

Respected Shri. Kanungo, Deputy Governor, The Reserve Bank of India, Respected Shri VASILY PODZYSHEV, Dy Governor, The Bank of Russia, Respected Shri Rajeshwar Rao Executive Director, RBI, Respected Shri Mahalingam, Whole Time Member, SEBI, Respected Shri Jayasimhan, CGM Investments of IRDA, Respected Panelists, Respected Speakers, my co-Directors of FIMMDA & PDAI, Special Invitees, Delegates, Ladies and Gentlemen

On behalf of the directors of FIMMDA, I am pleased to welcome you all to the 20th Annual FIMMDA-PDAI Conference being held here in the beautiful city of Moscow. I wish to thank the Reserve Bank of India for helping and encouraging us to make this conference possible and in also being present in the conference in large numbers. Without their blessing it would not have been possible to have this conference here with the kind of representation that we have from various stakeholders.

**This conference is also unique in two aspects. First**, it is the first time that we have had a **confluence of all the key regulators** of our financial markets attending this conference. And **second**, is the Country in which we are today assembled. **India and Russia** have been long standing allies and enjoy a warm and cordial bilateral relationship. Both the countries have many similarities, not least is the **currency exchange rate** that is close to parity. We both enjoy a rich and diverse **cultural heritage**. Our economies are also similar in structure as **private consumption and services** contribute the lion's share of output for both. Both countries have an **inflation targeting regime**, with India on an average targeting CPI of ~4% as a midpoint of the 2-6% range and the Russian Central Bank also having a 4% inflation target. Our countries have worked together in various spheres, especially **defense, trade, civil nuclear energy and hydrocarbons** among others. Our **honorable Prime Minister** is due to visit Russia later this week and this will further enhance the framework of bilateral cooperation between our nations. We are very happy to have this conference amongst a lot of camaraderie and friendship.

This conference is being held against a **global backdrop**, which has become increasingly challenging for global trade. Decades of engagement between countries fostering significant globalization are now being rewritten and conventional wisdom is being challenged at every turn. There seems to be a significant move away from this very globalisation through the ongoing trade wars between US & China, between South Korea & Japan and other political disruptions such as Brexit,. There is no doubt that globalization has fostered a period of high growth, low inflation, significant technological progress, more prosperity etc even as it has had an unintended consequence of a sharp increase in global income inequality. But we will never know the counterfactual - as to whether the rising inequality was due to the roots of globalisation or whether it was an inevitable process in growth.

Regarding this global backdrop of retreating from globalisation, let me put forward to you a very **eloquent and appropriate quote** by none other than our own Shri Kanungo in one of his recent speeches and I quote. ***“True, the process of globalisation has brought problems and discontent in its wake, but wisdom lies in addressing them rather than disbanding the process.”*** These very words give us the heart to be more positive and look forward to a global markets that integrates more, converges better and increase the linkages between various geographies and various products even as global trade finds ways to retreat away from globalisation..

**That is why the theme of our conference is also ably titled - Indian Financial Markets - Convergence with Global Markets**

- My speech today will be in 3 parts - first - a quick recap of the past as to what happened in the last financial year, second - the challenges that we face going forward, and lastly the opportunities that we all have going forward.

### **Part I - A recount of the past**

1. Financial markets - It has been the custom for the Chairman speech to include significant developments in the financial markets of the past year. But I would like to deviate from the same this year. Your Chairman knows too well as to how frustrating it is to sit through a

lecture about the past, that too when the room is full of traders who have actually gone through the volatilities and mood swings of the market. It is also especially frustrating to get reminded of the days in the financial year when we actually got caught on the wrong side of the tweets that move global markets nowadays. Hence let me sidestep that part and simply focus on the activities of FIMMDA

2. The entire team at FIMMDA has been focussed on the various activities that happen regularly as the backbone for the smooth functioning of the financial markets. I will enumerate a few today
  - a. **Dispute Resolution Committee:** A 14 member committee was constituted and is operating as the DRC from 1st October 2017. Between 1st April 2018 till 31st March 2019, the DRC has received about 18 references and reversed erroneous/off-market deals. The amount of loss averted was Rs. 25 Crores.
  - b. **Consultations with RBI & Ministry of Finance :** RBI has held pre-policy consultations with FIMMDA and PDAI regularly to know our views on the market and economy. In addition, the Finance Ministry has held consultations with teams from FIMMDA on many occasions to know our views and suggestions for market development.
  - c. **Interest Rate Futures & Options :** We continue to be active in deciding the new IRF contracts that were announced during the year. FIMMDA had called for two open member meetings and formed a core technical committee consisting of 8 members for the IR options. The points raised by the committee were referred to RBI . The Core group also drafted some templates for Swaptions, and the same will be finalised by the group. Meanwhile, Exchanges ( NSE) have written to RBI about their intention to launch Options on the most liquid bonds, which was agreed upon by our core group and we informed RBI accordingly. We understand that RBI has advised Exchanges giving approval to commence options.
  - d. **Certificates of deposits:** FIMMDA was also involved in revising the operational guidelines on Certificates of Deposits and

circulated draft guidelines to the members for their views/suggestions. The guidelines will be shortly finalized and circulated to the market.

- e. **Financial Benchmarks India Pvt Ltd:** FBIL added more benchmarks during the course of this financial year by publishing Forward Premia Curve, MIFOR as well as the USD-INR Reference Rate.
- f. **Valuation of G- Securities and SDLs:** We continue to be the calculating agent for the G Sec and SDL valuations. Meanwhile, the methodology of SDL valuation has undergone change after continuous exchange of ideas with members and brainstorming at FBIL. The new methodology as approved by FBIL and RBI is put in place wef 15th April 2019.
- g. **Training programmes:** During April'18 till 31st March 2019, FIMMDA conducted 13 training programmes benefitting 264 participants from member as well as non-member institutions. The courses were conducted by M/s Dun & Broad street as well as M/s Deloitte .
- h. **Valuation of Corporate Bonds:** Presently, FIMMDA is publishing the combined traded data of Corporate bonds at all Exchanges every day. Spread matrix is also published twice every month as per polls received from 21 submitters. In response to a demand to publish daily matrix, based on the elaborate study of 2 years traded data and discussions with market participants, a methodology was evolved to publish spread matrix for days falling in between two polled matrices. The same was published on test basis for about 2 months and on the basis of feedback, approvals from Board etc, started publication of the daily matrix wef 17th April 2018. FIMMDA also worked towards publication of Securities level valuations for Corporate Bonds on a daily basis. The same is being published on test basis wef April 2018 .The Security level valuations methodology is being discussed with the market participants to make it more robust, and subject to the readiness of the market participants , we wish to implement the same immediately.

- i. **Way forward** : In addition to the regular activities, the Board of FIMMDA regularly meets at least 6 times in a year. The board will also shortly deliberate the way forward for FIMMDA to undertake more activities as well as enhance their presence in the markets.
- j. **Minutes of the Conference** : The minutes of all the discussions during the conference will also be forwarded to the regulators for their deliberations.

**Let me now come to the second part of my speech - The Challenges that the financial community and the banking system face and need to manage**

- This is that time of the year when we need to look ahead. There are a number of significant challenges for treasuries of banks as management of risks undergoes significant changes.
- **Let me elaborate on Four broad challenges** that we need to be ready to face
  - Libor Cessation
  - Capital Guidelines
  - Margining guidelines
  - Central clearing and Client clearing
- **LIBOR Cessation**

One large and significant development that is expected to impact all banks is the massive change in the most prominent index or benchmark for Interest rate swaps - LIBOR, its cessation and the alternatives surrounding the same. Various Jurisdictions and Regulators are working on an alternative Risk Free Rate (RFR) as replacement for LIBOR for new transactions. USD Libor is the most liquid and widely traded and is expected to be replaced with SOFR - secured overnight financing rate. Similarly, SONIA for GBP LIBOR, ESTER for Euribor, TONAR for JPY LIBOR are the respective RFRs. It is expected that for legacy derivative transactions linked to LIBOR, there would be an industry wide fall back mechanism. Based on the current developments, the fall back mechanism would involve an addition of spread to a compounded

overnight risk free rate (RFR) to arrive at a term RFR. It is important that the language and methodology of fall back mechanism applicable to LIBOR be similar for both loans and their derivative hedges to avoid basis risks. In our markets, we would need to plan for the fall back and replacement of MIFOR which is a derived index from LIBOR for legacy transactions.

- **Capital Guidelines**

Many changes are also happening on the Capital / Risk Management frameworks, some are positive while some could be challenging.

The Fundamental Review of the Trading Book (FRTB) which is a comprehensive suite of capital rules developed by the Basel Committee on Banking Supervision (BCBS) as part of Basel III, will be applied to banks trading activities. The date of implementation internationally is January 1, 2022. Capital requirements for the trading book are expected to increase by 40 to 50%. RBI is expected to issue circular on FRTB.

RBI meanwhile has issued a draft guideline on Interest Rate Risk in the Banking Book (IRRBB), which measures the risk to Banks capital and earnings from movements in interest rates. The thresholds for determining a bank as an outlier has been tightened from 20% erosion of net worth at a 200 basis points to 15% erosion of T1 capital funds with a 400 basis point movement.

On the credit risk front, the Current Exposure Method (CEM), that measures exposure to a counterparty is proposed to be replaced by SACCR. Though RBI has issued the final guidelines; the implementation has been deferred without a specific timeline in view of pending implementation at the international jurisdictions and proposed amendments in netting laws in India. RWA exposure is expected to reduce if netting is enabled by law.

Indian Banks are currently using the standard approach for CVA for CVA capital computations. This framework is proposed to change internationally from January 1, 2022. The existing CVA standard incorporates only

variability in CVA arising from change in credit spreads and not other market risk factors such interest rate & forex movements. The proposed standard seeks to address the above issue. While RBI has not issued any draft guidelines on this yet, expect this also to come up to bring our capital framework in line with global standards.

- **Margining guidelines**

Another important structural change has been margining, both variation margin and initial margin of non-centrally cleared derivatives. While many Indian Banks have executed variation margin CSA, the timeline for implementing initial margining for financial institutions rules depends on the average aggregate notional amount (AANA) of non-cleared derivatives. It is expected that many Indian Banks will have to post initial margin from September 2020. We expect RBI to issue the relevant guidelines on Margining to facilitate this. While the regulator will issue the margining guidelines, the market needs to build adequate infrastructure for handling of initial margins, developing the technical capabilities, software and risk management techniques to be fully prepared for this.

- **Centralised Clearing and Client clearing**

As you all know, after the Global Financial Crisis, the G-20 countries have committed to strengthen the Over the Counter Derivatives (OTC) Markets. These include reporting of OTC derivatives to trade repositories, OTC derivatives traded on designated electronic platforms / exchanges and cleared through Central Counterparties (CCPs) for standard trades, and bilateral margining for the rest. Globally, there have been structural changes in OTC derivatives markets on account of these commitments. Central clearing has been one of the most important structural changes in the OTC derivatives market. This works in tandem with trade compression, elimination of economically redundant positions resulting in reduction of market values. In India, we have seen the introduction of guaranteed settlement for Rupee Derivatives. OIS Swaps and MIFOR swaps for interbank participants can now be centrally cleared through CCIL. Further, there is an anonymous platform which is facilitating this. The next step will be in terms of

opening this to other participants through a client clearing model, which is offered globally. This will fundamentally change the nature of credit risk in derivative instruments and can have far reaching effects.

### **Let me now step back and look at the Opportunities going forward**

Most of what I said above are challenges for the banking system in general from a risk management and capital allocation perspective. Let me take up the opportunities that we have to develop financial markets in our country as we go forward.

- **Rupee CDS** : The first is developing an active CDS market. The regulator has allowed **Rupee CDS** to trade in the market but we are yet to see traction in the same. We have the MOF also showing great keenness to energize this market.
  - This is one product that everyone wants and feels it will be useful but no one is willing to trade it.
  - The problems are with relation to absence of netting benefit, MFs only allowed to buy protection against underlying and cannot sell , end users not having a purchase position in CDS without an eligible underlying and last but not the least compulsory unwind of the CDS when bond is sold
- **Rupee IRF** - The second is to have an active IRF market in the true sense of the product. If you look at our history we have had two aborted failed attempts in IRF - the first was ZCB based cash settlement to then physical settlement of a security from the eligible basket. It was later that we created history by being the only fixed income market in the world to have single bond futures. But there are deficiencies in this product. We need a single contract that lives forever and not just for the life of the bond. We need a future on interest rates and not a future on a bond. The opportunity is to look at whether we can develop something similar to developed markets.
- **Rupee MMF** - This is not really path breaking product but could be very useful if lending against external benchmarks kicks off and we have both lending rates and deposit rates benchmarked to say repo rates or

some other benchmark and if we have a future trading on that benchmark it will provide ample opportunities for banks and corporates to hedge their immediate next fixings. Unfortunately there is no trading in it currently so for us in the markets it is an opportunity going forward.

- **Some of the other products that we don't have but that can be very useful are** Swap Futures, Spread trades and forward starting swaps. The ability to trade on the OIS curve on notional neutral basis as against a PV neutral is a development that we need especially when we have opened the OIS market to foreigners who are looking for those kind of products to trade. We need interbank to have an active markets that trade so that banks that face foreign entities can lay off their risk easily.
- **Strengthening the domestic participants** - A lot of regulations have been focussing on giving liberal limits for foreign entities. We need to ensure that we have an enabling environment for domestic players like MFs, Insurance Cos and Pension Funds to use these products more liberally.

## **Conclusion**

Let me conclude by saying that we have a range of topics that we will be discussing during the day that are topical, contextual and current. We need all of you to actively participate in the discussions. Utilise the conference as a knowledge builder for yourself as well as in imparting and sharing the knowledge that each one of you have. There are substantial number of polls that we are conducting both pre panel as well as live during the panel. Please download the FIMMDA-PDAI app right now if you have not already. It is an excellent opportunity to get market feedback. By all means enjoy the beautiful city of Moscow - enjoy its weather, experience the Russian culture and the events that we have organised for you. Take back sweet memories of this conference but also remember that as a market we have lots to do and each one of us will have to take the responsibility of making this market the most liquid, vibrant and sophisticated market amongst all EMs

**Thank you**