Capital account

6.52 Private capital flows (net) into emerging market and developing countries are projected to drop to just over US$80 billion in 2004, from US$120 billion in 2003 (World Economic Outlook- September 2004; IMF). The decline is principally on account of lower capital flows to the CIS and the Middle East countries. Capital flows into emerging Asia, however, continued to remain buoyant, and were projected to experience a more than 50 per cent increase to US$80 billion in 2004, against US$52.8 billion in 2003. While direct investment comprised the bulk of these inflows into emerging Asia, portfolio flows (net) were projected to more than double from US$5.5 billion in 2003 to US$12 billion in 2004.

6.53 The capital account of India's balance of payments gained further strength during 2003-04. The surplus in the capital account nearly doubled from its previous year's level (Table 6.2) to cross US$20 billion. There was, however, a significant change in the composition of the capital account. Unlike 2002-03, when foreign investment (net) flows were relatively subdued, such flows increased by more than US$10 billion over their previous year's level, contributing to more than 70 per cent of the capital account surplus in 2003-04. The heavy foreign investment inflows were primarily driven by a rapid increase in portfolio flows into India. Banking capital flows, comprising largely of non-resident deposits, made up for the rest of the capital account surplus.

6.54 The capital account remained in surplus during the first half of the current year, but at a reduced level compared to the corresponding period of the previous year (Table 6.2). A quarter-wise profile points to a much larger surplus of US$5.9 billion in the second quarter of 2004-05 (July-September), as against US$4.2 billion in the first quarter (April-June). The larger surplus in the second quarter is attributable to a pick-up in foreign investment inflows, contributed by growth in both direct investment and portfolio investment. There was a more than US$2 billion drop in net loan inflows during the second quarter, largely on account of a sharp rise in repayments of short-term credit and lower net receipts under external commercial borrowings (ECB). Banking capital (net) exhibited an outflow during the second quarter as against an inflow of US$1.1 billion in the first quarter.