COMPANY FDs & TATA NCD

Options in fixed income

Tata Capital's NCD looks attractive, but take the company FDs, offering double-digit returns, with a pinch of salt

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EQUITY MARKETS are in doldrums and banks are averse to lend. So, many companies have turned to traditional fund-raising methods, and fixed deposits (FD) are a dime a dozen. For retail investors too, FDs are a new and lucrative alternative offering double digit returns. Tata Capital, a non-banking finance company (NBFCs), is the latest to announce a fund-raising plan to finance its capital expenditure and working capital needs. It has launched a secured non-convertible debenture (NCD) to mobilise Rs 500 crore and, in return, pay up to 12 per cent returns per annum to the investors.

Although these schemes promise attractive returns, does it make sense to invest in such schemes? Let's take a closer look.

Options available

Company FDs

Fixed deposits in companies that earn a fixed rate of return over a period of time are called company FDs. Usually, manufacturing companies, financial institutions and NBFCs can accept such deposits. Deposits mobilised by these companies are governed by the Companies Act under Section 58A. You can get these either through broking agencies or directly with the companies.

RETURNS. The interest earned is taxable at the hands of the investor, as per the normal tax rules *(See: Company FD)*. Such schemes usually offer a tad higher rate of interest to senior citizens.

RISKS INVOLVED. Although such deposits offer high interest rates, these are unsecured deposits and have default risk involved. Therefore, always pay heed to the rating before buying any such deposit — look for AA or AAA schemes. Usually agencies like CARE, CRISIL and ICRA rate such products. An AAA rating signifies highest safety, and D or FD means default.

Tata Capital NCD

The non-banking finance company launched its NCD on February 2. It will remain open for subscription till the 24th of this month. Investors who have a demat account can invest a minimum amount of Rs 10,000 and earn interest on a monthly, quarterly, or annual basis *(See: Tata NCD)*. After the subscription, these debentures will be listed on the National Stock Exchange (NSE).

WHAT ARE NCDs? NCDs are certificates issued by companies to raise funds through the public issue. These instruments cannot be converted into equity shares and usually carry higher interest rates than the convertible ones.

RETURNS. The debentures offer a coupon rate of 11-12 per cent, depending upon the frequency of interest payment chosen. Interest earned on these NCDs is subject to tax at the hands of the investor. The effective post-tax returns for a person in the highest tax bracket will be 7.44 per cent in case of 11.25 per cent return, and 7.92 per cent in case of 12 per cent return.

LIQUIDITY. There are three ways in which investors can redeem these debentures. First: At the time of maturity, i.e. after five years. Second: Through the call or put option after three years. Third: Through the NSE. Before exercising the third option, investors must understand that the trading value of these NCDs will depend entirely on the interest rate scenario. The price of the NCD is inversely proportional to interest rate. Therefore, a rise in interest rates could result in a price below its issue price. Hence, it is possible that these NCDs trade at a lower price compared to their face value.

Financial planners, therefore, sound caution and suggest that NCDs should be held till maturity. "Hold these NCDs till maturity, unless interest rates fall sharply and there is a possibility of an early exit at a significant capital gain in the secondary market," says Vishal Dhawan, a Mumbai-based financial planner.

"Ideally, investors may plan to make a premature withdrawal at the end of 36 months by exercising the put option. On the NSE, the prices may fluctuate and should be used as an emergency liquidity measure. However, if the interest rates fall then you may get more than the face value by selling it on the NSE," says Veer Sardesai, Pune-based financial planner.

Who should invest?

Interest payment options make the scheme attractive for people who are looking at a regular flow of income. "Since the interest earned is taxable, it makes better sense for senior citizens who are not in the highest tax bracket," says Sardesai.

— With inputs from Himani Chandna

TATA CAPITAL NCD

	MONTHLY	QUARTERLY	ANNUAL	CUMULATIVE
Min. amt.	Rs 1,00,000	Rs 10,000	Rs 10,000	Rs 10,000
Face value	Rs 1,00,000	Rs 1,000	Rs 1,000	Rs 1,000
Coupon (%) [1]	11	11.25	12	12
Post-tax returns [2]	7.26	7.43	7.92	7.92
Put and call option [3]	36	42	36	36

[1] interest is payable per annum; [2] calculations are for the person in highest tax bracket; [3] in months; Maturity period for investment is five years

COMPANY FDs

COMPANY	CREDIT RATING	MIN INVEST	INTEREST PAYABLE	INTEREST RATE (%) 12M	INTEREST RATE (%) 36M	POST-TAX RETURNS (%)[1] 12M	POST-TAX RETURNS (%)[1] 36M
Tata Motors	AA+ by Crisil and LAA- by ICRA	20,000	Quarterly	10.00	11.00	6.60	7.26
HDFC	AAA by ICRA/ AAA by Crisil	10,000	Cumulative	9.45	9.20	6.24	6.07
ICICI Home Fin	AAA by CARE and MAAA by ICRA	10,000	Cumulative	10.15	9.90	6.70	6.53
LIC Housing Fin	AAA by Crisil	10,000	Quarterly	9.60	10.00	6.34	6.60
Mahindra Fin	na	25,000	Quarterly	10.75	11.75	7.10	7.76
HUDCO	na	50,000	Quarterly	8.50	9.25	5.61	6.11
EXIM Bank	na	10,000	Half-yearly	10.00	10.00	6.60	6.60

[1] *calculations are for the person in highest tax bracket; All figures in Rs except wherever mentioned*