‘Voluntary Retention Route’ (VRR) for investment by FPIs – Discussion Paper

Reserve Bank, in consultation with the Government of India and Securities and Exchange Board of India (SEBI), proposes to introduce a separate channel, called the ‘Voluntary Retention Route’ (VRR), to enable FPIs to invest in debt markets in India. Broadly, investments through the Route will be free of the macro-prudential and other regulatory prescriptions applicable to FPI investments in debt markets, provided FPIs voluntarily commit to retain a required minimum percentage of their investments in India for a period of their choice.

Participation through this Route will be entirely voluntary. The features of the Route are explained below in detail.

1. Objective

The objective of the VRR channel is to attract long-term and stable FPI investments into debt markets while providing FPIs with operational flexibility to manage their investments.

2. Eligible investors

Any entity registered as an FPI with SEBI is eligible to participate through this Route.

3. Overview

a. The total amount that may be invested via the Route shall be decided by the Reserve Bank from time to time based on macro-prudential considerations and assessment of investment demand.
b. Investments through this Route shall be in addition to the FPI investment limits (General Investment Limit) under the Medium Term Framework, as per A.P.(DIR Series) Circular No. 22 dated April 6, 2018, as modified from time to time.
c. The total amounts for investment through the Route shall be separately indicated for Government securities (Central Government securities as well as State Development Loans, VRR-Govt) and corporate debt (VRR-Corp).
d. The total amount for investment under VRR-Govt shall be individually allocated to FPIs through an auction process. A similar allocation shall be made separately for the total amount of investment under VRR-Corp.
e. Under the auction, the criterion for allocation of investment amount to each FPI (*called the Committed Portfolio Size, or CPS*) shall be the retention period proposed by the FPI in the bid.

f. The minimum retention period shall be three years, or as decided by RBI for each auction.

g. After allocation through the auction, successful FPIs shall invest the allocated *CPS* in debt instruments and remain invested at all times during the voluntary retention period, subject to the following relaxations:

   i. The minimum investment of an FPI during the retention period shall be 67% of the *CPS*. This requirement shall be adhered to on an end-of-day basis. For the purpose, investment shall not include cash or deposits.

   ii. The flexibility for modulating investments between 67%-100% of *CPS* is intended to enable FPIs to adjust their portfolio size as per their investment philosophy.

h. Amounts of investment shall be in terms of the face value of securities.

4. Auction process for allocation of limits

a. For every VRR auction, RBI shall announce the total investment amount to be auctioned (auction amount), and the minimum retention period applicable to allotments under that auction. Auctions shall be announced and carried out separately for VRR-Govt and VRR-Corp categories. The auction process shall be as under:

   i. An FPI shall bid two variables - the amount it proposes to invest and the retention period of that investment, which shall not be less than the minimum retention period.

   ii. No FPI (including its related FPIs) shall bid for an amount greater than 50% of the auction amount. For this purpose, the term “related FPIs” shall mean ‘investor group’ as defined in Regulation 23(3) of SEBI (Foreign Portfolio Investors) Regulations, 2014.

   iii. Bids will be accepted in descending order of retention period, the highest first, until the amount of accepted bids adds up to the auction amount.

   iv. Allotment at margin (i.e., at the lowest retention period accepted), if the amount bid at margin is more than the amount available for allotment, shall be as below:

      a) The marginal bid shall be allocated partially such that the total acceptance amount matches the auction amount.

      b) In case there are more than one marginal bids, allocation shall be made to the bid with the largest amount, and then in descending order of amount bid until the acceptance amount matches the auction amount.

c) In case the amount offered is the same for two or more marginal bids, the amount will be allocated equally.

v. RBI will have the full discretion to accept or reject any or all bids, either wholly or partially, without assigning any reason.

5. Management of portfolio

a. Successful bidders will be given a period of one month, starting from the date of announcement of auction results, to invest.
b. An FPI will be required to invest a minimum of 67% of the *CPS* within the one-month period. The retention period will commence from the end of the one-month period.
c. One month prior to the end of the committed retention period, an FPI will exercise its choice to continue investments under this Route by opting for an additional identical retention period.
d. In case an FPI decides not to continue under VRR at the end of the retention period, it may choose to liquidate its portfolio and exit, or it may shift its investments to the 'General Investment Limit'. This shifting would be subject to availability of limit under the 'General Investment Limit'.
e. FPIs, who under exceptional circumstances (which involves the FPI exiting from all its activities in India), wish to liquidate their investments under the Route prior to the end of the retention period, may do so by selling their investments to other FPI or FPIs. However, the FPI (or FPIs) buying such investment shall abide by all the terms and conditions applicable to the seller under the Route.
f. An FPI that violates any of its commitments under this Route shall be deregistered by SEBI.

6. Eligible instruments and tenor limits

a. Under VRR-Govt, FPIs will be eligible to invest in any Government security including T-bills. Similarly, under VRR-Corp, FPIs may invest in corporate debt instruments, including commercial papers.
b. Investments through the Route shall be exempt from the requirements in paragraphs 4(b), (e) and (f) of A.P. (DIR Series) Circular No. 31 dated June 15, 2018.

c. Income from investments through the Route may be reinvested at the discretion of the FPI. Such investments will be permitted beyond the CPS.

7. Access to other facilities

a. FPIs investing through the Route will be eligible to participate in repos for liquidity management, provided that the amount borrowed or lent under repo shall not exceed 10% of their investment under VRR. Securities sold under repo shall not bring the holdings below 67% of the CPS. Securities bought under repos shall not be reckoned for maintenance of the minimum 67% of CPS.
b. FPIs will be allowed to participate in any currency and interest rate derivative instrument, OTC or exchange traded, to hedge their interest rate or currency risk.

8. Other operational aspects

a. Utilisation of limits and adherence to other requirements of this Route will be the responsibility of both the FPI and its custodian.
b. FPIs shall enter into separate legal agreement/contract, enforceable within the jurisdiction of India, with their custodians, covering all relevant aspects of the VRR.
c. FPIs shall open a separate Special Non-Resident Rupee (SNRR) account for investment through the Route. All fund flows relating to investment through the Route shall reflect in this account.
d. FPIs shall also open a separate securities account for holding debt securities under this Route.
e. FPIs already registered with SEBI are not required to undertake fresh KYC for investment through this Route.