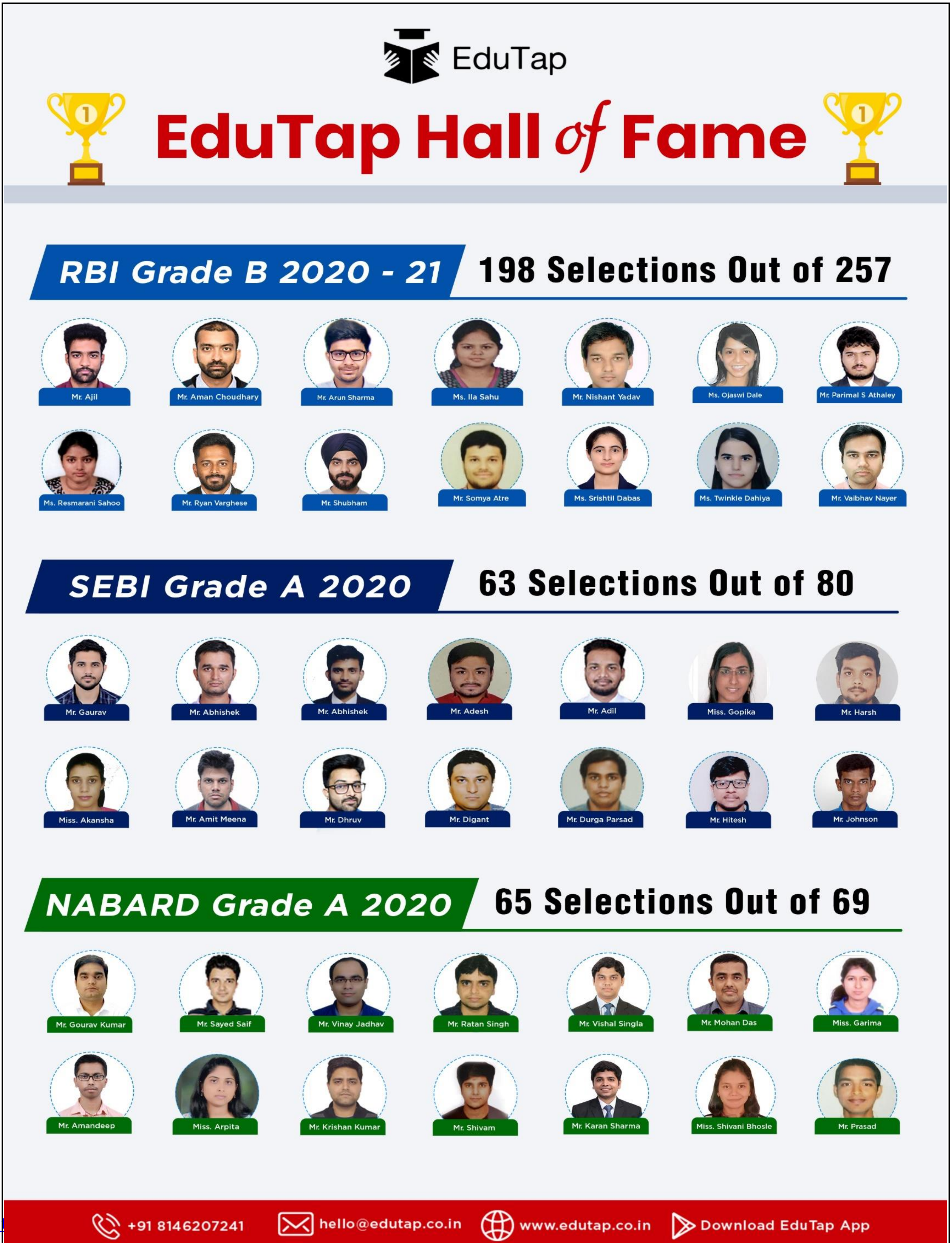
EduTap

SUMMARY SHEET

Forex Market


EduTap
EduTap Hall of Fame
RBI Grade B 2020 - 21
198 Selections Out of 257
Mr. Ajil
Mr. Aman Choudhary
Mr. Arun Sharma
Ms. Ila Sahu
Mr. Nishant Yadav
Ms. Ojaswi Dale
Mr. Parimal S Athaley
Ms. Resmarani Sahoo
Mr. Ryan Varghese
Mr. Shubham
Mr. Somya Atre
Ms. Srishtil Dabas
Ms. Twinkle Dahiya
Mr. Vaibhav Nayer
SEBI Grade A 2020
63 Selections Out of 80
Mr. Gaurav
Mr. Abhishek
Mr. Abhishek
Mr. Adesh
Mr. Adil
Miss. Gopika
Mr. Harsh
Miss. Akansha
Mr. Amit Meena
Mr. Dhruv
Mr. Digant
Mr. Durga Parsad
Mr. Hitesh
Mr. Johnson
NABARD Grade A 2020
65 Selections Out of 69
Mr. Gourav Kumar
Mr. Sayed Saif
Mr. Vinay Jadhav
Mr. Ratan Singh
Mr. Vishal Singla
Mr. Mohan Das
Miss. Garima
Mr. Amandeep
Miss. Arpita
Mr. Krishan Kumar
Mr. Shivam
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1 Introduction

1.1 Definition of Foreign Exchange and Market

As per the **Foreign Exchange Management Act (FEMA),1999, (Section 2):**

“Foreign exchange” means foreign currency and includes, —

a. Deposits, credits, and balances payable in any foreign currency,
b. Drafts, travellers’ cheques, letters of credit or acts of exchange, expressed or drawn in Indian currency but payable in any foreign currency,
c. Drafts, travellers’ cheques, letters of credit or acts of exchange drawn by banks, institutions or persons outside India, but payable in Indian currency.

1.1.1 Foreign Exchange Market

The foreign exchange market (also known as forex, FX, or the currencies market) is an over the counter (OTC) global marketplace that determines the exchange rate for currencies around the world. Participants in these markets can **buy, sell, exchange, and speculate** on the relative exchange rates of various currency pairs.

Foreign exchange markets are made up of **banks, forex dealers, commercial companies, central banks, investment management firms, hedge funds, retail forex dealers, and investors.**

2 Factors Determining Exchange Rate

Fundamental Reasons

1. Balance of Payment: In laymen terms Balance of Payment is the amount the country has to get from other countries. If balance of payment is positive for India it means India has to get net payment from other countries. If balance of payment is negative for India it means India has to give net payment to other countries.
2. Economic Growth Rate: High Economic growth rate leads to rise in imports and hence more foreign currency will outflow than inflow of foreign currency. So, demand for foreign currency will increase and Indian currency will become weaker
3. Fiscal Policy: Lower taxes can lead to higher economic growth. Read more about this in Fiscal policy chapter
4. Monetary Policy: Monetary policy also effects the value of currency. Read more about this in Monetary policy chapter
5. Interest rates: High Interest attract capital from foreign countries, leading to Indian currency becoming stronger

Technical Reasons

Government controls on restriction on currency can also impact currency rates.

Speculation

Speculative forces can have a major effect on exchange rates. For example, if lot of people think that dollar will increase in value then they will start buying dollars. In case lot of people start buying dollars then there would be huge demand for dollar and hence dollar would increase in value vis-à-vis rupee.

3 Settlement Mechanism

The delivery of FX deals can be settled in one or more of the following ways:

1. **Ready or Cash**: Settlement of funds takes place on the same day (date of deal), e.g., if the date of Ready/Cash deal is 5 October 2009 (Monday), settlement date will also be 5 October 2009.

2. **Tom**: Settlement of funds takes place on the next working day of the date of deal, e.g., if the date of TOM deal 5 October 2009 (Monday), settlement date would be 6 October 2009 (Tuesday, provided it is a working day for the markets dealing as well as where currency is to be settled). If Tuesday is a holiday, in any of the 2 countries, the settlement date will be next working day in both the countries

3. **Spot**: Settlement of funds takes place on the second working day after/following the date of contract/deal, e.g., if the date of Spot deal is 5 October 2009 (Monday), settlement date will be 7 October 2009. (Presuming all markets are working on 5, 6 and 7 October 2009). If not, it will the next working day in both the countries

4. **Forward**: Delivery of funds takes place on any day after Spot date, e.g., if the date of forward deal is 5 October 2009 (Monday), for value settlement date 30 October 2009 or 30 November 2009, it is a forward deal.

Generally, settlement takes place on Spot settlement basis in most of the trades

3.1 Spot and Forward Currency Exchange Rates

If you buy a currency today on today's rate and get the delivery on the second working day, then it is called spot rate. For example, today 1 USD = 60 rupee. You buy 100 dollars at this rate. You will get these 100 dollars in your account after 2 days or the second working day. This is called trading on spot rates or trading in cash market

Now suppose you enter into agreement with someone to buy 100 dollars on the 30th of the month at the rate of 1 USD = 62 rupees. This is called a transaction on forward rate, and this will be executed on a forward date in future. This is same as the concept of futures and forwards we discussed in unit in derivatives

Value Date
A value date is a future date that is used for determining the present value of a product or security that fluctuates in price. It is the date at which funds, assets, or money's value becomes effective.

3.2 Forward Margins – Premium and Discounts

Forward Rates = Spot Rate + Premium or Spot Rate – Discount

For example, if 1 GBP = 1.6000 in the spot rate and 1.6050 in the Forward rate then it means that GBP is trading at a premium of 50 pips in forward markets.

This also means that USD is trading at discount of 50 PIPS (Percentage in Points) in forward markets

3.3 Two-way Rates

The way we have quoted the rates above are single way rate

1 USD = 48 rupees means that 1 USD can be sold in 48 rupees

But generally, there are separate rates for buying and selling

Two-way rates are quoted as 1USD = 48.10/11 rupees. This means 1 USD is being sold at 48.10 rupee whereas 1 USD is being bought at 48.11 rupees. The difference between buying and selling price is 1 paise.

3.4 Cross Rates

When we deal in a market where rates for a currency pair are not directly available, the price for the said currency pair is then obtained indirectly with the help of cross rate mechanism. Suppose we intend to get a quote for Euro/rupee and no one is prepared to quote Euro/Rs directly in the market. We can work out a Euro/Rs quote through Euro/USD and USD/Rs quotes. Euro/USD quote would be available in the international markets and USD/Rs would be available in the domestic market. By crossing out USD in both the quotes, we can arrive at an effective Euro/Rs quote

Chain Rule
When rate between two currencies is not directly available, it has to be calculated through a 3rd currency which is called cross rate. This is done by using chain rule.

3.5 Direct and Indirect Quotes

Direct Quote:

- A direct quote is a currency pair quote where the foreign currency is expressed in per-unit terms of the domestic currency. A direct quote gives you the quantity of local currency needed to purchase one unit of foreign currency.

For example: Under Direct quotes, the local currency is variable, say: 1USD = Rs. 68.10

Indirect Quote:

- An indirect quote in the foreign exchange markets expresses the amount of foreign currency required to buy or sell one unit of the domestic currency. An indirect quote is also known as a "quantity quotation," since it expresses the quantity of foreign currency required to buy a unit of the domestic currency.

For example: Under Indirect quotes, the local currency is fixed, say: Rs.100 = 1.47USD

3.6 Fixed and Floating Rates

A fixed, or pegged, rate is a rate the government (central bank) sets and maintains as the official exchange rate. A set price will be determined against a major world currency.

Unlike the fixed rate, a floating exchange rate is determined by the private market through supply and demand. A floating rate is often termed "self-correcting," as any differences in supply and demand will automatically be corrected in the market.

3.7 Bid and Offer Rate

The bid rate is the maximum rate in the market which buyers of stock are willing to pay in order to purchase any stock or the other security demanded by them, whereas the offer rate is the minimum rate in the market at which sellers are willing to sell any stock or the other security which they are currently holding.

4 Risk Associated with Currency Exchange

The major risks associated with the dealing operations are:

1. Operational Risk
2. Exchange Risk
3. Credit Risk
4. Settlement Risk
5. Liquidity Risk
6. Gap Risk/ Interest risk/ Rate Risk
7. Market Risk
8. Legal Risk
9. Systemic Risk
10. Country Risk

11. Sovereign Risk

We have discussed all these risks in chapter Risk Management. Almost the same meaning and definition is applied here.

The Operation Risk is arising because human errors, technical faults, infrastructure breakdown, faulty systems and procedures or lack of internal controls.

The Exchange Risk is the most common and obvious risk in foreign exchange dealing operations and arise mainly because fluctuations in exchange rates and/ or when mismatches occur in assets/ liabilities and receivables/ payables.

Foreign exchange exposures can be classified into three categories

a) **Transaction Exposure:** Transaction exposure is the level of uncertainty faced by companies involved in international trade due to currency fluctuations. A high level of exposure to exchange rates can lead to major losses, although certain measures can be taken to hedge those risks.
b) **Translation Exposure**: Translation exposure is the risk of having changes in foreign exchange rates trigger losses on business transactions or balance sheet holdings. These losses can occur when a firm has assets, liabilities, equity, or revenue denominated in a foreign currency and needs to translate them back into its home currency.
c) **Operating/Economic Exposure**: Economic exposure, also known as operating exposure refers to an effect caused on a company's cash flows due to unexpected currency rate fluctuations. Economic exposures are long-term in nature and have a substantial impact on a company's market value.

Credit risk arises due to inability or unwillingness of the counterpart to meet the obligations at maturity of the underlying transactions. Credit Risk is classified into

I. Pre-settlement risk is the possibility that one party in a contract will fail to meet its obligations under that contract, resulting in default before the settlement date**. This default by one party would prematurely end the contract and leave the other party to experience loss if they are not insured in some way.**

II. Settlement risk is the possibility that one or more parties will fail to deliver on the terms of a contract at the agreed-upon time**. Settlement risk is a type of counterparty risk associated with default risk, as well as with timing differences between parties. Settlement risk is also called delivery risk or Herstatt risk.**

Liquidity Risk is the potential for liabilities to drain from the bank at a faster rate than assets. The mismatches in the maturity patterns of assets and liabilities give rise to liquidity risk.

Gap Risk/ Interest Rate Risk are the risk arising out of adverse movements in implied interest rates or actual interest rate differentials.

Market Risk: This is arising out of adverse movement of market variables when the players are unable to exit the positions quickly.

Legal Risk is arising because non-enforceability of contract against a counter party.

Systemic Risk is the possibility of a major bank failing and the resultant losses to counter parties reverberating into a banking crisis.

5 Guidelines by RBI and FEDAI

The Reserve Bank of India has issued 'Authorized Dealers' (AD) licenses to banks and all-India financial institutions to undertake foreign exchange transactions in India.

Categorization of Authorized Dealers:

- **Authorized Person** means an authorized dealer, money changer, off-shore banking unit or any other person authorized under sub-section (1) of section 10 to deal in foreign exchange or foreign securities.
- **'Authorized Dealer' (AD)** means a person authorized as an authorized dealer under sub-section (1) of section 10 of FEMA.
- **'Authorized Dealer (AD) Category I'** means entities which are authorized by the Reserve Bank to carry out all permissible current and capital account transactions as per directions issued from time-to-time
- **'Authorized Dealer (AD) Category II'** means entities which are authorized by the Reserve Bank to carry out specified non-trade related current account transactions, all the activities permitted to Full Fledged Money Changers and any other activity as decided by the Reserve Bank and shall include (i) Upgraded FFMCs; (ii) Select Regional Rural Banks (RRBs); (iii) Select Urban Cooperative Banks (UCBs); and (iv) Other entities.
- **'Authorized Dealer (AD) Category III'** means entities which are authorized by the Reserve Bank to carry out specific foreign exchange transactions incidental to their business / activities.
- **'Full Fledged Money Changer (FFMC)'** is a money changer authorized to purchase foreign exchange from non-residents visiting India and residents, and to sell foreign exchange for private and business travel purposes only.

Guidelines for Renewal of licences of existing FFMCs :

1. The applicant should be a company registered under the Companies Act, 1956/ Companies Act, 2013/ Registration of Companies (Sikkim) Act, 1961 having registered office within the area of jurisdiction of the respective Regional Office of the Foreign Exchange Department.

2. The Net Owned Funds required are as follows:

Category	Minimum NOF
Single branch FFMC	Rs.25 lakh
Multiple branch FFMC	Rs.50 lakh

Guidelines issued by RBI for Authorized Persons

1. AD Category I - Banks can open/close rupee accounts (non-interest bearing) in the names of their overseas branches or correspondents (except Pakistani banks operating outside Pakistan) without prior reference to RBI.
2. AD Cat I - Banks can open/close foreign currency accounts abroad to route foreign exchange transactions handled by then. Banks are also allowed to maintain balances in these accounts, as approved by their Board.
3. AD Cat-1 Banks are free to undertake investments in overseas markets in money market instruments and/or debt instruments, issued by foreign state with a residual maturity of less than one year and rated as per guidelines
4. Banks are also allowed to offer other derivative contracts, such as Interest Rate Swap or Coupon Swap or foreign currency Option or Interest Rate Cap or Collar or Forward Rate Agreement contract, to resident entities who have borrowed foreign exchange in accordance with the provisions of FEMA 199
5. Bank can also offer Foreign Currency - Rupee Swap to resident persons that has a foreign exchange or a rupee liability to hedge long term exposure, with certain conditions.

FEDAI and its Guidelines

FEDAI stands for Foreign Exchange Dealers Association of India. FEDAl is a non-profit making body, formed in 1958 with the approval of Reserve Bank of India, consisting of Authorized dealers as members. In terms of RBI directives, all authorized dealers are members of FEDAI and it is mandatory for them to follow the guidelines/directives issued by FEDAI

We will not go into details of guidelines issued by FEDAI because there is no need to go in that much depth

6 Numerical

Numerical 1: On 3.10.09, your exporter customer tenders an export bill for USD 500,000.00, drawn 120 days from the date of shipment, (shipment date 3.10.2009) due date 1.2.2010. Compute applicable rate, presuming (a) exchange margin of 0.15%, (b) Spot Rupee 48.14/15 and premium Spot – Jan 45/46 paise

Find the amount payable to the customer in rupee terms

Solution:
In this you have exported something, and you will get the amount of 500,000 USD after 120 days. So, you must calculate the amount of money you will get by selling 500,000 USD at the forward contract rate

Note: Just remember that if it is an export bill then you need to sell USD or any other foreign currency and if it is an import bill then you need to buy USD or any other foreign currency

Spot Rate to sell the USD = 48.14 and buy the USD is 48.15
Since we want to sell USD, we will use the rate 48.14
Exchange Margin of 0.15% means you will get this discount on selling USD
So, discount = .15% of 48.14 = 0.0722
Net spot rate after discount = 48.14 - .07222 = 48.0678
We can round off 48.0678 to 48.0675
Since you will get the amount after 120 days, so the future rate is having premium of 45 paise
So, we add the premium of .4500 to 48.0678 and we get 48.5175
So, by selling 1 USD we get 48.5175
By selling 500,000 USD we get = 500,000 * 48.5175 = 24258750

Numerical 2: You must pay the import bill of 100,000 GBP. The margin is .20%. The GBP/USD rates are 1.5975/85 and USD/INR rates are 48.14/15. Compute the rate for the customer

Solution: To pay the import bill of 100,000 GBP one needs to buy the GBP by paying in rupee. Here rate of GBP/INR is not given and instead rate of GBP/USD and USD/INR is given

Note: Just remember that if it is an export bill then you need to sell USD, or any other foreign currency mentioned on the bill and if it is an import bill then you need to buy USD, or any other foreign currency mentioned on the bill

So, we can calculate the GBP/INR by crossing the rates for GBP/USD and USD/INR

GBP/INR = 1.5975/1.5985 * 48.14/48.15 = 76.9036 / 76.9677

So, one can buy 1 GBP by paying 76.9677 INR and sell 1 GBP at 76.9036. Since we want to buy GBP, so our rate would be 76.9677

We also must add the margin of .20%. In the previous question we deducted the margin but in this question, we will add the margin. This is because during export (selling foreign currency) we need to deduct the margin and during import (buying foreign currency) we need to add the margin

So, adding .20% premium we get = 76.9677 + .20% of 76.9677 = 77.1217

Numerical 3: On 15th September, a customer requests for booking of a forward contract for the export bill of USD 150,000 to be realized on 1st December. The USD/INR spot rate is 48.45/50 and forward premium for November is 30/32 paise. The margin to be charged is 5 paise per USD. Find the forward rate the customer will get

Solution:

This is an export bill, so you need to sell USD.
Spot rate for selling USD = 48.45 and buying USD is 48.50. Since we want to sell the USD the rate for us would be 48.45
Since this is export bill so we deduct the margin
After margin deduction the rate is = 48.45 - .05 = 48.40
The forward premium is 30 paise for selling dollars. So, the forward rate would be = 48.40 + .30 = 48.70

Numerical 4: On 1st June, a customer books a forward contract for retirement of import bill of USD 100,000. The bill payment is due on 15th September. The spot rate for USD/INR is 48.27/29 and forward premium are as follows

June – 10/12
July – 21/23
August – 32/34
September – 43/45
August to 15th September – 6/7
Margin to be charged at .20%

Solution:

This is an import bill, so we need to buy USD

Rate of selling USD is 48.27 and buying USD is 48.29. So, rate applicable for us would be 48.29

Spot rate = 48.29

Add margin since this is an import bill

Rate after margin adjustment = 48.29 + .20% of 48.29 = 48.39

Now, we need to add the forward premium till 15th September

Bill needs to be paid on 15th September. So, we cannot use the September forward premium as such because that rate would mean the rate on 30th September.

First, we will add the forward premium till August = 48.39 + .34 = 48. 73

(In case you are confused, why we are adding 34 and not 32, this is because 32 paise is the premium for selling dollars and 34 paise is the premium for buying dollars. Since we are buying dollars we need to add 34 paise)

Now we will add premium from 1st August till 15th September which is given as 6/7

So, adding premium from 1st Aug to 15th September, we get 48.73 + .07 = 48.80

7 Electronic Modes of Transmission

1. **SWIFT**: SWIFT stands for Society for Worldwide Interbank Financial Telecommunications. This is a cooperative society, owned by member banks and financial institutions, providing secured telecommunication and one-point contact with more than 8,300-member financial institutions, spread over more than 209 countries. The system has built in security system with an automatic authentication of financial messages, through bilateral key exchange (BKE), and is available 24 hours a day and 365 days in a year
2. **CHIPS** (Clearing House Interbank Payment System), is a major payment system in the USA, operating since 1970. It is a fully automated; computer based messaging and net settlement payment system used by major banks for settlement of a large part of US dollar payments in the USA
3. **Fed wire**: It is another US payment system operated by Federal Reserve Bank, operated all over the US states since 1918, and handles majority of domestic payments. It is an automated computer-based messaging and payment system, working on gross settlement basis. All US banks maintain accounts with Federal Reserve Bank, and are allotted an 'ABA numbers' to identify the senders and receivers of payments
4. **Chaps**: Clearing House Automated Payments System (CHAPS), is a British equivalent to CHIPS, handling receipts and payments in LONDON. This system works on the same principles as CHIPS, working on the net payment settlement system

5. **Target**: Trans-European Automated Real-Time Gross Settlement Express Transfer system is an EURO payment system comprising 15 national RTGS systems working in EUROPE. These are interconnected by common procedures and uniform platform for processing high value payments by over 30,000 participating institutions across EUROPE
6. **RTGS**: Reserve Bank of India has implemented Real Time Gross Settlement (RTGS) system for the banks in India, where banks can remit funds to other banks through this mechanism, The RTGS system is managed by IDBRT, Hyderabad, which connects all banks to a central server maintained at RBI.
7. **NEFT**: This is another funds transfer facility for banks in India, which runs on a batch process method. This is used for small remittances by customers from an account with one bank to another account in another bank. The funds adjustment for NEFT is also done through the pool accounts maintained by individual banks

8 FEMA – Regulations by RBI

Reserve Bank of India, being the central bank of the country, is empowered under the statute to control and regulate the foreign exchange reserves and policies related to international trade, inflow/outflow of foreign exchange, as also has supervisory powers over the persons authorized to deal in foreign exchange. It has the responsibility of maintaining the external value of Rupee, and thus can issue instructions about exchange control from time to time.

FEMA (Foreign exchange Management Act) works under the supervision of RBI. Reserve Bank of India, has powers delegated under FEMA to issue guidelines, call for reports, data, as also to impose penalties, for violation of provisions of FEMA and for not complying to its directions

8.1 Important Provisions of FEMA

FEMA, 1999 was enacted by the statute of the parliament, and was brought into force i.e. 1. 6. 2000. The Act is applicable to all transactions in foreign exchange, undertaken in India or by persons resident in India

Earlier **FERA** use to regulate the currency exchange but now it is **FEMA** (Foreign exchange Management Act). The objective of FEMA is to facilitate external trade and payments and to promote the orderly development and maintenance of foreign exchange market in India,

Under FEMA any violation of the provisions of the Act is to be dealt under the Civil law only, while under FERA, it was to be dealt under Criminal law

There are many FEMA regulations running into thousands of pages which we do not recommend reading. Kindly keep yourself updated with the current affairs of FEMA as a question can be asked from that

We keep covering all the current affairs in our current affairs Magazine

Additional Information

- A resident of India, who has gone out of India on a temporary visit may bring into India at the time of his return from any place outside India (other than Nepal and Bhutan), currency notes of Government of India and Reserve Bank of India notes up to an amount not exceeding **Rs.25,000**. A person may bring into India from Nepal or Bhutan, currency notes of Government of India and Reserve Bank of India notes, in denomination not exceeding **Rs.100.**

- Travelers going to all countries other than (a) and (b) below are allowed to purchase foreign currency notes / coins only up to **USD 3000 per visit**. Balance amount can be carried in the form of store value cards, travelers cheque or banker's draft.
  Exceptions to this are
  a) travelers proceeding to Iraq and Libya who can draw foreign exchange in the form of foreign currency notes and coins not exceeding USD 5000 or its equivalent per visit;
  b) travelers proceeding to the Islamic Republic of Iran, Russian Federation and other Republics of Commonwealth of Independent States who can draw entire foreign exchange (up-to USD 250,000) in the form of foreign currency notes or coins.

  For travelers proceeding for Haj/ Umrah pilgrimage, full amount of entitlement (USD 250,000) in cash or up to the cash limit as specified by the Haj Committee of India, may be released by the ADs and FFMCs.

9 NRI Banking

9.1 NRI Definition

In terms of Regulation 2 of FEMA Act, Non-Resident Indian (NRI) means a person resident outside India who is a citizen of India.

9.2 NRI Accounts

An NRI Account refers to the accounts opened by a Non-Resident Indian (NRI) or a Person of Indian Origin (PIO) with a bank or financial institution which is authorized by the Reserve Bank of India (RBI), to provide various services.

Types of NRI Accounts

1) **NRE account**: An NRE account is a rupee-denominated bank account (**Savings or Term deposits**) opened in India in the name of an NRI, to park his foreign earnings. It is repatriable back to foreign currency. The interest you earn on the NRE account is tax free.
2) **NRO account:** These are Rupee accounts opened for the purpose of depositing income earned in India. One can repatriate the interest amount, the principal

amount can be repatriated within the set limits of up to USD 1 million in a financial year. Rent, dividends, and other sources of income are all possibilities. These accounts are taxed for income tax purpose

3) **FCNR Account**: The FCNR (Foreign Currency Non-Residential Account) permits Non-Resident Indians or Persons of Indian Origin to make term deposits in foreign currency. Only term deposits are allowed
4) **SNRR Account (Special Non-Resident Rupee Account):** Current account opened by any person resident outside India (Individual or Corporate) having some sort of business interest in India. SNRR account has been allowed to be used for specified transactions in trade, foreign investments, External Commercial Borrowings, etc., in lieu of sending inward/outward remittances by a person resident outside India in a convertible foreign currency for each transaction with a resident or vice-versa. SNRR is a non-interest earning account and its repatriable which means, SNRR account holders can move their money from India to their country of origin.

Difference between NRE and FCNR Account

Basis of Difference	NRE Account	FCNR Account	NRO	SNRR
Type of Accounts	Can be opened as Savings, Current Account, Term Deposit	Can be opened as Term Deposit	Savings, Current or Deposit	Current
Purpose	Opened by NRIs who earn income abroad and would like to remit it back to India	Opened by NRIs to park their overseas income in foreign currency in India without converting them into rupees.	It is an account of an NRI to manage the income earned in India	Business Purpose
Maintained in	Rupee	Foreign Currency e.g., USD, GBP, EURO, AUD, YEN, etc.	Rupee	Rupee
Repatriability	Principal as well as interest can be entirely repatriable	Principal as well as interest can be entirely repatriable	Can repatriate the interest amount, the principal amount can be repatriated within the set limits of USD 1 million in a financial year	Repatriable
Tax Exemptions	Tax-free in India	Tax-Free In India	Taxed	Taxes applicable on transactions

Currency Risk	Currency risk is there, there will be a loss in case rupee depreciates at the time of repatriation	No currency risk as the investment is made in foreign currency and is withdrawn in the same currency.	Not prone to risk unless you repatriate to foreign country	Yes, as the payment received in rupee if repatriated at later date

10 Foreign Currency Accounts in India

Resident Indians can maintain following foreign currency accounts in India

Exchange Earners Foreign Currency (EEFC) Accounts: Resident persons, companies or firms can open and maintain EEFC accounts, for the purpose to transacting foreign exchange business. Every recipient of foreign exchange can retain 100% of the amount in a foreign currency account, with any AD.

Resident Foreign Currency Accounts: Returning Indians, who were non-residents earlier and are now returning to India for permanent settlement, are permitted to open a foreign currency account with any AD, to keep their foreign currency assets held outside India, or any other monetary benefits from the employer outside India

Resident Foreign Currency (Domestic) Account - RFCD A person resident in India is allowed to open and maintain a Resident Foreign Currency account with an AD, out of the foreign exchange acquired by him in the form of currency notes, or travelers cheques, while on a visit to any country outside India, (not from business), or as an honorarium or gift for service rendered in India to any person who is not a resident of India, and is on a visit to India, or represent unspent foreign exchange acquired for travel abroad

Diamond Dollar Accounts: The facility of opening Diamond Dollar Accounts has been granted to diamond exporters, as the products they export is imported in raw form, from abroad. India imports, rough diamonds and exports polished diamonds to various countries in the world. As such, **since the diamond exporters usually need to remit a large part of their realization of export proceeds for payment of import bills**, they can park their foreign currency funds in these diamond dollar accounts and remit funds to retire their import bills, without incurring any exchange risk.

11 Export credit Insurance in International Trade

Export credit insurance in India is designed to protect the receivables of an exporter. It means that the insurance tool provides an assurance to the exporter about receiving the amount due from the foreign customer.

In India, Export credit insurance is provided by ECGC.

11.1 ECGC – Export Credit Guarantee Corporation of India

Export Credit Guarantee Corporation of India (ECGC) is an Indian enterprise that is administered by the Government of India through the Ministry of Commerce and Industry. ECGC which is wholly owned by the Indian Government.

The Government of India had initially set up the Export Risks Insurance Corporation in 1957. After the introduction of insurance covers to banks during the period 1962-64, the name was changed to Export Credit & Guarantee Corporation Ltd in 1964. It was changed to ECGC Ltd in August 2014.

Objectives

The Corporation has set before itself the following objectives:

1. To encourage and facilitate globalization of India's trade.
2. To assist Indian exporters in managing their credit risks by providing timely information on worthiness of the buyers, bankers and the countries.
3. To protect the Indian exporters against unforeseen losses, which may arise due to failure of the buyer, bank or problems faced by the country of the buyer by providing cost effective credit insurance covers in the form of Policy, Factoring and Investment Insurance Services comparable to similar covers available to exporters in other countries.
4. To facilitate availability of adequate bank finance to the Indian exporters by providing surety insurance covers for bankers at competitive rates.
5. To achieve improved performance in terms of profitability, financial and operational efficiency indicators and achieve optimum return on investment.
6. To develop world class expertise in credit insurance among employees and ensure continuous innovation and achieve the highest customer satisfaction by delivering top quality service.
7. To educate the customers by continuous publicity and effective marketing.

Financial Guarantees by ECGC

The main types of guarantees offered are:

A. **Packing Credit Guarantee:** Any loan given by exporter at the banks to an expo pre-shipment stage against a confirmed export order or letter of credit qualifies for Packing Credit Guarantee. Pre-shipment advances extended for export of services or for Construction works abroad are also eligible for cover under this guarantee. The bank will be entitled to claim 66 2/3 % of its loss from the corporation in the event of an exporter failing to discharge his liabilities to the bank.

B. **Post shipment Export Credit Guarantee:** Banks extend post-shipment finance to exporters through purchase, negotiation or discount of export bills or advances against such bills. The post shipment credit guarantee provides protection to banks against non-realisation of export proceeds and the resultant failure of the exporter to repay the advances availed. The percentage of loss covered under this guarantee is 75%.

C. **Export Production Finance Guarantee:** Export Production Finance Guarantee enables banks to sanction advances at pre-shipment stage to the full extent of the domestic cost of production. Here again, the bank would be entitled to 66 2/3% of its loss from the corporation.

D. **Export Finance Guarantee:** Export Finance Guarantee covers post-shipment advances granted by banks to exporters against export incentives receivable in the form of duty drawback. The percentage of loss covered under this guarantee is 75%.

E. **Export Performance Guarantee:** Exporters are often called upon to furnish a bank guarantee to the foreign parties to ensure due performance or against advance payment or in lieu of retention money. Export Performance Guarantee protects banks to the extent of 75% of the loss suffered by bank on account of such guarantees.

F. **Export Finance (Overseas Lending) Guarantee:** If a bank financing an overseas project provides a foreign currency loan to a contractor, it can protect itself from the risk of non-payment by obtaining Export Finance (Overseas Lending) Guarantee. The percentage of loss covered under this guarantee is 75%.