

Statement on the major feedback received for draft Master Direction (MD)

Subject: Rupee Interest Rate Derivatives (IRD) Directions

1. Section 2: Definitions

Para 2.1 (xv): 'Interest rate swap' is a derivative involving exchange of a stream of agreed interest payments on a 'notional principal' during a specified period.

Feedback: Sought clarity on whether 'Interest rate swap' include currency swaps / non-deliverable swap (NDS) transactions or not.

RBI Comments: Not considered as the feedback is a request for clarification and outside the scope of this regulation. The scope of the MD extends to Rupee IRDs. Currency swaps are covered in the Master Direction - Risk Management and Inter-Bank Dealings, 2016, as amended from time to time.

2. Section 3: Eligible Participants

Para 3.2: A non-resident may undertake IRD transactions through its central treasury or its group entity, where applicable.

Feedback: The feedback requested for 'residents' to also be made eligible to undertake IRD transactions through their central treasury or group entity.

RBI Comments: Not accepted. In terms of Section 45V of the RBI Act, 1934, transactions in derivatives shall be valid if at least one of the parties to the transaction is the RBI or an entity or agency falling under RBI's regulatory purview.

3. Section 4: IRDs on Recognised Stock Exchanges

Para 4.3: A non-resident may transact in exchange-traded IRDs for hedging.

Feedback: Request to enable non-residents to buy Interest Rate Futures (IRFs).

RBI Comments: Not accepted. Non-resident participation in debt markets in the country is permitted through outright purchase of bonds (government securities or corporate bonds).

4. Section 5: Interest Rate Derivatives in the OTC Market

(a) Para 5.1 (i): Eligible market-makers include scheduled banks; Standalone Primary Dealers (SPD); NBFCs – Upper Layer; and All India Financial Institutions.

Feedback: Clarification on whether an entity, otherwise eligible to act as market-makers, can access the market as users if it is not participating as market maker.

RBI Comments: Accepted. Para 5.2 (ii) revised to clarify that an entity otherwise eligible to be a market-maker can access the IRD market as a user.

(b) Para 5.3 (i): A Market-maker may offer the forward rate agreements, interest rate swaps, European interest rate call and put options, interest rate caps and floors, and interest rate collars and reverse interest rate collars.

Feedback: Request for interest rate cap spreads and floor spreads may also be permitted to be offered to retail users.

RBI Comments: Not accepted. Interest rate cap and floor spreads are complex IRD products. In view of the same, the suggestion to permit the same to be offered to retail users has not been accepted. However, specific requests from retail users for the products can be met by a market-maker in terms of para 5.2 (ii) (i) of the Directions wherein, subject to certain conditions, a retail user can be offered products available to non-retail users for the purpose of hedging.

Para 5.3 (ii): Market-makers may offer any IRD product including interest rate swaptions to a non-retail user except leveraged derivatives and derivatives containing a derivative instrument as underlying.

Feedback: The feedback requests for permitting (i) callable and cancellable swaps; (ii) all derivatives containing a derivative instrument as underlying; (iii) bond forward contracts; and (iv) IRDs on the RBI Policy Repo (Repo) rate.

RBI Comments

(i) and (ii) Not accepted: At present, the only derivative on derivative IRD product that is permitted is swaption, in which there is limited volumes and participation. Accordingly, the suggestion to expand the suite of derivatives with derivatives as underlying has not been considered at this stage.

(iii) Not considered as it is already covered. Bond forward transactions are covered under the Reserve Bank of India (Forward Contracts in Government Securities) Directions, 2025 dated February 21, 2025. A clarification has been included in para 1 of the MD.

(iv) Not accepted. The repo rate is not a market-determined benchmark. Exposures to the repo rate can be hedged by market participants using interest

rate derivatives based on rates/benchmarks set in the call money market, which is the market for the operating target for monetary policy.

(c) Para 5.3 (iv): Scheduled Commercial Banks (SCBs) and SPDs authorized under section 10(1) of FEMA, 1999, may undertake IRD transactions on Modified Mumbai Interbank Forward Outright Rate (MMIFOR) among themselves.

Feedback: The feedback requested MMIFOR-based IRDs be offered to users.

RBI Comments: Accepted. Para 5.3 (iv) has been modified to indicate that MMIFOR-based IRDs can be offered to users for the purpose of hedging.

(d) Para 5.5 (a) (iii): IRD transactions undertaken globally by the offshore related parties of the market-maker in India shall be reported individually by either the market-maker in India or its related party(ies) to the Trade Repository (TR) of Clearing Corporation of India Ltd. (CCIL).

Feedback: The feedback highlighted the difficulties, including associated operational challenges, in complying with the requirement of reporting of IRD transaction undertaken globally by related parties of market-makers.

RBI Comments: Not accepted. Reporting of INR derivative transactions undertaken by entities licensed / authorised in India and their related parties is important for enhancing transparency and efficient price discovery in the Rupee IRD market. Certain standalone primary dealers are already complying with similar reporting requirements. Hence, no major challenges in such reporting are envisaged. Any operational concerns in this regard have further been addressed through provisions of adequate flexibilities viz., staggered phasing in of requirements, exclusion of trades below a particular threshold.

(e) Para 5.5 (b): IRD transactions, including FCS-IRDs, by non-residents with market-makers undertaken for purposes other than hedging, shall be subject to an overall limit - the Price Value of a Basis Point (PVBP) of all outstanding IRD positions, including FCS-IRD positions shall not exceed ₹1,000 crore (PVBP cap).

Feedback: The feedback indicates that the imposition of a PVBP cap on each non-resident counterparty imposes significant operational burden and requests that intra-group transactions and offshore affiliates of market-makers be excluded.

RBI comments: Not considered as the concern is already addressed. The PVBP cap is applicable for all non-residents in the aggregate and not for an individual non-resident counterparty. The cap for the system is computed by CCIL and published at the end of every business day. The limit is not applicable for transactions undertaken for hedging or for transactions undertaken offshore in which both counterparties are non-residents.

(f) Para 5.6 (ii): A market-maker, deciding to undertake an OTC IRD transaction through a broker, shall ensure that the broker has been accredited by Fixed Income Money Market and Derivatives Association of India (FIMMDA).

Feedback: The feedback suggests that domestic market-maker banks may be permitted to deal with offshore counterparties through an offshore broker, without the need for such broker to be accredited by FIMMDA.

RBI Comments: Not considered as the suggestion is outside the scope of these regulations. The Directions are not applicable to offshore brokers.

(g) Para 5.7 (a) (i): A market-maker shall report all OTC IRD transactions undertaken by it to the TR of CCIL as per the following timelines within 30 minutes of the transactions. Structured derivative transactions can be reported before closure of the TR for the day while FCS-IRD transactions with non-residents can be reported before 12:00 noon of the following business day.

Feedback: The feedback requested that the reporting timelines be aligned with international practices of T+2.

RBI Comments: Not accepted. Reporting timelines are aligned to international best practices (reporting timelines globally vary from 15 minutes to T+2) and are already being adhered to by market participants. As such, these are not new requirements. Also, the requirements include flexibilities for transactions undertaken with non-residents and reporting of structured derivatives.