External Commercial Borrowings (ECBs)

6.71 The transformation of the current account of the BOP from a surplus to a deficit since 2004-05 has been accompanied by a turnaround of debt-creating capital categories from net outflows to inflows. After reaching a net inflow of more than US$4.3 billion in 2000-01, commercial borrowings had become larger and larger outflows until 2003-04. Such borrowings recovered to a record US$5.0 billion worth of net inflows in 2004-05 (Table 6.2). During the current year so far, ECBs have not only continued to remain net inflows, but have showed clear signs of consolidating further by exhibiting a growth of 80 per cent in April-September 2005 over the corresponding period of the previous year.

6.72 During 2004-05, disbursements of commercial borrowings increased sharply to US$8.5 billion compared with US$5.2 billion worth of disbursements in 2003-04. The corresponding repayments in 2003-04 and 2004-05, were US$8.2 billion and US$3.5 billion, respectively. Indeed, higher repayments on account of redemption of the Resurgent India Bond (RIB) proceeds were one of the main reasons behind ECBs becoming net outflows during 2003-04, while no such developments occurred during 2004-05. However, much higher ECB disbursements during 2004-05 also underscore a sharp increase in demand for ECBs. The enhanced demand is attributable to two factors. First, a step-up in domestic industrial activity since 2004-05 has increased the corporate sector's appetite for funds. Second, low interest rate spreads overseas have motivated Indian corporates to raise larger resources through foreign currency convertible bonds (FCCBs).The growing volume of ECB inflows during the current year indicates that the fundamentals driving demand for such inflows continue to remain strong.

6.73 Like in 2003-04, the current year witnessed the redemption of India Millennium Deposits (IMDs) issued in 2000 with a five year maturity. Given the outgo of around US$7.1 billion on IMD repayments, the growth in disbursement during the next two quarters will have to be significantly large so as to maintain ECBs as net inflows for the year. However, if ECBs do become net outflows, the rate of increase in the size of the capital account surplus, might actually get stunted.