credit card receivables, assets with bullet repayment and non-fund based facilities.

What is the committee's rationale?

- The secondary loan market in India is largely restricted to sale to Asset Reconstruction Companies and ad-hoc sale to other lenders, including banks.
- Notably, no formalised mechanism has been developed to deepen the market.
- Banks and NBFCs are currently the only participants in the primary and secondary loan markets.
- So, the taskforce felt that it was essential to widen the spectrum of participants to boost the secondary market.
- Besides, the secondary market in corporate debt is so illiquid.
- In the absence of sufficient liquidity, the market is not properly passing the price information about companies.
- So, a more structured form of price discovery would be far more efficient.

What is the way forward?

- Greater innovation and regulatory cohesion are needed across the board for debt and loan markets.
- This must be the priority for growing long-term finance and better pricing of debt.
- This is crucial to avoid investment crises such as those India is enduring.

Source: Economic Times, Business Standard

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