
External Commercial Borrowing: Quest in India

MS. SMITA GUPTA

Dean, Career college of Management, Bhopal, M.P. India

ABSTRACT:

External commercial borrowing is one mode of obtaining financial assistance from outside country for large projects and more particularly infrastructure development in India. ECB include commercial bank loans, buyer's credits, suppliers' credit, securitized instruments such as floating rate notes and fixed rate bonds etc.

Government permits the ECBs as an additional source of financing for expanding the existing capacity as well as for fresh investments. This article explains the various steps involved in availing external commercial borrowings the routes, cost ceiling use and security aspects of ECB, its benefits to borrow and impact and implications on economy. It also explains the guidelines issued in this regard by Government of India, reserve Bank of India.

Key Words: *External commercial borrowing, Foreign Reserves, Cost of financing, floating rate, FEMA*

ECONOMIC OVERVIEW

Global Trends

Highlighting the global risks prevailing on the horizon, International Monetary Fund in its second bi-annual outlook released in the first week of October 2013, pared its global growth forecast by 0.3 percent to 2.9 percent. Slower than expected growth in the current year is mainly due to sluggish growth in the emerging economies.

Domestic Trends

The latest data for the Indian Economy released for the first quarter of 2013-14 shows that the current account deficit (CAD) widened to 4.9 percent in the previous quarter.

Source: CII economy Matter

INTRODUCTION TO THE TOPIC:

ECB is an abbreviation for external commercial Borrowing which is governed by a set of guidelines issued by the Government of India/ Reserve Bank of India. It is source of funds for corporate from abroad with advantage of lower rates of interest prevailing in the international financial markets longer maturity period for financing expansion of existing capacity as well as for fresh investment. **Defined as** to include commercial loans [in the form of bank loans, buyer's credit, supplies' credit securitized instruments (eg floating rate notes and fixed rate, bonds CP) availed from non- resident lenders with minimum average maturity of 3 years.

Statutory Provisions:

Statutory Provisions are the set of rules that govern foreign investment in form of borrowings ECB regulations by MOF section 6(3)(d) of FEMA 1999 section 6 of notification no FEMA 3 dated 3-5-2000 and amended from time to time SEC 5(3) of ABOVE NOTIFICATION – IMPORT CREDIT SECTION 6(2) Puts CAP ON TOTAL ECB.

Routes for availing ECB

Data on ECBs are collected by RBI. Major regulators governing the ECB in India are exchange controllable department of RBI and ECB division in Department of Economic Affairs at Ministry Finance. ECB policy focuses on three aspects:

- Eligibility criteria for accessing external market
- Total amount of borrowings to be raised and their maturity structure
- End use of the funds raised.

ECBs can be accessed under two routes:

- (i) Automatic Route – where no prior approval of RBI/ Government is required.
- (ii) Approved Route – where prior approval of RBI/ Government is required.

Eligible Borrowers under Automatic routes:

Corporate including those in hotel, hospital, software, and infrastructure finance companies registered under the companies act.

SEZ Units- For their own requirement cannot transfer or lend ECB funds to sister concerns or DTA units.

NGO's engaged in microfinance activity- subject to satisfying the requirements specified by
RBI Entities that are excluded:

Financial intermediaries such as banks, financial installations (Fls), housing finance companies and NBFC,
Individual, Trusts and Nonprofit making organizations.

Recognized lenders

Recognized leader are international banks IFC, ADB etc. Multilateral export credit agencies supplier of equipments, foreign collaborators and foreign Equity Holders , Overseas organization lenders to NGOs.

Eligible Borrowers under the approval route:- • Financial Institutions dealing exclusively with infrastructure or export finance such as IDFC, IL&FS, Power Finance Corporation, Power Trading Corporation, IRCON and EXIM Bank. ECBs with minimum average maturity of 5 years can be raised by NBFCs from multilateral financial institutions. Corporates in service sector viz., hotels, hospitals and software companies can also avail ECBs up to USD 100 million in each financial year for import of capital goods.

Amount and Maturity of ECBs :

Amount and Maturity of ECBs UPTO \$20 mn----- MIN.AVG.MATURITY OF THREE YEARS \$20mn TO \$500mn-----Min.avg.mty 5years Maximum amount in a financial year\$500mn ECB upto\$20mn can have call/put option AFTER 3 YEARS.

All-In-Cost Ceilings:

All-In-Cost Ceilings All-in-cost includes interest, fees, expenses in foreign currency, except commitment fee, pre payment fee, withholding taxes and all fees payable in INRS MAMP
All-in-cost LIBOR+ of respective currency 3 to 5 years 300bps Above 5 years 500bps

End-User-Criteria:

End-User-Criteria Import of capital goods New projects Modernization/ expansion of existing projects in real sector including infrastructure, S.M.E's Infrastructure means sectors in Power, Telecom, Railways, roads and bridges, ports, industrial parks, water supply, sanitation, sewerage Overseas direct investment in J.V / W.O.S subject to FEMA 120 Acquisition of shares in disinvestment process-first stage and mandatory 2 stage NGO'S can use for micro finance lending to self help groups Bonafide micro credit purposes

Prohibited Users:

Prohibited Users On-lending or investment in capital market or acquiring a coy in India Real estate(except development of integrated township vide G.O.I. Press note 3 dated 4-1-2002 Working capital General corporate purpose Repayment of existing rupee loans Guarantees Prohibited Guarantees, Letter of Credit, Standby L/C, Undertaking, Comfort Letter Prohibition applies to Banks, FI'S, NBFC'S

Security: Security Choice of borrower and lender Compliance with REG.8 FEMA21 and REG.3 FEMA20, that is prior approval of RBI required for creation of charge immovable properties and shares in India

Procedure for raising ECB funds

Applicants are required to submit an application in form ECB through designed AD to their external commercial borrowing divisions along with necessary documents. Authorized dealers (ADs) may issue guarantee / LOU/LOC in favour of overseas supplier, bank and institutions. Upto USD 20 million per transaction for a period upto one year for import of all non-capital goods permissible under foreign trade policy (except Gold) and upto three years for import of capital goods.

However, the period of such guarantees /LOU/LOCs has to be co-terminus with the period of credit, reckoned from in the date of shipment.

- ECB proceeds should be parked overseas until actual requirement in India.
- Prepayment of ECB up to USD 500 million may be allowed by the AD bank without prior approval of Reserve Bank subject to compliance with the stipulated minimum

average maturity period as applicable to the loan. Pre-payment of ECB for amounts exceeding USD 500 million would be considered by the Reserve Bank under the approval route.

- Refinancing of existing ECB by raising fresh loan at lower cost is permitted subject to the condition that the outstanding maturity of the original loan is maintained.
- The designed authorized dealer (AD) has in general permission to make remittance of installments of principal, interest and other charges in conformity with ECB guidelines issued by Government/RBI from time to time.

Borrowers are required to submit form 83, in duplicate certified by the company secretary (CS) or chartered accounting to the designed AD. One copy is to be forwarded by the designed AD to the Director, Balance of payments statistics division, Department of statistical analysis and computer services (DESACS), Reserve bank of India, Bandra Kurla Complex, Mumbai-400051 for allotment of loan registration number.

The borrowers can drawdown the loan only after obtaining the loan registration number from DESACS, RBI.

Borrowers are required to submit ECB- 2 return (format in Annexure III) on monthly basis certified by the designed AD so as to reach DESACS, RBI within seven working days from the close of month to which it relates.

The primary responsibility to ensure that ECB guidelines are in conformity with RBI instructions is that of the concerned borrower. However, the designed AD is also required to ensure that raising/ utilization is as per the ECB guidelines at the time of certification.

Ads are permitted to crystallize the ECB liability arising out of guarantee provided for ECB raised by corporate, but after seeking approval from RBI. Ads desiring to crystallize their foreign currency liability into Rupees arising out of bank guarantee issued against ECBs are to make an application to External Commercial Borrowing Division of RBI through the head of the Ads giving the borrowers name, amount raised maturity, circumstance leading to invocation of BG/LOC date of default, its impact on the liabilities of the overseas branch of the AD concerned and other relevant factors.

Units located in SEZ are permitted to raise ECB, subject to the following conditions:

- (a) ECB is raised for their own requirement, and

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- (b) They shall not transfer or on-lend any borrowed funds to their sister concern or any other unit in domestic tariff area(DTA)
- Buyers' credit and suppliers' credit for three years and above come under the category of external commercial borrowings (ECB) which is governed by ECB guidelines.

CONCLUSION:

By allowing global money for refinancing domestic loans and selective on-lending ECBs have been permitted as an additional source of funds to encourage infrastructure and export financing.

RBI should allow the use to ECBs for wholly owned Subsidiaries or Special Purpose Vehicle of infrastructure sector companies to implement specific projects.

The RBI needs to support domestic companies looking to complete globally.

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