India Q3 FY2021 BoP: Current account reverts to deficit; capital account shines on strong investment inflows

Apr 6, 2021

Nihal Kumar

nihal.kumar@icicibank.com

- **Spurt in the trade deficit weighed on the current account, capital account posted healthy surplus on account of higher foreign investment**
- **FY2021 is expected to end with a robust current account surplus of ~0.8-1.0% of GDP, with an accompanying healthy BoP surplus of USD 85-90 bn**
- **Going ahead, higher oil prices coupled with imports catching up to pre-COVID levels will flip the current account back to a modest deficit in FY2022, while the accompanying BoP surplus will likely be sharply lower than that seen in FY2021**

Current account back to deficit, both imports and exports recovered to pre-pandemic levels; transfers rose significantly

- **After registering a surplus for three consecutive quarters, the current account posted a marginal deficit of** USD 1.7 bn (0.2% of GDP) in Q3 FY2021 versus a surplus of USD 15.5 bn (2.4% of GDP) in Q2 FY2021. Recovery in merchandise imports over the quarter widened the trade deficit. In contrast to goods trade, India's net services exports remained resilient and the surplus on the invisibles front rose to USD 32.8 bn from USD 29.9 bn in the previous quarter.
- **Exports rose slightly** on a quarterly basis but remained subdued in annual terms in Q3 as the US and several countries in Europe (India's major export destinations) were grappling with the second wave of COVID-19. On the other hand, **import contraction narrowed further in Q3 as industrial imports rose significantly aided by a rebound in domestic economic activities and festive buying, indicating gradual industrial momentum.** In addition, gold imports remained elevated amid festive and wedding demand. As a result, the trade deficit widened to USD 34.5 bn in Q3 from USD 14.8 bn in Q2 FY2021.
- **Net services receipts increased** both on sequential basis and on an annual basis. The receipt from travel, transportation and financial services fell slightly when compared to Q2 FY2021, whereas receipts from telecommunication and software services increased substantially during Q3.
- **Transfer receipts remained buoyant as private transfers ballooned on higher worker remittances.** The foremost factors driving the transfers included prospects of economic recovery abroad, gradual pickup in employment, relatively higher oil prices as compared to earlier in 2020, and the Dollar's depreciation bias.
- **Income related outflows rose sharply on an annual basis** in Q3 due to higher outflow of investment income.

Capital account surplus more than doubled aided by strong foreign investment

- **Overall capital account surplus (including errors and omission) rose sharply in Q3 FY2021** to USD 34.2 bn (more than double the previous quarter) as net FDI recorded robust inflows and FPI inflows surged leveraging better return offered in Emerging Markets amid abundant liquidity and ultra-easy monetary policy stance globally.

- **Robust foreign investment flows led to higher capital account surplus.** As noted by UNCTAD (2021), India's inward foreign direct investment (FDI) bucked the global trend and grew positively in 2020, boosted by investments in the digital sector. Over Q3, FDI inflows moderated to USD 17 bn as compared to net inflow of USD 24.6 bn in Q2, but inflows remained significantly higher than past trends. On the other hand, India's optimistic growth outlook and ample global liquidity also induced net foreign portfolio investment of USD 21.2 bn in Q3 (thrice the level in Q2). FPI inflows could be challenged to an extent going ahead, considering rising US yields. However, the overall outlook for foreign investment inflows remains positive.
- **External borrowings improved on a sequential basis.** However, ECB repayments still exceeded fresh disbursements over Q3, leading to a net outflow on that account. Short term loans to India increased somewhat, especially for the category of suppliers' credit upto 180 days. Non-residents made higher accretion to deposits with banks in India, and consequently, **banking capital pinned a lesser deficit as compared to Q2 FY2021.**

Overall, given the huge capital account surplus and the marginal deficit in the current account, the balance of payments clocked a surplus of USD 32.5 bn in Q3 FY2021, slightly higher than previous quarter.

External sector looks comfortable this year

We expect FY2021 to end with a robust surplus of 0.8-1.0% of GDP. Going ahead, traction in industrial imports will keep the trade deficit higher pushing the current account balance to negative territory. However, concerns over the second wave of Coronavirus domestically may take a toll on industrial demand in the near term. A normal monsoon and sturdy rural demand could boost the demand for gold over FY2022. Higher oil prices need to be watched as a possible headwind.

Exports may benefit incrementally as global trade picks up steam, and recovery seen in major trading partners is trade positive. As Indian exports have a higher income elasticity (effect of global demand) as compared to price elasticity (effect of a weaker Rupee), global trade recovery will drive export momentum further. Progress on US-India mini trade deal likely to assist exports going forward. In the medium term, the trigger could come from the self-sufficiency drive via the promising PLI schemes for the different sectors, which aims at reducing substitutable imports and enhancing exports.

Flows on the FDI account should remain robust over FY2022, given bright growth prospects in India. Increase in FDI limit in insurance sector is also noteworthy and progressive. While FPI inflows may moderate as compared to FY2021, the momentum is likely to remain positive, given the search for yields and tailwinds from aspects like inclusion of India in the Global Bond Indices, as and when it happens. **Overall BoP surplus is likely to moderate to USD 30 bn in FY2022 from USD 85-90 bn in FY2021.**

BOP details

(USD bn)	Q1 FY2021	Q2 FY2021	Q3 FY2021
Merchandise	-10.9	-14.8	-34.5
- Exports	52.3	75.6	77.2
- Imports	63.2	90.4	111.8
Invisibles	29.8	29.9	32.8
- Services	20.5	20.9	23.6
- Transfers	17.0	18.4	19.3
- Income	-7.6	-9.4	-10.1
Current Account	19.0	15.1	-1.7
Foreign Investment	-0.2	31.6	38.2
- FDI	-0.8	24.6	17.0
- Portfolio Investment	0.6	7.0	21.2
Loans	2.7	-3.8	0.2
Banking Capital	2.2	-11.3	-7.6
Other capital	-3.5	-0.4	3.5
Capital Account*	0.8	16.5	34.2
Overall BoP	19.8	31.6	32.5

(includes errors and omissions)*

Source: Reserve Bank of India, ICICI Bank Research

ICICI Bank: ICICI Bank Towers, Bandra Kurla Complex, Mumbai- 400 051. Phone: (+91-22) 2653-1414

Economic Research Group

Economics Research

Shivom Chakravarti	Senior Economist—Global Markets	(+91-22) 4008-1414 (ext 6273)	shivom.chakravarti@icicibank.com
Anushri Bansal	Senior Economist—Domestic Markets	(+91-22) 4008-1414 (ext 6220)	anushri.bansal@icicibank.com
Sumedha Dasgupta	Economist	(+91-22) 2653-1414 (ext. 7243)	sumedha.dasgupta@icicibank.com
Aniket Gaikwad	Research Analyst	(+91-22) 2653-1414 (ext. 8161)	aniket.gaikwad@icicibank.com
Asha Sasikumar	Research Analyst	(+91-22) 2653-1414 (ext. 7249)	asha.sasikumar@icicibank.com
Kaushal Aryan	Research Analyst	(+91-22) 2653-1414 (ext. 7249)	kaushalkumar.aryan@icicibank.com
Jyoti Sharma	Research Analyst	(+91-22) 2653-1414 (ext. 7249)	sharma.jyoti@icicibank.com
Tanisha Ladha	Research Analyst	(+91-22) 2653-1414 (ext. 7309)	tanisha.ladha@icicibank.com
Nihal Kumar	Research Analyst	(+91-22) 2653-1414 (ext. 7309)	nihal.kumar@icicibank.com

Treasury Desks

Treasury Sales	(+91-22) 6188-5000	Currency Desk	(+91-22) 2652-3228-33
Gsec Desk	(+91-22) 2653-1001-05	FX Derivatives	(+91-22) 2653-8941/43
Interest Rate Derivatives	(+91-22) 2653-1011-15	Commodities Desk	(+91-22) 2653-1037-42
Corporate Bonds	(+91-22) 2653-7242		

recipient for any purpose without ICICI Bank's prior written consent. If the reader of this message is not the intended recipient and has received this transmission in error, please immediately notify ICICI Bank, Economic Research Group, E-mail: erg@icicibank.com or by telephone at +91-22-2653-7233 and delete this message from your system.

Please also note that ICICI Bank (including its branches, and affiliates) is unable to exercise control or ensure or guarantee the integrity of/over the contents of the information contained in e-mail transmissions and / or attachments and that any views expressed in this e-mail and / or attachments are not endorsed by/binding on ICICI Bank. Before opening any attachments please check them for viruses and defects and please note that ICICI Bank accepts no liability or responsibility for any damage caused by any virus that may be transmitted by this email and/ or attachments thereto.

DISCLAIMER FOR DUBAI INTERNATIONAL FINANCIAL CENTRE ("DIFC") CLIENTS:

This marketing material is distributed by ICICI Bank Limited., Dubai International Financial Centre (DIFC) Branch, a category 1 Authorized Firm and regulated by the Dubai Financial Services Authority. This marketing material is intended to be issued, distributed and/or offered to a limited number of investors who qualify as 'Professional Clients' pursuant to Rule 2.3.3 of the DFSA Conduct of Business Rulebook, or where applicable a Market Counterparty only, and should not be referred to or relied upon by Retail Clients and must not be relied upon by any person other than the original recipients and/or reproduced or used for any other purpose.

DISCLOSURE FOR RESIDENTS IN THE UNITED ARAB EMIRATES ("UAE"):

Investors should note that any products mentioned in this document, any offering material related thereto and any interests therein have not been approved or licensed by the UAE Central Bank or by any other relevant licensing authority in the UAE, and they do not constitute a public offer of products in the UAE in accordance with the Commercial Companies Law, Federal Law No. 8 of 1984 (as amended) or otherwise.

DISCLOSURE FOR RESIDENTS IN HONGKONG

*This document has been issued by ICICI Bank Limited in the conduct of its Hong Kong regulated business (i.e. type 1 license) for the information of its institutional and professional investor (as defined by Securities and Future Ordinance (Chapter 571 of Laws of Hong Kong) (the "**SFO**")) customers; it is not intended for and should not be distributed to retail or individual investors in Hong Kong. Any person who is not a relevant person should not act or rely on this document or any of its contents. This document has not been reviewed, authorized or approved by any regulatory authority.*

ICICI Bank and/or its affiliates are full service financial institutions engaged in various activities which may include securities trading, commercial and investment banking, financial advice, investment management, principal investment, hedging, financing and brokerage activities. As a result, you should be aware that a conflict of interest may exist. In accordance with the regulatory requirements and its own conflicts of interest policies, ICICI Bank has in place arrangements, internal policies and procedures to manage conflicts of interest that arise between itself and its clients and between its different clients. Where it does not consider that the arrangements under its conflicts of interest policies are sufficient to manage a particular conflict, it will inform you of the nature of the conflict so that you can decide how to proceed.

DISCLOSURE FOR RESIDENTS IN SINGAPORE

*ICICI Bank Limited, India ("**ICICI India**") is incorporated under the laws of India and is regulated by the Reserve Bank of India. ICICI Bank Limited, Singapore branch ("**ICICI**") is regulated by the Monetary Authority of Singapore.*

As mentioned, ICICI India is regulated by the Reserve Bank of India. Hence, in relation to your dealing with ICICI India, you understand that your interest will be subject to protection of local laws and regulations in India, which may offer different or diminished protection than available under Singapore laws and regulations. You also understand that the Monetary Authority of Singapore will be unable to compel the enforcement of the rules of the local regulators.

For more detailed disclaimer, please visit https://www.icicibank.com/disclaimer/disclaimertnc.html