Macro Review
July 01, 2020 | Vol. 2, Issue. 23

Current account balance turns surplus in Q4FY20; FY20 CAD at -0.9%

India's current account balance contracted sharply for the third quarter in a row to turn into surplus of US$0.6bn or 0.1% of GDP in Q4FY20—the first in 13 years. This was primarily led by a sharp drop in non-oil imports (weak demand), strong growth in remittances, steady software earnings and lower overseas investment income payments. On the capital account, huge foreign portfolio outflows amid a strengthened risk-off environment in the wake of COVID-19 outbreak were largely offset by a higher FDI (foreign direct investment) and ECB (external commercial borrowings) inflows, resulting in a Balance of Payments (BoP) surplus of US$18.8bn in Q4FY20.

The Current Account Deficit (CAD) in FY20 moderated to three-year lows of 0.9% of GDP vs. 2.1% in FY19 due to a significant contraction in trade deficit and steady growth in services receipts and remittances. Record-high net FDI inflows (+40% YoY) and strong growth in ECB inflows more than compensated for lower foreign portfolio inflows and NRI deposits. Consequently, BoP surplus expanded to five-year high of US$59.5bn in FY20.

Exports are likely to fare better than imports as an aggressive policy response globally should help revive global demand faster. Moreover, a relatively more stringent and prolonged lockdown in India and its second-order impact in the form of job losses and decline in disposable incomes may keep discretionary demand weak for an extended period. This is expected to result in a significant contraction in trade deficit, aided by lower crude oil prices. Consequently, we expect a current account surplus in FY21 for the first time in 17 years (on an annual basis), partly offset by lower remittances. This would translate into a huge BoP surplus for yet another year, supported by strong FDI inflows, resulting in continued accretion to FX reserves (US$506bn as of June 19th, +US$48bn YTD).

- Weak domestic demand keeps trade deficit contained: India's trade deficit contracted to US$35bn in Q4FY20 from US$36bn in the previous quarter. This was largely led by a sharp drop in non-oil imports, reflecting weak domestic demand, even as exports also contracted in Q4FY20 as COVID-19 outbreak led to large-scale disruptions in global supply chains and demand, thereby resulting in delays and cancellations of orders. Oil imports, however, inched up, reflecting higher crude oil prices during Dec-Feb'20. Trade deficit in FY20 contracted by a sharp 12.6% YoY to US$158bn led by a steeper fall in imports as compared to exports.

Current account turned into surplus in Q4FY20 for the first time in 13 years.

FY20 CAD contracts from 2.1% of GDP in FY19 to 0.9% in FY20.

- Current account turns surplus in Q4FY20: Invisibles grew by a strong 16.5% YoY in Q4FY20 led by a steady growth in services receipts (+6.3% YoY), higher remittances (+13.9% YoY) and lower overseas investment income payments. This, along with lower trade deficit, led to current account turning surplus in Q4FY20 for the first time in 13 years to US$0.6bn or 0.1% of GDP. FY20 CAD also contracted to three-year lows of US$24.7bn or 0.9% of GDP from 2.1% in FY19 due to a huge contraction in trade deficit and steady growth in services receipts and remittances.
- Strong FDI/ECB inflows compensate for FPI outflows, translating into strong BoP surplus: On the capital account, substantial outflows by foreign portfolio investors (FPIs) in Q4FY20 amid a strengthened risk-off environment in the wake of COVID-19 outbreak were largely offset by a sharp rise in FDI and ECB inflows, resulting in a Balance of Payments (BoP) surplus of US$18.8bn. In FY20, BoP surplus expanded to five-year high of US$59.5bn, thanks to record-high net FDI inflows (US$43bn; +40%) and strong growth in ECB inflows (+120%), more than compensating for lower foreign portfolio inflows and NRI deposits.

Strong FDI/ECB inflows compensated for huge FPI outflows, translating into a BoP surplus of US$19bn/ US$59.5 in Q4FY20/FY20.

- Current account expected to remain in surplus in FY21: Exports are likely to fare better than imports as an aggressive policy response globally should help revive global demand faster. Moreover, a relatively more stringent and prolonged lockdown in India and its second-order impact in the form of job losses and decline in disposable incomes may keep discretionary demand weak for an extended period. This, along with lower crude oil prices, is expected to result in a further

CAD is expected to remain in surplus in FY21 due to further contraction in trade deficit.

contraction in trade deficit. Consequently, we expect a current account surplus in FY21 for the first time in 17 years (on an annual basis), partly offset by lower remittances from the Gulf nations (account for ~50% of total remittances) in the wake of a sharp drop in crude oil prices and muted software earnings amid weak global demand. This would translate into a huge BoP surplus for yet another year, supported by strong FDI inflows, resulting in continued accretion to FX reserves (US$506bn as of June 19th, +US$48bn YTD).

Figure 1: Balance of Payments – Quarterly account

US$ bn	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20
Current account	-15.8	-19.1	-17.8	-4.6	-15.0	-7.6	-2.6	0.6
CAD/GDP (%)	*-2.3*	*-2.9*	*-2.7*	*-0.7*	*-2.1*	*-1.1*	*-0.4*	*0.1*
Trade balance	-45.8	-50.0	-49.3	-35.2	-46.8	-39.7	-36.0	-35.0
Merchandise exports	83.4	83.4	83.1	87.4	82.7	80.0	81.2	76.5
Merchandise imports	129.1	133.4	132.4	122.6	129.5	119.6	117.3	111.6
Oil imports	34.8	35.3	38.5	32.4	35.4	29.9	31.5	33.8
Non-oil imports	94.3	98.1	93.9	90.2	94.1	89.7	85.8	77.8
Invisibles	29.9	31.0	31.5	30.6	31.8	32.1	33.4	35.6
Net services	18.7	20.3	21.7	21.3	20.1	20.9	21.9	22.0
Software earnings	18.6	19.3	19.9	19.9	21.0	21.1	21.5	21.1
Transfers	17.0	19.3	17.4	16.2	18.0	20.0	18.9	18.4
Other invisibles	-5.8	-8.6	-7.6	-6.9	-6.3	-8.8	-7.4	-4.8
Capital account	4.8	16.6	13.8	19.2	28.6	13.6	23.6	17.4
Foreign investments	1.4	7.6	5.2	15.9	18.8	9.8	17.6	-1.8
FDI	9.6	7.4	7.3	6.4	14.0	7.3	9.7	12.0
FII	-8.1	0.2	-2.1	9.4	4.8	2.5	7.8	-13.7
Loans	-4.3	6.9	2.9	10.3	9.6	3.1	3.1	9.9
ECBs	-1.3	2.2	2.0	7.5	6.1	3.3	3.2	10.3
Banking capital	10.1	0.5	4.9	-8.1	3.4	-1.8	-2.3	-4.6
NRI deposits	3.5	3.3	0.1	3.4	2.8	2.3	0.8	2.8
Others	-2.4	1.5	0.7	1.2	-3.2	2.5	5.2	13.8
Errors & Omissions	-0.3	0.6	-0.3	-0.4	0.4	-0.9	0.6	0.9
Overall balance (BoP)	-11.3	-1.9	-4.3	14.2	14.0	5.1	21.6	18.8

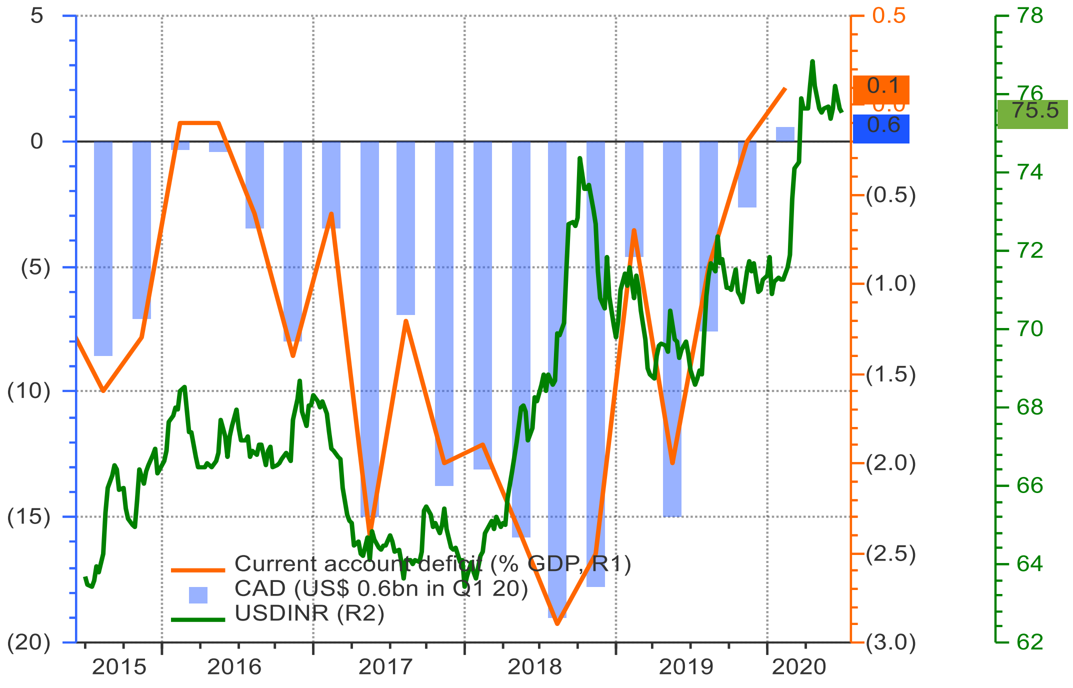
Source: RBI, CMIE Economic Outlook, NSE

Figure 2: Balance of Payments – Annual account

US$ bn	FY16	FY17	FY18	FY19	FY20
Current account	-22.2	-14.4	-48.7	-57.3	-24.7
CAD/GDP (%)	*-1.1*	*-0.6*	*-1.8*	*-2.1*	*-0.9*
Trade balance	-130.1	-112.4	-160.0	-180.3	-157.5
Merchandise exports	266.4	280.1	309.0	337.2	320.4
Merchandise imports	396.4	392.6	469.0	517.5	477.9
Oil imports	82.6	86.9	108.7	141.1	130.5
Non-oil imports	313.9	305.6	360.3	376.4	347.4
Invisibles	107.9	98.0	111.3	123.0	132.8
Net services	69.7	68.3	77.6	81.9	84.9
Software earnings	71.5	70.8	72.2	77.7	84.6
Transfers	62.6	56.0	62.4	69.9	75.2
Other invisibles	-24.4	-26.3	-28.7	-28.9	-27.3
Capital account	41.1	36.4	91.4	54.4	83.2
Foreign investments	31.9	43.2	52.4	30.1	44.4
FDI	36.0	35.6	30.3	30.7	43.0
FII	-4.1	7.6	22.1	-0.6	1.4
Loans	-4.6	2.4	16.7	15.9	25.7
ECBs	-4.5	-6.1	-0.2	10.4	23.0
Banking capital	10.6	-16.6	16.2	7.4	-5.3
NRI deposits	16.1	-12.4	9.7	10.4	8.6
Others	3.2	7.5	6.1	1.0	18.4
Errors & Omissions	-1.1	-0.5	0.9	-0.5	1.0
Overall balance (BoP)	17.9	21.6	43.6	-3.3	59.5

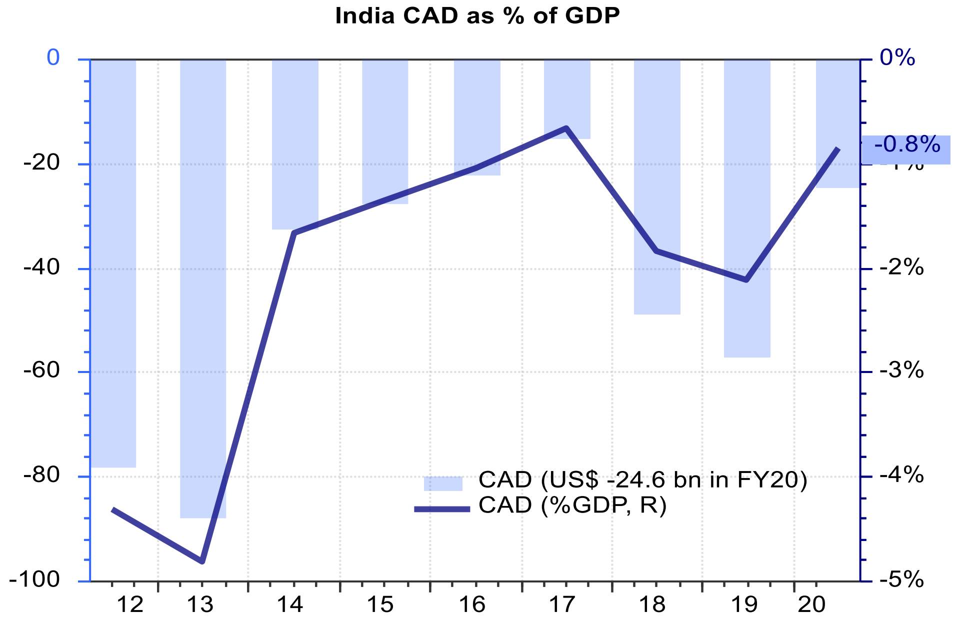
Source: RBI, CMIE Economic Outlook, NSE

Figure 3: Quarterly current account balance turns into surplus in Q4FY20**...**



Source: Refinitiv Datastream, NSE

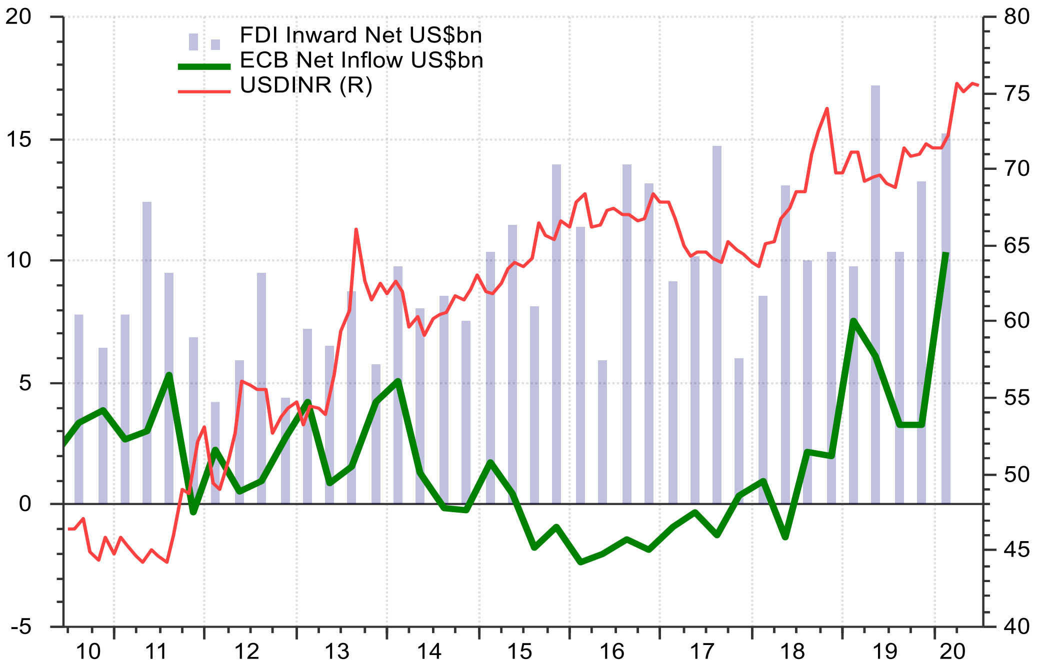
Figure 4: **...and** contracts to three-year low of 0.9% of GDP in FY20



Source: Refinitiv Datastream, NSE

Figure 5: Foreign direct investments reached record high in FY20; ECB inflows rose sharply…

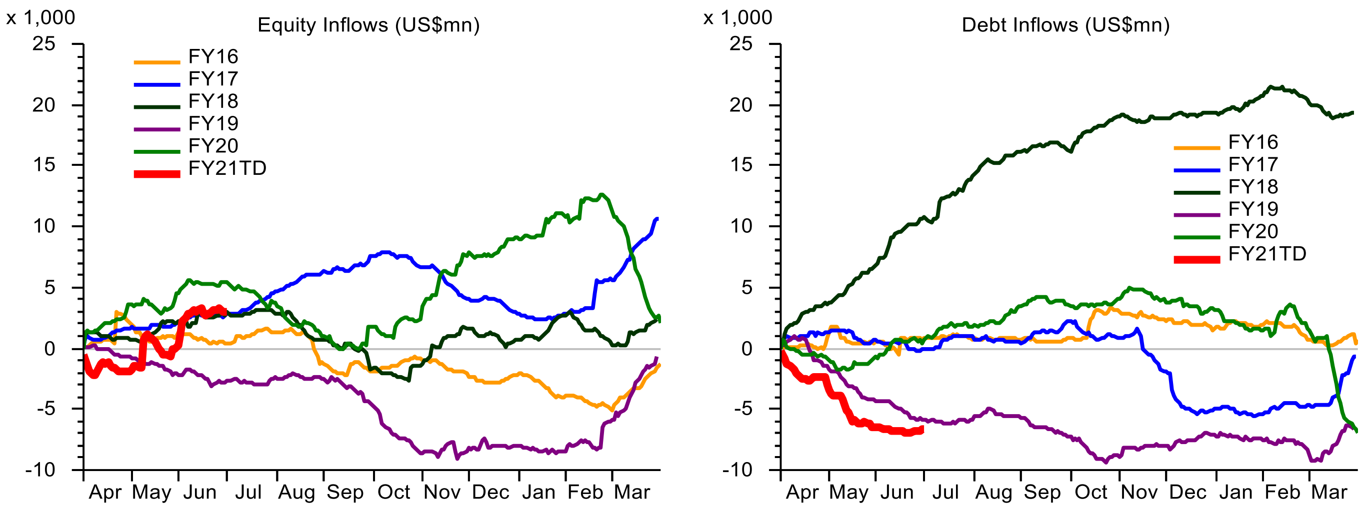
Net FDI and ECB inflows into India



Source: Refinitiv Datastream, NSE

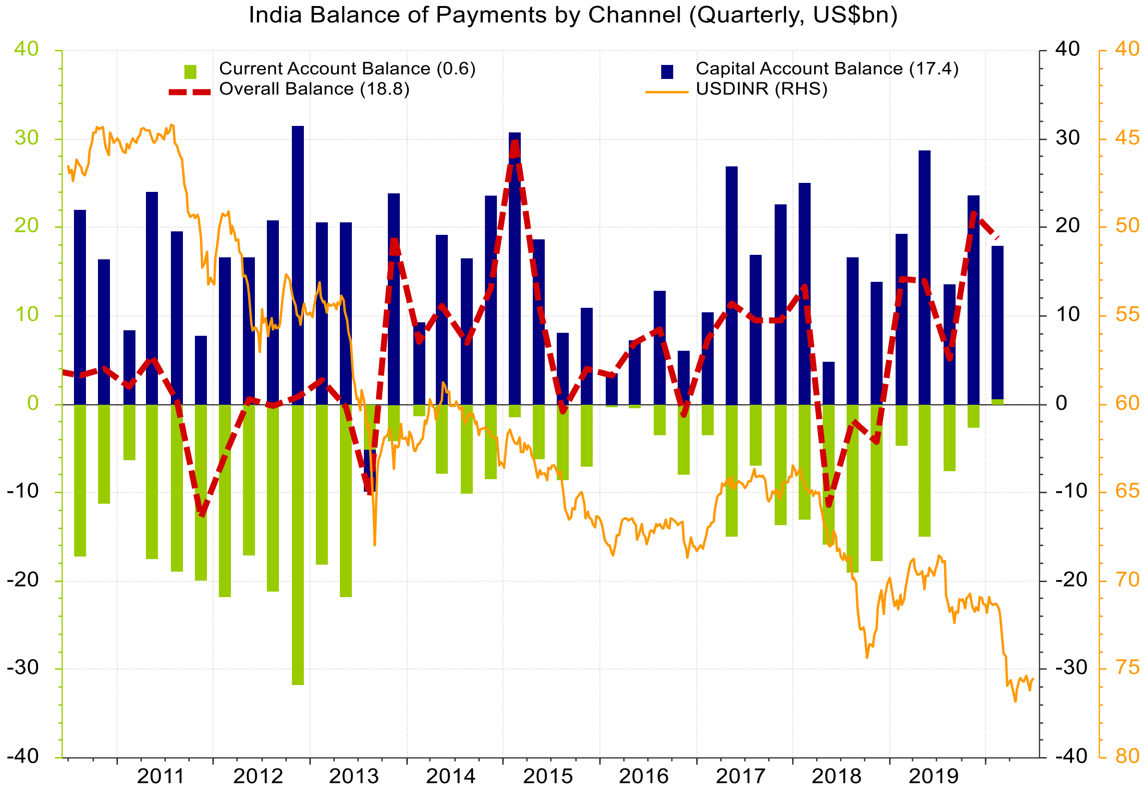
Figure 6: …Compensating for huge foreign capital outflows from equity as well as debt markets

Cumulative FII net flows over last five years (FY)



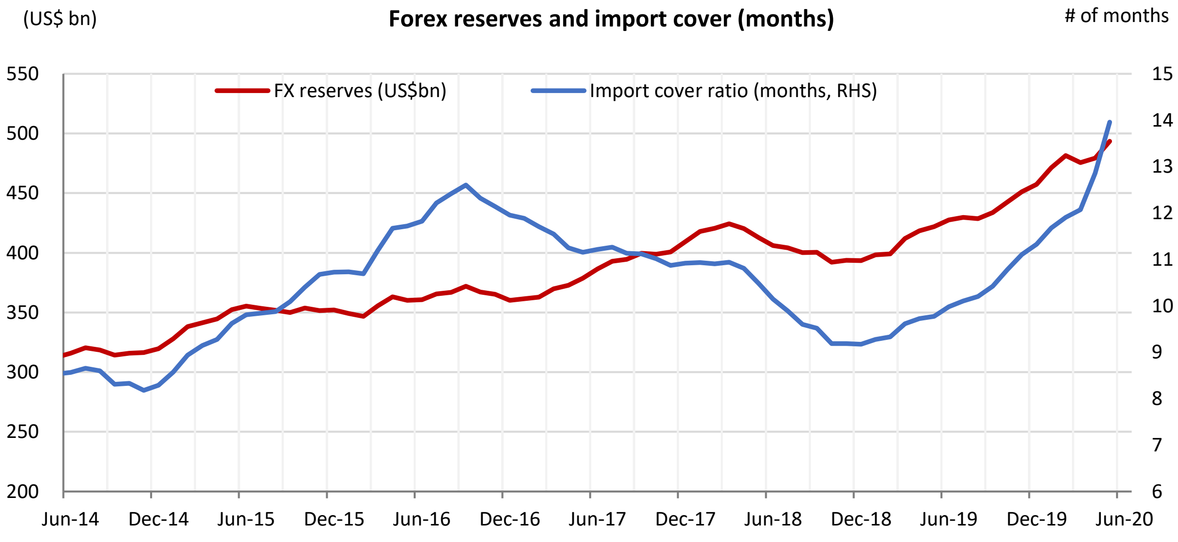
Source: Refinitiv Datastream, NSE

Figure 7: ...resulting in a huge BoP surplus in Q4FY20/FY20



Source: Refinitiv Datastream, NSE

Figure 8: Forex reserves are all all-time high levels, leading to a sharp rise in import cover



Source: Refinitiv Datastream, NSE

Economic Policy & Research

Tirthankar Patnaik, PhD	tpatnaik@nse.co.in	+91-22-26598149
Prerna Singhvi, CFA	psinghvi@nse.co.in	+91-22-26598316
Ashiana Salian	asalian@nse.co.in	+91-22-26598163
Runu Bhakta, PhD	rbhakta@nse.co.in	+91-22-26598163