Balance of Payments

6

CHAPTER

No country in today's globalized world can be fully insulated from what happens in the global economy and India is no exception to the rule. As the country is increasingly integrated into the world, it cannot remain impervious to developments abroad. The unfolding of the euro zone crisis and uncertainty surrounding the global economy have impacted the Indian economy causing drop in growth, higher current account deficit (CAD) and declining capital inflows. As in 2008, the transmission of the crisis has been mainly through the balance-of-payments (BoP) channel. Export growth has decelerated in the third quarter of fiscal 2011-12, while imports have remained high, partly because of continued high international oil prices. At the same time, foreign institutional investment flows have declined, straining the capital account and the rupee exchange rate that touched an all-time low of ₹ 54.23 per US dollar on 15 December 2011.

6.2 The situation, however, is showing signs of improvement in 2012. The rupee has appreciated by 2.6 per cent in January 2012 due to Reserve Bank of India (RBI) intervention, measures to augment supply of foreign exchange in the domestic market, steps to curb speculative activities, and general improvement in India's economic outlook. FII inflows have resumed, lending support to the balance of payments and exchange rate. The global outlook, however, remains uncertain with the situation in Greece teetering on the brink and increasing risk that the contagion will spread to the Portuguese economy. Such a scenario could have serious repercussions for the Indian economy.

Balance of Payment (BoP)

6.3 As per the Balance of Payment Manual (Fifth Edition), BoP comprises current account, capital account, errors and omissions, and change in foreign exchange reserves. Under current account of the BoP, transactions are classified into merchandise (exports and imports) and invisibles. Invisible transactions are further classified into three categories. The first component is Services comprising travel, transportation, insurance, government not included elsewhere (GNIE), and miscellaneous. Miscellaneous services include communication, construction, financial, software, news agency, royalties, management, and business services. The second component of invisibles is income. Transfers (grants, gifts, remittances, etc.) which do not have any *quid pro quo* form the third category of invisibles.

6.4 Under capital account, capital inflows can be classified by instrument (debt or equity) and maturity (short- or long-term). The main components of capital account include foreign investment, loans, and banking capital. Foreign investment comprising foreign direct investment (FDI) and portfolio investment consisting of foreign institutional investor (FIIs) investment and American depository receipts /global depository receipts (ADRs/GDRs) represents non-debt liabilities. Loans (external assistance, external commercial borrowings [ECB], and trade credit) and banking capital including non-resident Indian (NRI) deposits are debt liabilities.

6.5 The highlights of BoP developments during 2010-11 were higher exports, imports, invisibles, trade, CAD and capital flows in absolute terms as compared to fiscal 2009-10. Both exports and imports showed substantial growth of 37.3 per cent and 26.8 per cent respectively in 2010-11 over the previous year. The trade deficit increased by 10.5 per cent in 2010-11 over 2009-10. However, as a proportion of gross domestic product (GDP), it improved to 7.8 per cent in 2010-11 (8.7 per cent in 2009-10). Net invisible balances showed improvement, registering a 5.8 per cent increase in 2010-11. The CAD widened to US$ 45.9 billion in 2010-11 from US$ 38.2 billion in 2009-10, but improved marginally as a ratio of GDP to 2.7 per cent in 2010-11 vis-a-vis 2.8 per cent in 2009-10. Net capital flows at US$ 62.0 billion in 2010-11 were higher by 20.1 per cent as against US$ 51.6 billion in 2009-10, mainly due to higher inflows under ECBs, external assistance, short-term trade credit, NRI deposits, and bank capital. In 2010-11, the CAD of US$ 45.9 billion was financed by the capital account surplus of US$ 62.0 billion and it resulted in accretion to foreign exchange reserves to the tune of US$ 13.1 billion (US$ 13.4 billion in 2009-10).

Table 6.1: Balance of Payments : Summary (US$ million)

Sl. No.	Item	2006-07	2007-08	2008-09	2009-10	2010-11PR	2010-11 H1 (April-Sept. 2010)PR	2011-12 H1 (April-Sept. 2011)P
1	2	3	4	5	6	7	8	9
I	**Current Account**							
1	Exports	128888	166162	189001	182442	250468	107331	150909
2	Imports	190670	257629	308520	300644	381061	176213	236674
3	Trade balance	-61782	-91467	-119519	- 118203	-130593	-68883	-85765
4	Invisibles (net)	52217	75731	91604	80022	84647	39283	52923
	a Non-factor services	29469	38853	53916	36016	48816	21517	31060
	b Income	-7331	-5068	-7110	-8038	-17309	-8238	-9025
	c Transfers	30079	41945	44798	52045	53140	26004	30887
5	Goods & services balance	-32313	-52614	-65603	-82187	-81777	-47366	-54705
6	Current account balance	-9565	-15737	-27914	-38181	-45945	-29599	-32842
II	**Capital Account**							
1	Capital account balance	45203	106585	7395	51634	61989	38950	41061
	i External assistance (net)	1775	2114	2439	2890	4941	3036	705
	ii External commercial borrowings (net)	16103	22609	7861	2000	12506	5674	10592
	iii Short-term debt	6612	15930	-1985	7558	10990	6937	5940
	iv Banking capital (net)	1913	11759	-3245	2083	4962	839	19344
	of which							
	Non-resident deposits (net)	4321	179	4290	2922	3238	2163	3937
	v Foreign investment (net)	14753	43326	8342	50362	39652	30836	13657
	of which							
	a FDI (net)	7693	15893	22372	17966	9360	7040	12311
	b Portfolio (net)	7060	27433	-14030	32396	30293	23796	1346
	vi Rupee debt service	-162	-122	-100	-97	-68	-16	-32
	vii Other flows (net)	4209	10969	-5916	-13162	-10994	-8356	-9145
III	**Errors and omissions**	968	1316	440	-12	-2993	-2320	-2500
IV	**Overall balance**	**36606**	**92164**	**-20080**	**13441**	**13050**	**7030**	**5719**
V	**Reserves [increase (-) / decrease (+)]**	**(-) 36606**	**(-) 92164**	**20080**	**(-) 13441**	**(-)13050**	**(-)7030**	**(-)5719**

Source : RBI. *Notes* : PR: Partially Revised. P: Preliminary.

6.6 During the first half (H1–April-September 2011) of 2011-12, CAD in absolute terms was higher than in the corresponding period of the previous year, mainly due to higher trade deficit. The net capital flows in absolute terms were also higher during H1 of 2011-12 vis-a-vis the corresponding period of 2010-11 (Table 6.1).

Current Account

Merchandise trade

6.7 During 2010-11, exports crossed the US$ 200 billion mark for the first time, increasing by 37.3 per cent from US$ 182.4 billion in 2009-10 to US$ 250.5 billion. This increase was largely driven by engineering goods, petroleum products, gems and jewellery, and chemicals and related products. The improvement in exports was accompanied by a structural shift in the composition of the export basket from labour-intensive manufacture to higher value-added engineering and petroleum products. There was also a diversification of export destinations with developing countries becoming our largest export market in recent years.

6.8 Like exports, imports also recorded a 26.8 per cent increase to US$ 381.1 billion in 2010-11 from US$ 300.6 billion in 2009-10. Oil imports showed an increase of 19.3 per cent in 2010-11 (as against a decline of 7.0 per cent a year ago) and accounted for 28.1 per cent of total imports (30.2 per cent in 2009-10). Growth in imports has primarily been led by petroleum and related products and pearls and semi-precious stones. Detailed analysis is given in the chapter on international trade.

6.9 The trade deficit increased by 10.5 per cent to US$ 130.6 billion as compared to US$ 118.2 billion in 2009-10. This was primarily on account of higher increase in imports relative to exports on the back of a robust domestic economic performance in 2010-11. In terms of GDP, however, the trade deficit improved from 8.7 per cent in 2009-10 to 7.8 per cent in 2010-11 due to relatively higher increase in GDP at market prices vis-a-vis trade deficit.

6.10 The widening of India's CAD during H1 of 2011-12 reflects the impact of growth asymmetry between India and the rest of the world. India's export and import growth momentum, gained in 2010-11, continued during H1 of 2011-12.

6.11 During H1 of 2011-12, exports increased from US$ 107.3 billion during H1 of 2010-11 to US$ 150.9 billion, registering a growth of 40.6 per cent as compared to 30 per cent in H1 of 2010-11 over H1 of 2009-10. Exports in 2011-12 were driven mainly by buoyancy in items such as engineering goods and petroleum products. The resilience in export performance appeared to have resulted from a supportive government policy, focusing on diversification in terms of higher value-added products in the engineering and petroleum sectors and destinations across developing economies. Trade policy is supporting exports through schemes like the Focus Market Scheme (FMS), Focus Product Scheme (FPS), and Duty Entitlement Passbook Scheme (DEPB).

6.12 Imports of US$ 236.7 billion recorded an increase of 34.3 per cent during H1 of 2011-12 as against an increase of 27.3 per cent in H1 of 2010-11 over H1 of 2009-10. Rising crude oil prices, along with increase in gold and silver prices, have contributed significantly to the burgeoning import bill during H1 of 2011-12.

6.13 The trade deficit widened by 24.5 per cent to US$ 85.8 billion (9.4 per cent of GDP) during H1 of 2011-12 vis-a-vis US$ 68.9 billion (8.9 per cent of GDP) in H1 of the previous year, despite the higher export growth compared with imports in H1 of 2011-12

Invisibles

6.14 The invisibles account of the BoP reflects the combined effect of transactions relating to international trade in services, income associated with non-resident assets and liabilities, labour and property, and cross-border transfers, mainly workers' remittances.

6.15 In 2010-11, there was a sharp increase in both exports and imports of services. Services exports increased by 38.4 per cent from US$ 96.0 billion in 2009-10 to US$ 132.9 billion in 2010-11. Business services increased by 113.3 per cent from US$ 11.3 billion in 2009-10 to US$ 24.8 billion in 2010-11 and financial services by 75.7 per cent to US$ 6.5 billion in 2010-11 from US$ 3.7 billion in 2009-10. Receipts on account of software services also witnessed a rise, mainly on account of improved efficiency and diversified export destinations. Software receipts at US$ 55.5 billion, accounting for 41.8 per cent of total service receipts, showed an increase of 11.7 per cent in 2010-11 (7.3 per cent a year earlier). Software receipts were 12.4 per cent of total current receipts. Net service exports increased to US$ 48.8 billion in 2010-11 from 36.0 billion in 2009-10, registering 35.5 per cent increase.

6.16 Private transfer receipts, comprising mainly remittances from Indians working overseas, also increased by 3.7 per cent to US$ 55.6 billion in 2010-11 from US$ 53.6 billion in the previous year. Private transfer receipts constituted 12.4 per cent of current receipts (15.5 per cent in 2009-10). A modest increase was observed in other categories of receipts (transportation, insurance, communication, and GNIE).

6.17 Invisible payments increased by 36.2 per cent from US$ 83.4 billion in 2009-10 to US$ 113.6 billion in 2010-11. The growth of 36.2 per cent in invisible payments outstripped the 21.3 per cent growth recorded in 2010-11. Increase in invisible payments was mainly attributed to business services, financial services, travel, and investment income. Even though the surplus on account of service-sector exports was significantly higher in 2010-11, growth in net receipts on account of transfers was moderate and net outflow of investment income increased during the same period. As a result, the net invisible balance (receipts minus payments) posted an increase of 5.5 per cent to US$ 84.6 billion in 2010-11 as against US$ 80.0 billion in 2009-10. As a proportion of GDP, net invisible balance declined from 5.9 per cent in 2009-10 to 5.0 per cent in 2010-11. At this level, the invisible surplus financed 64.8 per cent of trade deficit as against 67.7 per cent during 2009-10.

6.18 During H1 of 2011-12, invisible receipts recorded an increase of 17.4 per cent to US$ 106.0 billion vis-a-vis US$ 90.3 billion during the corresponding period of 2010-11. All broad categories

Table 6.2 : Selected Indicators of the External Sector

Sl. No.	Item	2006-07	2007-08	2008-09	2009-10	2010-11PR	2010-11 H1 (April-Sept. 2010)PR	2011-12 H1 (April-Sept. 2011)P
1	2	3	4	5	6	7	8	9
1	Growth of exports – BoP (%)	22.6	28.9	13.7	-3.5	37.3	30.0	40.6
2	Growth of imports – BoP (%)	21.4	35.1	19.8	-2.6	26.7	27.3	34.3
3	Growth of non-factor services (credit) (%)	28.0	22.4	17.3	-9.4	38.4	32.7	17.1
4	Growth of non-factor services (debit) (%)	28.5	16.2	1.1	15.3	40.0	48.3	1.0
5	Exports/imports-BoP (%)	67.6	64.5	61.3	60.7	65.7	60.9	63.8
6	Exports/imports of goods and services (%)	86.2	83.0	81.8	77.2	82.4	77.7	80.0
7	Import cover of FER (No. of months)	12.5	14.4	9.8	11.1	9.6	10.0	7.9
8	External assistance (net)/ TC (%)	3.9	2.0	33.0	5.6	8.0	7.8	1.7
9	ECB (net)/TC (%)	35.6	21.2	106.3	3.9	20.2	14.6	25.8
10	NRI deposits / TC (%)	9.6	0.2	58.0	5.7	5.2	5.6	9.6
					As per cent of GDP mp			
11	Exports	13.6	13.4	15.2	13.4	14.8	13.9	16.5
12	Imports	20.1	20.8	25.0	22.0	22.6	22.8	25.8
13	Trade balance	-6.5	-7.4	-9.7	-8.7	-7.8	-8.9	-9.4
14	Invisible balance	5.5	6.1	7.5	5.9	5.0	5.1	5.8
15	Goods and services balance	-3.4	-4.2	-5.3	-6.0	-4.9	-6.1	-6.0
16	Current account balance	-1.0	-1.3	-2.3	-2.8	-2.7	-3.8	-3.6
17	ECBs	1.7	1.8	0.6	0.1	0.7	0.7	1.2
18	FDI (net)	0.8	1.3	1.8	1.3	0.6	0.9	1.3
19	Portfolio investment (net)	0.7	2.2	-1.2	2.4	1.8	3.1	0.1
20	Total capital account (net)	4.7	8.6	0.5	3.8	3.7	5.0	4.5

Source **: RBI. PR: Partially Revised. P: Preliminary.**

Notes: **FER: Foreign Exchange Reserves; TC: Total Capital Flow (net); GDPmp: Gross Domestic Product at current market prices.**

of invisibles, namely services, transfers, and income, showed increase. Growth in exports of services moderated to 17.1 per cent during H1 of 2011-12 as against 32.7 per cent during H1 of 2010-11, while growth in imports was substantially lower at 1.0 per cent during H1 of 2011-12 as against 48.3 per cent during H1 of 2010-11. On net basis, the services surplus increased to US$ 31.1 billion in H1 of 2011-12 from US$ 21.5 billion in the corresponding period a year earlier. Investment income receipts declined by 3.8 per cent to US$ 4.2 billion during H1 of 2011-12, while payments amounted to US$ 13.6 billion (US$ 12.2 billion a year earlier). Transfer receipts that primarily comprise personal transfers increased to US$ 32.3 billion during H1 of 2011-12 (US$ 27.2 billion a year earlier).

6.19 Invisible payments of US$ 53.0 billion during H1 of 2011-12 recorded an increase of 3.9 per cent over US$ 51.0 billion in H1 of 2010-11. Net invisibles balance (receipts minus payments) recorded a 34.6 per cent increase to US$ 52.9 billion (5.8 per cent of GDP) in H1 of 2011-12 from US$ 39.3 billion (5.1 per cent of GDP) in H1 of the previous year. At this level, the invisibles surplus financed about 62.0 per cent of trade deficit during H1 of 2011, as against 57.0 per cent during the same period a year earlier.

6.20 Goods and services deficit (i.e. trade balance plus services) decreased marginally to US$ 81.8 billion (4.9 per cent of GDP) during 2010-11 as compared to US$ 82.2 billion (6.0 per cent of GDP) in 2009-10. In fiscal 2011-12, it widened to US$ 54.7 billion up to H1 as compared to US$ 47.4 billion during the corresponding period a year earlier on account of increase in trade deficit. However, as a ratio of GDP, it marginally declined to 6.0 per cent in 2011-12 (up to H1) from 6.1 per cent in 2010-11 (up to H1) (Table 6.2).

Current Account Balance

6.21 The CAD increased to US$ 45.9 billion in 2010-11 from US$ 38.2 billion in 2009-10, despite improvement in net invisibles, mainly on account of higher trade deficit. However, as a proportion of GDP, CAD marginally improved to 2.7 per cent in 2010-11 as compared to 2.8 per cent in 2009-10 (Figure 6.1).

6.22 The CAD increased to US$ 32.8 billion in H1 of 2011-12, as compared to US$ 29.6 billion during the corresponding period of 2010-11, mainly on account of higher trade deficit. As a proportion of GDP, it was marginally lower at 3.6 per cent during H1 of 2011-12 vis-à-vis 3.8 per cent in H1 of the preceding year (Figure 6.2).

6.23 As per the latest data available from the Ministry of Commerce, at US$ 242.8 billion during April 2011-January 2012, exports registered a growth of 23.5 per cent over exports of US$ 196.6 billion during the same period in 2010-11. At US$ 391.5 billion, imports recorded 29.4 per cent growth during April 2011-January 2012 over the figure of US$ 302.6 billion during the corresponding period of the previous year. Consequently, trade deficit increased by 40.3 per cent to US$ 148.7 billion during April 2011-January 2012 as compared to US$ 106 billion in April 2010-January 2011.

Figure 6.1 **Current account balance, goods and services balance, trade balance, invisibles balance and net capital inflows as a per cent of GDP during 2006-07 to 2010-11**

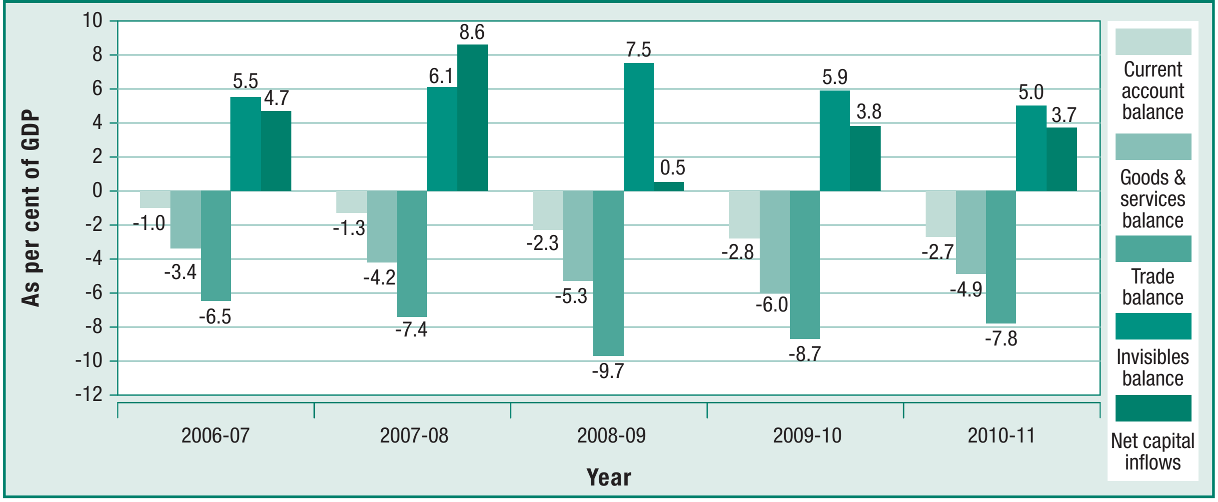
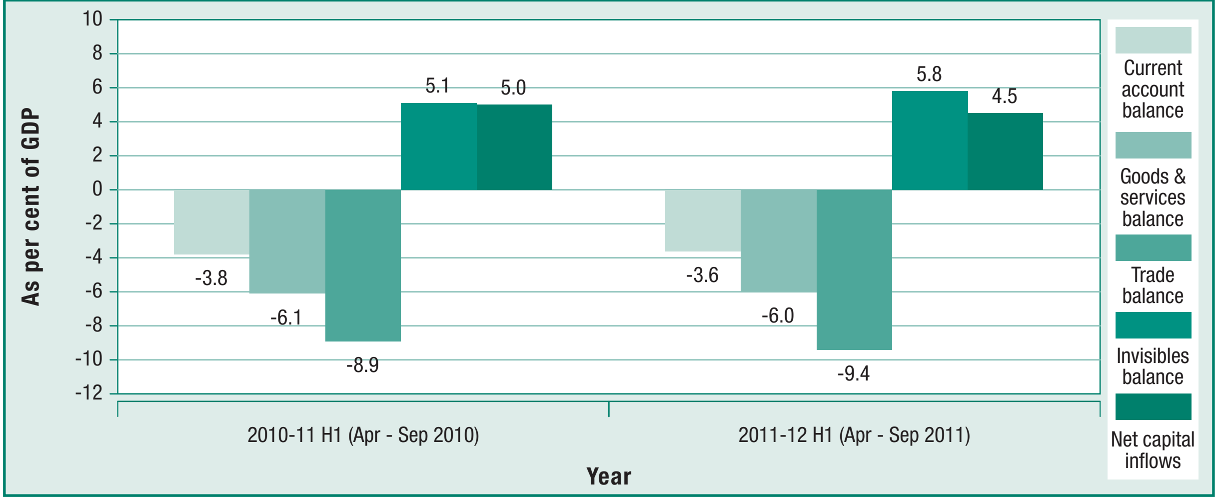


Figure 6.2 **Current account balance, goods and services balance, trade balance, invisibles balance and net capital inflows as a per cent of GDP during H1 of 2010-11 and 2011-12**



Capital Account

6.24 Capital inflows can be classified by instrument (debt or equity) and maturity (short-term or long-term). The main components of capital account include foreign investment, loans, and banking capital. Foreign investment comprising FDI and portfolio investment represents non-debt liabilities, while loans (external assistance, ECBs, and trade credit) and banking capital including NRI deposits are debt liabilities. In India, FDI is preferred over portfolio flows as the FDI flows tend to be more stable than portfolio and other forms of capital flows. Rupee-denominated debt is preferred over foreign currency debt and medium- and long-term debt is preferred over short-term.

6.25 Push and pull factors explain international capital flows. Push factors are external to an economy and inter alia include parameters like low interest rates, abundant liquidity, slow growth, or lack of investment opportunities in advanced economies. Pull factors like robust economic performance and improved investment climate as a result of economic reforms in emerging economies are internal to an economy.

6.26 In 2010-11, both gross inflows of US$ 499.4 billion and outflows of US$ 437.4 billion under the capital account were higher than gross inflows of US$ 345.8 billion and outflows of US$ 294.1 billion in the preceding year. In net terms, capital inflows increased by 20.2 per cent to US$ 62.0 billion (3.7 per cent of GDP) in 2010-11 vis-a-vis US$ 51.6 billion (3.8 per cent of GDP) in 2009-10 mainly on account of trade credit and loans (ECBs and banking capital).

6.27 The Non-debt flows or foreign investment comprising FDI and portfolio investment (ADRs/GDRs and FIIs) on net basis decreased by 21.4 per cent from US$ 50.4 billion in 2009-10 to US$ 39.7 billion in 2010-11. Decline in foreign investment was offset by the debt flows component of loans and banking capital which increased by 130.3 per cent from US$ 14.5 billion in 2009-10 to US$ 33.4 billion in 2010-11.

6.28 Inward FDI showed a declining trend while outward FDI showed an increasing trend in 2010-11 vis-a-vis 2009-10. Inward FDI declined from US$ 33.1 billion in 2009-10 to US$ 25.9 billion in 2010-11. Sector-wise, deceleration during 2010-11 was mainly on account of lower FDI inflows under manufacturing, financial services, electricity, and construction. Country-wise, investment routed through Mauritius remained the largest component of FDI inflows to India in 2010-11 followed by Singapore and the Netherlands. Outward FDI increased from US$ 15.1 billion in 2009-10 to US$ 16.5 billion in 2010-11. With lower inward FDI and rise in outward FDI, net FDI (inward minus outward) to India stood considerably lower at US$ 9.4 billion during 2010-11 (US$ 18.0 billion a year earlier).

6.29 Net portfolio investment flow witnessed marginal decline to US$ 30.3 billion during 2010-11 as against US$ 32.4 billion in 2009-10. This was due to decline in ADRs/GDRs to US$ 2.0 billion in 2010-11 from US$ 3.3 billion in 2009-10, even though FII inflows showed marginal increase to US$ 29.4 billion in 2010-11 from US$ 29.0 billion in 2009-10.

6.30 Other categories of capital flows, namely debt flows of ECBs, banking capital, and short-term credit recorded a significant increase in 2010-11. Net ECB inflow increased significantly to US$ 12.5 billion in 2010-11 as against US$ 2.0 billion in 2009-10. Similarly, short-term trade credit increased from US$ 7.6 billion in 2009-10 to US$ 11 billion in 2010-11, indicating strong domestic economic performance. Further, external assistance increased from US$ 2.9 billion in 2009-10 to US$ 4.9 billion in 2010-11.

6.31 The capital account surplus improved by 20.1 per cent to US$ 62.0 billion during 2010-11 from US$ 51.6 billion in 2009-10. However, as a proportion of GDP, it declined marginally to 3.7 per cent in 2010-11 from 3.8 per cent in 2009-10.

6.32 Net accretion to reserves (on BoP basis) in 2010-11, at US$ 13.1 billion, remained at more or less the same level as in 2009-10 (US$ 13.4 billion).

6.33 In fiscal 2011-12 (up to H1), under the capital account both gross inflows of US$ 244.2 billion and outflows of US$ 203.1 billion were higher than the gross inflows of US$ 207.5 billion and outflows of US$ 168.5 billion during the same period a year ago. In net terms, capital inflows increased moderately to US$ 41.1 billion in H1 of 2011-12 as against US$ 39.0 billion in H1 of 2010-11. While net FDI was higher at US$ 12.3 billion in H1 of 2011-12 as against US$ 7 billion in H1 of 2010-11, net portfolio investment substantially declined from US$ 23.8 billion to US$ 1.3 billion during the same period. This was on account of a major decline in FII flows to US$ 0.9 billion in 2011-12 (up to H1) from US$ 22.3 billion in H1 of 2010-11. Other capital flows, including ECBs and banking capital, also substantially increased. Net capital inflow as a proportion of GDP has shown moderation from 5.0 per cent in H1 of 2010-11 to 4.5 per cent in H1 of 2011-12.

6.34 Net accretion to reserves (on BoP basis) during H1 of 2011-12 was lower at US$ 5.7 billion as compared to US$ 7 billion in H1 of the previous year mainly due to widening of the CAD.

6.35 As per the latest available information on capital inflows, FDI inflows were US$ 35.3 billion during April-December 2011 (US$ 16.0 billion in the corresponding period of the preceding year). Portfolio inflows fell sharply to US$ 3.3 billion during April-December 2011 from US$ 31.3 billion a year earlier mainly reflecting uncertainty and risk in the global economy on account of the euro zone crisis.

Foreign Exchange Reserves

6.36 India's foreign exchange reserves comprise foreign currency assets (FCA), gold, special drawing rights (SDRs), and reserve tranche position (RTP) in the International Monetary Fund (IMF). The level of foreign exchange reserves is largely the outcome of the RBI's intervention in the foreign exchange market to smoothen exchange rate volatility and valuation changes due to movement of the US dollar against other major currencies of the world. Foreign exchange reserves are accumulated when there is absorption of the excess foreign exchange flows by the RBI through intervention in the foreign exchange market, aid receipts, and interest receipts and funding from the International Bank for Reconstruction and Development (IBRD), Asian Development Bank (ADB), International Development Association (IDA), etc.

6.37 FCAs are maintained in major currencies like the US dollar, euro, pound sterling, Australian dollar, and Japanese yen. Both the US dollar and euro are intervention currencies; however, reserves are denominated and expressed in the US dollar only, which is the international numeraire for the purpose. The movement of the US dollar against other currencies in which FCAs are held therefore impacts the level of reserves in US dollar terms. The level of reserves declines when the US dollar appreciates against major international currencies and vice versa. The twin objectives of safety and liquidity have been the guiding principles of foreign exchange reserves management in India with return optimization being embedded strategy within this framework.

India's foreign exchange reserves

6.38 Beginning from a low level of US$ 5.8 billion at end March 1991, India's foreign exchange reserves gradually increased to US$ 25.2 billion by end March 1995, US$ 38.0 billion by end March 2000, US$ 113.0 billion by end March 2004, and US$ 199.2 billion by end March 2007. The reserves stood at US$ 314.6 billion at end May 2008, before declining to US$ 252.0 billion at the end of March 2009. The decline in reserves in 2008-09 was inter alia a fallout of the global crisis and strengthening of the US dollar vis-à-vis other international currencies. During 2009-10, the level of foreign exchange reserves increased to US$ 279.1 billion at end March 2010, mainly on account of valuation gain as the US dollar depreciated against most of the major international currencies. In fiscal 2010-11, foreign exchange reserves have shown an increasing trend and reached

US$ 304.8 billion at end March 2011, up by US$ 25.7 billion from the US$ 279.1 billion level at end March 2010. Of the total increase in reserves, US$ 12.6 billion was on account of valuation gains arising out of depreciation of the US dollar against major currencies and the balance US$ 13.1 billion was on BoP basis. In 2011-12, the reserves increased by US$ 6.7 billion from US$ 304.8 billion at end March 2011 to US$ 311.5 billion at end September 2011. Out of this total increase, US$ 5.7 billion was on BoP basis and the balance US$ 1.0 billion was on account of valuation effect (Table 6.3). The component-wise details of foreign exchange reserves from 1950-51 to 2011-12 (up to December 2011) in rupee and US dollar are given in Appendices 6.1 (A) and 6.1 (B).

6.39 In the current fiscal, on month-on-month basis, the foreign exchange reserves have shown twin trends. The reserves reached an all time high level of US$ 322.0 billion at end August 2011. However, they declined to US$ 311.5 billion at end September 2011 before increasing to US$ 316.2 billion at end October 2011. In the months of November and December 2011, reserves again showed a declining trend. At end December 2011, they stood at US$ 296.7 billion, indicating a decline of US$ 8.1 billion from US$ 304.8 billion at end March 2011 (Figure 6.3). The decline in reserves is partly due to intervention by the RBI to stem the slide of the rupee against the US dollar. This level of reserves provides about eight months of import cover.

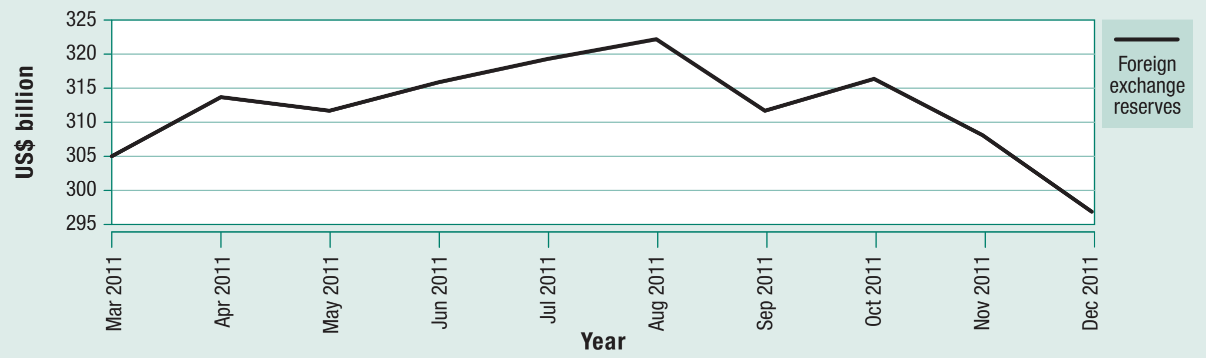
Table 6.3 : Sources of Variation in Foreign Exchange Reserves on BoP Basis and Valuation Effect

(US$ billion)

Sl. No.	Items	2009-10	2010-11 PR	April-September 2010-11 PR	April-September 2011-12 P
1	2	3	4	5	6
I	**Current account balance**	**-38.2**	**- 45.9**	**-29.6**	**-32.8**
II	**Capital account (net) (a to f)**	**51.6**	**62.0**	**38.9**	**41.1**
	a Foreign investment (i+ii)	50.4	39.7	30.8	13.6
	(i) FDI	18.0	9.4	7.0	12.3
	(ii) Portfolio investment	32.4	30.3	23.8	1.3
	of which:				
	FIIs	29.0	29.4	22.3	0.9
	ADRs/GDRs	3.3	2.0	1.6	0.5
	b ECBs	2.0	12.5	5.7	10.6
	c Banking capital	2.1	5.0	0.8	19.3
	of which: NRI deposits	2.9	3.2	2.2	3.9
	d Short-term trade credit	7.6	11.0	6.9	5.9
	e External assistance	2.9	4.9	3.0	0.7
	f Other items in capital account (includes Rupee Debt Service)	-13.3	- 11.1	-8.4	-9.2
III	**Errors and omissions**	**-0.01**	**- 3.0**	**-2.3**	**-2.5**
IV	**Overall balance (I+II+III)**	**13.4**	**13.1**	**7.0**	**5.7**
V	**Reserve change on BoP basis [increase (-) / decrease (+)]**	**-13.4**	**- 13.1**	**-7.0**	**-5.7**
VI	**Valuation change**	**13.7**	**12.6**	**6.8**	**1.0**
VII	**Total reserve change (V+VI)** (increase in reserves (+) / decrease in reserves (-)	**27.1**	**25.7**	**13.8**	**6.7**

Source : RBI. PR: Partially Revised. P: Preliminary.
Note : Total may not tally due to rounding off.

Figure 6.3 Foreign exchange reserves



6.40 A summary of changes in the foreign exchange reserves since 2006-07, with a breakdown into increase / decrease on BoP basis and valuation effect is presented in Table 6.4.

FCAs

6.41 FCAs are the major constituent of India's foreign exchange reserves. FCAs decreased by US$ 11.3 billion from US$ 274.6 billion at end March 2011 to US$ 263.3 billion at end December 2011.

6.42 In line with the principles of preserving the long-term value of the reserves in terms of purchasing power, minimizing risk and volatility in returns, and maintaining liquidity, the RBI holds FCAs in major convertible currency instruments. These include deposits of other country central banks, the Bank for International Settlements (BIS), and top-rated foreign commercial banks and securities representing debt of sovereigns and supranational institutions with residual maturity not exceeding 10 years, to provide a strong bias towards capital preservation and liquidity. The annualized rate of return, net of depreciation, on the multi-currency multi-asset portfolio of the RBI declined from 4.2 per cent in 2008-09 to 2.1 per cent in 2009-10 and further to 1.7 per cent in 2010-11.

Foreign exchange reserves of other countries

6.43 India continues to be one of the largest holders of foreign exchange reserves. Country-wise details of foreign exchange reserves reveal that India is the sixth largest foreign exchange reserves holder in the

Table 6.4 : Summary of changes in Foreign Exchange Reserves (US$ billion)

Sl. No.	Year	Foreign exchange reserves at the end of financial year (end March)	Total Increase(+)/ decrease (-) in reserves	Increase/decrease in reserves on a BoP basis	Increase/decrease in reserves due to valuation effect
1	2	3	4	5	6
1	2006-07	199.2	+ 47.6	+36.6 (76.9%)	+ 11.0 (23.1%)
2	2007-08	309.7	+ 110.5	+92.2 (83.4%)	+ 18.3 (16.6%)
3	2008-09	252.0	- 57.7	-20.1 (34.8%)	- 37.6 (65.2)
4	2009-10	279.1	+27.1	+13.4 (49.4%)	+13.7 (50.6%)
5	2010-11	304.8	+25.7	+13.1 (51.0%)	+12.6 (49.0%)
6	2011-12 (up to Sept. 2011)	311.5	+6.7	+5.7 (85.1%)	+1.0 (14.9%)

Source : RBI.
Note : Figures in parentheses indicate percentage shares of total change.

Table 6.5 : Foreign Exchange Reserves of some major countries

Sl. No.	Country	Foreign exchange reserves (end Dec. 2011) (US$ billion)
1	2	3
1	China	3181.1
2	Japan	1326.1
3	Russia	499.5
4	Brazil	352.0
5	Switzerland	340.6
6	India	296.7
7	China P R Hong Kong	285.5
8	Germany	262.3
9	Singapore	237.7
10	France	233.6

***Source* : IMF except for China.**

world, after China, Japan, Russia, Brazil, and Switzerland (Table 6.5) at end December 2011.

6.44 A comparative picture of foreign exchange reserves and import cover, as measured by the ratio of foreign exchange reserves to import of goods and services for select country groups and countries including India, is presented in Table 6.6. The ratio of reserves to import of goods and services of 'Emerging and Developing Economies' witnessed an improvement from 75.5 per cent in 2006 to 109.1 per cent in 2009 before declining to 102.4 per cent in 2010. Among the country groups, the ratio of 'Developing Asia including China and India' increased from 89.5 per cent in 2006 to 145 per cent in 2009, before declining to 131.2 per cent in 2010. In case of 'Middle East and North Africa' the ratio has improved steadily from 104.3 in 2006 to 118.9 in 2010.

Exchange Rate

6.45 The exchange rate policy is guided by the broad principle of careful monitoring and management of exchange rates with flexibility, while allowing the underlying demand and supply conditions to determine exchange rate movements over a period in an orderly manner. Subject to this predominant objective, RBI intervention in the foreign exchange market is guided by the objectives of reducing excess volatility, preventing the emergence of destabilizing speculative activities, maintaining adequate level of reserves, and developing an orderly foreign exchange market.

6.46 During 2010-11, the average monthly exchange rate of the rupee against the US dollar appreciated by 1.2 per cent from ₹ 45.50 per US dollar in March 2010 to ₹ 44.97 per US dollar in March 2011. Similarly, on point-to-point basis, the average exchange rate of the rupee [average of buying and selling rate of the Foreign Exchange Dealers Association of India (FEDAI)] appreciated by 1.1 per cent from ₹ 45.14 per US dollar on 31 March 2010 to ₹ 44.65 per US dollar on 31 March 2011. This was mainly on account of weakening of the US dollar in the international market in 2010-11.

6.47 The monthly average exchange rate of the rupee vis-a-vis the pound sterling, euro, and Japanese yen, however, depreciated in 2010-11. The monthly average exchange rate of the rupee vis-a-vis the pound sterling depreciated by 5.9 per cent from ₹ 68.44 per pound sterling in March 2010 to ₹ 72.71 in March 2011. Similarly, against the euro and Japanese yen, the monthly average exchange rate of the rupee depreciated by 1.9 per cent from ₹ 61.77 per euro in March 2010 to ₹ 62.97 per euro in March 2011 and by 8.7 per cent from ₹ 50.18 per 100 Japanese yen in March 2010 to ₹ 54.98 per 100 Japanese yen in March 2011.

6.48 On an annual average basis, the rupee appreciated against major international currencies except the Japanese yen in fiscal 2010-11. The annual average exchange rate of the rupee was ₹ 47.44 per US dollar in 2009-10, appreciating by 4.1 per cent to ₹ 45.56 per US dollar in 2010-11. Similarly, the annual average exchange rate of the rupee in 2009-10 was ₹ 75.76 per pound sterling and ₹ 67.03 per euro, which appreciated by 6.9 per cent and 11.3 per cent to ₹ 70.87 per pound sterling and ₹ 60.21 per euro respectively during 2010-11. The annual average exchange rate of the rupee per Japanese yen however depreciated by 4.1 per cent from ₹ 51.11 per 100 Japanese yen in 2009-10 to ₹ 53.27 per 100 Japanese yen in 2010-11.

6.49 In the current fiscal, there are two distinct phases in the exchange rate of the rupee. The rupee continued exhibiting a two-way movement with an appreciating trend till about July 2011, after which the trend reversed and it started declining sharply from September 2011 onwards, due to factors relating to the uncertain global economy.

6.50 On month-to-month basis the rupee depreciated by 14.6 per cent from the level of ₹ 44.97 per US dollar in March 2011 to ₹ 52.68 per US dollar in December 2011. On point-to-point basis, it depreciated by 16.2 per cent from ₹ 44.65 per US

Table 6.6 : International Comparison of Foreign Exchange Reserves (US$ billion) and Ratio of Reserves to Imports of Goods and Services

Sl. No.	Country / Country Group	2006	2007	2008	2009	2010	2011 (Projection)	2012 (Projection)
1	2	3	4	5	6	7	8	9
I	**Country**							
1	Russia	296.2	467.6	412.7	417.8	454.5	527.4	582.5
		(141.7)	(165.5)	(112.3)	(164.8)	(141.6)	(129.4)	(130.2)
2	China	1069.5	1531.3	1950.3	2417.9	2889.6	3479.5	4112.7
		(125.4)	(148.0)	(158.2)	(217.2)	(190.0)	(188.4)	(195.4)
3	India	171.3	267.6	248.0	266.2	291.5	319.7	354.9
		(75.5)	(95.1)	(71.3)	(73.8)	(66.4)	(62.1)	(60.3)
4	Brazil	85.2	179.5	192.9	237.4	287.5	366.1	412.9
		(70.7)	(113.8)	(87.6)	(135.9)	(117.7)	(120.3)	(128.0)
5	Mexico	76.3	87.1	95.1	99.6	120.3	140.3	150.3
		(27.4)	(28.5)	(28.5)	(38.7)	(36.8)	(35.9)	(37.1)
II	**Country Group**							
1	Developing Asia (excluding China & India)	248.7	330.0	335.8	393.9	488.0	581.3	658.2
		(42.6)	(49.1)	(41.7)	(60.6)	(58.3)	(58.2)	(60.6)

Source **: World Economic Outlook Database, September 2011.**

Note **: 1. Reserves are based on official holding of gold valued at SDR 35 an ounce. This convention results in a marked underestimation of reserves for countries that have substantial gold holdings.**

2. Figures in parentheses indicate ratios of reserves to imports of goods and services.

dollar on 31 March 2011 to ₹ 53.26 per US dollar on 30 December 2011. The rupee reached a peak of ₹ 43.94 per US dollar on 27 July 2011, and a low of ₹ 54.23 per US dollar on 15 December 2011 indicating depreciation of 19.0 per cent. Similarly, the monthly average exchange rate of the rupee depreciated by 11.5 per cent against the pound sterling, 9.1 per cent against the euro, and 18.7 per cent against the Japanese yen between March 2011 and December 2011.

6.51 A sharp fall in rupee value may be explained by the supply-demand imbalance in the domestic foreign exchange market on account of slowdown in FII inflows, strengthening of the US dollar in the international market due to the safe haven status of the US treasury, and heightened risk aversion and deleveraging due to the euro area crisis that impacted financial markets across emerging market economies (EMEs). Apart from the global factors, there were several domestic factors that have added to the weakening trend of the rupee, which include increasing CAD and high inflation.

6.52 As the rupee has been under pressure since July 2011, efforts have been made by the RBI to augment supply of foreign exchange and curb speculation in the foreign exchange market to stem rupee decline. These measures are discussed in detail in Box 6.1.

6.53 As a result of these measures, and increase in capital inflows, the depreciating trend in rupee exchange rate reversed. The monthly average exchange rate of the rupee appreciated by 2.6 per cent from ₹ 52.68 per US dollar in December 2011 to ₹ 51.34 per US dollar in January 2012. On point-to-point basis, the average exchange rate of the rupee has appreciated by 9.2 per cent from its lowest value of ₹ 54.23 per US dollar on 15 December 2011 to ₹ 49.67 per US dollar on 31 January 2012.

6.54 The month-wise exchange rate of the rupee against major international currencies and the RBI's sale/purchase of foreign currency in the foreign exchange market during 2011-12 are indicated in Table 6.7.

Box 6.1 : Recent Policy Initiatives to Stem Slide in Rupee Exchange Rate

A number of steps have been taken recently to stimulate capital inflows and curb speculation in foreign exchange market to stabilize the value of the rupee. Key details are as follows:

I Measures to increase supply of foreign exchange

Trade Credit

- All-in-cost ceiling for trade credit has been increased from 6 months Libor + 200 basis points (bps) to 6 months Libor + 350 bps.

ECBs

- The existing ECB limit under automatic approval route has been enhanced from US$ 500 million to US$ 750 million for eligible corporates. For borrowers in the services sector, the limit was enhanced from US$ 100 million to US$ 200 million.
- All-in-cost ceiling for ECB was revised as under:

Average maturity period	All-in-cost over 6 months LIBOR*	
	Existing	Revised
3 years and up to 5 years	300 bps	350 bps
More than 5 years	500 bps	500 bps

* for the respective currency of credit or applicable benchmark

- The change in the all-in-cost ceiling came into force with effect from 23 November 2011 and is applicable up to 31 March 2012, subject to review thereafter.
- The proceeds of ECBs raised abroad for rupee expenditure in India should be brought immediately. In other words, ECB proceeds meant only for foreign currency expenditure can be retained abroad pending utilization. The rupee funds however will not be permitted to be used for investment in capital marketsor real estate or for inter-corporate lending.

FII Investment

- The FII limit for investment in government securities and corporate bonds has been increased by US$ 5 billion each to US$ 15 billion and US $ 20 billion respectively, from earlier limits of US$ 10 billion and US$ 15 billion. The investment limit in long-term infrastructure corporate bonds, however, has been kept unchanged at US$ 25 billion. With this, overall limit for FII investment in corporate bonds and government securities now stands at US$ 60 billion.

NRI Deposits

- With effect from close of business on 23 November 2011, ***interest rates on fresh non-resident (external) rupee (NRE) term deposits*** for one to three years maturity increased to Libor/SWAP + 275 bps. The interest rates will also be applicable to deposits with maturity period exceeding three years and to deposits renewed after their present maturity period. ***Interest rate on Foreign Currency Non Resident Bank Deposit [FCNR (B)] deposits*** of all maturities contracted effective from the close of business in India as on 23 November 2011, will be within the ceiling rate of Libor/SWAP rates plus 125 bps for the respective currency/corresponding maturities.

II Major administrative measures as per RBI Press Release dated 15 December 2011.

i. Forward contracts involving the rupee as one of the currencies, booked by residents irrespective of the type and tenor of the underlying exposure, once cancelled, cannot be rebooked.

ii. All cash/tom/spot transactions by authorized dealers on behalf of clients will be undertaken for actual remittances/ delivery only and cannot be cancelled / cash settled.

iii. Forward contracts booked by FIIs, once cancelled, cannot be rebooked. They may, however, be rolled over on or before maturity.

iv. The Board of Directors of Authorized Dealers was allowed to fix suitable limits for various treasury functions with net overnight open exchange position and aggregate gap limits required to be approved by the RBI.

a. Net overnight open position limit (NOOPL) of authorized dealers would be reduced across the board and revised limits in respect of individual banks are being advised to the authorized dealers separately.

b. Intra-day open position / daylight limit of authorized eealers should not exceed existing NOOPL approved by the RBI.

Source : **RBI**

Table 6.7 : Exchange Rates of Rupee per Foreign Currency and RBI's Sale/Purchase of US Dollar in the Exchange Market during 2010-11 and 2011-12

Month	Average exchange rates (₹ per foreign currency)*				RBI Net sale (-) / purchase (+) (US$ million)
	US dollar	Pound sterling	Euro	Japanese yen**	
1	2	3	4	5	6
2010-11					
(annual average)	45.56	70.87	60.21	53.27	(+)1690
	(4.1)	(6.9)	(11.3)	(-4.1)	
March-2011	44.97	72.71	62.97	54.98	
	(1.0)	(0.8)	(-1.4)	(0.1)	
2011-12					
(monthly average)					
April-2011	44.37	72.72	64.25	53.31	-
	(1.4)	(-0.02)	(-2.0)	(3.1)	
May-2011	44.90	73.41	64.48	55.32	-
	(-1.2)	(-0.9)	(-0.4)	(-3.6)	
June-2011	44.83	72.79	64.52	55.65	-
	(0.2)	(0.9)	(-0.1)	(-0.6)	
July-2011	44.42	71.65	63.46	55.91	-
	(0.9)	(1.6)	(1.7)	(-0.5)	
August-2011	45.25	74.11	64.94	58.68	-
	(-1.8)	(-3.3)	(-2.3)	(-4.7)	
September-2011	47.63	75.12	65.47	62.03	(-) 845.0
	(-5.0)	(-1.3)	(-0.8)	(-5.4)	
October-2011	49.26	77.49	67.45	64.11	(-) 943.0
	(-3.3)	(-3.1)	(-2.9)	(-3.2)	
November-2011	50.86	80.25	68.91	65.60	(-) 2,918.0
	(- 3.1)	(- 3.4)	(- 2.1)	(- 2.3)	
December-2011	52.68	82.13	69.29	67.63	(-)7809.0
	(- 3.5)	(- 2.3)	(- 0.6)	(- 3.0)	

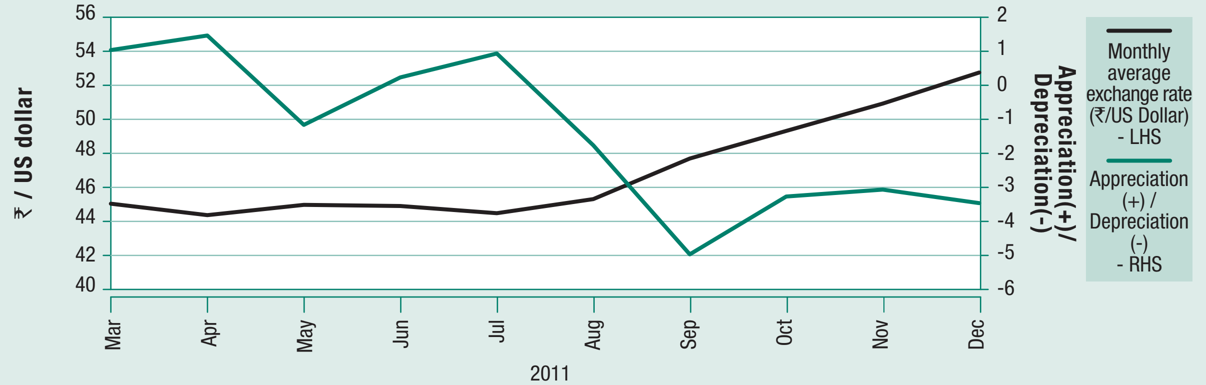
Source **: RBI.**
Notes : *** FEDAI indicative rate; ** Per 100 yen; Figures in parentheses indicate percentage appreciation (+) and depreciation (-) over the previous month / year. Some percentage figures may not tally due to rounding off.**

6.55 The monthly average exchange rate of the rupee per US dollar and its appreciation / depreciation during 2011-12 are depicted in Figure 6.4 .

Exchange Rate of Other Emerging Economies

6.56 Currency depreciation during 2011-12 was not specific to India. The currencies of other emerging

Figure 6.4 **Monthly average exchange rate (₹/US dollar) during March 2011 to December 2011 and appreciation/depreciation over the previous month**



economies, such as the Brazilian real, Mexican peso, Russian rouble, South Korean won, and South African rand, also depreciated against the US dollar, reflecting the increased demand for the US dollar as a safe haven asset in the wake of the sovereign debt crisis in the euro zone. Between July and November 2011, the Brazilian real has depreciated by 11.9 per cent, Russian rouble by 9.3 per cent, South Korean won by 6.2 per cent, and South African rand by 17.63 per cent.

6.57 The exchange rates of the rupee vis-à-vis select international currencies since 1991-92, year-wise, and during 2011-12, month-wise, are given in Appendix 6.5.

Nominal Effective Exchange Rate (NEER) and Real Effective Exchange Rate (REER)

The NEER and REER indices are used as indicators of external competitiveness of the country over a period of time. NEER is the weighted average of bilateral nominal exchange rates of the home currency in terms of foreign currencies, while REER is defined as a weighted average of nominal exchange rates, adjusted for home and foreign country relative price differentials. REER captures movements in cross-currency exchange rates as well as inflation differentials between India and its major trading partners. The RBI has been constructing six-currency (US dollar, euro for euro zone, pound sterling, Japanese yen, Chinese renminbi, and Hong Kong dollar) and 36-currency NEER and REER indices.

6.58 The six-currency trade-based NEER (base: 2004-05=100) depreciated by 2.1 per cent between March 2010 and March 2011 and by 13.5 per cent between March 2011 and December 2011. As compared to this, the monthly average exchange rate of the rupee appreciated by 1.2 per cent between March 2010 and March 2011, while in the current fiscal it depreciated by 14.6 per cent against the US dollar from ₹ 44.97 per US dollar in March 2011 to ₹ 52.68 per US dollar in December 2011 (Table 6. 8 and Appendix 6.6).

6.59 The six-currency trade-based REER (base: 2004-5=100) of the rupee appreciated by 4.1 per cent between March 2010 and March 2011. During 2011-12 (up to December 2011), the six-currency index showed depreciation of 10.8 per cent over March 2011 largely reflecting depreciation of the rupee in nominal terms, which mainly happened during the period August-December 2011.

Table 6.8 : Indices of NEER and REER of the Indian Rupee (Six-Currency Trade- based Weights)
Base 2004-05 (April-March) = 100

Month averages	NEER	Appreciation (+)/ depreciation (-) NEER over Previous Period/Month	REER	Appreciation (+)/ depreciation (-) REER over privious Period/Month
1	2	3	4	5
March 2010	92.19		111.43	
March 2011	90.29	-2.1	115.97	4.1
2011-12				
April 2011	90.43	0.2	117.43	1.3
May 2011	89.33	-1.2	116.46	- 0.8
June 2011 (P)	89.32	0	116.13	- 0.3
July 2011 (P)	90.34	1.1	117.72	1.4
August 2011 (P)	88.13	-2.4	115.68	- 1.7
September 2011 (P)	85.08	- 3.5	112. 46	- 2.8
October 2011 (P)	82.35	- 3.2	108.92	- 3.1
November 2011 (P)	80.00	-2.9	105.92	- 2.8
December 2011(P)	78.06	- 2.4	103.46	- 2.3

Source **: RBI.** **P: Provisional**

Table 6.9 : Exchange Rate of US dollar against International Currencies

Month/Year	GBP/USD	Euro/USD	USD/JPY	AUD/USD
1	2	3	4	5
March 2010	1.5082	1.3543	90.885	0.9095
March 2011	1.60315	1.4162	83.21	1.0336
US$ Appreciation (+) / Depreciation (-) (End March 2010– End March 2011)	-5.9	- 4.4	- 8.4	- 12.0
2011-12				
April 2011	1.6707	1.4806	81.11	1.0964
May 2011	1.6445	1.4392	81.545	1.0672
June 2011	1.6047	1.4503	80.535	1.0721
July 2011	1.6418	1.4384	76.895	1.0990
August 2011	1.6246	1.4374	76.61	1.0692
September 2011	1.5589	1.3391	77.14	0.9668
October 2011	1.6087	1.3858	78.185	1.0536
November 2011	1.5712	1.3448	77.55	1.0275
December 2011	1.5537	1.2942	76.95	1.0221
US$ Appreciation (+) / Depreciation (-) (End March 2011– End December 2011)	3.2	9.4	- 7.5	1.1

Source **: RBI.**

US dollar exchange rate in international market

6.60 In so far as international currencies are concerned, during 2010-11 the US dollar depreciated by 5.9 per cent against the pound sterling, 4.4 per cent against the euro, 8.4 per cent against the Japanese yen, and 12.0 per cent against the Australian dollar. In the current fiscal (up to end December 2011), the US dollar appreciated by 3.2 per cent against the pound sterling, 9.4 per cent against the euro, and 1.1 per cent against the Australian dollar. However, it depreciated by 7.5 per cent against the Japanese yen (Table 6. 9).

External Debt

6.61 At end March 2011, India's external debt stock was US$ 306.4 billion (₹ 13,68,477 crore) recording an increase of US$ 45.4 billion (17.4 per cent) over the end March 2010 level of US$ 261.0 billion (₹ 11,78,994 crore). Component-wise, long-term debt increased by 15.7 per cent to US$ 241.4 billion at end March 2011 from US$ 208.7 billion at end March 2010 while short-term debt based on original maturity, showed an increase of 24.2 per cent to US$ 65.0 billion from US$ 52.3 billion at end March 2010. Appendices 8.4(A) and 8.4(B) present the disaggregated data on India's external debt outstanding for the period from March 2001 to September 2011 in Indian rupee and US dollar terms respectively.

6.62 India's external debt stock increased by US$ 20.2 billion (6.6 per cent) to US$ 326.6 billion at end September 2011 over end March 2011 estimates of US$ 306.4 billion. This increase was primarily on account of higher commercial borrowings and short-term debt, which together contributed over 80 per cent of the total increase in external debt. The rise in short-term trade credits is in line with the increase in imports associated with reasonably strong domestic economic activity.

6.63 The maturity profile of India's external debt indicates the dominance of long-term borrowings. Long-term external debt at US$ 255.1 billion at end September 2011, accounted for 78.1 per cent of total external debt. Long-term debt at end September 2011 increased by US$ 13.6 billion (5.6 per cent) over the end March 2011 level, while short-term debt (original maturity) registered an increase of US$ 6.5 billion (10.1 per cent) (Table 6.10.).

Table 6.10 : India's External Debt Stock

At end-March	In US$ million			In ₹ crore		
	Long-term	Short-term	Total	Long-term	Short-term	Total
1	2	3	4	5	6	7
2005	116279	17723	134002	508777	77528	586305
2006	119575	19539	139114	533367	87155	620522
2007	144230	28130	172360	628771	122631	751402
2008	178669	45738	224407	714409	182881	897290
2009	181185	43313	224498	921469	220656	1142125
2010	208685	52329	261014	942806	236188	1178994
2011PR	241448	64990	306438	1078330	290147	1368477
2011 (end-June) PR	249010	68474	317484	1116205	306248	1422453
2011 (end-Sept.) QE	255071	71530	326601	1247863	349889	1597752

Source **: Ministry of Finance and RBI**
Note **: PR : Partially Revised QE : Quick Estimates.**

6.64 Under long-term debt, components such as commercial borrowings, NRI deposits, and multilateral borrowings taken together accounted for 61.3 per cent of total external debt at the end of September 2011 while other long-term debt components (bilateral borrowings, export credit, IMF, and rupee debt) accounted for 16.8 per cent. Thus long-term debt, taking into account all the components, accounted for 78.1 per cent of total external debt, while the remaining (21.9 per cent) was short-term debt at end September 2011 (Table 6.11.).

6.65 The currency composition of India's total external debt shows that the share of US dollar denominated debt was the highest in external debt stock at 55.8 per cent at end September 2011, followed by Indian rupee (18.2 per cent), Japanese yen (12.1 per cent), SDR (9.1 per cent), and euro (3.5 per cent). The currency composition of government (sovereign) debt indicates predominance of SDR denominated debt (37.3 per cent), which is attributable to borrowing from the IDA, i.e. the soft loan window of the World Bank under the multilateral agencies, and SDR allocations by the IMF. The share

Table 6.11 : Composition of External Debt (per cent of total external debt)

Sl. No.	Component	March 2010 PR	March 2011 PR	June 2011 PR	September 2011 QE
1	2	3	4	5	6
1	Multilateral	16.4	15.8	15.6	15.0
2	Bilateral	8.7	8.4	8.3	8.4
3	IMF	2.3	2.1	2.0	2.0
4	Export credit	6.5	6.1	5.9	6.0
5	Commercial borrowings	27.1	29.0	29.5	30.3
6	NRI deposits	18.3	16.9	16.6	16.0
7	Rupee debt	0.6	0.5	0.5	0.4
8	Long-term debt (1 to 7)	79.9	78.8	78.4	78.1
9	Short-term debt	20.1	21.2	21.6	21.9
10	Total external debt (8+9)	100.0	100.0	100.0	100.0

Source **: Ministry of Finance and RBI. PR : Partially Revised. QE : Quick Estimates.**

Table 6.12 : Currency Composition of India's External Debt and Sovereign External Debt

Sl. No.	Currency	Total external debt March 2010	March 2011PR	June 2011PR	Sept. 2011QE	Sovereign external debt March 2010	March 2011PR	June 2011PR	Sept. 2011QE
1	2	3	4	5	6	7	8	9	10
1	US dollar	53.2	53.6	54.3	55.8	26.5	26.8	26.7	26.5
2	SDR	10.7	9.7	9.5	9.1	41.7	38.1	38.2	37.3
3	Indian rupee	18.7	19.5	19.1	18.2	8.9	12.4	12.2	12.5
4	Japanese yen	11.5	11.4	11.1	12.1	18.6	18.8	18.9	19.9
5	Euro	3.6	3.7	3.7	3.5	4.3	3.9	3.9	3.8
6	Pound sterling	1.8	1.7	1.7	0.8	0.0	0.0	0.0	0.0
7	Others	0.5	0.5	0.6	0.5	0.0	0.0	0.0	0.0
	Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source **: Ministry of Finance and RBI.**
Note **: PR : Partially Revised QE-Quick Estimates.**

of US dollar-denominated debt was 26.5 per cent followed by Japanese yen denominated (19.9 per cent) (Table 6.12.).

6.66 Under India's external debt, government (sovereign) external debt stood at US$ 79.3 billion, while non-government debt amounted to US$ 247.3 billion at end September 2011. The share of government external debt in total external debt declined from 25.5 per cent at end March 2011 to 24.3 per cent at end September 2011. The ratio of government debt to GDP also posted a decline and remained in the range of 4.6 to 5.1 per cent over the past three years.

6.67 Over the years, India's external debt stock has witnessed structural change in terms of composition. The share of concessional in total debt has declined due to the shrinking share of official creditors and government debt and the surge in non-concessional private debt. The proportion of concessional in total debt declined from 42.9 per cent (average) during the period 1991-2000 to 28.1 per cent in 2001-10 and further to 14.7 per cent at end September 2011. The rising share of non-government debt is evident from the fact that such debt accounted for 65.6 per cent of total debt during the 2000s vis-a`-vis 45.3 per cent in the 1990s. Non-government debt accounted for over 70 per cent of total debt in the last five years and stood at 75.7 per cent at end September 2011.

6.68 The share of ECBs in India's total external debt has increased substantially over the past few years. While between end March 2001 and end March 2006, the share of ECBs in total external debt declined from 24.1 per cent to 19.0 per cent, the compound annual growth in such borrowings was 1.7 per cent. However, between end March 2006 and end March 2011, ECBs have registered a compound annual growth rate of 27.4 per cent with the share in total external debt climbing up to 30.3 per cent at end September 2011. The increase in ECBs in the recent period caused some concern given the depreciation of the rupee as it would mean a higher debt service burden in rupee terms that could impact profitability and the balance sheets of corporate borrowers.

6.69 The key external debt indicators are presented in Table 6.13. India's foreign exchange reserves provided a cover of 95.4 per cent to the total external debt stock at end September 2011 vis-à-vis 99.5 per cent at end March 2011. The ratio of short-term external debt to foreign exchange reserves was at 22.9 per cent at end September 2011 as compared to 21.3 per cent at end March 2011. The ratio of concessional debt to total external debt declined steadily and worked out to 14.7 per cent at end September 2011 as against 15.5 per cent at end March 2011.

6.70 India's external debt has remained within manageable limits as indicated by the external debt to GDP ratio of 17.8 per cent and debt service ratio of 4.2 per cent in 2010-11. This has been possible due to an external debt management policy of the government that emphasizes monitoring long- and short-term debt, raising sovereign loans on concessional terms with long maturities, regulating ECBs through end-use and all-in-cost restrictions, and rationalizing interest rates on NRI deposits.

Table 6.13 : India's Key External Debt Indicators (per cent)

Year	External Debt (US$ billion)	Total External Debt to GDP	Debt-Service Ratio	Foreign Exchange Reserves to Total External Debt	Concessional Debt to Total External Debt	Short-term External Debt* to Foreign Exchnage Reserves	Short-term External Debt* to Total Debt
1	2	3	4	5	6	7	8
1990-91	83.8	28.7	35.3	7.0	45.9	146.5	10.2
1995-96	93.7	26.9	26.2	23.1	44.7	23.2	5.4
2000-01	101.3	22.5	16.6	41.7	35.4	8.6	3.6
2005-06	139.1	16.8	10.1#	109.0	28.4	12.9	14.1
2006-07	172.4	17.5	4.7	115.6	23.0	14.1	16.4
2007-08	224.4	18.0	4.8	138.0	19.7	14.8	20.4
2008-09	224.5	20.3	4.4	112.1	18.7	17.2	19.2
2009-10	261.0	18.3	5.5	106.9	16.8	18.8	20.0
2010-11PR	306.4	17.8	4.2	99.5	15.5	21.3	21.2**
End-June 2011 PR	317.5	-	4.6	99.6	15.1	21.7	21.6
End-Sept. 2011 QE	326.6	-	-	95.4	14.7	22.9	21.9

Source **: Ministry of Finance and RBI.**

Notes**: - Not worked out for the broken period. PR : Partially Revised QE-Quick Estimates.**

***: Short-term debt is based on original maturity.**

****: Based on residual maturity, the short-term debt (US$ 129.1 billion) accounted for 42.2 per cent of total external debt at end March 2011 (RBI Press Release, dated 30 June 2011). Short-term debt by residual maturity comprises all the components of short-term debt with original maturity of up to one year and amounts falling due under long-term debt including NRI deposits during the one-year reference period.**

#: Works out to 6.3 per cent, with the exclusion of India millennium deposits (IMDs) repayments of US$ 7.1 billion and prepayment of US$ 23.5 million.Debt-service ratio is the proportion of gross debt service payments to external current receipts (net of official transfers).

International Comparison

6.71 A cross-country comparison of external debt of twenty most indebted developing countries, based on the data given in the World Bank's Global Development Finance 2012 which contains the debt numbers for the year 2010 and has a time lag of two years, showed that India was the *fifth* most indebted country, after the China, the Russian Federation, Brazil, and Turkey in 2010 in terms of stock of external debt. The ratio of India's external debt stock to gross national income (GNI) at 16.9 per cent was fourth lowest, with China having the lowest ratio at 9.3 per cent (Table 6.14.).

6.72 In terms of the cover of external debt provided by foreign exchange reserves, India's position was fifth highest at 103.5 per cent after China, Thailand, Malaysia, and Russia. A comparison of the share of short-term debt in total external debt across countries reveals that India's position was eighth lowest, with Pakistan having the lowest ratio.

Challenges and Outlook

6.73 A trade deficit of more than 8 per cent of GDP and CAD of more than 3 per cent is a sign of growing imbalance in the country's balance of payments. There is scope therefore to discourage unproductive imports like gold and consumer goods to restore balance. In this respect, some weakening of the rupee is a positive development, as it improves trade balance in the long run by increasing export competitiveness and lowering imports.

6.74 High trade and current account deficits, together with high share of volatile FII flows are making India's BoP vulnerable to external shocks. Greater attention therefore has to be given to improving the composition of capital flows towards FDI.

Table 6.14 : International Comparison of Top Twenty Developing Debtor Countries, 2010

Sl	Countries	Total External Debt Stock (US$ million)	Total Debt to GNI (per cent)	Short-term to Total External Debt (per cent)	Foreign Exchange Reserves to Total Debt (per cent)
1	2	3	4	5	6
1	China	548551	9.3	63.4	531.2
2	Russian Federation	384740	26.9	10.1	124.6
3	Brazil	346978	16.9	18.9	83.2
4	Turkey	293872	40.4	26.6	29.3
5	India	290282	16.9	19.4	103.5
6	Mexico	200081	19.5	19.5	60.3
7	Indonesia	179064	26.1	17.5	53.7
8	Argentina	127849	36.1	27.4	40.8
9	Romania	121505	76.4	20.6	39.5
10	Kazakhstan	118723	94.3	7.6	23.8
11	Ukraine	116808	85.9	22.7	29.6
12	Chile	86349	45.9	30	32.2
13	Malaysia	81497	35.4	43	130.7
14	Philippines	72337	36.2	8.7	86.2
15	Thailand	71263	23.4	54	241.4
16	Colombia	63064	22.8	13	44.5
17	Pakistan	56773	31.3	4	30.4
18	Venezuela	55572	14.3	27.8	53.4
19	Bulgaria	48077	104.8	32	35.8
20	South Africa	45165	12.7	27.2	97

Source **: World Bank, Global Development Finance 2012.**

Note **: Countries are arranged based on the magnitude of debt presented in Column 3 in the Table.**

6.75 The rupee has experienced high volatility in the last few years. Such volatility impairs investor confidence and has implications for corporate balance sheets and profitability in case of high exposure to ECBs when currency is depreciating. A more aggressive stance to check rupee volatility is therefore necessary.

6.76 The size of foreign exchange reserves could be a constraining factor in checking depreciation of local currency in the event of external shock and reversal of capital. It is therefore imperative that during times of surge in capital flows, when currency is under pressure to appreciate, measures are taken to build up reserve levels.