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India makes a dent in itsdebt

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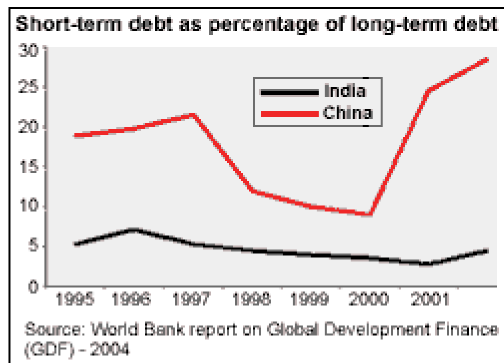
Recently, international rating agency Standard&Poor's (S&P) upped India's "BB" long-term foreign currency rating outlook to "positive" from stable, and the outlook on the "BB-plus" long-term local currency rating was lifted from negative to stable.

According to a statement issued by S&P, these revisions reflect India's improving external liquidity and better prospects for the government's debt burden to stabilize. In addition, they felt that India's robust foreign exchange reserves, which exceed its short-term debt by 2,000%, mitigate the risk of volatility in external confidence.

Indeed, ever since the 1991 economic crisis, which among other reasons was caused by a high concentration of short-term external debt in the total external debt basket, New Delhi has been constantly working to reduce the extent of this short-term debt - so much so that now the short-term external debt to total external debt is around 5%.

In this parameter, India's record is much better than that of China's.

The graph shows, ever since 1995, India maintained strict control over its short-



term external loans, which have been hovering in and about 5% of total external borrowing. But in the case of China, it has mostly been around 20% (with the exception of a few years), going up to as high as 28.5% in 2002. Not only this, but figures made available for developing countries in this report clearly show that India is in a much better position than many other countries, such as Indonesia (short-term debt accounting for 17.62% of long-term debt), Malaysia (17.28%), Thailand (20.10%), Czech Republic (40.91%), Russia (11.05%), Argentina (11.19%), Brazil (10.27%) etc. Collectively, the figure stood at 13.96% for all developing countries.

Overall, India's external debt to gross domestic product (GDP) ratio has been declining over the past decade. From 28.7% in 1990-91, the ratio has come down to 20.2% in 2002-03 (after reaching as much as 38.7% in 1991-92), according to the Finance Ministry.

During 1991-92, 1992-93, 1993-94 and 1994-95, the ratio stayed above the 30% mark. It was only in 1995-96 that the external debt to GDP ratio once again came down to 27%. From then on, the ratio has been consistently declining to reach 20% levels in 2002-03.

External debt is broadly classified into eight categories - multilateral, bilateral, International Monetary Fund (IMF), export credit, commercial borrowings, deposits by non-resident Indians (NRIs), rupee debt and short-term debt. Of these, multilateral, bilateral and IMF comprise loans either from governments of other countries or international organizations.

Export credit and commercial borrowings include bonds and foreign currency convertible bonds issued by Indian corporates. The rupee debts include repayment on account of civilian and non-civilian debt from the rupee payment area.

From December 2002 to December 2003, there was a decline in four of these categories - multilateral, export credit, commercial borrowings and rupee debt.

Borrowings from the IMF stayed put at zero, while bilateral, NRI deposits and short-term debts have registered a fall. In fact, India has actually resorted to pre-paying high cost external debts of late on the back of rising foreign exchange (forex) reserves. So much so that prepayment of foreign loans in the last year reduced the debt to multilateral agencies like the World Bank and the Asian Development Bank by 6.2% to $30.56 billion in 2003. More importantly, India now also has the status of "donor country".

Total external debt, as a result, grew little from December 2002 to December 2003, by approximately $6.8 billion. This is only a growth of 6.5% in total external debt from $105 billion to $112 billion over the period.

The primary factor leading to a rise in the external debt is the large inflows of NRI deposits in 2003, accounting for a total of $8 billion, which is higher than the total debt. The total debt amount has been tempered by a decline in multilateral and commercial borrowings.

The reason for the decline of the country's external debt to GDP ratio and the growth rate of external debt is that the rate of accumulation of external debt came down in the last decade as policy focus shifted in favor of non-debt creating flows such as foreign direct investment (FDI) and portfolio investments.

As a result, India transformed from a moderately indebted country to a less indebted country with a fall in debt-GDP ratio, a survey conducted by the United Nation's

Economic and Social Commission for Asia and Pacific (ESCAP) concluded. This result was arrived at by citing a World Bank classification.

According to ESCAP, despite the continuing weakness in the global economy, FDI flows into India grew by 2.4% to $4.0 billion in 2002, reflecting the ongoing improvement in infrastructure, further liberalization of foreign investment policies and the removal of economic sanctions on India by the United States. India's forex position also strengthened as a result of higher FDI and an improvement in the current account balance. So much so that as of the end of December 2003, India's forex reserves crossed the landmark $100 billion mark. Apart from the information technology boom, the ESCAP survey said "increase in reserves reflected higher remittances, quicker repatriation of export proceeds and non-debted inflows of capital".

As for 2004, while India's short-term debt to total forex reserves stood at only 6.87% in 2002, the same for China was 16.72%, Indonesia was 67.15%, while in the case of Argentina it was as high as 142.31%.

What is also heartening is that the debt-service ratio, measured in terms of total debt service payments to current receipts, also declined to 15.8% till March 2003 from 25.9% in 1994-95. The share of government debt in the total debt outstanding declined from 60.1% at March end 1995 to 39.2% in December end 2003. In fact, surging forex reserves for India now means that by the end of December 2003 foreign currency assets provided about 87% cover for the total external debt outstanding.

With India's good economic prospects, what with growth in GDP likely to push past 6% over the medium term, it is quite possible that India's rating could undergo further upward revisions.

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