A Commercial Paper (CP) is an unsecured, short-term debt instrument issued by a corporation, typically for meeting short-term liabilities.

- ***But what does this definition mean?***
- Most definitions end up looking very boring and sometimes leave us more confused than ever before! While they are known as definitions, they usually fail to define anything.
- In this lesson, I will try to *simplify* the concept of ‘Commercial Papers’ for you…

Understanding Commercial Papers – By Prof. *Simply* Simple

A Commercial Paper (CP) is

1. a money-market instrument
2. issued by large banks & corporations
3. to garner money from the market
4. to meet short term needs.

When & why was it introduced in India?

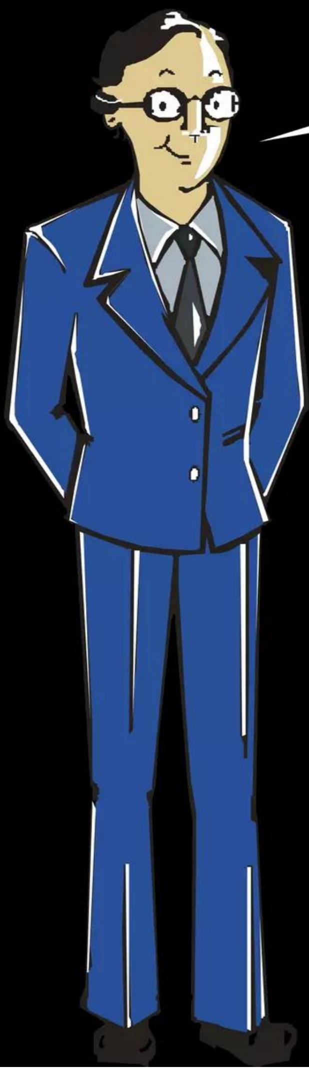
- It was introduced in India in 1990.
- It was aimed at providing highly rated corporates with a borrowing option.
- So while they could borrow from a bank, now with the help of a CP, they could also borrow from the open market.
- Since CP is used to borrow directly from the market, the rate of interest is lesser as compared to the banks.

Thus…

- A commercial paper is a lower cost alternative to borrowing from a bank.
- However not all organizations are in a position to issue CPs.
- Only reputed organizations whose papers have a good rating can borrow directly through CPs and save money.

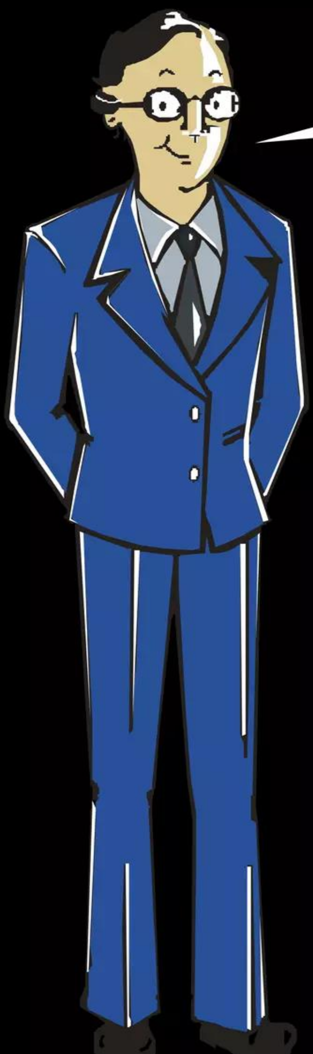
So who is eligible to issue CPs?

- Corporates
- Primary dealers
- Financial Institutions (FIs)



And who can invest in CPs?

- Individuals
- Banking companies
- Non-Resident Indians (NRIs) and
- Foreign Institutional Investors (FIIs) etc.



And for what maturity periods are CPs issued?

CPs can be issued for maturities between a minimum of 15 days and a maximum of up to one year from the date of issue.

Therefore it is used to fund the working capital or current requirements of organizations.

Some other things to remember about CPs…

- A major benefit of a CP is that it does not need to be registered with the Securities and Exchange Board of India (SEBI) as long as it matures before nine months (270 days).

- However, one important point to note is that the borrowed amount can only be used to fulfill current requirements. It is not meant be used for purchase of fixed assets, such as a new plant.

If you have understood CPs, let me tell you what Treasury Bills are…

- Treasury Bills or T- Bills are exactly the same as CPs.
- Except that while CPs are issued by corporates, T- Bills are issued by the Government for financing its working capital needs.

To Sum Up

- **What:** A Commercial Paper (CP) is an unsecured money market instrument issued by a corporation or bank in the form of a promissory note.
- **Why:** It provides the organization a borrowing option other than a bank.
- **When:** CPs are issued or sold when an organization needs to borrow money for its short term needs.
- **How:** Once a business becomes established, it can issue CPs after having them rated.