Keep tabs on interest rate scenario

Kalpesh Ojha

The cash management practices in an SME should take into consideration a few important things, like the existing interest scenario and the duration of maturity of the instruments in which funds are being deployed.

Credit quality of the instruments in which the funds are being deployed, which is directly linked to the underlying assets, should also be taken into consideration. The credit quality of the papers and assets although does not matter much if one is deploying funds for the extremely short term, say, from one day to about 7-10 days, but it does come into play once the horizon of investment is, say, a month or more.

The ratings considerations also play an important role when one is investing in the non-convertible debentures (NCDs) of companies. Currently, some of the NCDs are paying good rates, but one should take into account the ratings of these instruments before investing.

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Another aspect that an SME money manager should look into is the timing of the interest rate cycle. For example, currently the market is in a situation where the Reserve Bank of India (RBI) has just cut the CRR by 75 basis points and there are expectations that it may go for a cut in rates in its next policy meet on Thursday.

At this point if one invests in certificates of deposits (CDs), and if the RBI actually takes a rate cut decision, there would be some substantial gains in such investments post the rate cut.

For non-banking finance companies (NBFCs), Section 14A of Income Tax Act do not come into play, but for other companies it does. NBFCs are not so worried about the pre- and post-tax returns from investments.

Often SME fund managers get the opportunity to invest in schemes that will pay dividend soon. One can consider investing in such schemes, take the dividend and then sell at the post-dividend NAV to take advantage of the capital gains rules.

Ojha is VP, Shriram Transport Finance (As told to Partha Sinha)