KHAITAN &CO
Advocates since 1911

UPDATE

ERGO

Analysing developments impacting business

RBI RELAXES THE 20% CONCENTRATION LIMIT FOR FPIs TO INVEST IN THE INDIAN DEBT MARKET

27 February 2019

BACKGROUND

The Reserve Bank of India (RBI) through its circular dated 15 February 2019 (RBI Circular) relaxed one of the restrictions imposed on foreign portfolio investors (FPIs) while investing in the Indian debt market.

On 15 June 2018, the RBI had introduced certain conditions for FPIs looking to invest through the bond route in India (2018 Circular). Although under the 2018 Circular, the RBI had relaxed the minimum maturity period requirements for FPIs (reducing the period from 3 years to 1 year), it had also imposed single/group investor-wise limits in corporate bonds. As such, after the 2018 Circular came into effect, FPIs were (i) restricted from having an exposure of more than 20% of its corporate bond portfolio in a single corporate (including exposure to related entities); and (ii) required to ensure that investment by any FPI (including related FPIs), shall not exceed 50% of any issue of a corporate bond.

Although these restrictions were introduced in an attempt to incentivise FPIs to maintain a diverse portfolio of assets in the Indian debt market, the RBI in its *Statement on Developmental and Regulatory Policies,* stated that upon analysing market feedback, it has observed that the restriction in fact resulted in discouraging FPIs from investing in India. Therefore, in order to eliminate this roadblock and in an effort to attract long-term investors, the RBI, through the circular on 15 February 2019 has withdrawn the restriction that required FPIs to ensure that their corporate bond portfolio exposure in a single corporate entity (including related parties) does not exceed 20% (20% Restriction), thereby encouraging a wider spectrum of FPIs to access the Indian market. While the 20% Restriction has been done away with, FPIs are still required to ensure that investment by any FPI (including related FPIs), shall not exceed 50% of any issue of a corporate bond.

COMMENT

The RBI Circular comes at the wake of a slew of measures undertaken in the past couple of weeks to enhance foreign investment in the Indian debt market, such as opening up of the External Commercial Borrowing ("ECB") regime in India to a wider list of borrowers and investors/creditors. Similarly, with the proposed modifications to the FPI regime pursuant to the RBI Circular, FPIs would have complete freedom to invest in the debt instruments issued by any entity(ies) of their choice upto the extent they deem commercially viable without any impediment whatsoever on the quantum of their investment in these entities. Such flexibility offered to FPIs goes a long way towards increasing the investment of FPIs in the debt market of India. However, although the 20% Restriction has been done away with, the condition that a FPI entity (including through related FPI entities) can only invest upto 50% of the issue size of NCDs by a corporate still remains and the transactions would have to be structured appropriately so that these conditions can be complied with.

With these liberalisations, it is apparent that the objective is to increase the inflow of foreign debt investment into India. Apart from implementing liberalisations in the ECB and the FPI regime, in RBI's discussion paper (dated 5 October 2018), an alternative route for the FPIs with a long-term view, to enter the Indian debt market have been proposed. A separate channel, called the 'Voluntary Retention Route' (VRR), is being considered which would enable FPIs to invest in India through the debt route, free from the regulatory prescriptions applicable to FPI investments currently. This route is aimed at attracting long term investors committed to retain a required minimum percentage of their investments in India for a period of their choice and in line with their investment philosophy.

- *Manisha Shroff (Partner), Ahana Sinha (Principal Associate) and Ashwij Ramaiah (Associate)*

For any queries please contact: editors@khaitanco.com

Mumbai
One Indiabulls Centre, 13th Floor
Tower 1 841, Senapati Bapat Marg
Mumbai 400 013, India

T: +91 22 6636 5000
E: mumbai@khaitanco.com

New Delhi
Ashoka Estate, 12th Floor
24 Barakhamba Road
New Delhi 110 001, India

T: +91 11 4151 5454
E: delhi@khaitanco.com

Bengaluru
Simal, 2nd Floor
7/1, Ulsoor Road
Bengaluru 560 042, India

T: +91 80 4339 7000
E: bengaluru@khaitanco.com

Kolkata
Emerald House
1 B Old Post Office Street
Kolkata 700 001, India

T: +91 33 2248 7000
E: kolkata@khaitanco.com