EXTERNAL COMMERCIAL BORROWING

India always promotes capital inflows as an element of the growth plan.

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What are External Commercial Borrowing and its regulations?

India always promotes capital inflows as an element of the growth plan. The need for domestic capital and shortage in the current account forced the government in the past to go for foreign capital. Hence, foreign capital is money obtained from foreign countries to invest locally.

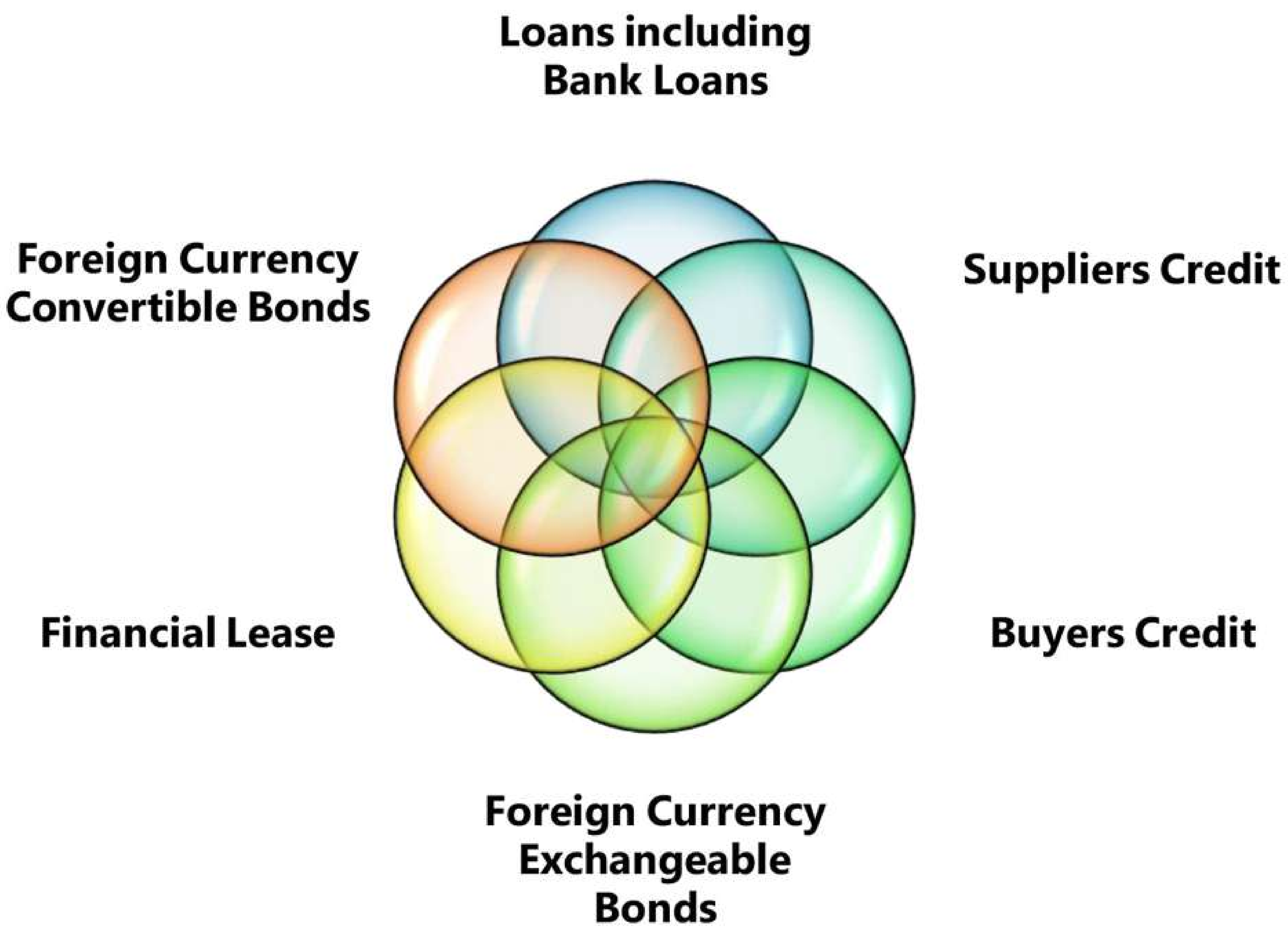
Foreign capital is not of the same kind as there are different types of foreign capital. The primary category is foreign investment including FDI (Foreign Direct Investment) and FPI (Foreign Portfolio Investment). Likewise, there are other types of foreign capital which include trade credit, NRI Deposits and the most important one for India – the External Commercial Borrowing (ECB).

What is External Commercial Borrowing?

External commercial borrowing (ECB) is loans in India made by non-resident lenders in foreign currency to Indian borrowers. They are used generally in India to ease access to foreign money by Indian corporation and PSUs (public sector undertakings).

Kinds of ECB

ECB includes:



Most of the loans are provided by foreign commercial banks and other financial institutions.

Benefits of External Commercial Borrowing

- ECBs provide the ability to borrow the large volume of funds
- The funds are available for comparatively long term
- Interest rate is also lower as compared to domestic finances
- ECBs are in terms of foreign currencies. Hence, they allow the company to have foreign currency to meet the import of machineries, etc.
- Companies can raise ECBs from globally recognized sources such as banks, export credit agencies, international capital markets, etc.

What are the existing routes for raising ECB?

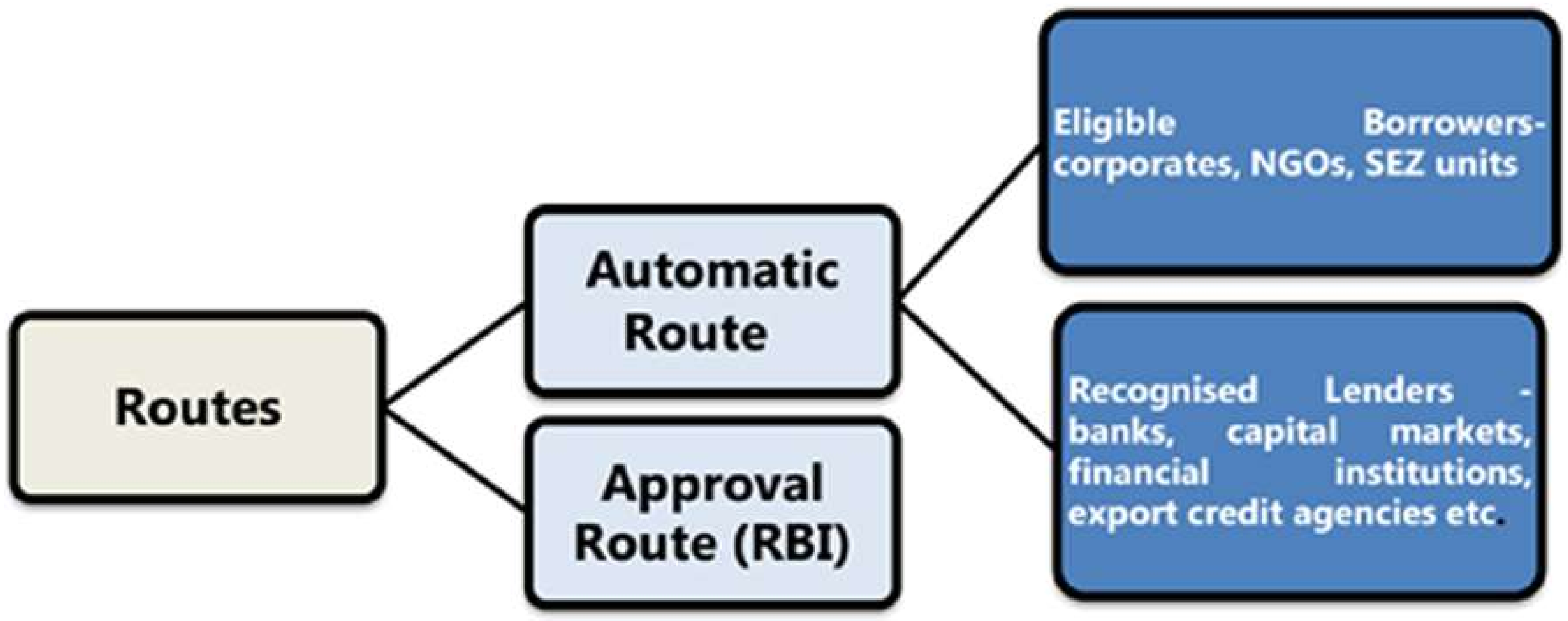
Automatic Route

- No approval of the RBI /GOI

- Get Loan Registration Number (LRN) from RBI by filing Form No. 83 through AD Bank
- Monthly filings with the RBI through AD Bank in Form ECB2

Approval Route

- Application to the RBI through AD Bank (Form ECB) on a prior basis
- RBI Empowered Committee to consider such request.
- Post-approval, obtain LRN and Monthly filings as under Automatic Route.



Currency of ECB

A borrower can raise ECB in Indian Rupees (INR) or in any other convertible currency. Any unit building Indian rupee denominated ECB is not allowable to convert the accountability which arises out of the ECB into foreign currency liability in any way.

Recognized Lenders/Investors as per ECB guidelines

Track 1	Track 2	Track 3
International banks	All entities mentioned under Track I (but excluding overseas offices/subsidiaries of the Indian banks)	All entities listed under Track I excluding overseas branches/subsidiaries of the Indian banks
International capital markets		In the case of NBFCs-MFIs, other eligible MFIs, not for profit companies and NGOs, ECB can also be availed from overseas organizations and individuals
Multilateral financial institutions (like IFC, ADB, etc.) / regional financial institutions and Government owned (either wholly or partially) financial institutions.		

Export credit agencies
Suppliers of equipment
Overseas long term investors
Foreign equity holders
Overseas branches/subsidiaries of Indian banks

Eligible Borrowers to raise ECB

Track 1	Track 2	Track 3
Companies in Manufacturing and Software Development	All entities listed under Track 1	All entities listed under Track 2
Shipping and Airline Companies	Companies in the Infrastructure Sector	NBFCs registered under RBI
SIDBI (Automatic Route) EXIM Bank (Approval Route)	REITs and INVITs	NBFC-MFI, NPOs engaged in MFI activity
Units in SEZ		Companies engaged in R&D, Training (other than an educational institution)
NBFC-IFC, NBFC-AFC		Companies supporting infra and logistic services
Holding Companies and CIC		Developers of SEZ/NMIZs
HFC, regulated by the NHB		Companies engage in the trade of maintenance, repair, and overhaul, and freight forwarding
Port Trusts		

All in Cost Requirements

Track 1	Track 2	Track 3
The all-in-cost ceiling is given through a uniform ceiling of 450 basis points per annum over the benchmark over six month LIBOR or applicable benchmark for the respective currency	The limit spread over the milestone will be 450 basis points per annum.	The limit spread over the benchmark will be 450 basis points per annum.
Any penal interest for default or breach of the covenant should not be more than 2 percent over and above the contracted rate of interest.		

Individual Limits

Sector	Maximum amount per FY
Companies in the manufacturing and infrastructure sectors, NFC-IFCs, NBFCAFCs, Holding Companies, CICs	USD 750 million
Companies in the Software Development Sector	USD 200 Million or equivalent
Companies in micro-finance activities	USD 100 Million or equivalent
All remaining entities	USD 500 Million or equivalent

Minimum Average Maturity Period - Method

The minimum average maturity for the three tracks is as follows:

Track I:

Medium-term foreign currency denominated ECB with a minimum average maturity of 3/5 years.

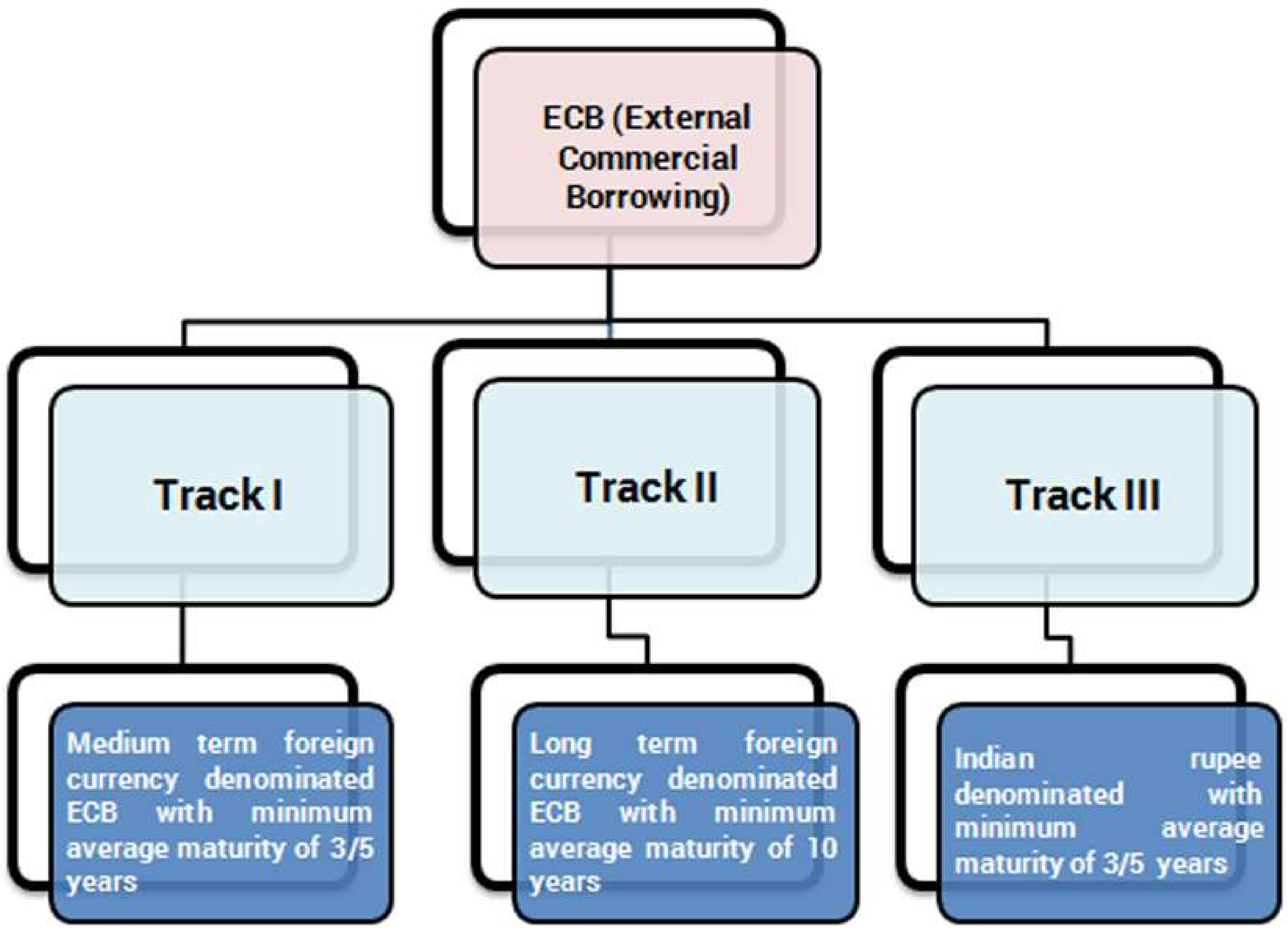
- 3 years for ECB up to USD 50 million or it's equal.
- 5 years for ECB ahead of USD 50 million or it's equivalent.
- 5 years for eligible borrowers under Companies in the infrastructure sector, Non-Banking Financial Companies-Infrastructure Finance Companies(NBFC-IFCs), NBFCs-Asset Finance Companies (NBFC-AFCs), Holding Companies and Core Investment Companies (CICs), irrespective of the amount of borrowing.
- 5 years for Foreign Currency Convertible Bonds (FCCBs)/ Foreign Currency Exchangeable Bonds (FCEBs) regardless of the amount of lending. Moreover, the call and put option, if any, for FCCBs shall not be exercisable earlier than 5 years

Track II:

Long term foreign currency denominated ECB with a minimum average maturity of 10 years.

Track III:

Indian Rupee (INR) denominated ECB with a minimum average maturity of 3/5 years.



End-use prescriptions for ECB

- Investment in the purchase of land or real estate excepting when used for affordable housing Investment in the capital market.
- Equity investment.

Moreover, for Tracks I and III, the subsequent negative end users will also apply excluding when raised from Direct and Indirect equity holders or a Group company. Please note that the loan is for a minimum average maturity of five years:

- Working capital purposes.
- General corporate purposes.
- Repayment of Rupee loans.

Lastly, for all Tracks, the following negative end use will also be relevant:

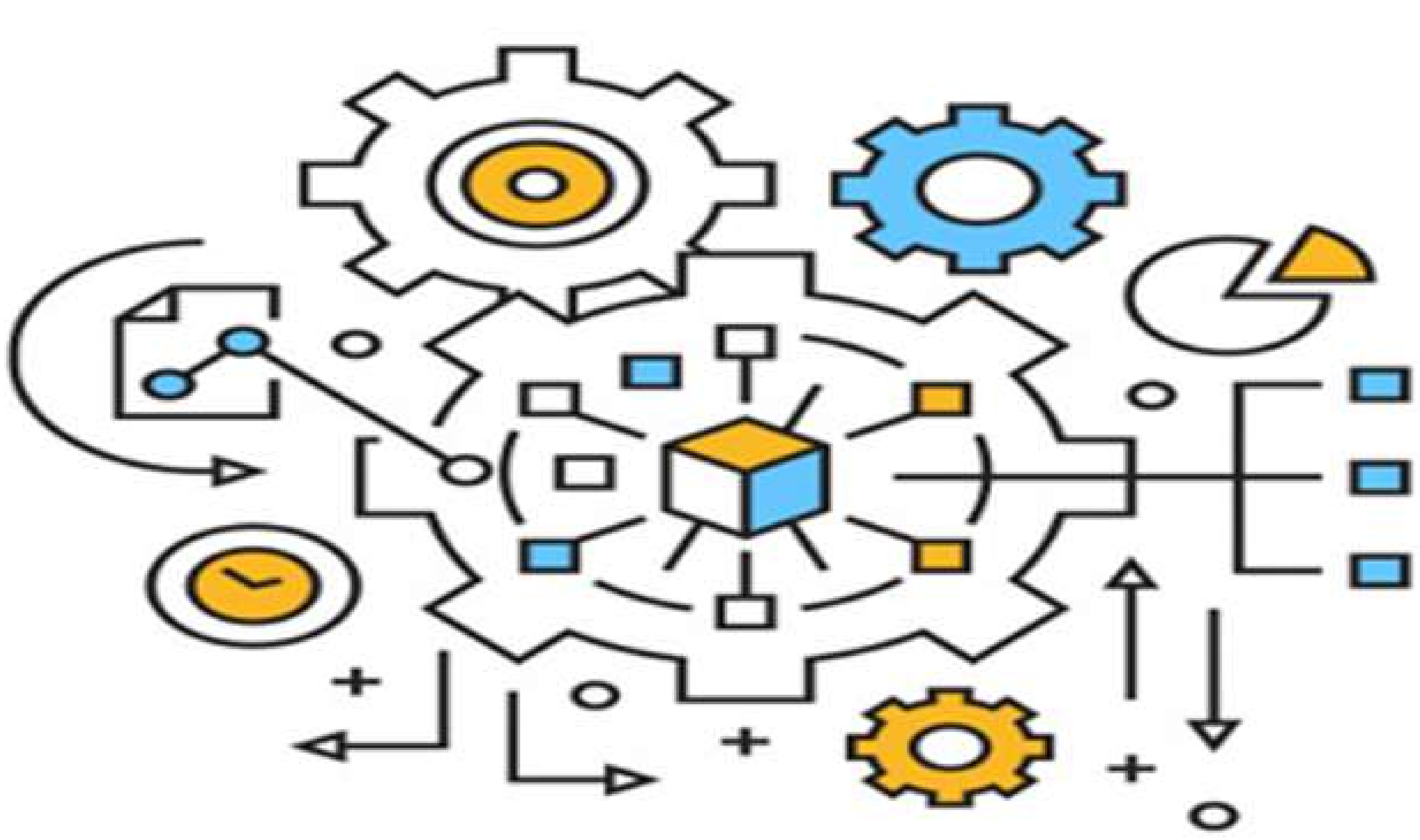
- On-lending to entities for the above activities from (a) to (f).

Conversion of ECB into equity

Conversion of ECB, including those which have been matured but still unpaid, into equity is allowable subject to the following circumstances:

- The activity of the borrowing company is covered under the automatic route for Foreign Direct Investment (FDI) or approval route wherever applicable, for foreign equity participation which has been obtained as per the existing FDI policy;
- The conversion, which should be with the lender's consent and without any additional cost, will not result in the breach of applicable sector cap on the foreign equity holding;
- Applicable pricing guidelines for shares are complied with;
- Reporting requirements under the ECB framework are complied with;
- If the borrower has availed of other credit facilities from the Indian banking system, including overseas branches/subsidiaries, the relevant prudential procedure issued by the Department of Banking Regulation, RBI, including instructions on restructuring are complied with; and
- Approval of other lenders, if any, to the same borrower is available or at least information about conversions is exchanged with other lenders of the borrower.

Procedure for raising ECB



The procedure for raising ECB under approval route requires the borrowers to come up to the RBI with a request in prescribed format Form ECB for examination through their AD Category I bank. Such cases are considered keeping in view the by and large plan, macroeconomic circumstances, and virtues of the specific proposals. ECB proposals acknowledged in the Reserve Bank above the defined threshold limit (refixed from time to time) are placed before the Empowered Committee set up by the Reserve Bank.

The Reserve Bank takes a final decision taking into account the suggestion of the Empowered Committee. Entities desirous of raising ECB under the automatic route may approach an AD Category I bank with their proposal along with the duly filled in Form 83.

Conclusion

Though external commercial borrowings come at fewer costs, it comes with various restriction and procedure that need to be followed. There exist a limit on the amount and maturity of the ECB. There are limitations concerning the end use of the funds also. The companies may use it for growth, but they cannot use it for onward lending, repayment of existing loans, real estate investments, and many such restrictions. ECB is one of the commonly availed sources of cheaper funds by eligible companies. However, the companies need to be careful about the exchange rate risk and brunt on balance sheet debt to use it effectively.

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Thank You!