Foreign Exchange Reserves

6.79 In spite of a deficit in the current account, the total stock of foreign currency assets went up by US$26.1 billion (on BOP basis) during 2004-05. At end-March 2005, India's total foreign exchange reserves (including foreign currency assets (FCA), gold, special drawing rights (SDR) and reserve tranche position (RTP) in the IMF) stood at US$141.5 billion, reflecting an increase of US$28.5 billion, as compared with US$113.0 billion at end-March 2004.

6.80 Unlike the recent years, the current financial year, till end-January 2005, has not experienced any addition to the stock of reserves. From a level of US$135.6 billion at the end of March 2005, FCA has dropped to US$133.8 billion at the end of January 2006, indicating an erosion of US$1.8 billion. Similarly, total foreign exchange reserves have declined by US$2.0 billion during the year to reach US$139.2 billion as on January 27, 2006. Month-wise movements in FCA indicate that except for the months of April, July, August, and October, FCA has declined in every other month during the period April-January 2005-06. The biggest declines were during the months of May and December 2005, of the order of US$3.0 billion and US$5.6 billion respectively. However, the sharp decline in reserves during December 2005 can be largely explained by the foreign exchange outgo on account of redemption of India Millennium Deposits (IMDs) (Box 6.11).

6.81 One of the obvious reasons behind the lack of accretion to reserves during the current year has been the widening of the current account deficit. However, even with such a deficit, on BOP basis (excluding valuation

Box 6.10 : India Millennium Deposits (IMDs)

Hardening of international crude oil prices in early-2000 escalated India's import bill and resulted in a decline in foreign currency assets of the RBI by around US$3 billion during April-October 2000. To cope with volatility in international oil price and to ensure a measure of comfort of foreign exchange reserves imparting stability to India's overall balance of payments position, India Millennium Deposits (IMDs) scheme was launched by the State Bank of India (SBI) for non-resident Indians (NRIs) during the last quarter of 2000 with the approval of Government of India and the RBI. Added objective of the scheme was to provide an investment opportunity for NRIs in long-term fixed income instruments. The tenor of IMDs was 5 years, and denominations were in US dollar, Pound Sterling and Euro, with the option of cumulating and non-cumulating interest. Government's guarantee, *inter alia*, covered Government's commitment to bear foreign exchange risk beyond 1 per cent per annum on a cumulative basis on the total pool of foreign currency deposits raised through the scheme and also tax benefits to the deposit holders. Amounts raised and interest rates offered were as follows:

Table: India Millennium Deposits

Currency	Amount collected (US$ million)			Interest rate
	Cumulative Deposits	Non-cumulative Deposits	Total	(% per annum)
A. US dollar	2861	2318	5179	8.50
B. Pound Sterling	186 (131)	59 (42)	245	7.85
C. Euro	60 (70)	13 (16)	73	6.85
D. Total (A+B+C)	**3107**	**2390**	**5497**	

Note: Figures in brackets indicate respective foreign currencies in million

The rupee proceeds of the deposits were utilised by the SBI for investment in Government Securities, on-lending to collecting banks as per the arrangement, and financing infrastructure projects and other lending. The IMDs matured on December 29, 2005. The redemption entailed total foreign exchange outgo of US$ 7,080 million which was entirely met by RBI by way of direct sale out of its foreign exchange reserves to SBI for equivalent rupee consideration. As Indian Rupee appreciated between calendar 2000 and 2005, there was an exchange gain of around 5 per cent and therefore no exchange loss was to be borne by the Government. The arrangements put in place jointly by RBI and SBI ensured that the redemption process was broadly seamless without impairing much the money, securities and foreign exchange markets.

changes), there was a net addition of reserves worth US$6.5 billion during April-September 2005. However, this accretion was offset to a very large extent by valuation losses (Table 6.13). Continuation of such losses, along with further expansion of the current account deficit during the remaining part of the year, may result in relatively lower accretion of foreign exchange reserves during the current year, compared with much higher volumes of such accretion during the last few years.

Table 6.13 : Sources of accretion to foreign exchange reserves

(US$ billion)

Items	2003-04	2004-05	April-September 2004	April-September 2005
I. Current Account Balance	14.1	-5.4	-0.5	-13.0
II. Capital Account (net) (a to f)	17.4	31.6	7.4	19.5
a. External Assistance	-2.9	1.9	0.3	0.4
b. External Commercial Borrowings	-2.9	5.0	1.5	2.7
c. Foreign Investment	13.7	12.1	2.5	7.4
d. Short-term Credit	1.4	3.8	1.9	0.9
e. Banking capital	6.0	3.9	0.6	3.0
Of which : NRI Deposits	*3.6*	*-1.0*	*-1.3*	*0.2*
f. Other items in Capital Account	2.1	4.9	0.6	5.1
III. Valuation Change	5.4	2.4	-0.3	-5.0
TOTAL (I+II+III)	**36.9**	**28.6**	**6.6**	**1.5**

Source : Reserve Bank of India