Harun R Khan: Indian foreign exchange market – recent developments and the road ahead

Inaugural address by Mr Harun R Khan, Deputy Governor of the Reserve Bank of India, at the 25th Annual Forex Assembly, organized by the Forex Association of India (FAI), Gurgaon, 4 October 2014.

* * *

Accompanying box can be found at the end of the speech.

The speaker acknowledges contributions of Shri Sudarsana Sahoo, Shri Anand Prakash & Shri Surajit Bose of the Reserve Bank of India.

1. It is indeed a pleasure to address the trading professionals in the Indian foreign exchange market at the Forex Association of India's 25th Annual Forex Assembly. The emerging and enchanting city of Gurgaon provides the right backdrop for holding such a conference as this city epitomizes phenomenal growth and development symbolizing the best of "Made in India" and "Make in India" and in a similar vein the Indian forex market has also witnessed tremendous growth and development in terms of depth and breadth, particularly since the adoption of market determined exchange rate regime about two decades ago.

2. The exchange rate of Rupee has witnessed both periods of intense volatility and periods of stability since May 2013 when the Fed Chairman Bernanke first hinted at early tapering of Fed's Quantitative Easing (QE) programme. Against this backdrop, I would like to start my address by briefly touching upon the developments in the domestic forex market, especially after Chairman Bernanke's testimony, and the measures taken by the RBI to restore orderly conditions in the market. Then I would also like to focus on the possible risks to the stability of the forex market going forward and how well is India placed now as compared to 2008 and 2013 to cope with large capital outflows if they were to materialize. Finally, I will discuss some of the major issues and concerns pertaining to the Indian forex market which are presently engaging the attention of the policy makers.

Developments in the forex market

3. In the aftermath of the global financial crisis and the Eurozone debt crisis, EMEs including India faced enhanced uncertainty, especially in the external sector on the back of both local and global developments. The worsening of India's external environment was amply reflected in the deterioration in various external sector vulnerability indicators between end-March 2011 and end-March 2013.The external debt to GDP ratio increased from 18.2 per cent to 22.0 per cent. On the other hand, the import cover of reserves, which stood at 9.5 months at end-March 2011 declined sharply to about 7.0 months at end-March 2013. The CAD-GDP ratio deteriorated from 2.8 per cent to 4.7 per cent during the period. The weak macroeconomic environment was reflected in the form of sharp deceleration in GDP growth rate (4.5 per cent in 2012-13 and 4.4 per cent in Q1 of 2013-14), high level of inflation (average WPI inflation of 7.4 per cent in 2012-13) and large fiscal deficit (4.8 per cent of GDP in 2012-13).

4. Though the trigger or the proximate cause for intense volatility witnessed in the domestic forex market during the period May-August 2013 was the heightened concerns about the possibility of early QE tapering, the more important cause was the existence of such weak macro-economic fundamentals. The possibility of early tapering of QE programme by the US Fed triggered large selloffs by the FIIs, especially in the bond market leading to heightened volatility of Rupee in line with other EME currencies. The hardening of long-term bond yields in the US and other advanced economies increased their attractiveness, prompting foreign investors to pull funds out of riskier emerging markets, which had received large capital inflows in search of higher yields. The Indian Rupee became one of the worst performers

during the period from the second half of May 2013 to August 2013. Rupee depreciated sharply by around 19.4 per cent against the US dollar from the level of 55.4 per US dollar on May 22, 2013 to a historic low of 68.85 per US dollar on August 28, 2013.

5. To stem the sharp and substantial depreciation of the Rupee, policy makers resorted to a mix of policy measures including forex market intervention, monetary tightening through reduction in banks' access to overnight LAF, increase in MSF rate and increase in daily minimum CRR maintenance requirements and administrative measures, such as, import compression of non-essential items like gold, opening of special dollar swap window for the PSU oil companies, special concessional swap window for attracting FCNR (B) deposits, increase in overseas borrowing limit of banks, bringing of outward FDI flows to the approval route, reduction in Liberalised Remittance Scheme (LRS) entitlement, disallowing banks from carrying proprietary trading in exchange traded derivatives, etc. The Reserve Bank made net sales to the tune of US$ 10.8 billion in the forex market during the period May-August 2013. The Reserve Bank also intervened in the forward market resulting in doubling of net forward liabilities to US$ 9.1 billion as at end-August 2013 from US$ 4.7 billion in July 2013. Apart from monetary and administrative measures, the flow encouraging measures, such as, enhancement of FII investment limit in government debt by US$ 5 billion to US$ 30 billion was undertaken in June 2013.

6. The special forex swap facilities extended by the Reserve Bank at concessional rate for fresh longer term FCNR (B) deposits and banks' overseas borrowings along with enhancement in their overseas borrowing limits led to forex inflows in excess of US$ 34 billion that aided in restoring stability of the Rupee. The Reserve Bank undertook the concessional swap facility as an exceptional measure with the broader public policy objective of bolstering the forex reserves for strengthening Bank's market intervention capability. Similarly, the swap windows to meet oil demand were conceived as a purely temporary dollar lending arrangement to OMCs. The swap window did attract a fair amount of criticism from the perspective of execution of the second leg but thankfully the Reserve Bank can look back at these temporary arrangements with a sense of satisfaction of restoring confidence and stability in the foreign exchange market and India's external sector outlook.

7. Alongside, various measures taken by the Reserve Bank and the Government of India including the fiscal steps taken to compress gold demand helped in stabilizing the financial markets, in general, and the forex market, in particular through sharp reduction in CAD and increase in capital inflows. Consequently, the Rupee made a smart recovery in September-October 2013. With the return of stability in the forex market, a calibrated unwinding of exceptional monetary and administrative measures of July 2013 was undertaken from September 2013 onwards.

8. Despite the announcement on December 18, 2013 of commencement of tapering by the US Fed starting from January 2014 and the subsequent announcements about the increase in its pace, the Rupee has generally remained stable, which indicates that the markets have broadly shrugged off QE tapering fears. The Rupee has remained relatively stable as compared to other major EME currencies like Brazilian Real, Turkish Lira South African Rand, Indonesian Rupiah and Russian Rouble. The daily volatility (annualised) of Rupee during the period from January 1 to September 30, 2014 remained at 5.9 per cent as against South African Rand (11.5 per cent), Brazilian Real (10.8 per cent), Turkish Lira (10.6 per cent), Russian Rouble (9.9 per cent) and Indonesian Rupiah (6.9 per cent). In terms of point-to-point variation, Rupee has marginally appreciated by about 0.5 per cent during the above period, while other currencies have witnessed depreciation, *viz.* Russian Rouble (16.9 per cent depreciation), South African Rand (7.4 per cent), Turkish Lira (5.8 per cent) and Brazilian Real (3.4 per cent).The contagion effect of sharp fall in Argentine Peso against the US dollar in the second half of January 2014 also did not have any major impact on the Rupee. Even the recent geo political crises in Ukraine, Iraq and Gaza did not have any significant impact on the Indian financial markets. This has led to some analysts describing Indian Rupee as the most agile out of the fragile currencies of EMEs.

9. The fact that weak macroeconomic fundamentals have a tendency to accentuate the contagion effect of any adverse external development was amply demonstrated during the May-August 2013 episode of volatility. Countries with large macroeconomic imbalances, especially large CAD, such as, Brazil, Turkey, India, Indonesia, etc., experienced much larger volatility as compared to other EDMEs with current account surplus/better fundamentals. In a scenario of intense volatility, traditional monetary policy defence at times proves inadequate as was experienced by other EDMEs like Turkey and Indonesia. Thus, a mix of measures, including administrative measures, coupled with effective communication by central banks helps in containing the exchange rate volatility. I feel that the main lesson from this episode of volatility for an EMDE central bank is to have sufficient tools in its toolkit and employ them in a flexible, proactive and pragmatic manner. In this context, having large forex reserves, which was earlier considered wasteful on account of quasi fiscal costs, has become a new virtue. Even the debate surrounding capital account liberalisation has decisively veered towards having some necessary capital controls in place to protect the EMDEs from the vagaries of international capital flows where a deluge is generally followed by sudden stops. The need for the EMDEs to have prudent capital controls in place has been duly recognised by the ardent votaries of full capital account liberalisation like the IMF. Unfettered capital account liberalisation is now *passé* and the new *mantra* is having certain necessary capital controls in place and use them proactively during episodes of heightened volatility.

10. As regards the movement of Rupee during the recent period, it has remained largely range-bound with strengthening bias on the back of sustained capital inflows and improving macroeconomic fundamentals. In a comparative sense in Q2 of 2014-15, the Indian Rupee depreciated 2.72 per cent against the US dollar while the Russian Rouble depreciated about 13 per cent, Turkish Lira by 6.5 per cent, the Brazilian Real by 10 per cent, and the South African Rand by 5.5 per cent. There has been continuing FII inflows to the domestic equity markets as well as resumption of FII inflows to debt market, especially since December 2013 (except in April 2014 when there was a net outflow). During 2014 so far, foreign portfolio inflows to debt and equity markets have been around US$ 34 billion with the larger part going to the debt segments. The substantial reduction in gold imports and increase in exports led to significant reduction in current account deficit to 1.7 per cent of GDP in Q1 2014-15 from 4.8 per cent in Q1 2013-14. In the recent period, inflation has decelerated (7.8 per cent CPI inflation in August 2014), growth has picked up (5.7 per cent in Q1 of 2014-15 as compared to 4.7 per cent in Q1 of previous year), fiscal deficit has reduced (4.5 per cent of GDP during 2013-14). India's forex reserves have increased by around US$ 40.3 billion in the past one year to around US$ 316 billion as on September 12, 2014.While the country's external debt may have risen to 1.8 per cent for the quarter ended June 2014, the share of short-term debt in the total debt has declined primarily due to restrictions on FII investments in the short end of the G-sec. It is equally important to note that short term debt as a percentage of reserves have also declined largely due to increase in the size of foreign exchange reserves. The sharp increase in forex reserves and improvement in macroeconomic fundamentals, including the short-term debt profile, have significantly enhanced the resilience of the economy to external shocks. Political stability in terms of formation of a new Government with clear mandate, Government's continued commitment to fiscal consolidation and sustained decline in oil prices have boosted the confidence in the country's macro-economy. The recent upgrade in country's outlook from negative to stable by S & P in a sense reflects and reinforces this new confidence. Thus, it can be said that India is in a much better position to withstand large capital outflows triggered by external developments. We, however, have to be alive to a few downside risks.

Downside risks

11. Downside risks in the form of still elevated retail inflation, continued weak economic performance, uncertainty surrounding global economic recovery, potential slowdown of capital flows to EMEs once interest rate cycle in advanced economies reverses, geopolitical

risks, etc., remain. We need to be particularly cautious of the likely impact of headwinds arising due to growing robustness in the growth outlook of the US and the strengthening of the US dollar and the dovish stance of the European Central Bank. These can cause problems to India's external sector. Additionally; the recent surge in equity markets has created concerns about under-pricing of risks with attendant implications for financial stability. Any abrupt correction of such risks may result in sharp fall in asset prices and enhanced volatility in global financial markets, especially in the EMDEs. Moreover, as we have seen while financial risk taking has gone up substantially, aided by accommodative policies of central banks of AEs, economic risk taking in conspicuously absent or muted. This has implications for global output growth and in turn trade growth trajectory; WTO, for instance, has lowered its world trade growth forecast for 2014 from 4.7 in in April to 3.1 in September. Further, though macro-economic fundamentals and business sentiments in the country have improved during the recent period, more needs to be done in terms of removing structural impediments, building durable business confidence and creating fiscal space to support investments in order to secure sustainable growth. In the long-run, the resilience and robustness of the macro-economy in conjunction with the depth, breadth and orderliness of the financial markets will determine the stability of the external sector as well as the overall financial sector.

12. Now I would like to turn to some of the major issues and concerns relating to the forex market, which are currently engaging the attention of the policy makers and, I hope, also of the market players.

Hedging of currency exposures by corporates

13. In the recent period, the global financial markets have been going through a phase of low volatility and the Indian markets have been no exception to this trend. A supportive policy environment backed by accommodative monetary policy stance of the central banks of the advanced economies (AEs) and visible signs of pick-up in growth in some of the AEs have contributed, in a large measure, to reduction in volatility. On the flip side in India, there is emerging anecdotal evidence of reduced propensity to hedge foreign exchange exposures arising out of a sense of complacency. The unhedged exposures in respect of External Commercial Borrowings (ECBs)/ Foreign Currency Convertible Bonds (FCCBs) lead to large scale currency mismatches in view of the bulk amount borrowed by domestic corporates for longer tenors with limited or no natural hedges. Further, the increasing use of bond route for overseas borrowings exposes the domestic borrowers to greater roll-over risk. As per indicative data available with the Bank, the hedge ratio for ECBs/FCCBs declined sharply from about 34 per cent in FY 2013-14 to 24 per cent during April-August, 2014 with very low ratio of about 15 per cent in July-August 2014. Large scale currency mismatches could pose serious threat to the financial stability in case exchange rate encounters sudden depreciation pressure. It is absolutely essential that corporates should continue to be guided by sound hedging policies and the financing banks factor the risk of unhedged exposures in their credit assessment framework. Banks have expressed the difficulty faced by them in pricing the unhedged exposures of the corporates in an environment of low pick up in credit growth. Given the implications of large unhedged forex exposures on the financial stability, it is necessary for the banking industry to act in unison to bring about an awareness amongst the corporates about the need for adopting and implementing a well-deliberated hedging policy so that the Indian forex market is spared of regular episodes of extreme volatility.

Foreign exchange derivatives – requirement of underlying exposure

14. The access to the OTC foreign exchange derivatives has been subject to production of documentary evidence in support of the underlying exposure except for hedging of probable exposures and special dispensations offered to SMEs, individuals and firms. The primary objective of the regulation has been to restrict the use of OTC foreign exchange derivatives by the corporate clients for hedging their exchange rate risks and not for trading in the instruments. Trading in derivatives requires sophisticated risk management skills and

financial acumen which are not the natural strengths of corporate entities barring a few large corporates who are into treasury operations as an independent profit centre. Further, the trading activities of authorised dealer banks are subject to strict governance and regulatory standards which the corporate entities even with sophisticated treasuries are not subjected to. The exchange rate being an important macroeconomic variable, unregulated trading in it has potential adverse consequences for macroeconomic and financial stability. The Reserve Bank is aware of active intra-day/short term trading by some corporate houses in the foreign exchange government securities market. In the past, the Reserve Bank has imposed restrictions on cancellation and rebooking of forward contracts by the corporates so as to curb their speculative trading that accentuates volatility of Rupee. As huge position taking by the corporates has the potential of destabilizing the market, particularly during periods of uncertainty, Reserve Bank would expect adherence to the spirit of its regulations by such non-bank entities.

15. The Reserve Bank is fully aware of the need to put in place customer-friendly procedures to encourage greater amount of hedging from the end-users. In the past, the bank has taken several measures to simplify the documentation requirements for facilitating easy access to foreign exchange derivatives; recently it has increased the limit of hedging without documentation to US$ 250,000. The facility of hedging the probable exposures based on past performance in respect of trades in merchandise goods and services has also provided flexibility in hedging in the absence of underlying documents supporting contracted exposures. The Reserve Bank had imposed certain restrictions in use of the past performance based facility by the importers in the backdrop of heightened volatility in exchange rate of Rupee last year. It has gradually removed the restrictions as the exchange rate started trading in a stable manner. As announced in the latest Monetary Policy statement of September 30, 2014, the eligible limit for importers under the past performance route has been restored to hundred percent. Some of the other important relaxations are listed in the Box.

16. There are difficulties involved in ensuring underlying verification in exchange traded derivatives (ETCD). It would, however, be imprudent to apply asymmetric regulations for OTC and exchange traded derivatives in respect of underlying requirements. The Reserve Bank has attempted to draw a balance between these two aspects while prescribing the latest regulations on participation of residents and foreign portfolio investors (FPIs) in exchange traded derivatives. Going forward, the Bank could consider further measures to simplify the documentation requirements.

Long term hedging – development of forward market beyond one year

17. The depth of Indian foreign exchange market has improved during the last one year with average daily inter-bank spot and FX swaps (mainly used for covering forwards) trading volume increased to US$ 8.7 billion and US$ 8.1 billion during August 2014 from US$ 7.2 billion and US$ 7.1 billion respectively during August 2013. The limitation, however, remains with the restricted spread of liquidity in the forward market which is mainly confined upto one year. As per the data reported to Trade Repository at the Clearing Corporation of India Ltd. (CCIL), the share of forwards beyond 1-year remains well below 1 per cent. Non-availability of long term forwards has often made hedging difficult, especially for exporters and corporates availing of external commercial borrowings. They have to resort to rolling over the short term forward contracts matching with the tenors of their underlying receivables/payables. Such roll-overs pose price risk depending upon the magnitude of variation in exchange rate at the time of roll-over. As you know, the development of long term forward market greatly depends on the extent of development of interest rate markets at the shorter end of the curve. A liquid term money market facilitates development of credible term benchmark rates that help development of long term swap markets. The long term interest rates guide the pricing of the long term forward contracts.

18. It has been a constant endeavour of the Reserve Bank to promote development of the term money market. Some of the recent initiatives include introduction of term repos as a part of Bank's liquidity operations, increasing the frequency of term repos to four times during a reporting fortnight, recent announcement for permitting re-repoing of government securities, etc. The market participants and the market representative bodies together have to take initiatives in this regard that would pave the way for development of long term forward market. Pending development of liquid term interest rate market, the active market participants in the forward market should together try quoting in the tenors beyond one year. As such, some banks trade in MIFOR (Mumbai Inter-bank Forward Offered Rate) wherein they take a view on long term forwards as the price of instrument is a combination of USD LIBOR and USD/INR forward premium of related tenors. They may take a lead role in quoting the long term forward rates based on their views they take in quoting MIFOR. I am confident that if 10 to 15 active banks take the initiatives, it may lead to decent liquidity in long term forwards. I would also urge the foreign exchange broker community to play a proactive role in this regard.

Enhancing liquidity in the OTC FX option market

19. It is quite disheartening to see that the trading activity in the option market has declined drastically during the recent period. As per the data reported to the CCIL Trade Repository (TR), the average daily volume in the inter-bank USD/INR option market remained at US$190 million in August 2014, a fall of about 45 per cent from the levels two years back. The average daily volume in the inter-bank USD/INR options is currently just about 2.6 per cent of that of inter-bank USD/INR forwards. The decline in the inter-bank option trading volume is attributed to fall in the usage of options by the clients as well as fall in the proprietary trading by banks.

20. It is a well-recognised fact that the option contracts provide lot of flexibility to the end users for hedging their currency exposures in cost effective ways. The plain vanilla option contracts may be combined in various ways for reducing the cost of hedging. The Indian currency option market needs to be rejuvenated to cater to the needs of various real sector economic agents. As you are aware, the Reserve Bank in its latest Annual Report has announced to expand the option market in the coming years to allow market participants to hedge more easily and cheaply. Going forward, the Reserve Bank will actively engage with the banks and other stakeholders in bringing out necessary regulatory changes to foster promotion of liquidity in the option market. As an important step in this direction, we would like market bodies like FAI/FEDAI to give us a well- deliberated feedback on the need to allow corporates to write covered options and also take on simple structures like call-spreads with appropriate safeguards.

FPI participation in the currency derivatives market

21. As you know, the Foreign Portfolio Investors (FPIs) were allowed to participate in the exchange traded currency derivatives (ETCD) on June 20, 2014 for the purpose of hedging the currency risk arising out of the market value of their exposure to Indian debt and equity securities. The participation of FPIs in the ETCD has, however, remained muted so far with open interest of about US$ 11 million as on September 30, 2014. The participation of FPIs in the OTC currency derivatives also remained quite low. As announced in the Annual Report, the Reserve Bank could consider further measures for extending access to the OTC currency derivatives to the international stakeholders over the medium term.

FPI participation in the G-sec market

22. In the recent past, Reserve Bank had noticed trends of volatile FII flows in the short-term debt market which were impacting the foreign exchange markets as well. In view of volatile FII flows in the short term government securities market, the Reserve Bank restricted FIIs/QFIs investments to only dated government securities having residual maturity of three

year or above. The overall G-sec investment limit, however, remained unchanged at US$ 30 billion. The policy objective was two-fold (a) containing the interest rate and exchange rate volatility and (b) developing the debt market by attracting long-term stable investment flows through endowment funds, pension funds, sovereign wealth funds, etc. In the meantime we have been smoothening the process and procedure relating to their investments, e.g., direct participation in trading , introduction of T+2 settlement and possible introduction of international settlement linked to domestic trading system. Going forward, Reserve Bank would calibrate further liberalization of the FPI investment limits in G-sec with the overall objective of prudential management of the capital account in general and mitigating the impact of speculative carry forward trade in particular.

Reforms in the financial benchmarks

23. The Vijay Bhaskar Committee on Financial Benchmarks has recommended several measures for strengthening the benchmark quality, setting methodology and governance framework of the Indian interest rate and foreign exchange benchmarks respectively. The Committee has recommended creation of an independent body by FIMMDA and FEDAI, either independently or jointly, for administration of the Indian interest rate and foreign exchange benchmarks so as to overcome the possible conflicts of interest with the benchmark setting process arising out of their current governance structure. It is heartening to note that the FIMMDA, FEDAI and IBA are in the process of forming an independent company jointly. I urge the three institutions to expedite the process so that the new company can take appropriate steps to implement the recommendations of the Committee at the earliest and become compliant with the IOSCO Principles on Financial Benchmarks already endorsed by the FSB working on the mandate from G-20.

24. As you know, based on the recommendations of Committee, the Reserve Bank has issued guidelines on April 16, 2014 specifying measures to be implemented by the banks and PDs acting as Benchmark Submitters for strengthening the governance framework for submission. The guidelines also stipulate that the FIMMDA and FEDAI will select the Benchmark Submitters on the basis of their standing, market-share in the benchmark/instrument linked to the benchmark and representative character and will put in place a Code of Conduct specifying various provisions including hierarchy of data inputs for submissions. I came to know that the Code of Conduct and the list of submitters for various interest rate and foreign benchmarks have been finalised. Reserve Bank would expect these submitter banks, Indian and foreign, and PDs to extend necessary support and cooperation for strengthening the benchmark determination process. The Benchmark Submitters selected by the Administrator have to necessarily participate in the polling process as stipulated in our guidelines.

OTC derivative data dissemination

25. In compliance to the G-20 commitment for creation of OTC derivative TR, the creation of TR for various OTC foreign exchange derivatives was completed on December 30, 2013 with roll-out of the fourth and final phase covering currency swaps, IRS in foreign currency and client trades in Rupee IRS. The reporting platform for inter-bank Rupee IRS and CDS were already in place. The Reserve Bank has announced in the latest Annual Report as part of its agenda for 2014-15 to institute an appropriate public dissemination system at the CCIL for disclosing the price and volume information relating to the major inter-bank OTC FX derivatives, such as, FX forwards and options to be reported to the TR. The price and volume dissemination will help promote greater market transparency and reduce information asymmetry. The Bank has also earlier indicated the usage of the reported OTC derivative transactions for its conduct of surveillance of OTC derivative markets, financial stability assessments and micro-prudential supervision.

26. It came to our notice that there have been several instances of wrong and delayed reporting of the transaction data to the TR. It must be appreciated that the correctness and

timeliness of data reported to the TR are the critical requirements for disseminating reliable information to public and making use of the data for various regulatory purposes. RBI has already advised the heads of the Treasury of the AD banks to put in place appropriate system to report correct transaction data in the specified formats within the stipulated timelines. I once again urge all the banks to strengthen their reporting system so that an effective and comprehensive dissemination system can be put in place at the earliest as this is in the interest of all the stakeholders.

Need for more number of FX trading platforms

27. The spot FX trading in India is mainly concentrated on a single trading platform with minimal volume getting cleared on the second platform. An electronic trading platform is an important market infrastructure which aids in efficient trade execution, price discovery and post-trade settlement. The concentration of trading in a single platform has adverse consequences for the stability and efficiency of the foreign exchange market. You may remember that the largest global foreign exchange market making banks partnered in 1990 to create an alternate electronic platform when the trading was mostly concentrated in a single platform. The existence of more than one trading platforms facilitates competition and reduces cost of trading. Although a large number of trading platforms may fragment market liquidity, a reasonable number of trading platforms in the Indian spot FX market with daily trading volume of about US$ 8 billion will not adversely impact the liquidity. There are at least two major platforms in the spot trading of many currencies. I would suggest that the FEDAI and market participants may work together to promote competing trading platforms in the overall interest of market stability and efficiency and reducing the cost of trading.

The way forward

28. The Indian foreign exchange market has come a long way in terms of variety of instruments, participants and the overall market turnover. Liberalization in exchange controls, simplification of operating procedures and introduction of several new instruments has provided greater flexibility to the market participants in undertaking foreign exchange operations and managing their currency risks. Given the growing size of India's presence in international trade and finance, more of course needs to be done to make the market broader, deeper and more vibrant. I have flagged certain proximate concerns and issues, although the list is not exhaustive, for this gathering to ponder over I am sure a congregation of this nature with a number of domain experts participating in the business sessions would also discuss some of these issues of proximate concerns. These and other strategic issues deliberated in such a forum would go a long way in delineating the future trajectory of development and regulation of the foreign exchange market of an aspiring EMDE like ours. I wish the conference a great success.

Thank you for your attention.

Box: Recent measures for easing certain foreign exchange restrictions

Sr. No.	Date	Measure taken	Earlier status
Hedging on Contracted Exposures			
1	July 4, 2013	AD banks, while offering hedging products under the contracted exposure route to their customers may obtain an annual certificate from the statutory auditors to the effect that the contracts outstanding with all AD category I banks at any time during the year did not exceed the value of the underlying exposures at that time. This measure has eased the burden of documentation for the end-users.	The auditor certificate was required to be obtained on a quarterly basis.
2	Jan 13, 2014	The facility of rebooking of cancelled contracts in case of contracted current account transactions, regardless of the tenor, and capital account transactions, falling due within one year, was restored.	The facility was earlier withdrawn on Dec. 15, 2011 and restored incrementally for exporters i.e. 25% on Jul 31, 2012, 50% on Sep 4, 2013 and 100% on Jan 13, 2014.
3	Jan 13, 2014	Forward contracts booked by FIIs/QFIs/other portfolio investors, once cancelled, can be rebooked up to the extent of 10 per cent of the value of the contracts cancelled.	The facility of rebooking of cancelled contracts was withdrawn on Dec. 15, 2011.
4	Apr 7, 2014	All resident individuals, firms and companies, permitted to book foreign exchange forward contracts up to USD 250,000 on the basis of a simple declaration without any further documentation.	Such contracts could be booked only up to US$ 100,000.
5	Sept 8, 2014	Coupon Hedging: FPIs have been permitted to hedge the coupon receipts arising out of their investments in *debt* securities in India falling due during the	Hedging of coupon receipts by FPIs was not permitted

Sr. No.	Date	Measure taken	Earlier status
		following twelve months. This measure provides flexibility to FPIs who intend to remain invested till maturity.	
Hedging on Probable Exposures (Past Performance basis)			
6	Mar 27, 2014	The restriction on passing on of the exchange gain on to the customer in the event of cancellation of the existing contracts was withdrawn and only contracts in excess of 75 per cent are now required to be delivered.	Since Dec. 15, 2011, all contracts booked on the basis of past performance had to be delivered. In case of cancellations, exchange gain, if any, was not to be passed on to the customer.
7	Sept 30, 2014	With a view to bringing at par both exporters and importers for hedging of currency risk arising out of probable exposures based on past performance, importers were permitted to book forward contracts, under the past performance route, up to 100 per cent of the eligible limit (same as exporters).	The limit for importers was reduced to 25% of the limit on Dec. 15, 2011. It was later raised to 50% on May 27, 2014.
FPIs participation in Exchange Traded Currency Derivatives (ETCD) Market			
8	June 20, 2014	Foreign Portfolio Investors (FPIs) who are eligible to invest in the Indian debt and equity assets under FEMA, 1999 were allowed access to ETCD market for hedging the currency risk arising out of the market value of their exposure to Indian debt and equity securities. FPIs can take both long (bought) as well as short(sold) position in FCY-INR pairs up to USD 10 million or equivalent per exchange without having to establish existence of any underlying exposure. An FPI cannot take a short position beyond US$ 10 million at any time and to take a long position beyond US$ 10 million in any exchange, it is required to have an underlying exposure. The onus of ensuring the existence of an underlying exposure rests with the FPI concerned.	FPIs were not permitted to participate in ETCD market.