



India and Malaysia Agree to Settle Trade in Indian Rupees

For Prelims: Trade Settlement in Rupees, ASEAN region, Reserve Bank of India (RBI), Special Rupee Vostro Accounts (SRVAs), India's Forex Reserves, Monetary policy.

For Mains: Significance of India's Move to Settle Trade in Indian Rupee, Challenges Related to Internationalisation of Rupees.

Why in News?

India and Malaysia have agreed to [settle trade in Indian rupees](#). This mechanism is expected to enhance India-Malaysia bilateral trade which touched **USD 19.4 billion during 2021-22**.

- **Malaysia** is the **third largest trading partner of India in the ASEAN region**, after Singapore and Indonesia that account for **USD 30.1 billion and USD 26.1 billion bilateral trade with India respectively**.

What is the Significance of India's Move to Settle Trade in Indian Rupee?

▪ About:

- In **July 2022**, the [Reserve Bank of India \(RBI\)](#) allowed the settlement of international trade in Indian rupees.
- In **December 2022**, India saw its first settlement of foreign trade in rupee with Russia – as part of the '**International Settlement of Trade in Indian Rupee**' mechanism initiated by the RBI.
- In **March 2023**, banks from **18 countries were allowed by the RBI to open [Special Rupee Vostro Accounts \(SRVAs\)](#)** to settle payments in Indian rupees.
 - It includes: **Botswana, Fiji, Germany, Guyana, Israel, Kenya, Malaysia, Mauritius, Myanmar, New Zealand, Oman, Russia, Seychelles, Singapore, Sri Lanka, Tanzania, Uganda, and the United Kingdom.**

▪ Benefits of Trading in Indian Rupees:

- **Controlling Depreciation of Rupees:**
 - India is a **net importer and the value of the Indian rupee has been declining consistently**.
 - Using the rupee for international trade transactions will help **check the flow of dollars out of India** and slow the depreciation of the currency albeit to a “very limited extent.
 - Thus most importantly, the move is expected to **reduce the pressure on [India's forex reserves](#)**.
- **Better Pricing for Goods and Services:**
 - With the ability to invoice trade in Indian rupees, Indian traders can achieve **better pricing for their goods and services**.
 - Also, this mechanism is expected to benefit both sides of the trade by **reducing currency conversion spreads**.
- **Towards Global Acceptance of Rupees:**

- International trade settlements in rupee are expected to gradually contribute to the **global acceptance of the currency**, and later make it possible to **repay loans taken** from fund banks like the Asian Infrastructure Investment Bank.

▪ **Challenges:**

- **Volatility of the Indian Rupee:**
 - The Indian rupee is known to be **volatile and subject to fluctuations** in the foreign exchange market, which may make it **less attractive as a settlement currency** for some international traders.
- **Complication in Controlling Domestic Supply:**
 - RBI's report warns that the '**internationalisation**' of the rupee can potentially **limit the ability of the central bank to control domestic money supply** and influence interest rates as per the domestic macroeconomic conditions.
 - Ultimately, it may lead to complications in terms of formulating the **monetary policy**.
- **Competition with Other Currencies:** The Indian rupee may face competition from other major currencies, such as the US dollar, Euro, and Yen, which are already widely accepted for international trade settlements.

What is a Vostro Account?

- It is an account that **domestic banks hold for foreign banks** in the **former's domestic currency**, in this case, **the rupee**.
 - Domestic banks use it to provide international banking services to their clients who have **global banking needs**.
- The bank holding the Vostro account acts as a **custodian of the foreign bank's funds** and provides various services such as **currency conversion, payment processing, and account reconciliation**.

Conclusion

India's willingness to take **concrete steps towards de-dollarisation of its international trade** and to make the **rupee a tradable currency is a significant step towards internationalisation of rupees**. But India must increase its exports, supported by **critical reforms that include capital account convertibility**, deepening financial markets to manage the **large-scale inflow and outflow of capital**.

UPSC Civil Services Examination Previous Year Question (PYQ)

Q1. Convertibility of rupee implies (2015)

- (a) being able to convert rupee notes into gold
- (b) allowing the value of rupee to be fixed by market forces
- (c) freely permitting the conversion of rupee to other currencies and vice versa
- (d) developing an international market for currencies in India

Ans: (c)

Q2. With reference to Balance of Payments, which of the following constitutes/constitute the Current Account? (2014)

1. Balance of trade
2. Foreign assets
3. Balance of invisibles
4. Special Drawing Rights

Select the correct answer using the code given below:

- (a) 1 only
- (b) 2 and 3
- (c) 1 and 3
- (d) 1, 2 and 4

Ans: (c)

Source: TH

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