

## Declining value of Rupee: Who are the culprits?

- EM Joseph

Today, the Indian Rupee is facing a fall in its value that is unprecedented and seemingly unending. Though the process of decline started a couple of years ago, the phase has been very rigorous in the recent times. It was trading around Rs.45 per dollar in August, 2011. It fell to Rs.55 in August, 2012. On the day this is written, it has nosedived to as low as Rs.64 against the dollar. It is anyone's guess as to what would happen if the threatened war on Syria is declared. The Iraq war led by George Bush senior and the accompanying volatility in oil prices did add to the Indian forex crisis of the 1990s. Will the war on Syria led by Obama be anything different?

This apart, the internal value of the Rupee too thanks to the chronic inflation is already causing grievous injuries on the purchasing power of the common man. Now it is the turn of its external value – the exchange value - that has filled the air with a whiff of panic. This has scared all, especially the foreign investors, the corporates who revel in external commercial borrowings and the prospective domestic consumers who cannot breathe comfortably without the imported extravaganza and the like. There is plethora of explanations about the steep decline in the Rupee value. The moot question now is: Who are the culprits?

### **The immediate threat!**

India's short term debt maturing within a year stood at \$172 billion at the end of March, 2013. This means India has to pay back \$172 billion by 31<sup>st</sup> March, 2014. In March, 2008, it was just \$54.7 billion. It means it has trebled in the last 6 years. This represents the widening of the Current Account Deficit (CAD) from 2.5% of GDP in 2008-09 to 4.8% in 2012-13. Much of this increase has been funded by debt flows. If this short term debt maturing within a year is paid back, it would simply wipe out about 60% of our total forex reserves.

External Commercial Borrowings are now 31% of India's total external debt of \$390 billion as at 31<sup>st</sup> March, 2013. Corporate borrowings payable by end March, 2014 constitutes about 44% of the debt maturing within this year i.e. \$172 billion. These were all borrowings done during the boom years after 2004 with 5–7 year maturity, and they have all come home to roost.

About 100 leading Indian corporate houses owe the bulk of this \$172 billion. They have managed to roll over their foreign borrowings in the past years as the US Federal Reserve had its liquidity conditions easy. If the Fedreserve reverses its easy liquidity stance, nobody knows how the corporates would manage to repay. If the worst comes to the worst, some companies may even crumble. The air is already thick with news and gossip about some companies trying to sell off portions of their assets. Suzlon, an Indian MNC and the fifth largest wind power producer in the world is in the process of selling 70 to 75% of its domestic manufacturing plants. The Jet Airways is negotiating with the Etihad Airways of Abu Dhabi about selling a portion of its controlling shares. The leading 100 corporates that have borrowed externally are precisely those who have borrowed internally too. 70% of the credit by the Indian banking sector has gone to such big sharks. If the companies go broke, the banking industry would be in great trouble.

In such a context, India needs another \$90 billion of net capital flows to meet its CAD projected at 4.7% of GDP by the Prime Minister's Economic Advisory Council for the coming fiscal.

## **Flawed explanations!**

Raghuram Rajan prior to his appointment as the governor of the RBI was the first to speak on the declining Rupee. He simply attributed the whole episode of declining Rupee to the announcement by Bernard Bernanke the chairman of the US Federal Reserve Board on 22<sup>nd</sup> May that 'quantitative easing' in US was coming to end. Though he announced the prospect of this happening, Fedreserve continues to buy government bonds in the market and keeps the long-term interests low, and also pumping liquidity into the system. Earlier, finance was flowing into other countries where interest rates were attractive and this shored up their currencies. As Bernanke made this announcement which was no more an intention, long-term interest rates started hardening in US that caused an appreciation of the dollar against the rest of the world currencies especially of the 'emerging market economies' like Brazil, South Africa, India and Indonesia.

This explanation makes a dubious suggestion as if Rupee started falling only after 22<sup>nd</sup> May. In fact, it had started its downward journey much earlier.

The second explanation given by many is about the growth of the US economy, and to be more specific about the reduction in its unemployment figures. It focuses on the strengthening of the Dollar but traces it to the revival of its economy. The Rupee's tumble, and fall in sensex by 700 points that occurred prior to the 'Black Monday' was attributed to the growth of US in a facile way. It is true that the dollar has strengthened. It is - as already explained - due to the hardening of long term interest rates based on the announcement of Bernanke about 'quantitative easing'.

This explanation has basically flawed on two counts. One is, it does not recognize the longer term tendency of Rupee's decline prior to 22<sup>nd</sup> May. The other that it predicts growth of the US economy in the teeth of hardening long-term interest rates makes little sense. Will not these higher rates snuff out growth? The best description offered about the present US economy is that it is "bumping along the floor". When it bumps up a little, lot of noise is made about its recovery; when it gets back to the floor, the noise subsides. Nothing more, nothing less.

## **Widening CAD!**

The third one is about the current economic woes of the India specific factors. The government is committed to attract foreign investment of all descriptions – FDI, portfolio investments, external commercial borrowings etc. to manage the massive Current Account Deficit of 4.8% of GDP. But it thinks it can at best attract foreign flows that would finance the CAD only to the extent of 2.5%; naturally, the unfilled gap is bound to put pressure on the Rupee.

That India's widening CAD is putting pressure on the Rupee is not to be disputed. We will come to it later. However, here again one cannot ignore the general tendency of currency depreciation in many countries including Brazil, South Africa and Indonesia. This raises two questions that call for an answer. The first question is why should there be widening of the CAD across countries? The second, why should there be such a wave of massive depreciations across them despite differences in the ratio of CAD between them? This necessarily has to be located in the larger global context.

## **Random gossip!**

There are also some other kinds of India specific explanations. Pranab Mukherjee while he was finance minister made an unsuccessful attempt to plug the 'Mauritius route' for the entry of FDI while presenting

the Budget, and this undermined the confidence of the investors; Chidambaram's loss of nerves in pursuing 'reforms', the recent desperate measures consisting of capital controls and import restrictions taken with a view to shoring up the Rupee have frightened the investors, and so on. All these are simply picked from random gossip or stray reactions of speculators. They need not be taken very seriously.

What is needed is a general explanation to which some India specific factors should also be added. All these however should be located in the structure of contemporary capitalism. Such an explanation can ill afford to ignore and exclude the protracted crisis that world capitalism is currently experiencing.

The talk of the US coming out of this crisis is quite unfounded. Except the hype about the 'green shoots' in the economy, small increase in GDP and employment figures etc., there is nothing much to write home about. Europe remains stuck up in the mire of crisis. China's growth rate is palpably slowing down. This in turn has started affecting Brazil and other Latin American countries that are major commodity exporters to China. In short, the global recession is now spreading. There were days in the past when the non-metropolitan economies gave the impression that they would escape recession through domestic fiscal stimulus. They had done so earlier when the recession was for a brief spell. The protracted nature of the current recession makes it simply impossible for them. The *modus operandi* of this spread is the widening of the CAD.

### **Export – Import mismatch!**

Even as the growth rate slows down in some advanced economies today, some third world economies including India still register some growth. This is happening when their exports have dwindled but imports continue to grow. This mismatch between exports and imports further widen the CAD. This is because of the continuing recession in the advanced capitalist world to which the rapidly-growing third world economies have hitherto been exporting.

In short neo-liberalism is not a new discovery of wisdom. Economies in the world including that of India had their worst experience in the 1920s and 30s during the colonial period. Peasants and agricultural workers faced acute declines in their incomes. It is this experience that led to the switching over to the *dirigiste* (state controlled) economy, moving away from the free market after independence.

### **Behavioral pattern of wealth holders!**

In this context, it is important to know the behavioral pattern of the global wealth-holders. For them, US – the home base of capitalism - is the centre, and other countries are peripheries. It is the centre where they feel safer – crisis or no crisis. They will not leave the centre because of a crisis in the centre. Even if the prospective rates of return were the same between India and US, they prefer US. Even if India offers higher rates of return, if they get panic-stricken on this or that count, they shift to the centre. They will certainly leave the periphery when there is crisis in the periphery. In other words, there is a basic asymmetry in the world economy such that wealth-holders never get panic-stricken at the centre; when they feel occasionally panic-stricken at the periphery, they shift to the centre. After all, centre is centre, and periphery is periphery. This basic understanding of the movement of capital is very much necessary in order to come to grips with the issue of the declining Rupee.

### **GOI's crime no less heinous!**

Putting the issue of declining Rupee in a larger global context does not exonerate the government of India. It has a prime-minister who is an economist and a finance-minister who is a neo-liberal soothsayer

with a large band of neo-liberal intellectuals around them. The finance minister who is crying hoarse today about the widening CDA had been doing precious little to contain it in the past three years since it started widening, say 2010-2011. The corporates were allowed to indulge in heavy external commercial borrowings that ran to billions of dollars even for their domestic requirements, and the wealthy were allowed to revel in import spree. The imports included gold, luxury cars and many other pricey things.

The government did not even fully avail the portion of the Rupee payments for oil offered by Iran for fear of the US. However, wisdom has dawned at least now to go in for it. By this, India can save \$8.5 billion in foreign exchange. Just imagine here how many billion Dollars we could have saved earlier, had we taken the right decision at the right time?

After all, every binge has a bill. But this simple truth did not strike the economist PM and the economics savvy FM or the so-called team of intellectuals. Now all these lapses and the backlog have pushed the Rupee down the slope. Even today, the remedies put forth by PC are in the nature of widening the CAD further. Import of gold is not banned; the import duty that has been hiked might discourage its import for a while. Import of other luxury items have not been banned either.

The PM and the FM appear quite unruffled over the developments except making some statements here and there to assuage the panic. There is something else behind this inaction of the government, and their attempts at brazening out the situation. It is their belief that the world economy is going to turn around fairly soon; that is, the basic crisis that has caused this trouble for the Rupee would itself disappear soon. It is only this unfounded belief that is going to push this country into a period of acute crisis. In India, this illusion is particularly strong because the boom years of metropolitan capitalism exactly coincided with India's entry into the neo-liberal regime. But the crisis in the centre – US – has put an end to all these illusions.

Snapping out of the neo-liberal dispensation is the only and the ultimate remedy. Till then, at least some control on flow of capital, restriction on imports etc should be put in place. However, they can at best be palliatives and not remedies.

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**P.S: In this article I have taken much from the expert opinion expressed by Prof. Prabhat Patnaik in the media through a number of his articles. This is because I was convinced by his supreme logic. Prof. Patnaik is an eminent economist and a political commentator. He was part of a four-member high power task force of the United Nations (UN) chaired by Joseph Stiglitz to recommend reform measures for the global financial system in the aftermath of the 2008 global crisis. I have taken the privilege of using a few words and phrases of the Professor *verbatim* so that the spirit and meaning of his arguments do not get lost or distorted in the process of my presentation. Hope, my readers would not mistake this for an exercise in plagiarism.- EM Joseph**

<p>E M Joseph was an employee of the LIC of India from 1966 to 2004. He was a trade-union functionary of the All India Insurance Employees' Association (AIIEA). He has been contributing articles to dailies, monthly magazines etc mostly in Tamil in a small way, committed to the cause of social change.</p>
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