V DEVELOPMENT AND REGULATION OF FINANCIAL MARKETS

The Reserve Bank pursued its efforts to impart liquidity to the G-sec market, while trying to diversify the investor base. Measures were also taken to develop the corporate bond market with a view to encouraging wider participation and to enhance liquidity in the repo market. The fluctuations in the foreign exchange market prompted the Reserve Bank to take several measures to contain volatility and encourage stable foreign inflows.

V.1 Keeping in view the rapidly evolving global developments, the Reserve Bank has focussed on ensuring the development of financial markets. Well-developed financial markets are not only important for the critical role they play in the transmission of monetary policy, but they also facilitate price discovery. To ensure that markets function in a non-disruptive manner while ensuring that systemic risks are contained, the Reserve Bank continued to play a key role in nurturing their growth and development.

GOVERNMENT SECURITIES MARKET

V.2 Measures were taken to develop and regulate the activities in the financial market, particularly the Government securities market and the corporate bond market. There has been a concerted effort on the part of the Reserve Bank in furthering the liquidity in Government securities market and related interest rate derivatives. At the same time, in view of the growing needs of the infrastructure sector and also of the overall development of financial markets, the development of the corporate bond market has been high on the agenda for Government of India and the regulators. Several measures have been taken by Government of India, RBI and SEBI to aid growth of corporate bond market in India. Some important measures to develop financial markets, *inter alia,* include (i) implementation of some of the recommendations of the Working Group on Enhancing Liquidity in Government Securities Markets, (ii) phasing out Tier-III capital for PDs, (iii) review of Commercial Paper (CP) and repo guidelines, (iv) ready forward contracts in corporate debt securities - permitting Scheduled Urban Cooperative Banks, (v) relaxation of investment norms to encourage participation of standalone PDs; and (vi) permission to standalone PDs for membership in SEBI-approved Stock Exchanges for trading in corporate bonds. (vii) review of Credit Default Swap (CDS) and repo in corporate bonds guidelines and (viii) standardisation of IRS contracts.

Report of the Working Group on Enhancing Liquidity in the Government Securities and Interest Rate Derivatives Markets

V.3 As announced in the Second Quarter Review of Monetary Policy of 2011-12, a Working Group comprising of market experts, officials from the Reserve Bank and other stakeholders was constituted (Chairman: Shri R. Gandhi). Based on its major recommendations, the following has been implemented:

- Reduction of the auction bid timing to 90 minutes (10:30 AM to 12:00 PM) from 120 minutes (10:30 AM to 12:30 PM);
- Conduct of the G-sec auction as a mix of both Uniform Price and Multiple Price formats;
- Change of the settlement cycle of the primary auction for T-bills from T+2 to T+1 basis;
- Re-issuance of State Development Loans by some of the State Governments;
- Migration of the secondary market reporting of OTC trades in G-Sec (outright and repo)

from PDO-NDS to NDS-OM and CROMS (Clearcorp Repo Order Matching System) respectively;

- Standardisation of OIS (Overnight Index Swap) MIBOR (Mumbai Inter Bank Offer Rate) benchmark in the IRS (Interest Rate Swap) market;
- Announcement of buy back/switching of Government Securities for ₹500 billion in Budget 2013-14 (Box V.1);
- Gradual upward revision of investment limit for FIIs in G-Sec to US$ 30 billion;
- Launch of Inflation-Indexed Bonds;
- Reduction of HTM portfolio progressively by at least 50 bps every quarter, beginning with the quarter ending June 2013, till it reaches a level of 23% of DTL.

Money Market

Revised CP Guidelines

V.4 Existing guidelines on issuance of CP were reviewed. The major changes incorporated have been the following:

- FIIs have been directed to adherence to the various provisions in force for investment in the Indian market.
- Call/put options are not permitted in CPs.
- Eligible participants shall obtain credit rating for issuance of CPs from any one of the SEBI-registered Credit Rating Agencies.
- The minimum credit rating shall be A3 (investment grade).
- The OTC trades in CP shall be settled through the NSCCL (National Securities Clearing Corporation Limited)/ ICCL (Indian Clearing Corporation Limited)/ MCX-SX-CCL (MCX-SX Clearing Corporation Limited).
- The settlement cycle for OTC trades in CP shall be either T+0 or T+1 basis.
- Buyback of CPs by issuers shall be through the secondary market and at prevailing market price.

Box V.1
Buyback/ Switches for Liability Management

Buyback/switches of Government Securities (G-Sec) are used for effective liability management by debt managers in several countries. Besides liability management, buyback/ switch operations provide flexibility for the debt management strategy, enabling it to pursue active and passive consolidation of G-Secs, and issue of G-Sec from annual maturity buckets without upper limit constraint. The active consolidation takes place when illiquid securities with small outstanding amount are swapped with one or more liquid securities, while passive consolidation occurs by reissuing securities. Switches facilitate passive consolidation by enabling on-the-run securities to be reissued with lesser upper limit constraint as redemption of such securities could be managed through swapping a part of their outstanding amount to another security of different maturity.

Another way of making buybacks cash-neutral is by undertaking such transactions intra-year (or even, inter-year), *i.e.*, buying back outstanding G-secs which are due for redemption in the same year. If buybacks of G-Secs are not backed by additional market borrowing of equivalent amount during the year, such transactions would involve net cash outgo. Buybacks with net cash outgo could be possible if either the government is running fiscal surplus or has built cash balances for such transaction. On the other hand, switches of G-secs by nature are always cash neutral as G-Sec of particular maturity is swapped with G-Sec of another maturity simultaneously.

The Reserve Bank has been pursuing a policy of passive consolidation through reissuance/ reopening of existing securities since April 1999 in order to benchmark the securities across the yield curve and improve fungibility and liquidity of securities. In 2003, a debt buyback scheme was introduced on a purely voluntary basis for banks that were in need of liquidity.

The Union Budget 2013-14 has announced buyback/ switches of G-Sec for an amount up to ₹500 billion. The objective of the proposed buyback/ switches is primarily to reduce the redemption pressure from the maturity buckets from 2014-15 to 2018-19.

- The IPAs (Issuing and Paying Agents) shall report the instances of buyback of CPs to the Reserve Bank.

Review of repo guidelines

V.5 In order to further develop the repo in corporate bond market, repo in corporate bond has now been permitted on CP, CD and NCD of less than one year of original maturity. The minimum haircut requirement in corporate debt repo has also been reduced from existing 10%/12%/15% to 7.5%/8.5%/10% for AAA/AA+/AA rated corporate bonds.

Corporate Bond Market

Ready Forward Contracts in Corporate Debt Securities- Permitting Scheduled Urban Cooperative Banks

V.6 With a view to encouraging wider participation and to enhance liquidity in repo in corporate bond market, scheduled UCBs have been permitted to participate from October 2012 in the repo market subject to adherence to conditions prescribed by the relevant department of the Reserve Bank of India.

Relaxation of investment norms to encourage participation of Standalone PDs in corporate bonds

V.7 With a view to enhancing the role of standalone PDs in corporate debt market, the following measures have been taken: (i) allow PDs a sub-limit of 50 per cent of net owned funds (NOF) for investment in corporate bonds within the overall permitted average fortnightly limit of 225 per cent of NOF as at the end of March of the preceding financial year for call /notice money market borrowing; (ii) permit PDs to invest in Tier-II bonds issued by other PDs, banks and financial institutions to the extent of 10 per cent of the investing PD's total capital funds; and (iii) permit PDs to borrow to the extent of 150 per cent of NOF as at the end of March of the preceding financial year through inter-corporate deposits.

Permission to standalone PDs for membership in SEBI approved Stock Exchanges for trading in corporate bonds

V.8 With a view to further developing the debt market in India, SCBs and standalone PDs have been allowed to become limited members of SEBI approved stock exchanges for the purpose of undertaking proprietary transactions in corporate bonds.

FOREIGN EXCHANGE MARKET

V.9 Given the volatility in the forex market, the Reserve Bank focused its attention on stemming the volatility. The policy initiatives were directed at rationalising and simplifying procedures and providing incentives to encourage foreign inflows, besides maintaining sustainability of the liberalisation process.

Foreign Investment

Foreign Direct Investment (FDI)

V.10 In order to further liberalise the regulatory framework to encourage foreign investors, the Reserve Bank took the following steps during the year 2012-13.

V.11 NBFCs (i) having foreign investment more than 75 per cent and up to 100 per cent, and (ii) with a minimum capitalisation of US$ 50 million, were allowed to set up step-down subsidiaries for specific NBFC activities, without any restriction on the number of operating subsidiaries and without bringing in additional capital. The regulation would enable even the NBFC with foreign investment of less than 100 per cent but more than 75 per cent to set up step-down subsidiaries without bringing in additional funds once minimum capitalisation requirements are met.

V.12 To further liberalise the FDI policy, 100 per cent FDI in single-brand retail, 51 per cent FDI in multi-brand retail and 49 per cent FDI in power exchanges have been permitted under the

government route. Further, foreign airlines have been allowed to invest in the capital of Indian companies and operate scheduled and non-scheduled air transport services up to the limit of 49 per cent of their paid-up capital under the government route.

V.13 In cases where non-residents (including NRIs) invest in an Indian company in compliance with the provisions of the Companies Act, 1956 by way of subscription to Memorandum of Association, the investments may be made at face value subject to their eligibility to invest under the FDI scheme. The relaxation of pricing norms would facilitate the setting up of a company as required by law.

V.14 A person who is a citizen of Pakistan or an entity incorporated in Pakistan has been permitted, with the prior approval of the Foreign Investment Promotion Board, to purchase shares and convertible debentures of an Indian company under Foreign Direct Investment (FDI) Scheme provided the Indian company receiving such FDI is not engaged or shall not engage in sectors/activities pertaining to defence, space and atomic energy and sectors/activities prohibited for foreign investment.

Foreign Portfolio Investment

V.15 The existing debt limits on investments by FIIs and long-term investors in government securities and corporate debt have been merged into two categories, *viz.*, (i) government debt limit (government securities of US$ 25 billion) and (ii) corporate debt limit (corporate debt securities of US$ 51 billion). The requirements of minimum lock-in period and residual maturity have been removed. The limit for foreign investment in Government dated securities has been enhanced by US$ 5 billion to US$ 30 billion. The enhanced limit of US$ 5 billion will be available only for investment in Government dated securities by insurance/ Endowment Funds, Foreign Central Banks.

V.16 FIIs have been permitted to use their investments in corporate bonds as collateral in the cash segment and use government securities and corporate bonds as collateral in the F&O segment. Thus, FIIs are eligible to offer government securities/ corporate bonds, cash and foreign sovereign securities with AAA ratings in both the cash and F&O segments.

V.17 FIIs have been allowed to approach any AD Category I bank to hedge their currency risk on the market value of the entire investment in equity and/ or debt in India as on a particular date, subject to terms and conditions. An FII intending to hedge the currency risk of one of its sub-account holders needs to obtain a mandate from the sub-account holder for this purpose. AD banks have been advised to verify the same along with the eligibility of the contract *vis-à-vis* the market value of the securities held in the concerned sub-account. Further, if an FII wishes to enter into a foreign exchange hedge contract for the exposure relating to that part of the securities held by it against which it has issued any PN/ODI, it must also have a mandate from the PN/ODI holder for the purpose.

V.18 It has been decided to allow limited two-way fungibility for IDRs, which is similar to the limited two-way fungibility facility available for ADRs/ GDRs.

Report of the Committee to Review the Facilities for Individuals under the Foreign Exchange Management Act (FEMA), 1999

V.19 Pursuant to the announcement in the Annual Monetary Policy Statement for 2011-12 and recognising the need to facilitate genuine foreign exchange transactions by individuals—Residents/ Non-Resident Indians (NRIs) and Persons of Indian Origin (PIOs)—under the current regulatory framework of FEMA, the Reserve Bank constituted a Committee (Chairperson: Smt. K.J. Udeshi). The Committee comprised external experts, representatives from select Authorised Dealer (AD) banks, the Foreign Exchange Dealers Association of India and the Indian Banks' Association.

V.20 The Committee made 31 recommendations and the Reserve Bank has implemented 20 of them; eight recommendations have not been implemented so far, and the remaining are being implemented in consultation with the government.

V.21 Banks can now grant fund and non-fund-based facilities (Rupee loans in India and foreign currency loans in India/ outside India) against NR(E)RA and FCNR(B) deposits to depositors or to third parties without any ceiling, subject to the usual margin requirements.

Opening of NRO accounts by individuals of Bangladeshi nationality

V.22 Authorised banks have been permitted to open NRO accounts for individual/s of Bangladeshi nationality without the approval of the Reserve Bank of India, subject to certain conditions.

Rationalisation of guidelines on position limits of ADs

Guidelines on NOOPL and AGL

V.23 According to the new guidelines, the Net Overnight Open Position Limit (NOOPL) may be fixed by the bank's Board and communicated to the Reserve Bank immediately. However, such limits should not exceed 25 per cent of the total capital (Tier I and Tier II capital) of the bank.

V.24 Further, for the present, it has been decided to withdraw the restrictions placed on open position limit of the Authorised Dealers involving Rupee as one of the currencies, (on both overnight and intra-day open positions).

V.25 The following instructions, however, continue to be effective. The positions in the exchanges (both futures and options) cannot be netted/ offset by undertaking positions in the OTC market and *vice versa*. The positions initiated in the exchanges shall be liquidated/ closed in the exchanges only.

V.26 The position limit for the trading member AD Category I bank in the exchanges for trading currency futures and options shall be US$100 million or 15 per cent of the outstanding open interest, whichever is lower. Further, AD Category – I banks have now been advised not to carry out any proprietary trading in the currency futures / exchange traded currency options markets. Transaction by the AD Category – I banks in the Currency Futures markets will have to be necessarily on behalf of their clients.

Off-shore exposures

V.27 For banks with overseas presence, the off-shore exposures should be calculated on a standalone basis as per the above method and should not be netted with onshore exposures. The aggregate limit (on-shore plus off-shore) may be termed the Net Overnight Open Position (NOOP) and will be subject to capital charge. The accumulated surplus of foreign branches need not be reckoned for calculation of the open position.

Aggregate Gap Limit (AGL)

V.28 As per the new guidelines, the AGL may be fixed by the Boards of the respective banks and communicated to the Reserve Bank immediately. However, such limits should not exceed 6 times the total capital (Tier I and Tier II capital) of the bank.

V.29 Authorised Dealers that have instituted superior measures such as tenor-wise PV01 limits and VaR to aggregate foreign exchange gap risks are allowed to fix their own PV01 and VaR limits based on their capital, risk-bearing capacity, *etc.* in place of the AGL and communicate the same to the Reserve Bank. The procedure and calculation of the limit should be clearly documented as an internal policy and strictly adhered to.

V.30 Cost-reduction structures have been allowed for hedging the exchange rate risk arising out of foreign currency loans availed of domestically against FCNR (B) deposits.

V.31 The facility of cancellation and rebooking is not permitted for forward contracts, involving Rupee

as one of the currencies, booked by residents to hedge current and capital account transactions.

V.32 However, if forward contract(s) booked by residents to hedge capital account transactions for tenors greater than one year are cancelled with one AD Category I bank, they can be rebooked with another AD Category I bank, subject to the following conditions:

i) the switch is warranted by competitive rates on offer, termination of the banking relationship with the AD Category I bank with whom the contract was originally booked;

ii) the cancellation and rebooking are done simultaneously on the maturity date of the contract; and

iii) the responsibility for ensuring that the original contract has been cancelled rests with the AD Category I bank that undertakes rebooking of the contract.

V.33 On review, it was decided to extend the flexibility to switch AD Category banks in regard of rollover of contracts to all hedge transactions undertaken by residents.

Money Transfer Service Scheme (MTSS) - Revised Guidelines

V.34 The Reserve Bank has recently issued revised MTSS guidelines including the necessary KYC/ AML/ CFT measures, which will help new Indian agents to operate under MTSS. This will ensure increased competition with the objective of bringing down both the cost of remittance and time.

Exchange Earners Foreign Currency (EEFC) accounts

V.35 EEFC account holders have been permitted to retain 100 per cent of their forex earnings subject to the condition that the sum total of accruals in the account during a calendar month are converted into Rupees on or before the last day of the succeeding calendar month after adjusting for utilisation of the balances for approved purposes or forward commitments.

Technical Committee on Services/ Facilities for the Exporters

V.36 Given the importance of export sector, especially in the current scenario, the Reserve Bank constituted a Technical Committee on Services/ Facilities for the Exporters (Chairman: Shri G. Padmanabhan). The terms of reference of the Committee included, among others, reviewing the existing policies/procedures relating to bank finance for exports and suggest measures to ensure timely, adequate and hassle-free flow of credit towards working capital, capital expenditure and other requirements of the sector, and, in particular SME units. In addition, measures to simplify and rationalise the existing procedures including the documentation, matters relating to transaction cost/ transition period, to examine specifically the special needs of exporting units located in SEZ were also part of the Committee's terms of reference.

V.37 In its Report submitted in April 2013, the Committee, among others, made recommendations relating to (i) reviewing of Gold Card Scheme for extension of export credit to exporters, (ii) inclusion of export finance under the priority sector advances for scheduled commercial banks, as appropriate; (iii) raising of foreign currency loans on pool basis for extension of export credit to exporters; (iv) allowing factoring on non-recourse basis; (v) financing to units in Domestic Tariff Area (DTA) / Special Economic Zone (SEZ); (vi) denomination of export credit limit in foreign currency; and, (vii) simplification of hedging procedure.

ECB Policy

V.38 In the case of corporates under investigation, it has been decided to permit all entities to avail of ECBs under the automatic route as per the current norms, despite the pending investigations/ adjudications/ appeals by the law-enforcing agencies, without prejudice to the outcome of such investigations/ adjudications/ appeals. Accordingly, in the case of applications where the borrowing entity has indicated the pending investigations/

adjudications/ appeals, Authorised Dealers while approving the proposal should intimate the concerned agencies by endorsing a copy of the approval letter. The same procedure will be followed by the Reserve Bank while approving such proposals.

V.39 Companies in the infrastructure and manufacturing sectors were allowed to avail of ECBs to repay outstanding Rupee loan(s) availed of from the domestic banking system and/ or for fresh Rupee capital expenditure, under the approval route. The overall ceiling for such ECBs is US$10 billion. The maximum limit of ECBs that can be availed of is 75 per cent of the average foreign exchange earnings realised during the immediate past three financial years or 50 per cent of the highest foreign exchange earnings realised in any of the immediate past three financial years, whichever is higher. The maximum ECB that can be availed by an individual company or group, as a whole, under this scheme is limited to US$3 billion.

V.40 Special Purpose Vehicles (SPVs) that have completed at least one year from the date of incorporation were also brought within the ambit of the above scheme. The maximum permissible ECB that can be availed of was fixed at 50 per cent of the annual export earnings realised during the previous financial year.

V.41 Companies in the infrastructure sector were allowed to avail of trade credit up to a maximum of five years to import capital goods, subject to certain conditions.

V.42 Refinancing of bridge finance (if it is buyers'/ suppliers' credit) to import capital goods with a long-term ECB was allowed to companies in the infrastructure sector under the automatic route.

V.43 It was decided to include Indian companies in the hotel sector (with a total project cost of ₹250 crore or more), irrespective of geographic location, as eligible borrowers under this scheme. ADs may certify the project cost at the time of forwarding the ECB application to the Reserve Bank.

V.44 It was decided to enhance the ECB limit for NBFC-IFCs under the automatic route from 50 per cent of their owned funds to 75 per cent of their owned funds, including the outstanding ECBs. NBFC-IFCs desirous of availing of ECBs beyond 75 per cent of their owned funds require the approval of the Reserve Bank and will, therefore, be considered under the approval route. It was also decided to reduce the hedging requirement for currency risk from 100 per cent of their exposure to 75 per cent of their exposure.

V.45 MFIs have been permitted to raise ECBs up to US$10 million or equivalent during a financial year for permitted end-uses, under the automatic route. ECBs by MFIs/NGOs should be fully hedged. The designated AD has to ensure at the time of drawdown that the forex exposure of the borrower is fully hedged.

Scheme for FCCBs

V.46 The FCCB buyback procedure was simplified. Buy-back of FCCBs has been allowed under the approval route at a minimum discount of 5 per cent on the accreted value. The buyback/ prepayment of FCCBs which expired on March 31, 2013 will be continued till December 31, 2013 and shall stand discontinued thereafter. This is in addition to the existing measures that allow fresh ECB/FCCB under the automatic route for redemption of FCCBs and the restructuring of FCCBs under the approval route.

Low-cost affordable housing

V.47 ECBs have been allowed for low-cost affordable housing projects as a permissible end-use, under the approval route. ECBs can be availed of by reputed developers/ builders (with minimum 3 years experience) for low-cost affordable housing projects, as well as Housing Finance Companies (HFCs) with minimum NOF of ₹ 3 billion and the National Housing Bank (NHB) to finance prospective

owners of low-cost affordable housing units. An overall limit of US$ one billion each has been prescribed for such ECBs for the financial years 2013-14 and 2014-15.

Bridge finance / long-term ECB facility for 2G spectrum

V.48 The successful bidders of the upcoming 2G spectrum allocation can avail of bridge finance for making upfront payment to the Government for spectrum allocation and replace the same with a long term ECB, both under the automatic route. The successful bidders making the upfront payment for the award of 2G spectrum initially out of Rupee loans availed of from the domestic lenders would be eligible to refinance such Rupee loans with a long-term ECB, under the automatic route. The successful bidders in the 2G auction will be allowed to avail of ECB under the 'automatic route' from their ultimate parent company without any maximum ECB liability-equity ratio subject to the condition that the lender holds minimum paid-up equity of 25 per cent in the borrower company, either directly or indirectly.

Period of realisation and repatriation to India

V.49 The period of realisation and repatriation to India of the amount representing the full export value of goods or software had been enhanced from 6 months to 12 months from the date of export up to March 31, 2013. The issue has been reviewed and it has been decided, in consultation with the government, to bring down the realisation period from 12 months to 9 months from the date of export, with immediate effect, valid until September 30, 2013.

V.50 A software exporter either under STPIs or SEZs/ EPZs/ 100 per cent EOU/ DTA, whose annual turnover is at least ₹10 billion or who files at least 600 SOFTEX forms annually on an all-India basis, will be eligible to submit statements in the revised format from January 1, 2013.

Import of Gold by nominated banks/agencies

V.51 The Working Group on Gold (Chairman: Shri K.U.B. Rao) had recommended aligning gold import regulations with the rest of the imports. The bulk of the gold imported by nominated banks is on consignment basis, whereby nominated banks do not have to fund these stocks. To moderate the demand for gold for domestic use, it was decided to limit the import of gold on consignment basis by banks for meeting the genuine needs of exporters of gold jewellery. Accordingly, gold imports on Documents against Acceptance (DA) basis were not permitted. All Letters of Credit (LC) opened by nominated banks/ agencies for import of gold under all categories was only on 100 per cent cash margin basis. This was followed up on July 8 with further measures, which restricted banks to trade only on behalf of their clients in currency futures/ options market. Thereafter, on July 22, the Reserve Bank rationalised the import of gold by making it incumbent for nominated banks/ nominated agencies to ensure that at least one-fifth of every lot of import of gold is made available for the purpose of export.

"Write-off" of unrealised export bills

V.52 Earlier, exporters were given limited powers of write-off, and AD Category I banks were permitted to accede to the requests for "write-off" made by the exporters, subject to the condition, *inter alia*, that the exporter had to surrender proportionate export incentives, if availed of, in respect of the relative shipments. To simplify and liberalise the procedure and to provide greater flexibility to exporters as well as Authorised Dealer banks, the instructions have been reviewed and the following liberalisation made in the limits of "write-offs" of unrealised export bills with certain terms and conditions.

Overseas Direct Investment

V.53 Overseas Direct Investment in Pakistan by Indian parties has been permitted under the approval route from September 7, 2012.

V.54 Earlier, *Navratna* Public Sector Undertakings (PSUs), ONGC Videsh Ltd (OVL) and Oil India Ltd (OIL) were allowed to invest in overseas unincorporated entities in the oil sector (for exploration and drilling for oil and natural gas, *etc.*), which was approved by the government without any limits under the automatic route. On review, it has been decided that the facility should be extended to overseas investments in incorporated joint ventures and wholly-owned subsidiaries in the oil sector (for exploration and drilling for oil and natural gas, *etc.*) by the *Navratna* PSUs, OVL and OIL, to be approved by the government, under the automatic route.

V.55 It has been observed that eligible Indian parties are using the overseas direct investments (ODI) automatic route to set up structures that facilitate trading in currencies, securities and commodities. Further, the Reserve Bank found that such structures have started offering financial products linked to the Indian Rupee (*e.g.*, non-deliverable trades involving foreign currency, rupee exchange rates, stock indices linked to Indian market, *etc.*).

V.56 It has been clarified that any overseas entity that has equity participation directly/ indirectly should not offer such products without the specific approval of the Reserve Bank given that currently the Rupee is not fully convertible and such products could have implications for the exchange rate management of the country. Any incidence of such product facilitation would be treated as a contravention of FEMA regulations and would attract action under the relevant provisions of FEMA, 1999.

DERIVATIVES MARKET

Review of Credit Default Swap (CDS) guidelines

V.57 To encourage participation in CDS, the existing guidelines were reviewed. Some of the measures taken are: (i) in addition to listed corporate bonds, CDS has also been permitted on unlisted but rated corporate bonds even for issues other than infrastructure companies; (ii) users have been permitted to unwind their CDS bought position with original protection seller at mutually agreeable or FIMMDA price. If no agreement is reached, then unwinding has to be done with the original protection seller at FIMMDA price; and (iii) permitting CDS on securities with original maturity up to one year like Commercial Papers, Certificates of Deposit and Non-Convertible Debentures with original maturity less than one year as reference / deliverable obligations.

Standardisation of IRS contracts

V.58 To improve tradability and facilitate centralised clearing and settlement of IRS contracts in future, IRS contracts have been standardised**.** The standardisation of IRS contracts has been achieved in terms of minimum notional principal amount, tenors, trading hours, settlement calculations, *etc.* To begin with, standardisation has been made mandatory for INR Mumbai Inter Bank Offer Rate (MIBOR)-Overnight Index Swap (OIS) contracts which are most liquid. The standardisation requirement is mandatory for all IRS contracts other than client trades.

Reserve Bank synergising development and regulation agenda

V.59 The Reserve Bank has been adopting a synergetic approach to push forward both the development of the financial markets and their regulation. As part of this approach, structural rigidities are being removed for better price discovery and for increasing both the depth and width of the financial markets. Effort has been made to develop and strengthen inter-linkages between market segments, fostering competition, increasing menu choices through innovations in products and market practices. Regulatory, legal, institutional and technological infrastructure are also being strengthened for orderly market activity. With increasing sophistication and probabilities of spillovers across markets and geographies, strengthening market regulation assumes importance so that balance sheet impact of financial volatilities are limited.