Keynote address by Shri Sanjay Malhotra, Governor

Reserve Bank of India

at the 24th FIMMDA-PDAI Annual conference, Bali, April 18, 2025

It is a pleasure to be here at the 24th FIMMDA-PDAI Annual Conference in Bali, an island that shares a deep and rich heritage with India, marked by centuries of cultural and commercial ties.

2. The past year has been eventful for financial markets globally. The initial optimism that global central banks were poised for synchronised easing of interest rates, seemingly reaching the final stage in their battle against high inflation, gave way to unprecedented uncertainty in recent months. In this backdrop, this conference provides an excellent opportunity for a fruitful exchange of ideas and vibrant discussions among financial market participants. I thank the organisers FIMMDA and PDAI for giving me this opportunity to participate in the conference and share my thoughts.

3. The Indian economy and the financial markets have demonstrated remarkable resilience while they are not immune to the vagaries of an uncertain and volatile global environment. As I mentioned in my statement post the recent monetary policy announcement, our domestic growth-inflation balance has improved significantly. There has been a decisive improvement in headline inflation which is projected to remain aligned to the target of 4 per cent in FY26. Global uncertainties and weather disturbances, however, pose risks to the inflation outlook. Even though we have projected a somewhat lower real GDP growth for FY26 at 6.5 per cent, India is still the fastest growing economy. Yet, it is much below what we aspire for. We have reduced repo rates twice and provided sufficient liquidity. In view of the rapidly evolving situation, especially on the global front, we are continuously monitoring and assessing the economic outlook. We will be agile and proactive in our actions on the policy front, as always.

4. Coming to the Indian financial markets, all market segments including FX, G-sec, Money Markets, have largely remained stable. While the Rupee came under a bit of pressure a few months ago, it has fared better thereafter and regained some lost ground. Equity markets experienced significant correction, as capital outflows accelerated, a trend seen in most emerging markets. The government securities market has however, remained rock-steady throughout the year. The gross market borrowings of the central and state governments, totalling ₹24.7 lakh crore in FY 2024-25, sailed through smoothly. The cost of borrowing for the central government came down by 28 basis points to 6.96 per cent in FY25 from 7.24 per cent in FY24. The secondary market in g-secs continued to be deep and active, partly aided by India's inclusion in global bond indices.

5. Meanwhile, we stand at the threshold of an exciting phase of transformation in India – a transformation that has faced many challenges, but is imbued with exciting opportunities – our demographic dividend, our skilled manpower and our ability to develop and harness technology to transform society. Against this backdrop, the theme of this year's conference — "India's Financial Markets: Navigating Through Shifting Tides" is timely and relevant.

Financial markets – looking back and forging ahead

6. If India is to navigate the shifting tides and fulfil its aspirations, financial markets will have to play a crucial role. As the marketplace for raising capital and trading

financial assets, financial markets are key enablers of economic growth. Financial markets have existed for centuries. They have evolved over time. The complexities of financial markets have baffled humanity for centuries with one of history's greatest minds, Sir Isaac Newton, after losing his fortune in the South Sea Bubble, famously lamenting that "*I can calculate the motions of the heavenly bodies, but not the madness of people*."[1] Integrity of operations and the fostering of trust are fundamental to any financial market. Indeed, ensuring these elements is one of the primary objectives of financial market regulation. While, we realise as Benjamin Graham said that in the short run, market is a voting machine, but in the long run, we have to ensure that it is a weighing machine.

7. In India, financial markets have evolved within a regulated framework, adapting to changing regulatory philosophies and approaches. Up until the last decade of the 20th century, India's financial markets were shaped by a conservative macro-financial stance. From the 1990s, the foundation of robust and well-functioning financial markets started being built. Interest rates were deregulated. The exchange rate was freed. The Rupee became fully convertible on the current account. The capital account was progressively liberalised. In the years that followed, even as the financial markets in India developed, the overarching approach was driven by the priorities of macroeconomic and financial stability. In recent years, however, our growing and more interconnected economy placed increasing demands on financial markets.

8. Against this backdrop, the Reserve Bank's efforts in recent years to develop financial markets have focused on supporting the needs of an aspirational economy. I won't go into the details, as the audience here is well-versed in the various regulatory changes that have been brought about in recent years. Instead, I will focus on what we have accomplished and the work that still lies ahead.

Financial markets: Recent trends

9. Over the past few years, we have witnessed significant developments that have transformed our markets into a dynamic and resilient force. Let me give a few statistics to illustrate:

- 80 per cent increase in average daily volumes in the overnight money markets from about ₹3 lakh crore in 2020 to over ₹5.4 lakh crore in 2024;
- 40 per cent increase in average daily volumes in the g-secs markets to ₹66,000 crore over the same period;
- Almost doubling of average daily turnover in the forex market from 32 billion USD in 2020 to 60 billion USD in 2024;
- 622 per cent increase in notional outstanding interest rate derivatives from around ₹18 lakh crore in 2015 to over ₹130 lakh crore at the end of FY25;
- 2,233 per cent increase in average daily client volumes in MIBOR OIS (the most liquid derivative product) from approximately ₹600 crore in 2015 to nearly ₹14,000 crore in 2024;
- 73 per cent growth in average daily volumes in FX forwards and swaps from US$ 15 billion to over US$ 26 billion over the last decade; and

[1] Brunnermeier, M., and Reis, R. (2023). "A Crash Course on Crises: Macroeconomic Concepts for Run-ups, Collapses, and Recoveries".

- Daily volumes of about US$ 7 billion in Non-deliverable forward (NDF) trades by domestic banks in recent months compared to negligible volumes on June 1, 2020, when it was first permitted.

10. The number of participants in the markets have also increased concomitantly:

- Several standalone primary dealers have been granted Authorised Dealer licences. The set of eligible market-makers has been expanded for the interest rate and credit derivative markets though interest here appears muted.

- In the last decade, the number of clients registered with the CCIL Trade Repository for interest rate derivatives has increased by about 3,233 per cent from about 300 to nearly 10,000 and for foreign exchange derivatives by 3,854 per cent from 2,200 to about 87,000. Of course, not all clients will be active participants.

- Non-resident participation has also increased in the g-sec market especially after the inclusion in global bond indices. Foreigners now hold 3.2 per cent of g-secs as compared to 1.7 per cent in August 2023, ahead of the first announcement of the inclusion. Non-resident participation in the derivative markets has also been growing.

11. There have been significant developments in financial market infrastructure as well. Repo and government securities markets predominantly function on electronic platforms, and are centrally cleared. Most forex spot and forward transactions as well as most MIBOR and Modified MIFOR based interest rate swaps also trade on electronic platforms and are centrally cleared. All OTC derivatives are reported to a trade repository.

12. There is also growing product diversity. While plain-vanilla products dominate the derivative markets, there has been a noticeable rise in customized products in both interest rate and forex derivatives, tailored to meet the diverse hedging needs of various stakeholders. Recently, forward contracts in government securities have also been permitted. The approach to structured products, particularly those with asymmetric payoffs, has remained cautious and responsible. We plan to continue the same approach.

13. We have made significant strides in the development of financial markets in our country. Motivated to fulfil the nation's evolving needs and aspirations and guided by learnings from successive crises, our markets have matured and advanced. Our market infrastructure is state-of-the-art. The levels of transparency are at par with the best in the world. Markets for government securities, foreign exchange, and key derivative products are highly liquid, relative to most peer economies and even to many advanced countries. With recent regulatory reforms, we have seen greater product and participant diversity, and the onshore and offshore markets have become tightly integrated.

14. These advancements are a testament to your dedication, innovation, and collaborative efforts. I congratulate all of you for your contributions in this joint endeavour. Today, we have vibrant financial markets which not only continue to support India's economic growth but also inspire global confidence. But there is more to be done. Let me briefly outline my thoughts on some of these areas.

Issues and concerns

The Government securities market

15. The g-sec market is perceived as one of the most liquid markets globally as evidenced by low bid-ask spreads and low impact cost. However, the turnover ratio (measured as the annual turnover to outstanding stock of securities) of dated government securities has remained modest at just over one (1). If the less liquid state government securities (SGSs) are included, the ratio falls to below one (1). Liquidity continues to remain concentrated in few securities, thinning out for longer maturities. Secondary market trading is dominated by banks and primary dealers with many large institutional investors remaining “buy and hold” investors. Of the 3,000 plus institutional investors in g-secs, the top ten participants contributed a third of the overall turnover during 2024.

16. One continuing endeavour of the Reserve Bank has been to increase retail participation in the g-sec market. The launch of ‘RBI Retail Direct’ facility in November 2021, was one initiative in this direction. Recently, a mobile app for Retail Direct has been introduced. RBI also recently permitted retail clients of SEBI-registered non-bank stockbrokers to access NDS-OM. All of this makes it imperative to ensure that sufficient secondary market liquidity is available to such investors to be able to participate in the market at reasonable prices. Liquidity and pricing also need to improve for participants like cooperative banks, pension and provident funds with smaller deal sizes. Banks and primary dealers may need to play a much more active role to this end.

The Money Markets

17. The money markets in the country remain almost entirely overnight. Despite many efforts over the years to develop a term money market, for example by removing statutory pre-emptions on inter-bank liabilities and by conducting term repos/reverse repos of varying maturities, term markets remain missing especially in the 3 days to three months segment. Though alternatives such as overnight indexed swap rates and yields on treasury bills are being used, there remains a need for the development of a risk-free term structure to act as a benchmark for pricing of interest rate products, including loans.

18. The dwindling liquidity in the call money market – whose rate is the operating target for monetary policy – also requires attention. This market is also critical for the robustness of the MIBOR, the benchmark for the interest rate derivative market. Also of concern are the asymmetries which arise on occasions between different money market rates– the rate at which RBI provides liquidity, the call money rate, the market repo rate and TREPS rate. This calls for more proactive functioning by banks – the entities with sole access to RBI’s liquidity facilities, the call money market and the repo markets – to ensure that RBI’s liquidity measures are promptly and seamlessly transmitted to the broader market.

The FX markets

19. The foreign exchange markets are reasonably liquid with narrow bid-ask spreads. There is growing transparency in this market. All FX derivatives are reported to the Trade Repository and reporting of cash, tom and spot transactions has commenced[2]. A bulk of FX spot transactions are traded on electronic trading platforms (ETPs). Authorised trading platforms are also available for forward transactions but there appears to be a preference for such trades to take place bilaterally. Trading on

[2] In terms of notifications RBI/2024-25/89/FMRD.MIOD.07/02.05.002/2024-25 dated November 8, 2024 , on “Reporting of Foreign Exchange Transactions to Trade Repository”, Authorised Dealers have started to report all inter-bank FX contracts undertaken by them to the Trade Repository of CCIL with effect from February 10, 2025.

ETPs enhances transparency and market efficiency. We would like to see an increasing share of transactions done on ETPs.

20. In January 2020, banks were permitted to deal in FX beyond onshore market hours. While volumes are not significant, we do see banks transacting both prior to and post onshore market hours. Such trading, however, is largely confined to the period immediately before and after domestic FX market hours, suggesting that we are still some distance away from a true 24*5 market.

21. Fair treatment of customers and transparency in forex pricing for the smaller and less sophisticated customers continues to engage our attention. Much more can be and needs to be done here. Divergence in pricing in FX markets for the small and large customers are far wider than what can be justified by operational considerations. FX-Retail, a transparent platform for undertaking FX transactions, has witnessed a lukewarm response and our feedback is that this is largely due to the reluctance of banks to offer the platform to their customers. There are regulations in place to ensure transparency in pricing for retail customers including a mandate for disclosing the mid-market or interbank rate to customers. As an industry, there is a need for market-makers to introspect and assess in what ways they can effectively deliver on these regulatory and fiduciary mandates.

22. The Reserve Bank has recently announced that access to FX Retail will also be provided through the Bharat Connect platform. In the first phase, a pilot to facilitate purchase of US dollars by individuals is planned. Subsequently, its scope will be expanded based on the experience gained. I would appeal to all the financial market participants including Authorised Dealers to extend their full cooperation in ensuring that the pilot is implemented smoothly and successfully.

23. We also continue to see banking channels being used for activities on unauthorized FX trading platforms. This calls for greater vigilance and stronger efforts by banks to create awareness among their customers about the perils of using such platforms[3].

The derivative markets

24. The size of the derivatives market, while growing, remains small in absolute terms and relative to our GDP. There are other issues apart from that of size. The liquidity in the interest rate derivative markets, for example, is limited to one or two products. Despite many efforts over the years, the interest rate futures market or the credit derivative market are yet to pick up. Market-making remains confined to banks, both in FX and interest rate derivatives. While this is not surprising, given that the Indian financial system is bank-dominated, the presence of a wider variety of players has the potential to enhance market depth, add to the diversity of views and foster greater competition and efficiency. Meanwhile, developments elsewhere, including the need for more proactive management of risks by different stakeholders, have made the further development of these markets an imperative.

25. In this context, you are aware that an increasing number of bank loans are getting priced off external benchmarks, mostly the policy repo rate. The swap market based on an overnight rate may not be best suited to hedge such exposures especially as it is also used to express views on expected monetary policy movements. As was observed by the Committee on the MIBOR Benchmark, most developed countries have at least two major benchmarks – one used to take a view on the future

[3] The Reserve Bank, on its part, has been regularly updating the Alert List of unauthorized forex trading platforms and conducting awareness campaigns to educate users.

movements of the policy rate and another used by the real sector to hedge risks. At least, a market for basis swap instruments needs to develop to manage the associated basis risks. The Committee also recommended the development of a Secured Overnight Rupee Rate (SORR) based on the secured overnight market. I understand that the Financial Benchmarks India Limited (FBIL) is developing the benchmark. Going forward, derivatives based on the SORR will also need to be developed.

Concluding remarks

26. Today, financial markets stand at a cusp of transformation between global and domestic headwinds, unprecedented opportunities and growing public expectations. When transformations such as these take place, there are many moving parts which need to come together like the pieces of a jigsaw and many stakeholders who have critical roles to play. FIMMDA and PDAI have been playing critical roles in fostering the development of Indian financial markets. In many ways though not formally so, FIMMDA has functioned as a self-regulatory organization (SRO) in the fixed income and money markets of the country. I am aware that FIMMDA has applied for recognition as an SRO under the framework for the recognition of the SROs in financial markets issued by RBI. While we are examining the request, we expect to see FIMMDA and PDAI continue partnering with us in further developing financial markets in India.

27. As India forges ahead to take its rightful place in the emerging global order, financial markets have a crucial role to play. Financial markets will need to facilitate efficient and cost-effective funding for realising the aspirations of the country. They will need to enable the economic agents to manage their risks more efficiently amidst shifting global and domestic tides. They will also need to ensure fairness to every stakeholder as they chart ahead and make themselves robust, resilient, and future-ready.

28. As I conclude, I invite you to reflect on the intricate and dynamic wheels of finance that shape not only our markets but the very foundation of India's economy. These wheels, powered by transparency, trust, and innovation, require each cog — every participant in this room — to perform its role with purpose and integrity. Let us move forward with a shared commitment to manage risks wisely, foster growth responsibly, and ensure the integrity of our financial markets.

Thank you.