Relaxation of RBI norms on External Commercial Borrowings

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External Commercial Borrowings

- Reserve Bank of India ("RBI") permits Indian companies to raise loans overseas through the External Commercial Borrowings ("ECB") regulatory framework.
- ECBs are a major source of foreign capital, giving Indian companies access to foreign debt for longer maturity periods at comparatively low interest rates.
- Following are certain restrictions on companies borrowing through the ECB route:
  - Restrictions on amount of loan that can be obtained by a company;
  - Sectoral restrictions on ECB borrowings;
  - End use restrictions on funds obtained;
  - Interest rate ceilings;
  - Restrictions on maturity period.

Types of ECBs

- RBI acts as regulator for ECBs, issues master directions, circulars, and clarifications, as applicable.
- New governing framework for ECBs came into effect from 30 November 2015. Under this, ECBs fall within three buckets or '**tracks**':
  - **Track I**: ECBs denominated in foreign currency with 3/5 year average maturity;
  - **Track II**: ECBs denominated in foreign currency with over 10 years average maturity;
  - **Track III**: ECBs denominated in Indian Rupees (Also known as Masala Bonds).

Relaxations to ECB Policy

- RBI recently released a circular on 27 April 2018 further relaxing the ECB guidelines.
- Seen as a business-friendly move that will give more Indian companies access to cheap foreign capital, as well as rationalise compliance requirements.
- Four major changes brought in by the circular:
  - Rationalisation of all-in-cost ceiling for ECBs;
  - Enhancement of leverage of ECB liability;
  - Expansion of ‘eligible borrowers’ for the purpose of ECBs;
  - Simplification of end-use restrictions for borrowers under ECBs.

Rationalisation of all-in cost ceiling

1

- ECB regulatory regime places restrictions on the charges received by the foreign lender providing loans under ECB, expressed as 'All-in cost'.
- All-in cost includes all costs payable to foreign lender, including rate of interest, other fees, expenses, charges & guarantee fees.
- Does not include commitment fees, pre-payment fees/charges and withholding tax payable in INR.
- Circular has harmonised all-in-cost ceiling across ECB tracks and maturity periods.

- **Earlier all-in ceiling**:

Track I	Track II	Track III
▪ **Minimum average maturity 3 to 5 years**: Limit of 300 bps over LIBOR ▪ **Minimum average maturity of more than 5 years**: Limit of 450 bps over LIBOR	Limit of 500 bps over LIBOR	In line with market conditions

- **Changes brought in by circular**:
  - Uniform all-in cost ceiling for **all ECB Tracks** of **450 basis points** over the **RBI benchmark rate.**
  - RBI Benchmark rate determined as:
    - 6 month USD LIBOR (or applicable benchmark for respective currency) for Track I and Track II ECBs; and
    - Prevailing yield of Government of India securities of corresponding maturity for Track III ECBs.

Enhancing leverage of ECB liability

- ECB regulatory regime places restrictions on loans raised from direct foreign equity holders.
- This is expressed as ‘leverage’, a ratio between the ECB liability and the foreign equity.
- **Earlier leverage restriction**:
  - ECB Liability to Equity ratio was **4:1** for ECB raised from direct foreign equity holder under automatic route.
- **Change brought in by circular**:
  - ECB Liability to Equity ratio limit increased to **7:1** for ECB raised from direct foreign equity holders under automatic route.
  - Hence, borrowing capacity of Indian companies from direct foreign equity holders enhanced.

Expanding ‘eligible borrowers’ for ECBs

- After the circular, pool of borrowers under ECBs expanded to include:
  - Housing finance companies regulated by National Housing Bank, under all ECB tracks;
  - Registered port trusts, under all ECB tracks;
  - Companies engaged in the business of maintenance, repair, overhaul and freight forwarding, only under Track-III ECBs.
- However, housing finance companies & port trusts raising ECBs under Track-I required to:
  - Hedge 100% of their ECB exposure; and
  - Have a board approved risk management policy.

Simplification of end-use restrictions

- ECB regulatory regime places end-use restrictions on funds borrowed by Indian companies via ECB route.
- ECBs can only be undertaken for uses that fall within positive list, or do not find mention in the negative list.
- **Earlier position:**
  - Track I ECBs had a positive end-use list, and a specified category of borrowers.
  - Track II and III ECBs had a negative end-use list.
- **Change brought about in by circular:**
  - Simplified end-use restrictions by prescribing only negative lists for **all tracks of ECBs.**
  - ECBs cannot be undertaken for end-uses specifically mentioned in negative list; no restrictions on end-uses not specifically mentioned in negative list.

- Negative List for all tracks now includes following:
    - investment in real estate or purchase of land, excluding affordable housing and SEZs
    - investment in capital markets; and
    - equity investments in domestic companies.
- For Track I and Track III ECBs, following additional end-use restrictions apply:
    - working capital purposes;
    - general corporate purposes; and
    - repayment of INR loans
- Above restrictions for Track I and Track III ECBs not to apply if loan taken for a minimum average maturity of 5 years, from equity holders or group companies.
- Onward lending to companies for any of the purposes enlisted above also prohibited under all tracks.

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