



Global trade settlement in INR: Understanding the implications





Background

The Reserve Bank of India (RBI) has issued guidelines¹ on a new mechanism that will enable invoicing and settlement of trade between domestic importers/exporters and other countries in Indian rupees (INR). The decision is aimed at promoting global trade growth, with an emphasis on trade from India. Through this step, the Central Bank also seeks to support the increasing interest of the global community in the rupee.

With this arrangement in place, invoicing, payment and settlement of exports and imports can be carried out in INR. The step comes amidst the rupee touching record lows against the United States dollar (USD) and in the aftermath of the war in Ukraine.

Key highlights of the RBI circular

1. Opening of special vostro accounts

- All Category-I Authorised Dealer (AD) banks have been permitted to open special rupee vostro accounts of the correspondent bank(s) of a partner trading country.
- In the case of an Indian exporter undertaking exports of goods and services through this mechanism, the export proceeds shall be paid in INR from the balances in the designated special vostro account of the correspondent bank of the overseas importer.
- On the other hand, for an Indian importer, the payment shall be credited to the special vostro account in INR against the invoice for the supply of goods and services from the international exporter.

2. Prevalent trade products like letter of credit (LC) and bank guarantee (BG)

- LC and other trade-related documentation may be decided upon mutually between banks of the partner trading countries under the Uniform Customs and Practice for Documentary Credits (UCPDC) and Incoterms.
- BG issuance is permitted subject to adherence to the provisions of Foreign Exchange Management Act (FEMA) Notification No. 8 and the provisions of the Master Circular on Guarantees and Co-acceptances.

3. Use of surplus balance

- The INR surplus balance in special vostro accounts can be used for payments for projects and investments, export/import advance flow management and investment in Government treasury bills and securities.

¹ <https://rbi.org.in/Scripts/NotificationUser.aspx?Id=12358&Mode=0>

4. Reporting and approval process

- The reporting of cross-border transactions needs to be done in adherence to the guidelines under FEMA, 1999.
- If a bank of a partner trading country approaches an AD bank in India to open a special vostro account, approval has to be sought by that AD bank from the RBI's Central Office in Mumbai.
- The AD bank in India also has to ensure that the correspondent bank is not from a country/jurisdiction in the updated Financial Action Task Force's (FATF's) public statement on high-risk and non-cooperative jurisdictions.

What does this mean for our economy and trading community?

- This step may provide a boost to India's trade with countries under global sanctions.
- Countries which have been cut off² from the SWIFT payment gateway can trade with India through this mechanism as it allows mutual agreement between partner countries for the safe and secure exchange of messages.
- With India's trade deficit having widened³ to a record low in May 2022, this step may help in curbing domestic currency volatility and promote exports from India in other countries which are facing a forex shortage.
- The Central Bank has also deliberated on its Asian peer, the Chinese yuan, and how the yuan has been globalised by China by attracting global manufacturers and increasing gold purchases using yuan. The yuan and INR will become important determinants of the currency market in view of the export competitiveness between India and China.



2 <https://www.bloomberg.com/news/articles/2022-03-01/eu-agrees-to-block-russian-banks-from-swift-sparing-key-firms>

3 <https://www.cmie.com/kommon/bin/sr.php?kall=warticle&dt=20220704141242&msec=576>

What are the key enablers for this arrangement?

Banks and corporates across the country may look at these key areas to enable an efficient transition to the new mechanism for carrying out trading transactions:

Systems and IT infrastructure change: Assessment of operational and technological impact across the invoicing and settlement process for all trade finance products

Pricing and risk processes: Incorporation of INR in the pricing and risk systems and processes, along with the inclusion of this currency in regulatory reporting

Compliance and approval processes: Due approval from the RBI's Central Office for the incorporation of vostro accounts as well as due diligence on correspondent banks to avoid participants from non-cooperative jurisdictions

Tax and accounting impacts: Identification of the tax benefits for exporters, such as rebates and incentives (earlier available for trading in USD); impact of the change in the invoicing and settlement currency and of the fluctuation in market-determined exchange rates on the accounting regime

Management information system: Changes in both internal and regulatory reporting to capture the exposure on account of the new arrangements

How can PwC help?

The introduction of INR in the arena of cross-border trading transactions will require a complete transition and overhauling of trading firms under the careful oversight of the regulator. This impact will be seen across banks as well as corporates. Below are some of the ways in which PwC can help these organisations during the transition phase:

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| <ul style="list-style-type: none">• identifying and implementing systems and process changes | <ul style="list-style-type: none">• assessing and managing the impact on pricing, risk and valuation models | <ul style="list-style-type: none">• supporting the numerous compliance and approval processes |
| <ul style="list-style-type: none">• providing customer communication templates to help business expansion | <ul style="list-style-type: none">• managing tax and accounting-related implications | <ul style="list-style-type: none">• enhancing the management information system. |



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