RBI’s FCNR(B) Swap Facility Mobilises $127 Billion, Shifts Foreign Exchange Risk and Tests Banking Sector Resilience

Published On: 14-09-2026

Recent Developments:

- The **Reserve Bank of India (RBI)** introduced a concessional US dollar–rupee foreign exchange swap facility in June 2026 to encourage banks to mobilise fresh **Foreign Currency Non-Resident (Bank) [FCNR(B)] deposits** with three-to-five-year maturities.
- The facility attracted **$127.22 billion through FCNR(B) deposits** by August 31, 2026, accounting for nearly 90% of the total $136.37 billion mobilised through the broader swap programme, which also covered external commercial borrowings and overseas foreign currency borrowings.
- The RBI closed the **FCNR(B)** mobilisation window on **August 31, 2026**, earlier than the originally envisaged September-end timeline, after inflows significantly exceeded expectations.
- The development has shifted attention from **mobilisation of foreign currency** to the management of foreign exchange risk, particularly because the RBI swap covers the principal but not the interest payable to depositors.

About FCNR(B) Deposits:

Nature and Key Features:

- **FCNR(B) deposits** are term deposits maintained by non-resident Indians with Indian banks in **foreign currency**, rather than in Indian rupees.
- Both the **principal and interest are denominated in foreign currency**, with US dollars being the dominant currency for such deposits.
- Since the depositor does not bear direct rupee depreciation risk on the foreign-currency amount, **FCNR(B)** deposits provide an attractive savings instrument for NRIs.
- Deposits generally have maturities ranging from **one to five years**, while the special 2026 swap facility specifically targeted fresh deposits with three-to-five-year maturities.

The Special RBI Swap Facility:

Rationale and Design:

- The RBI introduced the facility in June 2026 amid **external-sector pressures**, including elevated crude oil prices, geopolitical uncertainty and the need to strengthen foreign exchange liquidity.
- Under the arrangement, banks could mobilise eligible fresh **FCNR(B)** deposits and obtain a **US dollar–rupee foreign exchange swap from the RBI**, reducing the banks’ hedging burden on the principal.
- The RBI also temporarily removed the interest-rate ceiling for eligible fresh **FCNR(B)** deposits with three-to-five-year maturities, allowing banks greater flexibility to attract NRI funds.
- The facility was substantially more successful than initially expected, with **FCNR(B)** inflows alone ultimately reaching **$127.22 billion**.

Significance for India:

- The inflows strengthened the availability of **foreign currency**, supported India's balance of payments and contributed to a sharp increase in the RBI's foreign exchange reserves.
- India's foreign exchange reserves reached a record **$785.7 billion** in the week ending September 4, 2026, although the increase reflected multiple capital-flow factors and not **FCNR(B)** deposits alone.
- For banks, the deposits provided a significant source of **foreign-currency funding and liquidity**, with Moody's noting their positive effect on Indian banks' funding capacity.

How the Foreign Exchange Risk Is Divided:

RBI Covers the Principal:

- The RBI's swap arrangement covers **only the principal amount** of eligible **FCNR(B)** deposits and does not cover the interest component.
- Consequently, the RBI effectively absorbs the foreign exchange hedging cost associated with the principal, protecting banks against adverse movements in the rupee–dollar exchange rate.
- The estimated hedging cost can be significant, with market estimates placing it at around **3% annually**, although the actual economic cost depends on market conditions and the duration of the exposure.

Banks Bear the Interest Risk:

- Banks remain responsible for arranging the foreign currency required to pay **interest to FCNR(B) depositors** because the RBI swap does not cover the interest component.
- This creates a separate foreign exchange exposure for banks, particularly because many deposits have three-to-five-year maturities and interest payments can become substantial when the rupee depreciates.
- The risk therefore has not disappeared; instead, it has been **allocated between the RBI and commercial banks**.

Why Some Banks Have Left Interest Exposure Unhedged:

Cost of Hedging:

- Hedging the foreign exchange exposure associated with future interest payments can cost banks around **3% annually**, making complete advance hedging expensive.
- Foreign banks have generally shown greater willingness to hedge this exposure, while several Indian private-sector and state-owned banks have retained significant unhedged positions.
- Some banks prefer to purchase dollars in the **spot market when interest payments become due**, rather than paying the cost of a long-term hedge today.

The Risk of a Weaker Rupee:

- The strategy remains manageable if the rupee stays relatively stable, but a sharp depreciation could significantly increase the rupee cost of meeting dollar-denominated interest obligations.
- For example, a **$1 million interest payment** would require ?9.5 crore at ?95 per dollar but ?10 crore if the exchange rate moves to ?100 per dollar.
- A bank that has hedged the exposure is protected against this movement, whereas an unhedged bank must absorb the additional rupee cost.

RBI's Cost-Benefit Position:

Reserve Accumulation and Investment Returns:

- The RBI's principal-related hedging cost should be assessed against the benefit of receiving foreign currency that can be added to the country's reserve assets and subsequently invested.
- If foreign currency assets generate returns of around **4.5–5%**, such returns could potentially offset a hedging cost of around 3%, depending on the duration and market conditions.
- The arrangement therefore represents not merely a fiscal cost but a **balance-sheet trade-off** between the cost of hedging and the return generated from reserve assets.

Liquidity Management Challenge:

- The large inflow also created a substantial **rupee liquidity surplus** in the domestic banking system because the foreign exchange mobilisation generated corresponding domestic-currency liquidity.
- The RBI has subsequently used liquidity-management instruments, including foreign-exchange swaps and government bond sales, to absorb excess liquidity and maintain orderly money-market conditions.

Broader Economic Implications:

External Sector and Rupee Stability:

- The scheme strengthened India's foreign exchange position during a period of pressure on the rupee and provided an additional buffer against external shocks.
- Higher reserves improve confidence in India's ability to meet **external payment obligations**, manage disorderly currency movements and absorb temporary capital-flow disruptions.

Banking Sector Risk:

- The major concern is the **maturity mismatch and foreign exchange exposure** created by unhedged interest obligations.
- If the rupee depreciates sharply near the maturity of deposits, banks may need to purchase large quantities of dollars in the spot market, potentially increasing demand for foreign currency precisely when market conditions are stressed.
- This could amplify short-term pressure on the rupee and increase banks' funding costs.

Monetary Policy and Liquidity:

- Large foreign currency inflows can increase domestic rupee liquidity, complicating the RBI's task of keeping short-term market rates aligned with its monetary-policy stance.
- The RBI's subsequent liquidity-absorption operations demonstrate the interaction between **foreign exchange management, monetary policy and banking-system liquidity**.

Way Forward:

Strengthen Risk Management:

- Banks should conduct **stress tests** for different rupee depreciation scenarios and assess the foreign currency liquidity required for future interest payments.
- Greater transparency regarding banks' unhedged foreign exchange exposure would help regulators and investors evaluate systemic risks.

Balance Reserve Accumulation with Cost:

- The RBI should evaluate the **net economic cost** of the swap by comparing hedging expenses, reserve-asset returns and broader macroeconomic benefits rather than considering the hedging cost in isolation.
- Future facilities should be calibrated according to reserve requirements, external financing conditions and the banking system's capacity to absorb foreign currency liabilities.

Maintain Liquidity Discipline:

- Large capital inflows should be accompanied by appropriate **sterilisation and liquidity-management measures** to prevent excessive domestic liquidity from weakening monetary-policy transmission.
- The RBI can employ foreign-exchange operations, variable-rate liquidity operations and open-market operations according to evolving market conditions.

Conclusion:

- The 2026 **FCNR(B)** swap facility successfully mobilised foreign currency on a scale far beyond expectations, with **$127.22 billion** raised through **FCNR(B)** deposits by August 31.
- Its central policy innovation was to shift the foreign exchange risk on the **principal to the RBI**, while leaving banks responsible for the currency risk associated with interest payments.
- The arrangement strengthened India's reserves and banking-sector foreign currency liquidity, but the sizeable unhedged interest exposure means that part of the currency risk has been **deferred rather than eliminated**.
- The ultimate success of the facility will therefore depend not only on the reserves accumulated but also on how effectively the RBI and banks manage **foreign exchange risk, liquidity, maturity concentration and systemic stability**.

Value Addition for UPSC:

Key Concepts:

- **FCNR(B):** Foreign-currency term deposits maintained in India by non-resident Indians.
- **Forex Swap:** A transaction involving the exchange of currencies with an agreement to reverse the transaction at a specified future date.
- **Currency Risk:** The possibility of financial loss arising from adverse movements in exchange rates.
- **Sterilisation:** Central-bank operations used to offset the domestic liquidity impact of foreign exchange interventions.

Prelims Facts:

- **FCNR(B) deposits are denominated in foreign currency**, unlike rupee-denominated non-resident deposit schemes.
- The 2026 special **FCNR(B)** swap facility was introduced by the **RBI in June 2026**.
- Eligible deposits under the special facility generally carried **three-to-five-year maturities**.
- The RBI swap covered the **principal but not the interest**.
- **FCNR(B)** deposits mobilised under the facility reached **$127.22 billion by August 31, 2026**.
- The broader RBI foreign exchange mobilisation programme attracted **$136.37 billion** across **FCNR(B)**, external commercial borrowings and overseas foreign currency borrowings by August 31, 2026.