Rupee-Rufiyaa trade

The currency deal with Maldives is a game-changer

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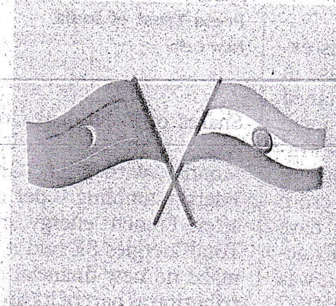

The Memorandum of Understanding (MoU) recently signed between the Reserve Bank of India (RBI) and the Maldives Monetary Authority (MMA) is a pivotal move that enables the use of the Indian Rupee (INR) and Maldivian Rufiyaa (MVR) for bilateral trade settlements. While the benefits are substantial, the success of this framework will hinge on addressing potential challenges with prudence and foresight.

India, as one of the Maldives' largest trading partners, supplies essentials such as food, construction materials, pharmaceuticals, and machinery, while the Maldives primarily exports fish and tourism services to India.

Facilitating trade in local currencies presents significant advantages, enhancing efficiency and reducing costs for both nations.

Reduction in Transaction Costs: Traditionally, trade transactions involve conversion via a third-party currency, predominantly the US Dollar, incurring considerable forex costs. This framework eliminates such conversion needs, reducing financial burdens on businesses, particularly small and medium enterprises (SMEs) operating on tighter margins.

Enhancement of Trade Efficiency: The initiative minimises settlement times, ensuring faster payments for exporters and importers.

Strengthening Bilateral Trade Stability: With the Maldives relying heavily on imports, this framework fosters a more predictable trading environment by shielding businesses from global currency fluctuations. For India, it aligns with the strategic goal of internationalizing the Indian Rupee and deepening regional economic ties.

Boosting Local Currency Markets: Promoting INR-MVR trading within the foreign exchange market strengthens both currencies and enhances their economic sovereignty.

Supporting Regional Economic Integration: This MoU reflects India's 'Neighbourhood First' policy, emphasizing mutual growth and collaboration.

THE CHALLENGES

Some of the challenges that need to be addressed are:

Currency volatility: Robust hedging mechanism for both the INR and MVR are vital to curb volatility risks.

Liquidity constraints: The nascent INR-MVR trading pair lacks sufficient liquidity. Developing a mature market will require coordinated efforts from financial institutions in both countries and active participation from the private sector.

Regulatory and operational complexities: Seamlessly integrating regulatory frameworks for invoicing, settlements, and dispute resolution is essential.

Resistance to change: Businesses accustomed to trading in US Dollars may initially resist adopting local currencies due to perceived risks or lack of familiarity. Awareness campaigns and incentives for early adopters will be crucial to overcoming this inertia.

Dependence on economic stability: The framework's success hinges on sustained macroeconomic stability in both nations.

Maldives' heavy reliance on imports and tourism-based foreign exchange inflows makes it vulnerable to global currency fluctuations. By stabilising trade transactions, the local currency framework could provide a buffer against external economic shocks and preserve forex reserves.

For India, this partnership represents an opportunity to showcase the Rupee's role as a regional currency and to enhance its influence in South Asia.

Additionally, both countries are members of organizations like South Asian Association for Regional Cooperation (SAARC) and the Indian Ocean Rim Association (IORA), which provide broader platforms for advancing such initiatives.

The success of this framework could serve as a model for similar agreements with other neighbouring nations.

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