



## Vostro Accounts

**Prelims:** Foreign Trade, Currency Depreciation & Appreciation, Global Sanctions, Balance of Payments

**Mains:** Internationalization of Rupee, Effect of global sanctions on economy of India, Benefits and challenges of settling trade in Rupee, Intervention of government in economy

### Why in News?

**20 Russian banks have opened [Special Rupee Vostro Accounts \(SRVA\)](#) with partner banks in India for the settlement of payments in rupee for trade between India and Russia.**

- Also, all major domestic banks have listed their nodal officers to sort out issues faced by exporters under the arrangement.

### What is the Background?

- In July 2022, the **RBI** had unveiled a [mechanism to settle international transactions in rupee to promote the growth of global trade](#), with emphasis on exports from India, as well as **pushing rupee as an international currency**.
  - It is also expected to enable trade with sanction-hit nations such as Russia.
- According to the mechanism finalized by the RBI, **banks of partner countries can approach authorized dealer banks in India for opening special rupee vostro accounts**. The authorized dealer bank will then have to seek **approval from the central bank** with details of such an arrangement.

### What is SRVA arrangement?

- **About:**
  - A vostro account 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 SRVA is an **additional arrangement to the existing system that uses Freely convertible currencies** and works as a complimentary system.
    - The [existing systems](#) require maintaining balances and position in such currencies like US dollar and pound to facilitate trade.
- **Framework:**
  - **Three important components** namely invoicing, exchange rate and settlement are there.
    - **Invoicing** entails that all exports and imports must be denominated and invoiced in Indian National Rupee (INR).
    - **The Exchange Rate** between the currencies of the trading partner countries would be market-determined.
    - **The Final Settlement** also takes place in INR.

#### ▪ **Functioning:**

- The **authorized domestic dealer banks** are required to **open SRVA accounts for correspondent banks** of the partner trading country.
- **Domestic importers** are required to **make payment (in INR) into the SRVA account** of the correspondent bank against the invoices for supply of goods or services from the overseas seller/supplier.
- Similarly, **Domestic exporters** are **to be paid the export proceeds (in INR)** from the balances in the designated account of the correspondent bank of the partner country.
- Indian **exporters may receive advance payment** against exports from overseas importers in Indian rupees through the above Rupee Payment Mechanism.
  - But, it would be **foremost priority** of the domestic bank **to ensure that the available funds are used to meet existing payment obligations** i.e., already executed export orders or export payments in the pipeline.
- All reporting of cross-border transactions is to be done in accordance with the extant guidelines under the [Foreign Exchange Management Act \(FEMA\), 1999](#).

#### ▪ **Eligibility Criteria of Banks:**

- The authorized domestic bank would seek approval from the apex banking regulator providing details of the arrangement when banks from partner countries approach for opening SRVA.
- Domestic banks are responsible to **ensure that the correspondent bank is not from a country mentioned in the Financial Action Task Force (FATF)'s list of High Risk & Non-Co-operative jurisdictions**.
- Authorized banks can open multiple SRV accounts for different banks from the same country.

### **What is the Purpose of the Arrangement?**

- **Reduced Demand of Forex:** [The Economic Survey \(2022-23\)](#) had argued that the framework could **largely reduce the “net demand for foreign exchange, for the settlement of current account related trade flows”**
  - It will further arrest fall of rupee as demand for forex reduces.
- **Reduced Vulnerability to External Shocks:** Reduced dependence on foreign currencies, would make the country **less vulnerable to external shocks**.
- **Rupee as International Currency:** In the long-term it will **promote Rupee as an international currency** once the rupee settlement mechanism gains traction
  - As per the Bureau for International (BIS) Settlements' Triennial Central Bank Survey 2022, the **U.S. dollar accounts for 88% of all trades. The INR accounted for 1.6%**.
- **Trade with Sanctioned Countries:**
  - Ever since sanctions were imposed on Russia, trade has been virtually at standstill with the country due to payment problems.
  - As a result of the trade facilitation mechanism introduced by the RBI, we see the payment issues with Russia easing.

### **What is a Nostro Account?**

- A Nostro account is an account held by a bank in another bank. It allows the customers to deposit money in the bank's account in another bank. It is often used if **a bank has no branches in a foreign country**. Nostro is a Latin word that means “ours”.
  - Let's presume bank "A" does not have any branches in the Russia, but bank "B" does. Now, to receive the deposits in the Russia, **"A" will open a Nostro account with "B"**.
  - Now, if any customers in the Russia want to send money to "A", they can deposit it **into A's account in "B"**. "B" will transfer the money to "A".
- The main difference between a deposit account and a Nostro account is that the former is held by individual depositors while **foreign institutions hold the latter**.

## UPSC Civil Services Examination Previous Year Question (PYQ)

### Q. 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)**

[Source:TH](#)

PDF Refernece URL: <https://www.drishtias.com/printpdf/vostro-accounts-1>

