ISDA. Safe, Efficient Markets
Celebrating 40 Years

ISDA India Derivatives Markets Forum
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Opening Remarks
Scott O'Malia, ISDA Chief Executive

Good morning and welcome to the India Derivatives Markets Forum. It's great to hold this event in Mumbai for the second time and to have the opportunity to meet with market participants and policymakers.

I'd like to start by thanking Shri T. Rabi Sankar, deputy governor of the Reserve Bank of India (RBI), for being with us today and delivering keynote remarks. The RBI has played a central role in the development of India's over-the-counter (OTC) derivatives market in recent years, putting in place a series of measures that have laid the foundations for safe and efficient trading. At ISDA, we value the ongoing dialogue we have with the RBI, and we look forward to many more years of fruitful collaboration.

Travelling to different parts of the world to meet with ISDA members and regulators is one of the highlights of my job, but there's always something special about visiting India. I think it's the strong sense of opportunity and energy that you get from this rapidly growing economy. The International Monetary Fund forecasts economic growth in India will remain at 6.5% into next year, putting it ahead of most other economies. With the world's largest population, India is on track to rise from the fifth to the third largest global economy by 2030 – an astonishing rate of growth.

But India's derivatives market remains small, with OTC interest rate derivatives turnover accounting for roughly 0.1% of the global daily average in 2022. We think there's an opportunity here. Derivatives are vital for healthy, competitive and liquid financial markets and help spur economic growth. According to a new report we'll shortly publish to mark ISDA's 40th anniversary, 87% of nearly 1,200 companies across seven major stock indices use OTC derivatives for a variety of purposes. By creating stability and helping firms to reduce risk, secure cheaper funding and enhance performance, derivatives enable companies to plan for the future with greater confidence, encouraging investment and growth.

ISDA is committed to working with the RBI and local market participants to support the development and growth of India's OTC derivatives market. Last year, we published a whitepaper that set out a series of market and policy recommendations. I'll talk in these remarks about the important steps that have already been taken and the priorities ahead.

A safe and efficient derivatives market depends on many things, but the enforceability of close-out netting is a critical foundation. By allowing parties to shrink their obligations to a single net payment in the event of a default, netting drastically reduces credit risk and increases the capacity for firms to trade and lend. Regulators also allow close-out netting to be risk-reducing for the purposes of capital requirements, encouraging greater participation in local capital markets by foreign and domestic institutions, boosting competition and liquidity.

India has already taken this vital step, and the legislation that passed in September 2020 to recognize netting enforceability was a seminal milestone for the further development of the derivatives market.

Critical as netting may be, it's not the only ingredient for a thriving, mature derivatives market. An appropriate regulatory framework that is consistent with other jurisdictions is also vital. Over the past 15 years, a series of regulatory reforms have been implemented around the world to improve the resilience of the derivatives market, driven by commitments made by the Group-of-20 (G-20) leaders in 2009. These include central clearing, trade reporting and margin requirements for non-cleared trades.

Led by the RBI, a regulatory framework has been developed for India's derivatives market that reflects the G-20 commitments. It is vital that market participants are able to trade efficiently on a cross-border basis – this relies on consistency and recognition of equivalent regulations in other jurisdictions.

Clearing of derivatives in India has been well established for a long time, with the Clearing Corporation of India Limited (CCIL) offering clearing of a wide range of products, including interbank dollar-rupee forward transactions, rupee interest rate swaps and forward rate agreements. The RBI has also required the exchange of variation margin for non-cleared derivatives since May 2023, which has helped to improve financial stability and reduce systemic risk.

Now, the focus has turned to initial margin (IM). On April 1 – three weeks from today – IM requirements for non-cleared derivatives will come into effect in India, marking another milestone in the market's development.

Crucially, the IM framework will allow Indian branches of foreign banks to rely on substituted compliance when entering into non-cleared derivatives transactions with another foreign bank branch or an Indian bank in scope of the rules. This avoids a scenario in which a foreign bank branch would have had to comply with multiple rule sets when transacting with an Indian counterparty. ISDA engaged extensively with the RBI on this issue as the IM rules were developed. We commend the central bank for its pragmatic approach that will significantly improve operational efficiency and competition in the Indian market.

Since the IM rules were finalized last year, ISDA has been working closely with members to get the necessary documentation and margin calculation models in place. The ISDA Standard Initial Margin Model (ISDA SIMM) provides a single, common methodology for the calculation of margin requirements, enabling counterparties to reduce costs and cut the potential for disputes. After nearly nine years, the ISDA SIMM has a proven track record in supporting the efficient exchange of IM and the model enjoys strong support from the official sector. ISDA conducted training on the ISDA SIMM in Mumbai in November, and we will continue to work with market participants to enable them to access the model.

Implementation of the IM rules will be a significant step in strengthening risk management and aligning with global standards, but there are several outstanding operational and legal issues that must be addressed.

One of the key concerns is the potential for disputes if different IM amounts are calculated for a single portfolio without clarity on which takes priority. This would require market participants to engage directly to determine whether an IM calculation override is appropriate. This process can be inefficient, time-consuming and costly.

Another vital step in preparing for the implementation of IM rules is a thorough review of custodial arrangements to ensure consistency with other major jurisdictions. This will enable foreign bank branches to access local custodial services, while ensuring compliance with the IM rules in their home jurisdictions. In recent years, an ISDA-led review of custodial arrangements and documentation in different jurisdictions has become a crucial part of diligent industry preparation for the implementation of the rules.

ISDA would welcome a dialogue with CCIL to better understand the operational and legal structure of its custody platform. This would allow us to develop the industry-standard documentation that is required to facilitate implementation of the IM rules in India.

By collaborating closely with members and policymakers on these important issues, we will pave the way towards an effective IM framework that is consistent with other major jurisdictions. As we prepare for the April 1 deadline, it’s important to point out that the work won’t end on that date. ISDA will support market participants that expect to be in scope of the rules from the start, but we will also help new entities that come into scope later on to understand the requirements and access the ISDA SIMM.

Before wrapping up, let me reiterate that ISDA is here in India for the long haul. As I mentioned at the start of these remarks, our whitepaper last year presented a comprehensive set of recommendations to support the further development of India’s OTC derivatives market.

The recommendations are broadly focused around five key areas:

1. Broaden product development, innovation and diversification;
2. Foster adoption of similar market and risk principles across regulatory regimes;
3. Enhance market access and diversification of participants;
4. Ensure growth in a safe and efficient manner; and
5. Encourage greater alignment with international principles and practices.

Since the paper was published, our priority has been to discuss the recommendations with policymakers and market participants to determine the areas that should be prioritized. I’m pleased to say we’ve seen strong engagement across the buy and sell side and are actively discussing ways to improve and expand access to the derivatives market. We have a panel lined up this afternoon with buy-side market participants who will explore this issue in more detail.

ISDA is also working to support the development of long-tenor interest rate derivatives and the liberalization of certain asset classes, including OTC commodity derivatives.

This is a very exciting juncture for India's derivatives market. As we reflect on the impressive progress that has been made in recent years and prepare for the implementation of the IM requirements next month, we must also think about what comes next. I'm looking forward to hearing the insights of our speakers throughout the day, and I hope you find the sessions informative and constructive.

Thank you.