YOUR MONEY

Investing in NBFC bonds: Strike a balance between return and rating

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With the Reserve Bank of India (RBI) nudging non-banking financial companies (NBFCs) to reduce their dependence on banks, and mutual funds becoming conservative after the Franklin Templeton incident, NBFCs are increasingly turning to the bond market to raise funds. According to PRIME Database, they have raised ₹73,820 crore through corporate bonds since August 1, 2024. This surge in bond issuance offers opportunities to retail investors, especially with the minimum investment limit being reduced from ₹1 lakh to ₹10,000.

Attractive opportunities

With more NBFCs tapping the bond market, interest rates are currently attractive. "The US Federal Reserve has cut interest rates by 50 basis points. The RBI will likely follow suit in one or two quarters. So, it makes sense to lock into the current high rates," says Anshul Gupta, co-founder and chief investment officer, Wint Wealth.

Vishal Goenka, co-founder, IndiaBonds.com, highlights that with central banks likely to reverse the rate cycle soon, bond prices may appreciate, resulting in capital gains for investors. "Corporate bonds, particularly those in the three-five year maturity bucket, offer good opportunities. Even AAA-rated bonds are offering close to 7.5 per cent, at least 300 basis points above expected inflation," says Sandeep Bagla, chief executive officer (CEO), Trust Mutual Fund. Gupta of Wint Wealth adds that slightly higher-risk bonds can deliver double-digit returns, outperforming the 7-7.5 per cent offered by bank fixed deposits.

Invest for stability

Higher-rated bonds are generally safer and less volatile. "They can offer a steady, predictable income stream, crucial for those seeking regular payouts," says Goenka. Bonds lend stability to a portfolio, which is particularly valuable during volatile market phases. Investors now also have a broad range of issuers, tenures, and risk profiles to choose from.

Risks to consider

One key risk is interest-rate risk: If the RBI raises rates, the value of existing bonds declines. "Longer-term bonds are more sensitive to interest-rate changes," says Ankit Gupta, founder director, BondsIndia.

Then there is credit risk, especially high in lower-rated bonds. "Bonds also carry the risk of downgrades in ratings due to worsening financial conditions," says Bagla. Liquidity is another factor, as lower-rated bonds can be difficult to sell. Additionally, bonds carry reinvestment risk. "If they mature or are called back early, you may not be able to reinvest at the same rate, especially in a low interest-rate environment," says Gupta of BondsIndia.

Run these checks

When evaluating bonds, returns shouldn't be the sole factor. Pay close attention to the bond's credit rating. It should ideally be AA or higher. "Higher ratings mean lower default risk," says Goenka. Review the issuer's financials, including its debt levels. "Check who else is lending. If major lenders are involved, they would likely have done their due diligence," says Gupta of Wint Wealth.

Consider whether the bond's interest rate is fixed or floating, as this impacts returns in a changing rate environment. If the bond is callable, be cautious. Gupta of BondsIndia warns that if the issuer redeems early, that could affect your long-term return potential.

Avoid bonds with long maturities. Gupta of Wint Wealth recommends a tenure of one to two years to reduce the risk of default due to worsening finances. Avoid investing in bonds offering returns above 12 per cent. Gupta of Wint Wealth refers to such rates as a red flag.

Finally, diversify investments across multiple issuers and sectors.

RETURNS INCREASE AS RATINGS FALL

Name of security/Coupon	Maturity date	Credit rating	Yield (%)
8.15% Axis Finance	May 22,'29	AAA/Stable	8.05
8.35% M & M Rural Housing Finance	Jun 22,'29	AAA/Stable	8.20
9.65% Adani Enterprises	Sep 12,'27	A+/Positive	9.80
10.30% Indostar Capital Finance	Sep 25,'27	AA-/Stable	11.00
9.84% Spandana Sphoorty Financial	Jun 28,'26	A+/Stable	11.30
9.75% Sammaan Capital	Jul 23,'29	AA/Stable	12.00
11.4% Keertana Finserv	Jun 13,'27	BBB/Stable	14.10
12% Vedika Credit Capital	Mar 25,'27	A-/Stable	14.25
11.90% Akara Capital Advisors	Dec 3,'26	BBB/Stable	15.10

Source: BondsIndia