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**A STUDY ON ASSESSING THE RUPEE'S POTENTIAL
TOWARDS BECOMING INTERNATIONAL CURRENCY**

Master Thesis Report submitted in partial fulfilment of the requirement for the award of the
degree of

Master of Business Administration (MBA)

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EXECUTIVE SUMMARY

The Indian economy has always proved to be a very strong economy in terms of growth as it has become one of the largest economies in the world. Through this economic growth, however, the Indian Rupee is still a small portion in the world monetary currency transactions, when compared to the currencies of other emerging economies. It is a paradox that calls into serious doubts the role of the Rupee in international trade and finance. As the GDP growth in India has increased tremendously, the economic impact on the global monetary system has been very low despite the fact that the presence of the rupee within the global monetary system has been very low. This research will seek to determine the reasons that underlie this mismatch and the possibility of INR pursuing a more visible international reputation. One of the main obstacles to be discovered in the present research is the structural vulnerability of the Indian trade and financial ecosystem that does not allow the Rupee to grow outside of the country. Although the remittance inflows and the increasing exports play a positive role, trade imbalances and the volatility of the capital flows pose ambiguities to the stability and reliability of the Rupee as an international currency. When comparing them to other emerging market currencies like the Chinese Yuan and Brazilian Real it can be seen that strategic policy interventions and development of financial markets have been important factors in boosting their use in the world market.

The underrepresentation of the INR in global financial markets is not merely a statistical anomaly; it reflects deeper structural, institutional, and policy-related constraints that have historically limited the currency's external adoption. Trade imbalances, particularly those driven by India's persistent dependence on crude oil and commodity imports, have placed recurrent pressure on the Rupee's exchange rate stability. Capital flow volatility, incomplete capital account convertibility, and the absence of deep offshore INR markets have further constrained the currency's utility as an instrument of international trade and investment. These structural vulnerabilities, embedded within India's trade and financial ecosystem, serve



as primary barriers to the Rupee's internationalisation and must be addressed through a coherent and sustained policy framework.

The paper discusses the ways of how such actions can be adopted in the Indian scenario to make the Rupee stronger. In an effort to deal with these issues, the study identifies major policy suggestions that would assist in enhancing the stability of the Rupee and its adoption by other countries. Strategies to strengthen the foreign exchange reserves of India, maintain the exchange rates and facilitate the international trade settlements using the Rupee are pertinent. Also, diversifying the financial markets in India, increasing the liquidity of INR in the international markets and the capital account policies could be used to gain investor trust and prompt more people to use the Rupee. The paper states the importance of India adopting a multi-dimensional strategy that integrates economic reforms, trade policies and financial market developments to spur the internationalization of the rupee. Through these aspects, this study aims to give a good insight into the current state of the Indian Rupee, whether it can be globalized and the steps that it needs in its globalization strategy. The conclusion presents a very important source to the policymakers, economists and financial institutions aiming to increase the economic impact of India in the world by reforming its currency. Since India is on the path of transforming itself to be a leading economic force, consolidating the position of the Rupee as an international currency will be a crucial move towards consolidating its presence in the global economy arena.

On the basis of this analysis, the study advances a set of policy recommendations designed to strengthen the INR's international standing. These include the strategic accumulation of foreign exchange reserves, the development of an offshore INR market, the expansion of INR-denominated trade settlement agreements, the deepening of domestic bond and capital markets to attract global investors, and the gradual liberalisation of the capital account under a prudent regulatory framework. In aggregate, the study argues that INR internationalisation is not an unattainable objective, but one that requires a multi-dimensional, strategically sequenced approach that combines macroeconomic stabilisation, institutional reform, and active financial diplomacy. As India continues on its trajectory toward becoming a leading



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force in the global economy, the consolidation of the Rupee's position as an internationally recognised and utilised currency represents both an economic imperative and a strategic opportunity. This research aims to contribute a rigorous, evidence-based perspective to that important policy conversation.



CHAPTER 1: INTRODUCTION AND LITERATURE REVIEW

1.1 Historical Origins of Currency and Global Monetary Systems

Throughout history, currency has played a vital role in facilitating trade, economic growth, and the development of civilizations. The earliest forms of currency were barter-based, where goods and services were exchanged directly. However, as societies grew more complex, the need for a standardized medium of exchange led to the adoption of commodity money, such as gold, silver, and other precious metals. The first recorded use of metal coins dates back to the Lydian civilization in the 7th century BCE, and over time, various regions developed their own monetary systems. The emergence of paper money in China during the Tang Dynasty marked a significant evolution in currency, eventually influencing the global financial systems. Today, currency exists in multiple forms, from physical cash to digital and cryptocurrency, reflecting the ongoing advancements in economic structures worldwide.

In ancient India, the concept of currency exchange can be traced back to the Mahajanapada period (600 BCE - 300 BCE), when different kingdoms issued their own coins, known as punch-marked coins. These coins, made of silver and copper, facilitated trade among the sixteen major Mahajanapadas, allowing for a structured economic system. Alongside coins, various trade routes and banking practices emerged, with moneylenders and merchants playing a crucial role in financial transactions. The existence of such an early monetary system reflects India's deep-rooted economic history, which laid the foundation for future developments in trade and currency exchange. The ancient Indian economy, with its extensive trade networks spanning Central Asia, the Middle East, and the Roman Empire, functioned on a sophisticated financial system that relied on both metal currency and the early forms of credit instruments.

1.2 The Economic Significance of Currency Internationalisation

The internationalization of a currency brings significant economic advantages to a nation. A widely accepted currency reduces exchange rate risks, facilitates global trade, and lowers



transaction costs for businesses engaged in international transactions. It strengthens the country's financial market by increasing the demand for domestic assets and bonds, leading to greater economic stability. Countries with internationally accepted currencies also experience increased foreign investments and enhanced global financial influence. Additionally, an international currency allows governments to borrow at lower costs and conduct global trade using their own currency, reducing dependence on foreign reserves. The ability to settle international payments in domestic currency further strengthens economic sovereignty, providing nations with greater control over monetary policies and reducing exposure to external economic shocks.

1.3 The Rise of the US Dollar as the Dominant Global Reserve Currency

The rise of the US Dollar (USD) as the dominant global reserve currency can be traced back to the Bretton Woods Agreement of 1944, which established the USD as the primary currency for international trade and finance. The agreement pegged major global currencies to the Dollar, which was backed by gold, making it the most stable and widely accepted currency. Even after the collapse of the gold standard in 1971, the USD retained its global dominance due to the sheer size of the US economy, its deep and liquid financial markets, and the widespread trust in US institutions. The petrodollar system, where oil transactions are primarily conducted in USD, further strengthened its global position. Today, the USD remains the most used currency for international trade, financial reserves, and global investments, largely due to the strength of the US Treasury market, the dominance of American multinational corporations, and the global influence of US monetary policy. Despite occasional challenges, such as inflationary pressures and rising national debt, the Dollar continues to serve as the world's de facto reserve currency, accounting for a significant share of global foreign exchange reserves.

The petrodollar system, which emerged in the 1970s following agreements between the United States and major oil-exporting nations to price petroleum exclusively in Dollars, provided an additional structural prop for Dollar demand. As energy constitutes the most



universally traded commodity in the global economy, the Dollar's role as the de facto currency of oil transactions ensured persistent global demand for Dollar-denominated assets. Today, despite challenges arising from rising US fiscal deficits, periodic inflationary pressures, and growing calls for currency diversification in global reserves, the Dollar continues to account for the largest share of global foreign exchange reserves, international trade invoicing, and cross-border financial transactions. Its supremacy reflects not only the size of the US economy but also the institutional depth of its financial markets and the credibility of its monetary governance framework.

1.4 The Euro as a Major Reserve Currency

The Euro (EUR) emerged as a major reserve currency with the formation of the Eurozone and the launch of the European Economic and Monetary Union (EMU) in 1999. The introduction of the Euro consolidated multiple European currencies into a single, unified monetary system, significantly increasing its appeal in global trade and finance. The European Central Bank (ECB) plays a crucial role in maintaining the Euro's stability, making it a preferred reserve currency for central banks worldwide. Over time, the Euro has gained prominence due to the economic strength of the Eurozone, the size of its trade bloc, and the deep liquidity of its bond markets. The Euro is the second most held reserve currency after the US Dollar, often used as an alternative in international trade and financial agreements. However, challenges such as political fragmentation within the Eurozone, economic disparities among member states, and periods of financial crises have occasionally limited the Euro's rise to the level of the USD. Nonetheless, with a strong regulatory framework and continued economic integration, the Euro remains one of the most influential global currencies.

Beyond transactional efficiency, an internationally accepted currency strengthens a country's financial markets by generating sustained demand for domestic assets, bonds, and equities from foreign investors. This demand deepens market liquidity, improves price discovery, and contributes to the overall resilience of the domestic financial system. Nations whose



currencies are widely held also enjoy what economists term "exorbitant privilege": the ability to finance fiscal deficits and external imbalances at lower interest rates, since global demand for their currency-denominated assets reduces borrowing costs. The United States has long benefited from this structural advantage through the dominance of the US Dollar. Equally important is the dimension of economic sovereignty: a country that can settle its international trade and financial obligations in its own currency is less vulnerable to external monetary shocks and enjoys greater autonomy in the conduct of its monetary policy.

1.5 The Rise of Asian Currencies in Global Finance

The rise of the Japanese Yen (JPY) and the Chinese Yuan (CNY/CNH) as reserve currencies in the global economy is a result of strategic economic policies, financial market development, and geopolitical shifts.

Japan, after its post-World War II reconstruction, experienced rapid industrialization and became the world's second-largest economy by the late 20th century. The Plaza Accord of 1985, which aimed to depreciate the US Dollar and strengthen other major currencies, played a crucial role in elevating the Yen's global status. Over time, Japan's stable financial system, strong trade surplus, and deep capital markets contributed to the Yen becoming a safe-haven currency, widely used in international trade and foreign exchange reserves. Today, while the Yen remains an important reserve currency, its international influence has been somewhat constrained by prolonged economic stagnation, low interest rates, and Japan's highly conservative monetary policies.

The Chinese Yuan (CNY), also known as the Renminbi (RMB), has emerged as a significant player in the international financial system, particularly following China's economic reforms in 1978 and its subsequent rise as a global economic powerhouse. The internationalization of the Yuan accelerated after China launched the CNH (offshore Yuan) market in 2010, allowing global investors to trade the currency freely outside mainland China, particularly in Hong Kong. The inclusion of the Yuan in the International Monetary Fund's (IMF) Special Drawing Rights (SDR) basket in 2016 marked a major milestone, signaling its growing



acceptance as a reserve currency. China has actively promoted the Yuan for international trade settlements, particularly through Belt and Road Initiative (BRI) agreements, currency swap arrangements, and cross-border payment systems like CIPS (China's alternative to SWIFT). As China continues to expand its economic influence, the Yuan's role as a reserve currency is expected to grow, although concerns about capital controls and financial transparency remain key challenges in its full internationalization.

1.6 The Indian Rupee: A Historical Overview (1947 to Present)

Following India's independence in 1947, the Indian government introduced a new monetary framework, and the Reserve Bank of India (RBI) assumed full control over currency issuance and monetary policy. In 1957, the Rupee was decimalized, replacing the traditional annas system with a division of 100 paise per Rupee. Initially, the INR was pegged to the British Pound and later to the US Dollar under a controlled exchange rate system. However, economic challenges, including balance of payments crises and inflationary pressures, led to several devaluations of the Rupee, notably in 1966 and 1991, as India shifted toward a more open economic model. The economic liberalization of 1991 marked a turning point for the Rupee, transitioning India into a market-driven exchange rate regime, leading to increased foreign investment, international trade, and financial globalization.

In recent decades, the INR has seen significant fluctuations, influenced by global market dynamics, trade imbalances, and capital flows. The increasing integration of the Indian economy with global markets has led to both opportunities and challenges in maintaining exchange rate stability. Despite India's economic growth, the Rupee has struggled to gain a stronghold as an international currency due to trade deficits, external borrowing, and the dominance of the US Dollar in global transactions. Efforts have been made to promote the use of the Rupee in international trade agreements, particularly with neighboring countries and key trading partners.

The devaluations of 1966 and 1991 were consequential turning points in the Rupee's history. The 1991 crisis, precipitated by a severe balance of payments deficit and near-depletion of



foreign exchange reserves, catalysed a fundamental reorientation of India's economic strategy. The liberalisation reforms that followed dismantled many of the structural rigidities of the previous regime, opened the economy to foreign capital and trade, and initiated a transition toward a more market-determined exchange rate system. The Rupee has since been managed under a flexible exchange rate framework, with the RBI intervening periodically to moderate excessive volatility rather than to defend a fixed parity.

In the decades following liberalisation, the INR has experienced both the opportunities and vulnerabilities associated with greater integration into global financial markets. India's expanding trade relationships, growing foreign direct investment inflows, and position as the world's largest recipient of remittances have provided important sources of foreign exchange support. At the same time, the currency has remained susceptible to external shocks, including global commodity price cycles, shifts in US monetary policy, geopolitical disruptions, and capital flow volatility. Today, the Indian Rupee stands at a juncture where the structural conditions for a greater international role are gradually maturing, but where decisive and coherent policy action is still required to translate that potential into reality.

Today, the Indian Rupee stands at a critical juncture, with discussions around its internationalization gaining momentum. With India's growing economic influence, expanding trade networks, and strategic financial policies, the INR has the potential to play a more significant role in global finance. However, to achieve this, India must strengthen its foreign exchange reserves, deepen financial markets, enhance currency convertibility, and reduce external vulnerabilities. The journey of the Indian Rupee reflects the broader evolution of India's economic landscape, from ancient trade routes to a modern, globally connected economy.

1.7 Problem Statement

“Less Share of INR in The Total Volume of Currency Denominations Exchanged in The International Economy, Despite of Growth In Indian Economy.”



Despite being one of the fastest-growing economies in the world, India's currency, the Indian Rupee (INR), holds a disproportionately low share in global financial transactions. While India has made significant strides in economic development, trade expansion, and financial market reforms, the Rupee remains largely absent from international currency reserves, trade settlements, and foreign exchange markets compared to other emerging market currencies like the Chinese Yuan (CNY) and the Japanese Yen (JPY). The global dominance of the US Dollar (USD) and the Euro (EUR), along with limited international confidence in the Rupee's stability, has restricted its adoption for cross-border transactions. Despite India's growing role in global trade and investment, the Rupee continues to be underutilized in international markets, necessitating an in-depth analysis of the factors limiting its global adoption and the policies required to enhance its role as a recognized and widely used international currency. India's relative underperformance in this regard, despite its substantial economic size, suggests that the constraints are not purely structural but are also a product of institutional inertia, incomplete financial market development, and an insufficiently proactive internationalisation strategy.

This research therefore seeks to investigate the determinants of the INR's limited international adoption, to assess its potential for greater global utilisation relative to comparable emerging market currencies, and to identify the specific policy and institutional reforms that could accelerate its internationalisation. The study does so by analysing macroeconomic data encompassing exchange rate dynamics, trade flows, balance of payments components, remittance patterns, and central bank reserve management practices, thereby providing an empirically grounded foundation for its analytical and policy conclusions.

1.8 Review of Relevant Literature

1.8.1 Bahaj and Reis (2024) — Jumpstarting an International Currency

In their exploration of a journey to currency internationalization, Bahaj and Reis (2024) use the example of the Chinese Renminbi (CNY). They discuss the main economic and policy



steps taken by China which have assisted the Renminbi to become more globally accepted, like bilateral currency swap agreements, financial market reforms, and trade settlement policies.

The authors bring out the instrumental roles of government-led initiatives such as the Belt and Road Initiative (BRI) and setting up offshore Yuan markets (CNH) in increasing the international footprint of the Chinese currency.

Bahaj and Reis (2024) Kyriacos Symeonidis's paper argues that to a currency be accepted internationally apart from having a strong economic base there should be continuous policy support and global trade integration.

This research offers a comparative model for evaluating the challenges and opportunities that the Indian Rupee (INR) internationalization will have to face.

1.8.2 Banerjee (2023) — The Indian Financial System and the Quest for Monetary Power

Banerjee (2023) looks at the history of the Indian Rupee internationalization attempts and also the issues of the system that have held it back. The paper traces the evolution of India's monetary policy, trade settlement agreements, and the liberalization of the financial market over different periods of time.

Discussing India's prior endeavors, Banerjee describes the efforts through bilateral agreements with neighbors, the launch of INR-denominated trade settlements, and very limited steps towards capital account convertibility.

According to the results, India, to some extent, has succeeded in regional trade promotion through the Rupee. However, problems such as exchange rate volatility, trade imbalances, and capital flow restrictions have restrained the currency from gaining wider global acceptance.

In the opinion of Banerjee, if the Rupee is to be recognized internationally, India would have to build up its foreign exchange reserves, expand its financial markets and increase the trust in its monetary policy.



1.8.3 Medlin (2023) — What Drives Central Bank Swap Line Use?

Medlin (2023) delves deep into the subject of the central banks' currency swap lines and evaluates their influence on currencies' internationalization. The paper illustrates the concept of currency swap agreements whereby two central banks mutually exchange their currencies to ensure liquidity stability and thus, facilitate trade. It is especially an instrument that helps to boost a currency's global utilization.

This study underscores the role of the US Federal Reserve's swap lines and China's Renminbi advancement strategy as the two main players, the latter being the case through swap agreements with the emerging economies.

It argues that if Indian Rupee were to become a currency of international status, India would need to increase its swap agreements network with the main trading partners so as to provide liquidity support in the global markets.

Medlin's work thus further points to the crucial role of financial cooperation at bilateral and multilateral levels in a currency's international stability and credibility. Medlin demonstrates that the Federal Reserve's extensive swap line network has been instrumental in sustaining Dollar dominance during periods of global financial stress, while China's strategic expansion of Renminbi swap agreements with emerging economy central banks has meaningfully advanced the Yuan's international reach. For India, Medlin's findings carry a direct policy implication: the expansion of INR-denominated swap arrangements with key trading partners would reduce INR liquidity risk in foreign markets, lower transaction costs for bilateral trade, and contribute to the currency's credibility as a medium of international exchange.

1.8.4 Reserve Bank of India IDG Report (2022) — Internationalisation of INR

The RBI's 2022 report on INR internationalization provides a policy-driven perspective on the necessary frameworks and mechanisms to enhance the global role of the Indian Rupee. The report outlines four key pillars essential for currency internationalization: trade and financial market integration, monetary stability, regulatory reforms, and geopolitical positioning. It highlights the importance of increasing INR-denominated trade settlements,



expanding offshore INR markets, and deepening India's bond and forex markets to support international demand for the Rupee. The report also discusses the challenges of partial capital account convertibility, emphasizing the need for a gradual and well-regulated approach to currency liberalization. The RBI's recommendations provide a strategic roadmap for policymakers seeking to enhance the Rupee's international status, emphasizing the role of institutional reforms, central bank diplomacy, and trade policy adjustments. The IDG report also addresses the challenge of capital account convertibility with appropriate caution, advocating a gradual and well-regulated liberalisation trajectory that preserves financial stability while expanding the currency's external utility. This report provides this study with an essential policy benchmark and a set of reform priorities against which empirical findings can be assessed.

1.8.5 Chinn (2014) — Emerging Market Economies and the Next Reserve Currencies

Chinn (2014) analyzes the potential of emerging market currencies in shaping the next generation of global reserve assets, focusing on factors that determine a currency's reserve status. The study argues that while advanced economies have traditionally dominated global finance, the rise of China, India, and Brazil has shifted economic power toward emerging markets, creating opportunities for currency diversification in global reserves. Chinn identifies key prerequisites for a currency to achieve reserve status, including macroeconomic stability, deep financial markets, strong institutional credibility, and trade influence. The paper highlights the Chinese Renminbi as a case study, showcasing how policy-driven internationalization strategies have contributed to its growing reserve currency role. Chinn's findings suggest that for the INR to become a global reserve currency, India must undertake structural economic reforms, enhance market efficiency, and foster greater financial openness while managing macroeconomic risks effectively.

His assessment of the Indian Rupee's position within this analytical framework suggests that while India satisfies several macro-level criteria, critical gaps remain in the depth of its financial markets, the openness of its capital account, and the global reach of its institutional



financial networks. Chinn's work is significant for this study because it establishes a theoretically grounded set of criteria against which INR's readiness for internationalisation can be assessed.

1.9 Research Gaps Identified

1.9.1 Comparative Macroeconomic Analysis of INR Relative to Peer Emerging Market Currencies

Despite extensive research on currency internationalization, there remains a lack of comparative analysis of macroeconomic factors influencing the potential of the Indian Rupee (INR) in relation to other emerging market currencies. While previous studies have examined the general conditions required for a currency to attain international status, most analyses focus on advanced economies or dominant emerging currencies such as the Chinese Yuan (CNY) and Brazilian Real (BRL). Existing literature often emphasizes broad economic indicators but does not provide a detailed, systematic comparison of INR's potential against other emerging market currencies based on central banks' policies, financial stability, and trade dynamics. This research seeks to address this gap by analyzing macroeconomic factors such as net effective exchange rates (NEER), currency pair exchange rates, remittances, trade balances, and capital account policies to assess INR's strengths and limitations in the global financial system. By doing so, this study aims to provide a data-driven perspective on INR's competitive standing among other emerging currencies.

1.9.2 Analysis of China's Internationalisation Strategy Beyond Trade

Another significant research gap is the limited analysis of the various strategic steps taken by China beyond imports and exports to enhance the global standing of the Renminbi. While numerous studies have focused on China's export-driven economic model and trade policies, fewer have explored the financial, institutional, and policy-driven measures that contributed to the Yuan's increasing role as a reserve currency. China's success in internationalizing the Renminbi has been multifaceted, involving Bilateral Currency Swap Agreements (BSA), the expansion of offshore Yuan markets (CNH), the Belt and Road Initiative (BRI), the



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development of cross-border interbank payment systems (CIPS), and diplomatic trade agreements encouraging Yuan-based transactions. While India's policymakers have studied China's trade-based approach, a detailed examination of these additional financial and institutional strategies remains insufficient. This study will bridge this gap by evaluating China's holistic approach beyond trade policies and exploring how India can adapt similar or alternative strategies to strengthen INR's global standing.

Understanding the full architecture of China's internationalisation strategy is essential for evaluating which elements might be adapted, wholly or in modified form, to the Indian context. This study aims to bridge that gap by providing a holistic assessment of China's currency strategy and drawing out its implications for INR's internationalisation pathway.



CHAPTER 2: RESEARCH METHODOLOGY

2.1 Objectives of the Study

The Indian Rupee (INR) has remained largely underutilized in the global financial system despite India's rapid economic growth and increasing integration into international trade and investment networks. While emerging market economies such as China, Brazil, and South Korea have made significant progress in increasing the global use of their respective currencies, the Rupee's international acceptance has been relatively limited. The objective of this study is to conduct a comparative analysis of INR's potential against other emerging market currencies and to identify the economic, financial, and policy-driven strategies that can be adopted to strengthen and internationalize the Rupee.

Second, the study aims to identify and evaluate a set of policy and institutional strategies that India could deploy to enhance the international role of the Rupee. Together, these objectives are designed to produce both an analytically robust diagnosis of the INR's current international standing and an evidence-based policy roadmap for its internationalisation.

One of the primary objectives of this study is to evaluate the Rupee's potential relative to other emerging market currencies such as the Chinese Yuan (CNY), Brazilian Real (BRL), Russian Ruble (RUB), and South African Rand (ZAR). This involves analyzing the macroeconomic fundamentals that determine a currency's international acceptance, including:

- Exchange rate stability and volatility - Comparing INR's performance in foreign exchange markets with other emerging currencies.
- Trade competitiveness - Assessing India's trade balance and whether bilateral and multilateral trade agreements support INR-based settlements.
- Foreign exchange reserves and capital flow dynamics - Understanding the role of capital inflows (FDI, FPI, remittances, and external borrowings) in shaping INR's stability.



- Financial market depth and liquidity - Evaluating whether INR has sufficiently developed domestic bond and capital markets to attract global investors.
- Role of central bank policies - Comparing RBI's monetary policies with those of other central banks in managing currency stability and international acceptance.

By conducting a comparative analysis, this study aims to identify where INR stands in the global financial hierarchy and what economic and financial factors contribute to the success or failure of a currency in achieving internationalization.

2. Identifying Policies and Strategies for INR Internationalization

While analyzing INR's current standing is essential, the second key objective of this study is to explore policy recommendations and strategic frameworks that can be implemented to strengthen and internationalize the Rupee. The internationalization of a currency requires a structured and multi-layered approach, involving coordinated efforts in monetary policy, trade agreements, financial market development, and international cooperation. This study will analyze various strategic measures including:

- Bilateral and Multilateral Trade Settlements in INR - Exploring ways in which India can expand INR-denominated trade by encouraging major trading partners to settle transactions in Rupees rather than US Dollars. This includes assessing current Rupee trade settlement agreements and potential trade partnerships that could be strengthened.
- Expanding Central Bank Currency Swap Agreements - Studying how India can increase currency swap arrangements with other central banks, similar to China's approach, to enhance Rupee liquidity and promote its use in global transactions.
- Developing Offshore INR Markets - Understanding the role of offshore financial centers and how India can create offshore Rupee hubs (similar to China's CNH market) to facilitate greater global usage of INR.



- Capital Account Liberalization and Forex Market Reforms - Evaluating the feasibility of gradual capital account convertibility, ensuring that INR can be used more freely for global investments while maintaining financial stability.
- Strengthening Financial Market Infrastructure - Assessing the depth of India's bond and equity markets, encouraging INR-denominated assets to be used as global investment instruments. This includes studying the potential of INR bonds and international participation in India's financial markets.
- Macroeconomic Stability and Monetary Policy Strengthening - Reviewing RBI's policies to ensure inflation control, currency stability, and predictable monetary frameworks that build confidence in the Rupee as a globally accepted currency.

Through this detailed analysis, the study aims to provide a structured policy roadmap that can guide policymakers, financial regulators, and economic strategists in formulating effective measures to enhance INR's global standing.

2.2 Key Variables Examined

2.2.1 Net Effective Exchange Rate (NEER)

The Net Effective Exchange Rate (NEER) is a crucial measure that reflects the value of a currency in relation to a weighted basket of multiple foreign currencies, adjusted for trade proportions. NEER helps assess the competitiveness of the Indian Rupee (INR) against a diverse set of trading partners, rather than focusing on just one bilateral exchange rate, such as INR/USD. A rising NEER suggests that the Rupee is appreciating against its trading partners, which can make exports less competitive but imports cheaper. Conversely, a declining NEER indicates depreciation, making Indian exports more attractive in global markets but raising import costs. For this study, analyzing NEER will provide insights into how INR has fared in global currency markets and whether its trends align with the currency internationalization strategies of other emerging economies.



2.2.2 Currency Pair Exchange Rates

Currency pair exchange rates represent the value of one currency relative to another and are fundamental to understanding international trade, investment flows, and forex market stability. The study examines key INR currency pairs, including USD/INR, EUR/INR, CNY/INR, JPY/INR, and GBP/INR, to analyze their stability, volatility, and trend patterns. The USD/INR pair is particularly significant, given the dominance of the US Dollar in global trade and India's heavy reliance on dollar-denominated transactions. Comparisons with other emerging market currencies, such as CNY/INR and BRL/INR, will help assess how the Rupee is positioned in global financial markets. Understanding exchange rate fluctuations, particularly in response to monetary policy decisions, capital flows, and trade imbalances, is essential in determining INR's potential for wider international acceptance.

2.2.3 Remittances

Remittances play a critical role in India's economy, contributing significantly to foreign exchange reserves and overall balance of payments stability. India is among the world's largest recipients of remittances, with inflows primarily coming from the Middle East, the United States, and Europe, where a large Indian diaspora is employed. These remittance inflows provide a steady source of foreign exchange liquidity, influencing the Rupee's exchange rate movements and strengthening its resilience against external shocks. A key aspect of this study is analyzing whether remittance inflows can be leveraged as a strategic tool for INR internationalization, particularly by facilitating more transactions in Rupee-denominated accounts rather than in foreign currencies. By evaluating historical remittance trends and their impact on INR's valuation, this study will determine how remittances can contribute to making the Rupee a stronger contender in global markets.

Second, they represent a potential channel through which INR adoption could be promoted internationally: if a larger proportion of remittance transactions were denominated and settled in Rupees, it would expand the currency's transactional footprint and contribute incrementally to its global visibility.



2.2.4 Imports and Exports

The trade balance, consisting of imports and exports, is a fundamental driver of currency demand and stability. India's trade profile is characterized by high dependence on crude oil and gold imports, which create persistent trade deficits, making INR vulnerable to external shocks. On the other hand, exports in sectors like IT services, pharmaceuticals, and manufacturing contribute positively to foreign exchange earnings. Comparing India's trade structure with other emerging economies, such as China and Brazil, will provide insights into how trade competitiveness impacts a currency's global acceptance. Countries with strong export-driven economies, such as China, have been able to promote their currencies in global trade settlements, reducing reliance on foreign exchange reserves. This study will examine whether India can adopt similar mechanisms to promote INR usage in international trade agreements, bilateral settlements, and currency swap arrangements. The resulting persistent current account deficit exerts structural downward pressure on the INR and limits its attractiveness as a medium of international trade settlement. This study analyses India's trade balance trends in comparative perspective, assessing how the structure of trade in other emerging economies, particularly China's export surplus model, has shaped the international acceptance of their respective currencies.

2.2.5 Capital Account and Current Account

The capital account and current account are essential indicators of a country's financial health and influence a currency's stability in international markets. The current account reflects India's trade balance, remittances, and net income flows, whereas the capital account tracks foreign investments, external borrowings, and foreign exchange reserves. Persistent current account deficits (CAD) can weaken the Rupee by increasing demand for foreign currencies, while robust capital inflows through FDI and FPI can support INR stability. A comparative analysis of India's capital and current account trends against other emerging economies will help determine whether the Rupee is positioned for increased global transactions and financial market integration. Additionally, studying the RBI's policies on



capital account convertibility will provide key insights into whether gradual liberalization can help INR become a more widely accepted international currency.

For the purposes of this study, analysing India's BoP structure, and comparing it with that of China and other emerging economies, is essential for understanding the structural drivers of INR exchange rate movements and for assessing the institutional reforms, particularly those related to capital account convertibility, that would be required to support greater INR internationalisation.

2.3 Research Methodology

2.3.1 Research Design and Data Collection

This study employs a mixed-method approach, integrating both quantitative and qualitative analysis to comprehensively evaluate the factors influencing the internationalization of the Indian Rupee (INR). The research methodology is designed to provide a data-driven assessment of INR's potential, specifically in comparison to other emerging market currencies, while also exploring suitable policy frameworks that can facilitate its global adoption. The methodology consists of multiple components, including data collection, quantitative analysis of currency behavior, and qualitative assessment of internationalization frameworks.

Data Collection

The data comes from a variety of reputable sources, guaranteeing a thorough and trustworthy dataset for analysis. Important data sources consist of:

- Real-time currency value fluctuations are captured by open market exchange rate data.
- The Bank for International Settlements (BIS) Triennial Surveys, which offer information on transaction volumes, currency turnover, and trends in the world's foreign exchange market.



- Macroeconomic indicators from the World Bank, such as GDP growth, inflation, interest rates, and capital flows, are essential for comprehending how the overall economy affects currency fluctuations.
- Central banks' websites, including those of the Reserve Bank of India (RBI), People's Bank of China (PBoC), and other emerging market central banks, to examine monetary frameworks, policy measures, and currency management tactics.

Because the data is gathered over a number of years, it is possible to analyze historical trends and make sure that the conclusions take into account both short-term market fluctuations and long-term structural factors influencing the global adoption of INR.

2.3.2 Quantitative Analysis Methods

This study's quantitative component focuses on the dynamics of currency exchange and how important macroeconomic variables affect currency internationalization. The relationship between INR and other major and emerging market currencies is examined using a variety of statistical and econometric methods. The following are the main elements of the quantitative analysis:

1. Examining Currency Index Rates and Exchange Pairs:

In order to evaluate the Rupee's exchange rate stability and competitiveness in international markets, the study compares the INR's performance to important currency pairs (USD/INR, EUR/INR, CNY/INR, JPY/INR, and other emerging market currencies). Furthermore, an analysis of the Net Effective Exchange Rate (NEER) and Real Effective Exchange Rate (REER) helps determine the INR's potential for broader international adoption by revealing its purchasing power in relation to a basket of foreign currencies.

2. Analysis of Rolling Standard Deviation

The study uses a rolling standard deviation approach to measure currency volatility, evaluating the changes in the INR's exchange rate over various time periods. This method aids in evaluating the level of exchange rate stability and the volatility of the INR in relation



to other emerging market currencies. Reduced volatility makes a currency more appealing for cross-border transactions by boosting trader and investor confidence. By conducting this analysis, the study evaluates whether INR's exchange rate behavior aligns with the stability required for a globally accepted currency.

3. Analysis of Correlation

To ascertain the direction and strength of the relationship between currency exchange rates and macroeconomic variables, such as:

- Differences in interest rates
- Foreign exchange reserves and the trade balance (exports and imports)

This study seeks to determine which macroeconomic factors have the greatest impact on changes in the INR's exchange rate and its acceptance around the world by finding statistically significant correlations.

2.3.3 Qualitative Analysis Framework

A qualitative evaluation is required to comprehend the institutional and policy frameworks that affect currency internationalization, even though quantitative approaches offer statistical proof. This research performs a thorough qualitative analysis of:

- Frameworks appropriate for the internationalization of the INR, examining the policy models of other developing nations like Brazil (BRL), China (CNY), and Japan (JPY).
- Central Bank interventions and policies, especially the RBI's role in regulating capital flows, international trade settlements in Indian rupees, and currency stability.
- The function of trade agreements and financial markets, evaluating India's initiatives to encourage Rupee-denominated transactions in bilateral currency swap agreements and cross-border trade.
- The difficulties and dangers associated with currency internationalization, with an emphasis on possible policy limitations, macroeconomic hazards, and geopolitical factors.



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CHAPTER 3: DATA ANALYSIS AND INTERPRETATION

3.1 Conceptual Background: Functions of Money and Currency Internationalisation

Functions of money:

In any economy, money has three basic purposes: it is a store of value, a medium of exchange, and a unit of account. These roles are applicable to both the public and private sectors, each of which has a unique impact on international trade, financial stability, and economic transactions. In the context of currency internationalization, money plays a crucial role because a globally recognized currency must successfully carry out these three tasks both domestically and internationally.

As a medium of exchange, money eliminates the inefficiencies inherent in barter by providing a universally accepted instrument through which goods, services, and financial obligations can be transacted. In the international context, this function translates into a currency's capacity to facilitate cross-border trade and financial settlements. A currency that is widely accepted as a medium of exchange in international markets enjoys a structural advantage in reducing transaction costs for domestic firms engaged in global trade, since it eliminates the need for costly currency conversion and hedging. The US Dollar's dominance as a medium of exchange in global oil, commodity, and financial markets exemplifies this function at its most powerful expression.

As a unit of account, money provides a standardised metric for pricing goods, services, and financial instruments, enabling transparent valuation across disparate markets and jurisdictions. A currency's use as a unit of account in international trade invoicing and financial contract denomination reflects the degree of trust that global market participants place in its stability and predictability. Currencies that serve as units of account for commodity pricing, such as the Dollar for crude oil or the Euro for intra-European trade, benefit from a self-reinforcing demand dynamic that further entrenches their international status.



As a store of value, money preserves purchasing power over time, enabling individuals, firms, and governments to accumulate wealth and manage inter-temporal financial obligations. In the international sphere, this function manifests in the composition of central bank foreign exchange reserves. Central banks hold reserve currencies not merely for transactional convenience but because they represent reliable and liquid stores of national wealth. The INR's negligible presence in global foreign exchange reserves is indicative of limited international confidence in its long-term stability as a store of value, a perception that India's macroeconomic policy framework must work to systematically address.

The value store function:

This guarantees that money will always have purchasing power. In order to stabilize the national economy and intervene in currency markets when necessary, governments must maintain international reserves in the form of foreign exchange, gold, and other assets. Through currency substitution and investment, money acts as a store of value in the private sector. Businesses and individuals hold foreign currencies or financial assets to protect wealth from inflation or currency depreciation. A currency that is widely recognized as a store of value, such as the US dollar (USD) or the euro (EUR), gains credibility internationally and is more likely to be used in international investment and trade.

Exchange function medium:

By lowering the inefficiencies of barter systems, money serves as a medium of exchange that promotes trade and financial transactions. In order to preserve financial stability and competitive trade conditions, governments use currency as a tool for foreign exchange (FX) intervention. Businesses and individuals in the private sector depend on money for financial transactions and trade invoicing, which guarantees smooth cross-border business operations. A currency's ability to serve as a commonly used medium of exchange in international trade - where countries prefer to settle transactions in a stable and liquid currency - determines its level of internationalization.

The function of the unit of account



Money's unit of account function offers a uniform metric for pricing financial instruments, goods, and services. By tying the value of the domestic currency to a more stable foreign currency, such as the USD, governments use their own currency as an anchor for local currency pegging. This aids in controlling inflation and fluctuations in exchange rates. Money is used by businesses in the private sector to denominate trade and financial transactions, allowing for precise pricing and valuation of international contracts. A currency like the USD or Chinese Yuan (CNY), that is frequently used as a unit of account, has a higher chance of becoming a reserve currency.

The Indian Rupee (INR) needs to play a bigger part in these three essential roles if it is to be recognized internationally. In addition to being actively utilized in trade settlements and widely held as a store of value, INR should be accepted as a standard unit of account in international financial markets. India can significantly advance the Rupee's status as a globally competitive currency by improving its stability, liquidity, and international acceptance.

3.2 INR in the Global Foreign Exchange Reserve System

The Indian Rupee (INR) and major reserve currencies in the global financial system differ significantly, as evidenced by the data from the survey on holdings of currencies in official foreign currency assets. Only 0.01% of global foreign exchange assets were valued in Indian rupees as of 2014, demonstrating the currency's incredibly small role in global finance. On the other hand, with more than 60% of all holdings, the US dollar (USD) is the dominant worldwide reserve currency. This emphasizes how crucial the USD is to international trade, financial reserves, and monetary stability for economies around the world.

In Asian currencies, the Japanese Yen stands out as the main one, its pretty much leading the way there. Then there is the Chinese Renminbi, which is picking up more notice around the world because of stuff like those currency swap deals China has set up, and also the offshore markets for the Yuan, plus getting into the IMF's special basket back in 2016. That all seems to be helping it gain ground steadily.



The Euro is important too, it kind of shows how strong the European economy is and the way the Eurozone affects trade and money matters globally.

Other currencies from places like Brazil with the Real, South Africa and the Rand, or Russia and the Ruble, they do not have huge parts in the global picture, but still they are used more than the Indian Rupee out there. Its interesting how even small shares add up in emerging markets, or at least that is what it feels like from what I have read.

The Indian Rupee does not really hold much in global foreign exchange reserves. That makes me think its not getting much international use, and India ends up depending a lot on other currencies for trade and money stuff. There are a few reasons for this situation.

Like, the trade deficit is one thing, and then there is no full convertibility on the capital account. Offshore markets for INR are pretty limited too. Plus, the US dollar dominates how commodities are priced everywhere. It feels like all that keeps the Rupee stuck.

India mostly does trade in foreign currencies, especially the dollar. China is different, they push for Renminbi in deals abroad, but here it is not like that yet. Some bilateral agreements could help encourage using INR more, I suppose, in trade and even reserves.

To make it stronger globally, policies need to come in that promote it for transactions. Strengthening the economy overall, making financial markets deeper, and settling trade in Rupees might work. Without those steps, it will just stay on the edges, relying heavily on outside currencies for everything. That part gets a bit messy to figure out fully.

3.3 INR in SWIFT Payment Transactions and OTC Derivative Markets

Top 20 currencies recorded in SWIFT database (2019-24)

When it comes to international financial transactions, the Society for Worldwide Interbank Financial Telecommunication, or SWIFT for short, is the main system that banks around the world use to process cross-border payments quickly and efficiently. If we look at the data from January 2019 to December 2024, we can see which currencies are used the most for international payments, based on the total value of transactions. The US Dollar is clearly the



dominant currency, which is not surprising given its status as the primary reserve currency. Following closely behind are the Euro, British Pound, and Japanese Yen.

However, it's also worth noting that the Chinese Renminbi has been gaining ground, which reflects China's efforts to increase the use of its currency in global trade. This shift is significant, as it indicates a growing trend towards greater diversification in international financial transactions. By examining the data, we can gain a better understanding of the current state of global finance and the role that different currencies play in it. The use of these currencies in international transactions has important implications for the global economy, and it will be interesting to see how their relative positions change over time.

A notable observation is the complete absence of the Indian Rupee (INR) from the list, despite India being one of the world's largest economies by GDP. The exclusion of INR from SWIFT's most-used currencies indicates its minimal role in international trade settlements and cross-border financial transactions. In contrast, several other emerging market currencies, such as the Mexican Peso (MXN), South African Rand (ZAR), and Russian Ruble (RUB), have achieved greater international recognition, primarily due to active policy measures, financial market reforms, and strategic trade agreements implemented by their respective governments.

The OTC derivatives market provides a complementary and equally instructive perspective on currency internationalisation. OTC instruments, which include currency forwards, swaps, and options, are used by market participants to manage foreign exchange risk and to speculate on currency movements. The volume and depth of OTC activity in a given currency reflects both the liquidity of its spot market and the degree of international demand for instruments denominated in that currency. The data reveal that while the USD and EUR dominate OTC markets by a substantial margin, the Chinese Yuan has witnessed significant growth in OTC activity since 2010, consistent with its broader internationalisation trajectory. The INR, while showing some incremental growth in OTC volumes as the second most active emerging market currency in this segment, continues to lag substantially behind the



Renminbi, pointing to the need for deeper forex market development and greater international participation in INR-denominated instruments.

The absence of INR in global SWIFT transactions highlights the challenges India faces in positioning its currency as a widely accepted medium of exchange in global financial markets. Several factors contribute to this, including India's continued reliance on USD for trade settlements, lack of extensive Rupee-based trade agreements, and limited offshore INR markets. Unlike China, which has aggressively promoted the Renminbi through swap agreements, digital payment initiatives, and offshore Yuan trading hubs, India has yet to take substantial steps toward expanding INR's global footprint.

Volume of OTC instruments by currencies

The Over-the-Counter (OTC) market functions as a vital component of worldwide financial operations by creating market access for currency derivatives and bonds and all other financial products. The graphs presented compare the value of OTC instruments in major currencies (USD, EUR) with those in emerging market currencies (CNY, INR, ZAR, BRL, and RUB). The data shows that OTC transactions which use USD and EUR as their base currency have grown substantially because these currencies control international financial markets. The market for USD-based OTC instruments shows continuous growth because investors trust the US financial system while the Euro maintains its strong market position through active capital markets and the European Union trade system.

The Chinese Yuan (CNY) establishes itself as the leading trend among emerging market currencies which shows a dramatic increase in over-the-counter trading markets after the year 2010. The surge results from China implementing its strategic financial policies which include establishing offshore Renminbi markets and creating bilateral swap agreements and promoting the Yuan as a required method for trade and financial settlements. The Indian Rupee (INR) operates as the second most active emerging market currency in the OTC segment which shows gradual growth but still lags behind the Chinese Renminbi. The Brazilian Real (BRL) and South African Rand (ZAR) and Russian Ruble (RUB) demonstrate



moderate market activity which shows change because of economic conditions and trade policy developments.

India encounters difficulties when trying to establish its currency as a worldwide medium of exchange because the international SWIFT system does not support Indian Rupees. Several factors contribute to this, including India's continued reliance on USD for trade settlements, lack of extensive Rupee-based trade agreements, and limited offshore INR markets. India has not yet taken significant actions to increase the global presence of its currency according to the comparative example of China which has actively advanced its Renminbi through multiple channels including swap agreements and digital payment initiatives and offshore Yuan trading hubs.

3.4 Macroeconomic Overview of the Indian Economy

3.4.1 GDP Growth and Macroeconomic Resilience

GDP:

India has consistently demonstrated robust GDP growth rates over the years, particularly during the period from 2016 to 2019, where it outperformed other emerging economies. Despite the economic slowdown triggered by the COVID-19 pandemic in 2020, India quickly rebounded with strong growth in 2021 and 2022, reflecting its resilience and adaptability. While other economies, particularly the Eurozone, Brazil, and South Africa, showed periods of negative growth or stagnation, India's consistent positive growth trajectory indicates macroeconomic stability and a strong underlying economic structure. Such growth is essential for enhancing INR's credibility as a potential global currency.

3.4.2 Remittances and Their Strategic Significance

India establishes itself as the world leader in remittances because its remittance flows exceed all other main economies and developing nations throughout the entire year. The country depends on remittances as a consistent foreign exchange resource which helps maintain its current account balance and build its foreign reserves. India receives remittance inflows



which are three times greater than China and Brazil and Russia according to 2023 data. The government should promote Indian Rupee usage in remittance transactions because most remittances occur in foreign currencies.

3.4.3 Trade Structure and the Current Account Deficit Challenge

The graphs show India's trade patterns between 2015 and 2021 which reveal that between these two periods the country experienced economic growth while suffering from ongoing trade deficits. Indian export growth has progressed at an upward pace yet this growth failed to protect the country from worsening trade deficits which emerge because import levels increased more than export levels. This pattern differs from the trade patterns of all major economies together with emerging markets which include China and Brazil and Russia and the United States. India achieves its export success because its economy maintains strength in information technology and pharmaceutical and textile and manufacturing sectors.

The graph shows that India experienced continuous export growth throughout the years which reached its highest point between 2019 and 2021. The improvement occurred because India developed new export products and established better trade agreements and because the world markets started to demand more Indian services and goods. Indian export growth has not reached the necessary level to balance out the increasing pace of import growth which has been rising more quickly during that same time frame. The graph shows India's imports through time which displays a complete upward movement from its starting point to 2021.

The country experiences rapid import growth because its citizens demand high quantities of crude oil and gold and electronics and machinery which together create a large part of India's import total. India's trade deficit worsens because of its ongoing need for imported energy sources and capital goods which also decrease the value of the Rupee during external economic disruptions. China maintains a permanent trade surplus through its export-based economic system which strengthens the Chinese Yuan (CNY) throughout international markets. The Indian Rupee (INR) suffers from limited international potential because India lacks the ability to create an export-focused economic system.



This trade structure stands in sharp contrast to China's, where a persistent and substantial merchandise trade surplus has been a key pillar of the Renminbi's international credibility. China's trade surplus generates consistent outflows of its currency into global trade circuits, which in turn creates foreign demand for Yuan-denominated assets. India's trade deficit dynamic operates in the opposite direction, generating structural demand for foreign currencies rather than for the Rupee. Addressing this asymmetry requires not merely an export promotion strategy but a deeper structural transformation of India's economic model, including the accelerated development of domestic energy production, the expansion of value-added manufacturing, and the diversification of export markets.

3.5 Comparative Analysis of Currency Volatility

1. Volatility among INR and developed currencies

The graph presents a comparative analysis of currency volatility between the Indian Rupee (INR) and major global currencies, including the Chinese Yuan (CNY), US Dollar (USD), and Euro (EUR) which are major reserve currency assets. This analysis has been conducted using a six-month rolling standard deviation method over a nine-year period, providing a comprehensive assessment of volatility trends and fluctuations over an extended timeframe. The rolling standard deviation technique helps in capturing short-term variations while smoothing out daily fluctuations, thereby offering a more reliable measure of underlying volatility.

The findings clearly indicate that the INR exhibits significantly higher volatility compared to the currencies of developed economies like the USD and EUR. Throughout the nine-year period, the INR shows frequent and pronounced fluctuations, suggesting a lack of stability and higher risk perception in international markets. In comparison, the USD and EUR demonstrate consistently low and steady volatility, reflecting their status as established reserve currencies with strong institutional support, robust financial markets, and predictable monetary policies. Interestingly, the Chinese Yuan (CNY), although an emerging market currency, shows lower volatility than the INR. This relative stability is a result of China's



stringent capital controls, deliberate currency management practices, and proactive measures aimed at promoting internationalization. The inclusion of CNY in the IMF's Special Drawing Rights (SDR) basket has further enhanced its credibility and contributed to its reduced volatility.

The high volatility of INR can be attributed to several factors, including exchange rate fluctuations, trade deficits, capital flow volatility, and India's heavy reliance on crude oil imports. Additionally, the lack of a fully convertible capital account and limited participation in offshore INR markets contribute to the observed instability. External factors such as global economic uncertainty, geopolitical tensions, and commodity price shocks also play a critical role in influencing the volatility of the INR.

The INR's relatively elevated volatility, while lower than some of its BRICS peers, remains a material obstacle to its international adoption. Volatility in a currency's exchange rate increases the costs of cross-border transactions, complicates the pricing of international contracts, and reduces the attractiveness of the currency as a store of value for foreign central banks and investors. The sources of INR volatility are multifaceted and include India's chronic dependence on crude oil imports, which makes the Rupee sensitive to global commodity price shocks; the structural current account deficit, which creates persistent outward demand for foreign exchange; the incomplete nature of capital account convertibility, which limits the depth of INR's forex market; and periodic episodes of capital flow reversals driven by shifts in global risk appetite or US monetary policy.

The comparative analysis with the CNY is particularly illuminating. The Chinese Yuan's relatively contained volatility, despite being an emerging market currency with significant capital control restrictions, reflects the success of China's managed exchange rate system and its institutional framework for currency stabilisation. China's People's Bank of China (PBoC) employs a daily reference rate mechanism that constrains the Yuan's permissible daily trading range, while its substantial foreign exchange reserves provide a formidable buffer against speculative attacks. While the full replication of China's capital control model would



not be appropriate or desirable for India, the analytical comparison highlights the potential for institutional exchange rate management mechanisms to meaningfully reduce INR volatility, thereby enhancing its attractiveness as an international currency.

3.6 Correlation Matrix Analysis: NEER and Balance of Payments Components

The study investigates how BRICS currencies including INR and CNY and ZAR and BRL and RUB display different volatility patterns against the US Dollar which has been observed over nine years through a six-month rolling standard deviation method. The method tracks how each currency moves through time while showing how extreme their USD value changes become. The analysis shows distinct differences in how these currencies experience changes in their value which depend on global events and economic policies.

The initial graph displays all BRICS currencies which reveal that Russian Ruble (RUB) experienced extreme volatility during the observed period. The Russian-Ukraine conflict caused this increase because it resulted in economic sanctions and capital flight and increased geopolitical tensions. The Ruble experienced high volatility during this time because of its susceptibility to external disruptions and geopolitical threats. The increased volatility makes RUB an untrustworthy international currency because it no longer meets internationalization requirements.

3.7 Understanding China's Investment-Driven Currency Management Strategy

The correlation matrix analysis applied to the relationship between NEER movements and balance of payments components for both INR and CNY yields a set of findings that are analytically significant for understanding the structural differences between the two currencies' international behaviour. For the CNY, the strongest correlations are observed with the current account (0.51) and capital account (0.36) aggregates, while merchandise trade (0.07) and services trade (negative correlations) show weak or inverse relationships. This pattern reveals that China's NEER is primarily driven not by the direct mechanics of trade but by the managed deployment of capital flows, offshore investment returns, and policy-



directed financial instruments. China's currency management strategy operates through the capital account channel rather than the trade channel, with the PBoC using capital inflow management and strategic overseas investment to maintain NEER stability.

Through sovereign wealth fund deployments, the Belt and Road Initiative's financing activities, and state-directed outward foreign direct investment, China has constructed a global investment network that generates steady inflows of foreign currency denominated returns. These returns, when repatriated, strengthen the current account balance and support the Yuan's effective exchange rate without depending on the inherently volatile dynamics of merchandise and services trade. This investment-driven model of currency management represents a strategic departure from the trade-centric approach that characterises the monetary management of most emerging economies, and it offers important lessons for India's internationalisation strategy.

The INR exhibits a contrasting structural profile. Its NEER shows the strongest positive correlation with foreign currency assets (0.40), followed by gold reserves (0.29), SDRs (0.27), and remittance transactions (0.24). The correlations with the capital account (-0.07) and current account (-0.05) are weak and negative, indicating that broader balance of payments dynamics have a limited immediate influence on the Rupee's effective exchange rate. The dominant role of foreign exchange reserves in determining INR's NEER stability suggests that India's currency management is primarily reactive, with the RBI deploying reserve assets to stabilise the exchange rate in response to external pressures rather than proactively managing capital flows to build structural NEER strength. This reserve-dependent strategy, while effective in the short term, may not provide the durable foundation for the sustained exchange rate stability that international currency status requires.

This graph excludes the Ruble, provides a clearer comparison of the remaining BRICS currencies: INR, CNY, ZAR, and BRL. The Indian Rupee (INR) appears to be less volatile compared to the South African Rand (ZAR) and Brazilian Real (BRL) but shows a volatility pattern closely following that of the Chinese Yuan (CNY). The comparative stability of INR



relative to ZAR and BRL indicates that India's macroeconomic policies, foreign exchange reserves, and financial market regulations have been relatively effective in minimizing excessive fluctuations.

The comparative analysis of volatility between INR and CNH shows multiple similarities which indicate INR will develop into an international currency. The currencies of INR and CNH show moderate stability which exceeds the stability of BRICS currencies that include BRL and ZAR and RUB because their governments maintain effective policies and rules which control currency movement. The two currencies show identical volatility patterns because they respond to global economic disturbances and market movements in the same way.

The evidence shows that India has the economic foundation and institutional strength and market capacity which enable the country to establish its currency as an international currency just like China did. The Indian Rupee receives support from strong remittance payments and high GDP growth and growing trade connections which mirror the strategic benefits that China experienced during its process of becoming an international currency. India needs to establish economic policies which will help it reach its full economic potential by replicating Chinese policies to promote trade between India and China through INR and to develop markets for offshore Rupee and to improve capital account conversion. INR will achieve a stronger position in worldwide financial networks through internationalization because it shares common features with CNH.

Analysis of correlation matrices:

1. EXPORTS AND IMPORTS

DEVELOPED ECONOMIES:

The USD exhibits strong correlations with both exports and imports because its merchandise trade relationships with both export and import activities show a correlation value of 0.77 and 0.78 respectively. The USD's NEER movements show strong connection with United States merchandise trade activities because the two components show high correlation. The



USD functions as the main global currency which makes its value changes important for international trade because they create direct effects on worldwide trade operations. The strong correlation between the two variables shows how USD functions as the main currency for international trade transactions and invoicing and central bank reserve storage.

The EUR demonstrates weak export and import correlations which show that its effective exchange rate does not depend on European trade patterns. The Eurozone economic system consists of various national economies which affect their trade competitiveness and their trade relationships with foreign countries. The EUR's NEER response to financial movements and monetary policy decisions and geopolitical developments exceeds its direct trade relationship with international markets. The CNY demonstrates almost no connection to both exports and imports because its merchandise trade activities do not affect the Chinese currency's NEER value.

China's managed exchange rate system keeps its exchange rate stable because it prevents trade changes from affecting the currency's actual value. China's Yuan promotional strategy relies on bilateral swap agreements and offshore CNH markets to diminish NEER response to standard trade metrics.

The USD demonstrates strong positive relationships with service trade exports and imports which show 80 percent and 79 percent export and import connections respectively thus proving its market impact extends to all trade categories. The EUR exhibits weak links to both exports and imports because its NEER operates through more complex elements that extend beyond services trade. The most significant finding shows that CNY exhibits negative links to exports which decrease by 29 percent and to imports which decline by 37 percent.

The relationship shows that CNY increases its NEER value which results in decreasing China services trade yet the opposite happens when CNY value decreases. China uses protectionist strategies together with capital controls to maintain currency stability while monitoring international financial movements.



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The analysis highlights that the USD's dominance in both merchandise and services trade is unmatched which strengthens its position as the world's primary reserve currency. The weak correlations for the EUR suggest that its status as a global currency is more influenced by regional integration and financial markets than by direct trade relations. The CNY correlations display only minor negative connections which demonstrate that China has succeeded in protecting its NEER from normal trade flow patterns through its currency control operations.

BRICS ECONOMIES

The correlation matrices for BRICS economies (INR, CNY, ZAR, BRL, RUB) against merchandise and services trade reveal important insights into how each currency's Net Effective Exchange Rate (NEER) interacts with its export and import performance. The analysis uses a color-coded system which designates high positive correlation through blue hues while red colors show low or negative correlation results. The INR and RUB show moderate positive correlations with both exports and imports in their merchandise trade relationship. The INR shows a 0.28 correlation value with exports and imports which demonstrates a sustainable connection between its NEER and trade metrics.

The INR effective rate fluctuations demonstrate partial alignment with India's merchandise trade changes which occur at a weaker intensity than the USD correlation patterns established beforehand. The RUB demonstrates even higher positive correlations (0.41 for exports and 0.44 for imports). The high correlation value between Russia's NEER and its trade performance emerges because the country depends on energy exports which experience high sensitivity to currency exchange rate fluctuations.

The ongoing Russia-Ukraine conflict has created new developments regarding Russia-Ukraine trade patterns based on previous studies of market volatility. The BRL negative correlations (-0.53 for both exports and imports) demonstrate that Brazilian Real NEER movements create opposite effects on trade between Brazil and other countries. Brazil's trade policies and economic conditions show structural problems which lead to decreased



international attractiveness for the currency. The CNY and ZAR show negligible correlations with their merchandise trade metrics which demonstrates that their NEERs remain unaffected by trade movements.

The services trade market operates with its established pattern which maintains a stable appearance. The Indian Rupee exhibits weak positive relationships with exports and imports which show correlation values of 0.15 and 0.13 respectively. The correlations between India's service exports and imports with the Rupee's NEER show only a slight impact on the latter. The situation becomes significant because India maintains strong capabilities in service exports especially in IT and financial services. The RUB maintains positive correlations with a 0.36 value for both exports and imports which demonstrates that Russia's NEER responds to shifts in merchandise and services trade. The CNY exhibits negative correlations which show that China's NEER increase results in a decrease of its services trade activities. The results confirm earlier research which shows that CNY exchange rate management creates a trade performance gap.

The ZAR displays very slight negative relationships with both exports and imports because it shows no connection between South Africa's NEER and its trade activities. The BRL demonstrates negative trade relationships with services which show that the Brazilian Real fails to maintain proper connection with its economic fundamentals. The comparison among BRICS currencies shows that the INR maintains moderate connection with trade metrics which especially applies to merchandise trade because this relationship enables further internationalization through stronger trade linkages. The performance of RUB shows a strong connection between Russian currency and trade metrics, while the weak or negative correlations for CNY, ZAR, and BRL suggest structural issues or deliberate policy interventions that diminish.

Merchandise Trade Comparison

The INR shows moderate positive correlations (0.28) with both exports and imports, indicating that India's NEER is somewhat responsive to merchandise trade changes. This



suggests a market-driven approach where INR reflects trade performance. In contrast, the CNY exhibits negligible correlations (0.07), reflecting China's managed exchange rate regime, which isolates the Yuan from trade dynamics. While INR shows some alignment with trade metrics, CNY's low correlation is a result of deliberate policy interventions rather than natural market forces.

Services Trade Comparison

The INR shows weak but positive correlations (0.15 for exports, 0.13 for imports), indicating that India's services sector contributes modestly to the Rupee's stability. Conversely, the CNY exhibits negative correlations (-0.29 for exports, -0.37 for imports), suggesting that appreciation of the Yuan negatively impacts China's services trade. Unlike China, India's services trade offers a potential advantage for enhancing INR's international acceptance, given its steady contribution to foreign exchange earnings.

Chinese Economy Challenges:

The current structural inconsistency exists because CNY exhibits weak links with export and import activities while maintaining strong links with current account (0.51) and capital account (0.36) activities. The CNY NEER shows little connection to actual trade movements because China depends heavily on exports yet shows almost no relationship with physical trade (0.07) while showing negative links to service trade (-0.29 for exports, -0.37 for imports). Offshore investments and controlled capital inflows explain current account correlations because trade balances do not account for these factors.

The capital account shows strong links with exports and imports which indicates that these two factors do not drive capital account activities. The Chinese government maintains its currency stability through investment projects and foreign direct investment (FDI) and through revenue generated by international business operations. China employs capital account dynamics to enhance the CNY NEER because its methods depend on investments and government regulations instead of direct trade statistics.

Understanding the Correlation between CNY and current account components



The study investigates how CNY affects the various elements of the current account. The analysis of the Chinese Yuan (CNY) and its Net Effective Exchange Rate (NEER) reveals interesting patterns when correlated with various components of the current account. The current account broadly includes net exports, remittances, and returns from offshore investments. The observed correlation between CNY's NEER and the current account shows a strong relationship which is proven by its 0.51 value. The research shows through its detailed analysis that only certain components of the current account produce the observed value of this relationship. The correlation between CNY's NEER and net exports (which are calculated by subtracting imports from exports) shows almost no relationship. Merchandise trade shows an insignificant correlation of 0.07 for both exports and imports which indicates that China's NEER movement keeps itself mostly independent from actual trade performance. The services trade shows negative correlations of -0.29 for exports and -0.37 for imports which show that Yuan appreciation harms China's services industry. The negative correlation shows that China directly participates in international trade but its NEER movement does not follow standard trade patterns because the country exports large amounts of goods.

The first finding shows that remittance payments which they send back home to their families lead to only a slight effect on how the current account interacts with CNY's NEER. The data shows that remittances have a -0.37 correlation with CNY's NEER which demonstrates a negative relationship. The negative correlation shows that CNY appreciation leads to decreased remittance value compared to other economic factors or it shows that remittance inflows do not serve as a primary strength for the Chinese Yuan. China has established itself as an economy which relies less on remittances than countries like India therefore we can conclude that remittances do not improve the current account's relationship with CNY's NEER.

Returns from offshore investments:



China has expanded its international investment activities through its implementation of multiple strategic programs which include the Belt and Road Initiative and its use of sovereign wealth funds and foreign direct investments and asset acquisitions across different nations. The offshore investments produce returns through interest and dividends and profits, which China subsequently repatriates to its home country.

The capital inflows to the country enhance the current account balance, which results in positive effects on the Chinese Yuan's nominal effective exchange rate. Offshore investment returns deliver consistent foreign currency, which differs from remittances and exports that depend on outside market demand and currency value changes. The strong positive relationship between the CNY's NEER and the current account exists because of these consistent patterns. China's investment activities in developing nations through the BRI program guarantee that economic returns will continuously return to China, which helps maintain the Yuan's value.

The observation demonstrates how China maintains its unique approach to currency management through its offshore investment activities which secure stability and value for the CNY through its NEER. China proves its capacity to generate foreign currency through trade by diversifying its financial sources beyond merchandise exports and service exports. China established an extensive network of offshore investments which generates stable returns to achieve a positive connection between its current account balance and the CNY's NEER.

The research results show that CNY develops through a process which differs from how other emerging market currencies develop, including the Indian Rupee. India depends on export revenue and remittance income to strengthen its current account, whereas China uses its offshore investments to build currency stability, which serves as a path to internationalization. India must understand this distinction because it wants to use similar strategies which will help the INR achieve worldwide recognition.



CHAPTER 4: FINDINGS AND DISCUSSION

4.1 Key Findings

The empirical analysis conducted in this study yields several key findings that collectively illuminate the structural dynamics of INR internationalisation and the comparative lessons available from the Chinese Yuan's experience. First, China's NEER is primarily driven by capital account dynamics and offshore investment returns rather than by the direct mechanics of bilateral trade, reflecting a deliberate and institutionally sophisticated approach to currency management that operates through financial channels rather than trade channels. This investment-oriented strategy has been central to the Yuan's growing international credibility and its inclusion in the IMF's SDR basket.

Second, India's NEER stability is disproportionately dependent on the management of foreign exchange reserves and the steady inflow of remittances, reflecting a reactive rather than proactive approach to currency management. While this strategy has been effective in moderating short-term volatility, it does not provide the structural foundation for the sustained exchange rate strength and predictability that international currency adoption requires. Third, the INR's volatility profile, while lower than that of the BRL, ZAR, and RUB, remains higher than that of the CNY and considerably higher than those of major reserve currencies, suggesting that further institutional and policy investment in exchange rate stabilisation mechanisms is warranted.

Fourth, the absence of the INR from SWIFT's list of actively used international payment currencies, and its limited role in OTC derivatives markets, reflects the cumulative effect of insufficient trade settlement infrastructure, the absence of offshore INR markets, and India's continued dependence on Dollar-based invoicing across most major trade categories. Fifth, the comparison of INR and CNY correlation structures reveals that India's currency management strategy and its institutional framework for capital account management lag behind those of China in sophistication and strategic coherence, pointing to specific areas where institutional reform and policy capacity building are most urgently required.



The following are the main conclusions drawn from the examination of the correlation matrices involving NEER, components of the Balance of Payments, and Forex reserves for INR and CNY:

1. Investments and Capital Accounts Drive China's NEER

The current account (0.51) and capital account (0.36) exhibit a strong positive correlation with CNY's NEER. Trade is not the primary driver, though, as evidenced by the nearly zero correlation with merchandise trade (0.07) and the negative correlation with services trade (-0.29 for exports, -0.37 for imports). Rather, the main contributors are policy-driven capital inflows and returns from offshore investments.

2. India's NEER Relies on Remittances and Reserves

The strongest positive correlation (0.40) between INR's NEER and foreign currency assets is followed by moderate correlations with gold reserves (0.29), SDR (0.27), and RTP (0.31). Additionally, there is a moderately positive correlation (0.24) with remittances. Weak negative correlations with the capital account (-0.07) and current account (-0.05) indicate that broader BoP metrics have little impact.

3. Inconsistency in China's Correlations

The NEER of CNY exhibits nearly no correlation with imports and exports, but it is highly correlated with current and capital accounts. Instead of trade, the main drivers are capital account activities and offshore investments.

4. India's Moderate Compliance with Trade Measures

The NEER of the INR exhibits weak correlations with imports and exports but moderate correlations with remittances (0.24) and forex reserves (0.40), suggesting that reserves and financial inflows have a greater impact than trade.

5. China's Investment-Oriented Strategy



China's strategy of using offshore investments and controlled capital inflows to stabilize the currency is highlighted by the strong correlation between CNY's NEER and current and capital accounts.

6. The Reserve-Dependent Strategy of India

Remittances and foreign exchange reserves are more important to India's NEER than trade or capital accounts. This points to a reactive approach that prioritizes controlling external shocks over proactive capital growth.

7. Consequences for the Internationalization of INR

For NEER stability, China's investment-driven strategy works better. To increase the INR's acceptance around the world, India must improve its NEER's correlation with more general economic metrics, especially capital accounts.

4.2 Recommendations

India can take a multifaceted approach to increase the INR's acceptance worldwide by learning from China's successful Yuan internationalization strategy. The following suggestions are put forth:

4.2.1 Developing a Strategic Offshore Investment Portfolio

India should concentrate on strategically investing overseas through foreign direct investment, infrastructure projects, and sovereign wealth funds. As China has done through programs like the Belt and Road Initiative (BRI), building a strong portfolio of offshore investments can produce consistent returns that support the INR's NEER. India should strategically expand its portfolio of overseas investments through sovereign wealth fund deployments, outward foreign direct investment, and participation in multilateral infrastructure financing initiatives. As demonstrated by China's experience through the Belt and Road Initiative, a well-managed network of offshore investments generates consistent returns denominated in foreign currencies that can be repatriated and invested in INR-denominated assets, thereby creating structural demand for the Rupee that does not depend



on the short-term dynamics of trade balances. India's nascent sovereign wealth fund architecture should be developed and deployed with an explicit currency internationalisation mandate.

4.2.2 Expanding the Network of Bilateral Currency Swap Agreements

The currency's worldwide presence would be strengthened by making sure that returns from foreign investments are valued and repatriated in Indian rupees. Promoting bilateral trade agreements that support INR settlements and urging Indian businesses to bill their overseas earnings in INR are two ways to accomplish this. The Reserve Bank of India should pursue the negotiation of an expanded network of bilateral currency swap agreements, modelled on China's strategy of using swap arrangements as instruments of financial diplomacy. These agreements would provide INR liquidity to foreign central banks, reduce the transaction costs of bilateral trade, and signal India's commitment to the Rupee's international role. Priority should be given to swap agreements with India's largest trading partners and with economies in the Global South where Indian trade relationships are growing rapidly.

4.2.3 Establishing Offshore INR Financial Markets

India needs to diversify its sources of income beyond direct trade in order to attain sustainable NEER stability. India can lessen its reliance on trade in goods and services to stabilize the Indian rupee by concentrating on returns from foreign investments and creating non-trade-related financial inflows. The establishment of an offshore INR market, analogous to the CNH market developed in Hong Kong, represents one of the most structurally significant steps India could take to advance INR internationalisation. An offshore market would allow international investors to hold and trade INR-denominated assets without being subject to domestic capital controls, thereby broadening the currency's global investor base and enhancing its liquidity. International financial centres, including Singapore, Dubai, and Mauritius, already host significant Indian diaspora communities and Indian financial institution presences that could serve as anchor participants in an offshore INR market.



4.2.4 Gradual Capital Account Liberalisation and Financial Market Deepening

The Indian Rupee can become more liquid as a result of returns from offshore investments, strengthening its resistance to outside shocks. An increase in INR transactions worldwide would also enhance the currency's reputation as a medium of exchange in global marketplaces. India should pursue a calibrated and sequenced liberalisation of its capital account, moving gradually from the current partial convertibility regime toward a more open framework that allows greater international participation in domestic financial markets while preserving macro-prudential safeguards. This liberalisation should be accompanied by the development of deeper and more liquid domestic bond markets, including the promotion of INR-denominated sovereign and corporate bonds for international investors, which would create additional channels through which global demand for the Rupee can be expressed.

4.2.5 Promoting INR-Denominated Trade Invoicing and Settlement

India ought to encourage its trading partners to bill in Indian rupees. Encouraging the use of INR in international trade settlements would increase demand for the currency and make it a more desirable choice for central banks and foreign investors. Finally, India should implement a systematic programme to promote INR-denominated invoicing and settlement in its bilateral trade agreements. Priority sectors for this initiative should include the services sector, where India holds a strong comparative advantage, and sectors where India has significant market power as a buyer or seller, such as pharmaceuticals, agricultural commodities, and defence equipment. The promotion of INR trade invoicing should be supported by digital payment infrastructure, regulatory facilitation, and the negotiation of bilateral frameworks that incentivise trading partners to accept Rupee-denominated contracts.



CHAPTER 5: CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

The correlation matrix analysis reveals important distinctions between China's and India's methods for handling their respective currencies, CNY and INR. India's NEER is still reliant on foreign exchange reserves, remittances, and associated financial inflows, whereas China's NEER is heavily impacted by capital account activity and offshore investments. Despite weak correlations with trade metrics, China's investment-oriented strategy, which mainly depends on returns from offshore assets and regulated capital inflows, has been successful in preserving NEER stability.

India must diversify its sources of income and lessen its reliance on foreign reserves and remittances in order to increase the INR's acceptance around the world. INR's NEER could be strengthened and its internationalization encouraged by implementing a more aggressive investment-driven strategy akin to China's. India can improve the stability and international relevance of its currency by creating a network of offshore investments, promoting trade invoicing in INR, and encouraging returns denominated in INR. For policymakers looking to promote the Indian Rupee's internationalization, this comparative analysis offers insightful information.

The comparison with China's Renminbi internationalisation strategy is instructive not because it offers a template to be replicated wholesale, but because it demonstrates the transformative power of deliberate and coherent policy design in shaping a currency's international trajectory. China's success in advancing the Yuan's global role was not a passive consequence of its economic rise but the result of a sequenced programme of institutional innovation, financial market development, and strategic financial diplomacy. India's policymakers must bring a comparable degree of strategic intentionality to the task of INR internationalisation.



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The structural challenges facing the INR, including its persistent trade deficit, incomplete capital account liberalisation, limited offshore market development, and exchange rate volatility, are real and consequential. However, they are not insurmountable. The evidence from this study suggests that India's growing economic weight, its exceptional position as the world's largest remittance recipient, its robust GDP growth trajectory, and the expanding reach of its trade relationships provide a meaningful and growing foundation upon which a more internationally prominent Rupee can be built.

For policymakers, economists, and financial institutions engaged in shaping India's global economic strategy, the internationalisation of the Rupee represents both a challenge and an opportunity, one that demands not merely reactive management of external pressures but proactive and visionary engagement with the evolving architecture of the international monetary system. This research aims to contribute a rigorous and evidence-based contribution to that important and ongoing strategic conversation.



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