Task Force on Offshore Rupee Markets

The **Task Force on Offshore Rupee Markets,** set up by the **Reserve Bank of India (RBI)** in February 2019 and chaired by **Smt. Usha Thorat**, former Deputy Governor, RBI, submitted its report to the Governor recently.

The Task Force was set up to examine the issues relating to the **offshore Rupee markets** and recommend appropriate **policy measures** while factoring in the requirement of ensuring **stability of the external value of the Rupee** including **measures for incentivising non-residents** to access the onshore foreign exchange market.

Key Recommendations

- Indian banks should not be allowed to deal in the offshore rupee derivative market — or **Non-Deliverable Forward (NDF) markets —** for the present.
  - The onshore rupee derivatives market is currently more deep and liquid as compared to the offshore rupee market and participation of the Indian banks in the offshore market might, over time, take away this advantage.

NDF is a foreign exchange derivatives contract whereby two parties agree to exchange cash at a given spot rate on a future date. The contract is settled in a widely traded currency, such as the US dollar, rather than the original currency.

- **Extension of onshore market hours** to improve access of overseas users and permit Indian banks to freely offer prices to global clients around the clock.
  - Banks should be allowed to freely offer prices to non-residents at all times either by a domestic sales team or by using staff located at overseas branches.
  - Also, wide access to the forex-retail trading platform to non-residents would be a major incentive to use the onshore market.
- Enabling rupee derivatives (settled in foreign currency) to be traded in the **International Financial Services Centers (IFSC)** in India.
- To allow users to undertake **forex transactions up to USD 100 million in over the counter (OTC) currency derivative market** without the need to establish underlying exposure (security that must be delivered when a derivative contract is exercised).

- To **facilitate non-residents** to **hedge** their foreign exchange exposure onshore by:
  - Establishing a **central clearing and settlement mechanism** for non-resident transactions in the onshore market;
  - Implementing **margin requirements** for non-centrally cleared OTC derivatives and allowing Indian banks to post margins abroad;
  - **Aligning the tax treatment** of foreign exchange derivatives with that in major international centres; and
  - **Centralising the KYC requirements** across financial markets with uniform documentation requirement.

'Onshore' currencies simply mean buying the currencies locally, whereas 'offshore' currencies mean buying the currencies outside the national boundaries

Currency derivatives

- These are **exchange-based futures and options contracts** that allow one to hedge against currency movements.
- In simple words, one can use a currency future contract to exchange one currency for another at a future date at a price decided on the day of the purchase of the contract.
- In India, one can use such derivative contracts to hedge against currencies like Dollar, Euro, U.K. pound and Yen.
- While all such currency contracts are cash-settled in rupees, the Securities and Exchange Board of India **(SEBI)**, in July 2018, gave a go-ahead to start cross currency contracts on euro-dollar, pound-dollar and dollar-yen.

Trade in currency derivatives

- The two national-level stock exchanges, (Bombay Stock Exchange) BSE and the (National Stock Exchange) NSE, have currency derivatives segments.
- One can trade in currency derivatives through brokers.

Over the Counter (OTC) Market

- Prior to the introduction of currency derivatives on exchanges, there was only the OTC – over the counter – market to hedge currency risks and where forward contracts were negotiated and entered into.
- It was kind of an **opaque and closed market** where mostly banks and financial institutions traded.
- Exchange-based currency derivatives segment is a **regulated and transparent market** that can be used by small businesses and even individuals to hedge their currency risks.

Source: IE