

# MP-IDSA

## *Issue Brief*

# India-Bangladesh Trade Settlement in Indian Rupee

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## **S***ummary*

The initiative aimed at facilitating bilateral trade between India and Bangladesh through the use of Indian rupees initially, and subsequently Bangladeshi Taka, is set to benefit both countries. The integration of the INR into trade transactions enables Bangladesh to minimise currency-related expenses and capitalise on the stability and potential advantages offered by the rupee's exchange rate dynamics.

India–Bangladesh relations have strengthened since January 2009, following the assumption of power by the Sheikh Hasina government. Presently, both nations share an unprecedented level of mutual trust. This dynamic has yielded not only improved political relationship but also economic progress. Trade and commerce have flourished, fostering prosperity for both populations. Bangladesh, which exported goods valued at a mere US\$ 498.42 million in 2011–12, has now increased its exports to US\$ 1990 million in 2021–22.<sup>1</sup> Similarly, Indian exports to Bangladesh have also increased from US\$ 4743.30 million in 2011–12 to US\$ 13690.00 million in 2021–22.

Interestingly, the disruptive impact of the COVID-19 pandemic on global trade and commerce has engendered a closer bond between these neighbouring countries. Both parties deftly seized the crisis as an opportunity, opting to transport goods via railway. This innovative approach not only curtailed transportation costs but also streamlined business processes. Moreover, it ensured the timely availability of essential commodities to the Bangladeshi populace and sustained local industries.

Nonetheless, the subsequent deceleration of the global economy has uniquely affected the Bangladeshi economy. Presently, the nation confronts a crisis stemming from dwindling foreign exchange reserves. With India and Bangladesh agreeing to settle the payments for their international trade partly in Indian rupee, it can reduce pressure on Bangladeshi dollar reserves.

## Shift in Global Currency Dynamics

The dominance of the dollar has gradually declined over the last few decades as the role of the US in global trade has diminished. At the turn of the century, the dollar accounted for more than 70 per cent of global reserves. According to IMF data, this share declined to 65.46 per cent in 2016 and further to 59.02 per cent in 2023.<sup>2</sup>

The move accelerated after the United States aggressively raised policy rates to control a record surge in inflation caused by the prolonged pandemic and the Russia–Ukraine conflict. This monetary tightening in the US prompted investors to withdraw their funds from Asian economies, triggering currency depreciation in most of these economies.

Sharp currency depreciation typically leads to higher inflationary pressures due to increased import prices for food and energy. It also worsens the current account balance

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<sup>1</sup> [“India Bangladesh Exports and Imports”](#), High Commission Of India, Dhaka, Bangladesh.

<sup>2</sup> [“World Currency Composition of Official Foreign Exchange Reserves”](#), International Monetary Fund.

and can result in countries facing difficulties in paying for essential imports or servicing external debts. Bangladesh is currently grappling with such a situation, with its currency having depreciated by 25 per cent since last year.

The dollar accounted for nearly 90 per cent of global foreign exchange transactions in 2022, making it the most traded currency. All members of the Asian Clearing Union, including South Asian countries, Iran and Myanmar, have reached a consensus on 6 July 2023 to settle trade in local currencies, such as the rupee, to reduce dependence on the US dollar and the euro.<sup>3</sup>

China is actively participating in this movement due to its dominant position in global trade and its status as the world's second-largest economy. In 2022, China was the largest trading partner for 61 countries in terms of combined imports and exports. In contrast, the US held this position for 30 countries. In the wake of sanctions on Russia, China has pushed to conduct more trade using the yuan with the objective to reduce its reliance on the dollar.<sup>4</sup> During a state visit to Beijing in April 2023, Brazilian President Luiz Inácio Lula da Silva reportedly called for reduced reliance on the US dollar in global trade.

Malaysia's Prime Minister Anwar Ibrahim also suggested the establishment of an "Asian Monetary Fund" to reduce dependence on the US dollar during a recent visit to China. At the ASEAN finance ministers and central banks meeting in Indonesia in March 2023, policymakers discussed the concept of reducing their reliance on the US dollar, Japanese yen, and euro, and instead transitioning to settlements in local currencies.

As countries seek alternatives to the US dollar and negotiate bilateral trade settlements, this shift is reflected in the declining share of the dollar in global foreign exchange reserves. According to the International Monetary Fund, the global foreign exchange reserves stood at US\$ 11.96 trillion at the end of 2022, with the US dollar's share at 58.36 per cent, marking a 26-year low.

India's foreign currency assets (FCA) totalled US\$ 514 billion on 7 April 2023, with approximately 40 per cent estimated to be non-dollar assets. This suggests that around US\$ 310 billion of India's foreign currency assets are denominated in US dollars.<sup>5</sup>

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<sup>3</sup> Anup Roy and Khine Lin Kyaw, [“India-Dominated Clearing Union Moves Toward Rupee Settlement”](#), Bloomberg, 6 July 2023.

<sup>4</sup> Amy Hawkins, [“China’s War Chest: How Beijing is Using its Currency to Insulate Against Future Sanctions”](#), *The Guardian*, 8 May 2023.

<sup>5</sup> Rajiv Ranjan Singh, [“Bangladesh Joins Rupee Cohort, Sign Deals to Settle Trade in Rupees”](#), *Fortune India*, 27 April 2023.

## **Indian Initiative to Elevate Rupee as a Global Currency**

In July 2022, India embarked on a significant initiative by allowing foreign trade settlements in INR. This move was facilitated by the Reserve Bank of India (RBI), reflecting a strategic shift towards international trade conducted in the Indian rupee. In March 2023, India announced that the RBI had granted permission to banks from 18 countries to establish special rupee nostro accounts, enabling them to execute transactions in Indian rupees. The prominent countries included in this list are Sri Lanka, Israel, Russia, Germany, Singapore, the UK, and recently, Bangladesh.

The decision to broaden the list of eligible countries aligns with India's vision to elevate the status of the rupee as a global currency. The RBI has established a mechanism to facilitate international trade settlements in INR. The initiation of trade settlements with Bangladesh in the rupee signifies a positive stride in this direction. Expanding the utilisation of the rupee in trade transactions is poised to contribute to India's aspiration of positioning its currency as a potential reserve currency, alongside established reserve currencies such as the US dollar, the euro, the Chinese renminbi, the Japanese yen, and the British pound sterling.

## **India–Bangladesh Bilateral Trade**

India is the second-largest import source for Bangladesh, trailing only behind China. Dhaka's exports to India reached a total of US\$ 1990 million in 2021–22, whereas imports from India amounted to a US\$ 13.69 billion in the same period.

In FY23 (until February), Indian exports to Bangladesh tallied at US\$ 10.63 billion, equivalent to 2.6 per cent of India's total exports. Conversely, Bangladesh's imports from India during the same period totalled US\$ 1.86 billion, constituting 0.28 per cent of India's overall imports.<sup>6</sup> Furthermore, if we take into account trade transactions conducted through unofficial channels, the volume of bilateral trade between the two nations expands even further. In this scenario, shifting towards trade settlements in Indian rupees is anticipated to alleviate the strain on Bangladesh's foreign exchange reserves.

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<sup>6</sup> Ibid.

## Bangladesh Takes Steps to Reduce Over-Reliance on Dollar

In its effort to lessen its reliance on the US dollar for foreign trade settlements, Bangladesh has commenced the use of the rupee to conduct bilateral transactions with India starting from 11 July 2023. Both the Bangladesh Bank and the RBI have granted permission to two Indian banks to facilitate bilateral trade settlements in Indian rupees (INR). The Bangladesh Bank has authorised three banks—Sonali Bank, Eastern Bank, and State Bank of India (country office) in Bangladesh—to establish nostro accounts<sup>7</sup> with their counterparts in India. On the Indian side, SBI and ICICI Bank are participating in this initiative.

Under the new arrangement, Bangladeshi exporters will receive their earnings in rupees, which will be deposited in their nostro accounts with ICICI Bank and SBI. These funds will then facilitate Bangladesh's import transactions with India. Initially, trade settlements will occur in INR, with a later transition to BDT (Bangladeshi Taka) once the two Indian banks establish nostro accounts with Bangladesh's EBL and Sonali Bank. Sonali Bank and Eastern Bank Limited will establish Rupee Nostro accounts with India's ICICI Bank and SBI. Once this system starts functioning smoothly, other banks from both countries will be allowed to participate in this process.

## Bangladesh Adopts Rupee Trade: Benefits

The commencement of cross-border trade settlements between Bangladesh and India using the INR marks a significant milestone in the expanding bilateral commerce, with particular implications for Bangladesh. Prior to the inclusion of the rupee as a currency for cross-border transactions, Bangladesh predominantly settled trades in the US dollar, followed by the pound sterling and the euro.

However, the Russia–Ukraine conflict in February 2022 brought about disruptions in international payments for goods and services due to scarcity of the US dollar in various nations and the imposition of a ban on the employment of the global payments network, SWIFT, for transactions involving Russia.<sup>8</sup>

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<sup>7</sup> A nostro account is an account held by a bank within a foreign bank, denominated in the currency of the host country. Its purpose is to facilitate foreign exchange activities and international trade involving different currencies.

<sup>8</sup> Refayet Ullah Mirdha, “[Indo-Bangla Trade in Rupee to Benefit Bangladesh: MCCI](#)”, *The Daily Star*, 9 July 2023.

Bangladesh’s foreign exchange reserves have also dwindled due to heightened import expenditures in contrast to relatively moderate remittances and export earnings. Bangladesh is now struggling to pay for imported fuel because of the dollar shortage.<sup>9</sup>

As of 6 July 2023, Bangladesh's foreign exchange reserves have decreased from US\$ 41.8 billion in 2022 to US\$ 29.97 billion, a decline of about 28 per cent. Confronted with this foreign exchange crisis, the Bangladesh Bank (BB) has responded by adopting the practice of settling bilateral trade utilising the currency of its neighbouring country. BB Governor Abdur Rouf Talukder had previously expressed the country's intention to engage in trade with India using the rupee, up to an extent that corresponds to the nation's export earnings. This new arrangement enables Bangladesh to conduct foreign trade with India amounting to US\$ 2 billion, which is equivalent to its current annual export proceeds from India.

The inclusion of the INR among the currencies for cross-border trade marks a significant transition for Bangladesh. According to the central bank of Bangladesh, the country’s total imports stood at US\$ 75.60 billion in 2021–22. Hence, the strategic shift towards trade settlement in rupee will not immediately reduce the dependence of Bangladesh on dollar. Initially, the scope of import payments would be limited to approximately US\$ 2 billion, equivalent to Bangladesh's export earnings from India. As a result, an immediate surge in Bangladesh's foreign currency reserves is not expected. Over the past year, these reserves have declined by about 28 per cent due to elevated import expenditures juxtaposed with lower-than-projected export and remittance earnings.

Trade analysts in Bangladesh view this development as a positive stride, one that will foster stronger trade bonds between neighbouring countries, decrease reliance on the US dollar, and reduce business expenditures.<sup>10</sup> Lower trade costs will contribute to improved competitiveness, potentially attracting a larger customer base and, consequently, boosting Bangladesh's exports to India. The ongoing challenges related to the country's forex reserves have somewhat constrained Bangladesh's ability to open letters of credit. Settling letters of credit in the rupee could alleviate this predicament to some extent.<sup>11</sup> The full benefits of rupee-denominated trade could materialise if

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<sup>9</sup> Arun Devnath, [“Bangladeshi Banks Plan India Rupee Transactions as Reserves Fall”](#), *The Economic Times*, 7 July 2023.

<sup>10</sup> Sohel Parvez, [“Trade in Rupee to Save at least Tk 1 per dollar: EBL CEO”](#), *The Daily Star*, 9 July 2023.

<sup>11</sup> Ahsan Habib, [“How Much Will Bangladesh Benefit?”](#), *The Daily Star*, 18 July 2023.

Bangladesh manages to augment its exports to India. Historically, India has extended lines of credit to Bangladesh, which could potentially ease pressure on forex reserves in the future.

Opting for a market-based exchange rate could prove advantageous for Bangladesh. Over the past year, the taka has experienced a steep depreciation against the US dollar, while the rupee has not witnessed such a drastic decline. The taka has depreciated by around 10 per cent against the INR within the past year, whereas it has weakened by about 25 per cent against the US dollar. Therefore, the practice of settling trades in rupees stands to benefit Bangladesh.

The rupee and the taka have not exhibited parallel fluctuations against the US dollar, implying that a more substantial depreciation of the Bangladeshi currency could work to its advantage. However, it's important to acknowledge that the rupee itself might fluctuate in future.

Engaging in INR trading offers cost-efficiency as it eliminates the need for currency hedging. Conversely, trading in US dollars involves expenses associated with hedging against currency fluctuations.

In essence, the integration of the INR into trade transactions offers a strategic avenue for Bangladesh to optimise its trade operations, minimise currency-related expenses, and capitalise on the stability and potential advantages offered by the rupee's exchange rate dynamics.

## **A Dual Currency Card in the Offing**

The shift to settlement of bilateral trade in Indian Rupee has made both India and Bangladesh to also think of a dual currency card. The issue of dual currency cards was discussed during a meeting of Bangladesh's National Economic Council, presided over by Prime Minister Sheikh Hasina. In this meeting, Bangladesh Bank Governor Abdur Rouf Talukder reportedly mentioned that this initiative could alleviate strain on foreign currency reserves, considering the substantial amount spent on various expenses in India.

Each year, Bangladeshi nationals spend approximately US\$ 2 billion on medical care, tourism, and education in India. Moreover, India ranks among the top three import destinations for Bangladesh. BB Governor Talukder stated that a dual currency Taka–

Rupee card could be introduced in September 2023. This card will enable travellers to conduct transactions in both Bangladesh and India, providing a convenient solution.<sup>12</sup> Apart from local transactions, users of this Pay Card will also enjoy the convenience of being able to spend up to US\$ 12,000 worth of rupees when traveling to India.<sup>13</sup>

In contrast to the current practice, which necessitates acquiring US dollars before entering India and subsequently converting them to rupees upon arrival, this card's utilisation would effectively help travellers mitigate potential exchange rate losses.<sup>14</sup>

## Conclusion

The new initiative aimed at facilitating bilateral trade between India and Bangladesh through the use of Indian rupees initially, and subsequently Bangladeshi Taka, is set to benefit both countries. This arrangement will not only be advantageous for businessmen on both sides, but also for the general populace. Particularly, it will prove to be of great assistance to Bangladeshis who frequently travel to India for purposes such as trade, tourism, education, and medical treatment. Additionally, it will be beneficial for certain Indians employed as experts in Bangladeshi companies.

However, it is important to note that this initiative will not replace the US dollar, rather, it will complement it. Trading in Indian rupees offers several advantages, including a decrease in the overall demand for the US dollar, reduced costs resulting from currency conversions, and a shorter processing time required for trade transactions. The success of this endeavour will also hinge on the participation of the private sector. Exporters must be willing to receive their earnings in local currencies instead of the US dollar.

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<sup>12</sup> Mukul Sharma, [“Rupee and Taka to Replace Dollar as Currency of Exchange between India, Bangladesh”](#), *Wion News*, 7 March 2023.

<sup>13</sup> [“Taka-Rupee Dual Currency Card to be Launched in September: BB Governor”](#), *Prothomalo*, 11 July 2023.

<sup>14</sup> [“Bangladesh Plans to Launch Taka-Rupee Debit Cards by December”](#), *bdnews24.com*, 11 July 2023.



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