Corpsec Hotline

May 31, 2008

LOOSENING THE REINS: RBI RELAXES ECB LIMITS

On May 29, 2008, the Reserve Bank of India ("RBI") issued A.P. (DIR Series) Circular No.43 (RBI/2007-08/339), amending certain aspects of the External Commercial Borrowings ("ECB") guidelines under RBI/2005-06/87 A.P. (DIR Series) Circular No.5 Dated. August 01, 2005.

Current Position:

At present, pursuant to A. P. (DIR Series) Circular No. 04 (RBI/2007-2008/112) borrowers proposing to avail ECB up to USD 20 million for Rupee expenditure for permissible end-uses require prior approval of the Reserve Bank under the Approval Route.

Amended Position:

The RBI has decided that henceforth:

1. borrowers in the infrastructure sector may avail of ECB up to USD 100 million for Rupee expenditure for permissible end-uses under the Approval Route;
2. in the case of other borrowers, the existing limit of USD 20 million for Rupee expenditure for permissible end-uses under the Approval Route has been enhanced to USD 50 million.

The all-in-cost ceilings in respect of ECB are modified as follows:

Average Maturity Period	All-in-Cost ceilings over 6 Months LIBOR	
	Existing	Revised
Three years and up to five years	150 bps	200 bps
More than five years	250 bps	350 bps

The above changes will apply to ECB both under the automatic route and the approval route.

Analysis and Implications:

All other aspects of ECB policy such as USD 500 million limit per company per year under the Automatic Route, eligible borrower, recognized lender, end-use of foreign currency expenditure for import of capital goods and overseas investments, average maturity period, prepayment, refinancing of existing ECB and reporting arrangements remain unchanged.

The amendment appears to arise primarily in the context of India's burgeoning infrastructure sector and also in the context of the need for increased investment in other sectors of the economy. Another much touted reason for the relaxation is the need of the RBI to shore up a depreciating rupee, and to allay inflationary pressures.

Currently ECB can be raised only for investment (such as import of capital goods, new projects, modernization/expansion of existing production units) in the real sector, the industrial sector including small and medium enterprises (SME) and the infrastructure sector in India. The infrastructure sector is defined as (i) power, (ii) telecommunication, (iii) railways, (iv) road including bridges, (v) ports, (vi) industrial parks and (vii) urban infrastructure (water supply, sanitation and sewage projects). However, the terms "real-sector" and "industrial sector" continue to remain without definition.

This circular does not amend the requirements by the RBI that borrowers proposing to avail of ECB up to the newly enhanced limits for Rupee expenditure for permissible end-uses would be required to park such funds overseas until actual requirement in India. Further, the need for a prior RBI Approval for ECB upto the enhanced limit remains unchanged.

Kartik Ganapathy, Head of the Corporate and Securities Practice says that "the consequence of this change appears to be primarily to signal a change in RBI policy based on macro-economic indicators in India. The enhancing of limits, and all-in-cost ceilings, are certainly significant but do not appear to be the main story here".

- Arjun Rajgopal & Kartik Ganapathy
You can direct your queries or comments to the authors

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