



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](#)

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