

THE MALADY OF FALLING RUPEE

Fluctuation in the value of its currency has been a historic phenomena in India. Tracing back the history of monetary economics one can witness the first major depreciation of Indian currency occurred in the era of the Delhi Sultanate under the regime of Muhammad bin Tughlaq. 'Prince of the Moneyed' as he is widely called, was the first to introduce the system of token currency in India. Enhanced forgery of such coins due to lack of a legal tender reduced its value drastically. The kingdom was afflicted by maladies of fiscal deficit and thus indebtedness, spiraling inflation and devastation of trade and commerce in the country. In this regard, while the monetary system has been revolutionized and modernized over the decades the problems faced by the fluctuation in the value of a currency till date remains unchanged.

Similarly variation of the demand and supply of money, from times immemorial has affected its value. The Government of India, initially following a Fixed Exchange Rate regime, has over fifteen years since independence held the rate of depreciation of Rupee constant at the rate of 3.25 per cent. The pace of depreciation gathered acceleration when the country faced the problem of twin deficits in the 1960s. Spiraling inflation and a demand for liberalization of trade in India by the international economies further worsened the situation. Post the New Economic Policy and India's emergence in the international trade mainstream sent a second jolt whereby the country faced its last monetary depreciation in 1991. The shift in the Exchange Rate regime from fixed to partially and then to full flexible rates was the main reason behind the fall. Thus fall in value of Rupee that occurred in the 90s was devaluation rather than a depreciation. It was a policy decision taken by the Government to enhance Indian export in the international market.

The steep fall in the value of Rupee against Dollar that the country has been witnessing since the past one year is a blended outcome of both national and international events and happenings. The country past one year has faced a dip in its exchange rate at 18 per cent which it did not face since the last 20 years. Since possibilities of history repeating itself always remains and so it did in the last one year. The major fall in the rate of exchange between rupee and dollar has been caused by mounting deficits in various fields. International oil prices are paid by countries in terms of US Dollar. The galloping oil prices to a level above \$100 a barrel has enhanced the demand for Dollar in the Indian market and thus have depreciated Rupee. The extensive imports made by the Government of India for oil, fertilizer and gold have added to the depreciative forces by creating a Current Account Deficit. India is one of the largest consumers of these items and on the face of ever rising demand for these commodities, domestic production is highly inadequate necessitating imports at high costs.

The widening of the Current Account Deficit is a determinant influencing the negative Balance of Payment (BoP) being faced by the country. Disappearance of Dollar from the Indian market and fall in value of Rupee has made imports costly and exports cheaper. Under such a situation it is natural to believe that a rise in exports would reduce the deficit being faced by the current account. However the credit fiasco both in USA and the Euro Zone has reduced foreign income and thus their demand for Indian products. Thus, a rise in import prices coupled with no equivalent rise in exports has widened the BoP deficit instead of bridging it.

The credibility of the country to repay its debts is not questioned if the BoP account depreciates. However, such a question inevitably arises when the fiscal deficit of the country widens. Pertaining to the wide expenditure sanctioned in the Annual Budgets the possibility of mounting fiscal deficit is not uncommon. The extensive expenditure on purchase of fertilizer and provisions for subsidy in the same has raised unplanned expenditure of the Government immensely. This spending has not been financed by additional tax revenue. A continued exemption in taxation in different sectors and to different income brackets has reduced tax income over the years. This reduction has also been coupled with the delay in the implementation of DTC and GST which is expected to increase the prospective income of the Government. The fear that the Government coffers would steadily decline within a short span has forced the US FDIs and FII's to withdraw from the Indian economy thereby creating a dearth of Dollar Reserve and deteriorating the value of money.

The growing fiscal deficit is obnoxious in terms of being the facilitator of inflation. Inflation can not only serve as the indicator of the fall in value of money but also as its reason. In the circumstances, inflation in the country has changed its nature from being demand pull to cost push. Besides a slow rise in industrial production is the primary reason behind the internal cause of inflation. If inflation in one of the trading country exceeds the other, the value of the currency of the later falls. This is exactly the situation being faced by India and USA. Since inflation in the former exceeds that of the later, the value of Rupees has faced a fall in terms of Dollar. Policy paralysis and lack of effective economic reform within the country has failed to control its spiraling inflation. The rising price levels and a handicapped Governmental policy have also discouraged FDIs and FII's thereby further reducing the Dollar Reserve in the country.

With the Euro Zone Crisis and the fall in credibility of Euro the international investors are swapping currency from Euro to Dollar. This has raised the demand for Dollar and reduced its supply. China being the most attractive haven for investors presently holds a vast reserve of Dollar. The dearth of Dollar and the outflow of FII's from India are caused by one such reason. This has also added to the rate of depreciation of Rupees.

The reasons which have caused a fall in the value of Rupee against Dollar are more or less in a vicious circle. Since an open economy can combat the external irritants once it has fought with its in built maladies, it is very essential to strengthen the internal economy by re-structuring before formulating external policies. A rise in value of Rupee can be expected only when the internal problem of inflation and deficits are solved. A strong economic policy and its effective implementation is thus the need of the time. With the plugging of these holes the susceptibility to international economic effects would not be difficult to be overcome. The vital question therefore is-when the decisions of policy rectification are going to be taken? In this regard Bharat Chamber of Commerce organized an Interactive Session with the eminent economists of West Bengal, on the 8th of June, 2012 to chalk out the possibilities and the future consequences of a continued fall in the rupee value. The Session was addressed by Professor Abhirup Sarkar, Department of Economics, Indian Statistical Institute and Vice Chairman, West Bengal Industrial Development Corporation Limited and Dr. Dipankar Dasgupta, former professor of Indian Statistical Department.