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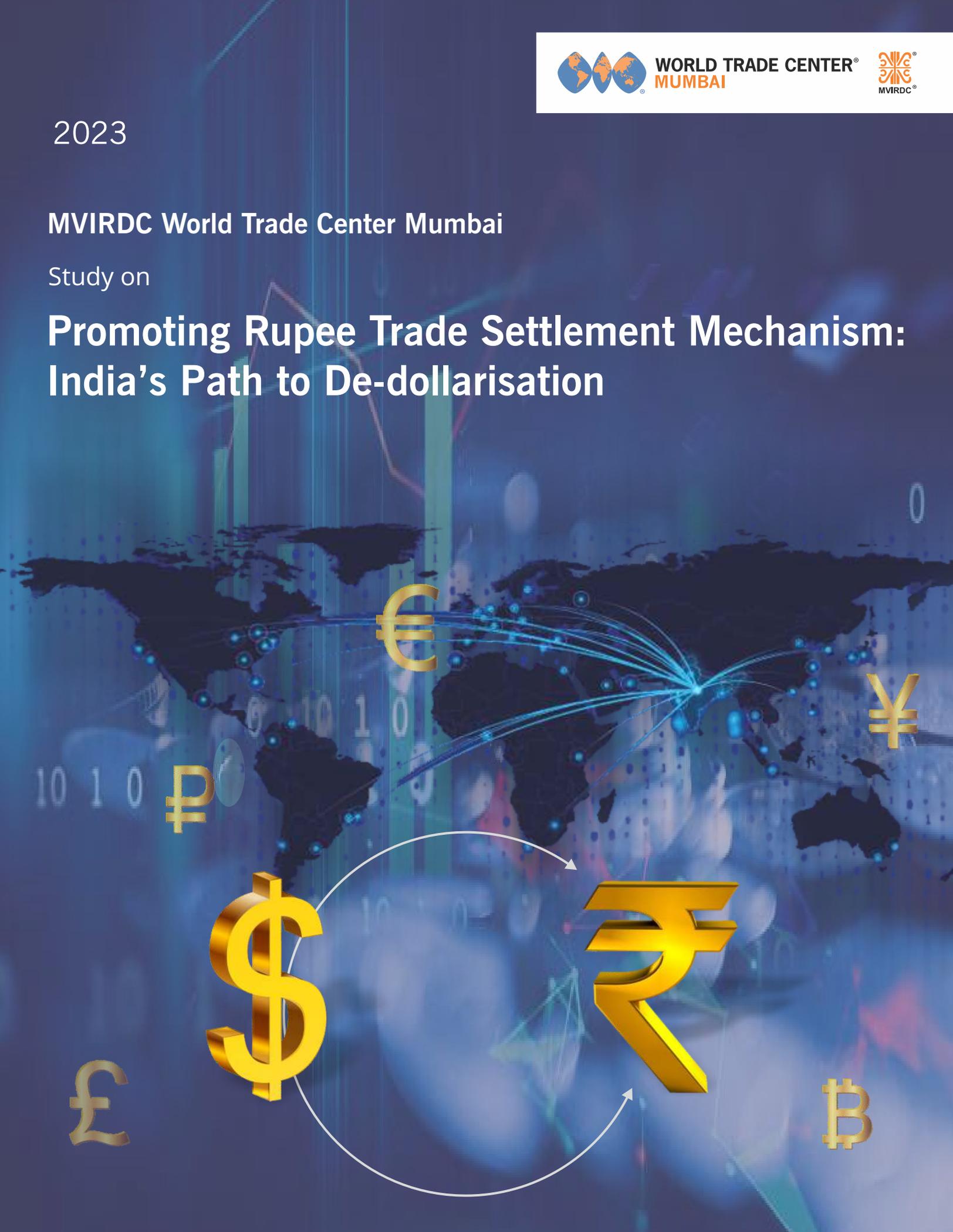


2023

MVIRDC World Trade Center Mumbai

Study on

Promoting Rupee Trade Settlement Mechanism: India's Path to De-dollarisation





Bharat Ratna Sir M. Visvesvaraya
(15 September, 1860 - 14 April, 1962)

FIFTY YEARS AND COUNTING

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FOREWORD

I am delighted to learn about the study "Promoting Rupee Trade Settlement Mechanism: India's path to de-dollarisation" written by M. Visvesvaraya Industrial Research and Development Centre (MVIRDC), World Trade Center, Mumbai. The study effectively captures India's de-dollarization, trade reliance, rupee internationalization, and provides actionable policy recommendations.

Under the dynamic leadership of Hon'ble Prime Minister Shri Narendra Modi ji, India is among the fastest-growing countries on a global scale and holds a position among the foremost destinations for foreign direct investment in the world. To establish an alternative payment and settlement system, it is evident that we should explore trade settlement in the local currency. As India's global economic ties expand, there is a necessity for alternative payment methods to address dollar-dominated payment issues. In this regard, rupee trade settlement will benefit Indian traders and aid countries with trade deficits. It is praiseworthy that the Reserve Bank of India allowed invoicing and payments for international trade in Indian currency.

This report is a valuable addition to the existing literature and policy documents on rupee internationalization, offering a fresh perspective based on stakeholder feedback. It provides insightful recommendations and inputs from esteemed organizations, such as the Indian Banks' Association, the Foreign Exchange Dealers' Association of India, and the Export-Import Bank of India, along with perspectives from exporters, importers, academics, and forex consultants. Furthermore, the identification of 24 potential partner countries with which India has a balanced bilateral trade relationship for the purpose of promoting rupee trade settlement mechanism is a significant contribution to this subject.

I congratulate MVIRDC for bringing out this remarkable composition and wish them success in all their future endeavours.

Piyush Goyal



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Promoting Rupee Trade Settlement Mechanism: India's Path to De-dollarisation

By MVIRDC World Trade Center Mumbai

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Preface

Global currency is the cornerstone for international trade, remittance, investment and other cross-border financial transactions. For the last 100 years, US dollar has been the widely accepted currency for settling international transactions. However, the disadvantages of over-dependence on US dollar for developing countries coupled with the shifting global economic power balance in favour of emerging markets, have given rise to fresh debates on alternative global currency to replace the US dollar. Reliance on the US dollar as a reserve currency exposes developing countries to external sector risks and imposes a huge cost on their industry for managing forex risk. By promoting their local currencies for foreign trade settlement, developing countries can reduce their external sector risks and hence will be less compelled to hold huge foreign exchange reserves.



Against this backdrop, 'internationalisation of rupee' has gained fresh policy attention in India in recent years. India's ambition to increase the global stature of its currency aligns well with its vision of becoming a developed economy by 2047. At a time when India's merchandise and services exports are touching new heights, the use of rupee in cross-border transactions will facilitate the international operations of Indian exporters and importers.

The Reserve Bank of India and the central government have been taking various measures to promote use of Indian rupee for current account transactions such as invoicing of cross-border trade. While efforts to promote local currency settlement of trade with select countries such as Russia and Eastern European nations were taken as early as 1950s, these efforts have borne limited success. I am confident that India's rupee internationalisation effort will gain momentum in the coming years with the recent policy measures and eventually lead to acceptance of local currency for settling capital account transactions such as cross-border investments. India's rapidly growing economy, political stability and strong financial system will also aid the process of internationalisation of rupee.

I am happy to note that MVIRDC WTC Mumbai has conducted this study to assess the country's preparedness for globalizing its currency and identify actionable measures to strengthen global acceptance of the currency. This study has been prepared after extensive primary survey with exporters, India EXIM Bank, Indian Banks' Association, Foreign Exchange Dealers Association of India (FEDAI) and forex risk management professionals.

With more than three decades having passed since India moved from a fixed exchange rate system to a market determined exchange rate, the next logical step is to develop a deep and unified global market for the Indian rupee to support its internationalisation. The moment is opportune as the emergence of fast digital payment systems will aid efficient cross-border remittance in local currencies.

This report highlights high trade deficit and absence of a liquid forex market for rupee as major obstacles for internationalising Indian rupee. Therefore, the study has identified 24 potential partner countries with which India has a balanced bilateral trade relationship to promote rupee trade settlement mechanism.

I am confident that the findings and policy suggestions in this report will add to the existing literature on this subject and promote further public debate on strategizing a roadmap for India's rupee internationalisation.

Dr. Vijay Kalantri

Chairman
MVIRDC WTC Mumbai

Executive Summary

Historically, geopolitical and economic events have influenced the choice of global currency or reserve currency which is used to denominate and settle cross-border transactions. Before the 19th century, Spanish dollar was a popular currency in most part of the world on account of the country's colonial power and maritime dominance. During the 19th and early 20th century, British Pound became a popular global currency on the back of the country's colonial and economic superiority. Since the first world war, however, the British dominance in global currency market diminished and gave way to US dollar by virtue of the growing strength of the American economy.



In the last few decades, currency union in the Europe and the extraordinary influence of China in the global economy and foreign trade positioned Euro and Chinese yuan as suitable candidates for US dollar as global reserve currency. However, none of these currencies could de-throne US dollar as the preferred global reserve currency because of inherent shortcomings in their economies.

The current geopolitical turmoil in the Europe, rising trade tensions, US sanction on foreign countries, weak forex reserves of some developing countries, the rise of crypto currencies, emergence of digital payment systems and aspirations of some countries to promote their currencies in global market have all led to a renewed debate among experts about 'de-dollarisation'.

Against this backdrop, India has been taking steps to de-dollarize its trade by promoting internationalisation of its domestic currency, the rupee. India's economy has remained resilient over the years accompanied by a growing external sector. As of FY 23, India's total merchandise trade stood at USD 1.16 trillion with merchandise exports valued at USD 451 billion and imports at USD 714 billion. Considering this significant trade deficit, the effort to move away from the dollar is a substantial step for the country to gain a prominent position in international trade.

In a move to promote exports from India as well as trade in INR, the Reserve Bank of India (RBI), implemented the Special Rupee Vostro Accounts (SRVAs) in July 2022 as an additional arrangement to the existing Rupee Vostro Account. By allowing for invoicing and payments for international trade in INR, India has also launched the rupee trade settlement mechanism for bilateral trade with different countries.

The extant Foreign Trade Policy of the country, introduced in 2023, has complemented the RBI's efforts of promoting the rupee as an international currency by including relevant provisions and extending the existing export schemes for export proceeds realised in Indian currency.

Despite these policy measures, the rupee trade settlement mechanism has not gained traction. This study has been prepared against the backdrop of these events and it aims to understand the possible challenges in internationalisation of the rupee as well as to propose actionable policy recommendations for the same. The study also incorporates views of the trading community as well as associations in promoting the rupee trade settlement mechanism.

Rupa Naik

Executive Director
MVIRDC WTC Mumbai

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Objectives of the study:

- To understand the need for de-dollarisation of India's trade
- To examine alternative options for India's path to de-dollarisation
- To examine the challenges and bottlenecks in internationalisation of rupee
- To propose actionable policy recommendations to promote the rupee trade settlement mechanism

(To download the full report contact us - research@wtcmumbai.org)