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Impact of Rupee Devaluation on the Growth of India Economy - A Study on Rebounding Strategies

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Abstract: **Sustainability of Rupee valuation in the pat one year has shown worrying concerns to the nation. Unpredictable down turn of rupee value has consequently resulted in rising gap between the value of imports and exports rates and this movement has brought out the economic down turn especially in the past one year. Raising inflation, slowing down of GDP rate in the last one year has largely influenced the rupee devaluation and economic growth. In view of this emerging problem which is showing its consequences on economic development and financial services, the present paper will focus on the impact of rupee devaluation on the growth of financial services sector. Further, the paper will also focus on problems and consequences that may emerge from the problem of rupee devaluation. The paper is also aimed to suggest rebounding strategies for the strengthening of rupee value there by facilitating the growth of financial services in India.**

Key words: **CAD, FDIs, FIIs, inflation, RBI.**

I. INTRODUCTION TO THE ERA OF RUPEE

The rupee historically changed its name from the Sanskrit word ‘rupya’ which was first used during the era of ‘Dravidian kingdom’. Later, the word has redefined as rupyarupa in the era of Chandragupta Maurya. The currency was redefined during the era of Britishers and finally, it has received the official status as ‘Rupee’ in the 20th century. “Rupyakam”, the mother name of ‘Rupee’, national currency of India has been in the crisis due to continuous depreciation in the recent past. The Indian currency has great significance in the world market and in fact; many neighbor nations have initiated the Rupee name for their currency. The Central Bank of India, i.e., Reserve Bank of India (RBI) and the Government of India possessing the issuing authority of banknotes and coins respectively.

The value of Indian currency, i.e., Rupee has initially valued in exchange of annas (i.e., 1 rupee is regarded as 16 annas). After independence, it was come into exchange in terms of paise, where as 1 rupee regarded as 100 paise. The earlier laws including Indian Coinage Act, 1955 and the redefinition of Naya Paise to Paise in the year 1964 has officially made the standard conversion rate in India.

The rupee has historically surpassed several critical eras both before and after independence. Before 19th century, the conversion rate of rupee is done with exchange of gold and silver coins, later in the era of Britishers; it has received some standard set of exchange rate. The post independence has witnessed tremendous transformation of Indian rupee value. The economic environment has largely liquidated the value of Indian rupee especially after independence. The high restriction of foreign trade, huge deficit and ever fluctuating inflation rates has largely influenced the Indian rupee value. The regulatory bodies including RBI and Finance ministry has been implementing the strategies to cope up and stabilize its value since 1965. The Indo Chinese War and Indo-Pakistan wars in 1960s have largely affected the Indian rupee. To add the fuel, the declining growth, huge expenditure on safety and defense, heavy dependence on agriculture for growth and rising imports from other countries has made the rupee to depreciate further. The instability in measuring inflation rate, declining economic growth till 1990s has largely depreciated Indian rupee against US Dollar. Despite the deficits in Government budget, the government of India has made a key beneficial strategy by initiating reforms in Indian economy. This phenomenon has helped the rupee value to stabilize by the early period of 21st century. The rapid development in service industries including ITES, Banking, Insurance and manufacturing industries including Pharma, Iron & other allied industries has benefited the Indian rupee to strengthen itself. Later, the recession which has touched world’s economy has made its impact on Indian rupee value. The period of 2012-13 has recorded the lowest GDP rate with 5% after the year 1991 has largely fueled for the depreciation of rupee value. By the mid of 2013, the Indian rupee has started to face the ever recording lowest conversion rate. In the month of august, 2013 it has received the lowest exchange rate of 70 rupees per 1 US Dollar.

II. PROBLEM OF THE STUDY

The declining Indian rupee has serious impact on the whole economy and to the emerging service sector in particular. The statistics of rupee devaluation especially in the last couple of years has shown negative impact and in the last 8 months, it has shown further worrying concerns due to lessening of growth in many sectors. In view, of this emerging scenario, the present paper will make an emphasis on the problem of rupee devaluation and its impact on financial services in particular. Apart from understanding of the problem of rupee devaluation, the paper also witnesses the rebounding strategies to counter the problem.

III. OBJECTIVES OF THE STUDY

Based on the preliminary investigation and defining of the problem, the present paper will focus on the following objectives.

1. To understand the scenario of declining of rupee value and its impact on the growth of Indian economy.

2. To identify the problems and consequences with reference to rupee devaluation.
3. To study the rebounding strategies for the strengthening of rupee value.

Finally, the study is aimed to provide findings and suggestions on the basis of analysis.

IV. METHODOLOGY OF THE STUDY

The paper is mainly based on the secondary data sources. The contribution of primary data is limited to personal interviews, and discussions with financial advisors, banking professionals and personnel from financial services. For this purpose, convenience sampling method is applied for collection of primary data. The secondary data is collected from the reports of RBI, Ministry of finance, Ministry of Commerce & Industry, Economic Advisor report to GOI, Independent reports from national and International research agencies, news papers and internet sources.

V. SCENARIO OF INDIAN RUPEE DEVALUATION

The devaluation history of Rupee shows unpredictable changes in a span of 100 years. In 1913, the value of Rupee is very higher and the exchange rate is fixed as 1 Rupee is equivalent to 25 US dollars. By the time of Independence in 1947, 1 Rupee value reached to 1 US dollar. Where as when it comes to the post liberalized era, i.e., in 2013, 1 Rupee valued 0.016 US dollar (which means 1 US dollar values 61.33 Rupees). In a span of 100 years, Rupee value has declined around 750 times to an US dollar.

The volatility prevailing in foreign exchange rates and various macro economic factors have directly influenced the Indian Rupee value. Indian Rupee is traditionally valued on the basis of flow of imports and exports from the nation, flow of capital, changes in inflation rates, fluctuations in the market due to government's decisions, flow of investments between countries, GDP rate, cost of borrowing and short term & long term interest rate differentials. The Rupee devaluation increases inflation rate and as a result, it shows the adverse affects on fiscal deficit there by the input costs across many sectors will increase sharply. The economy slow down has been witnessing due to sharp fall in GDP rate and Rupee depreciation. The economy slow down started to show adverse effects on India through rising inflation, raising unemployment and gradual slow down of agricultural and industrial growth.

The Rupee which has been depreciating from the last 6 months has risen sharply in the month July-August, 2013 period by crossing over 10% with in a month. High Current Account Deficit (CAD) which has shown highest in 2012-13 at a rate of 4.8% of GDP has been worrying India continuously though the government has been applying rebounding strategies. The poor growth of efforts and insufficient FDI inflows failed to stop the fall of Rupee valuation. The overseas investors pullout out of nearly Rs.18,500 crore from Indian capital market in a single month, i.e., July, 2013 shows as one of the factors for slump. The rising import bill has curtailed government's effort to put hold on Rupee decline. The Gold imports have increased to 162 tonnes in the month of May to June period by raising the gap between imports and exports.

The strengthening of US dollar index by 3.52% in the last six months has directly influenced the exchange rate and further the poor economic growth in the manufacturing, agricultural and mining sectors have failed to gain interest on foreign investors to turn towards India. The economic growth rate of 5% GDP rate, which is lowest since economic reforms have taken place in 1991, has curtailed the thoughts of FIIs and FDI flows in India. The value of exports as on July, 2013 is Rs.1544.27 crores in comparison with imports value of 2277.6 crores by the end of July, 2013. The gap is clearly indicating the economy scenario and showing the signs of down turn in the era of rupee deprivation.

The rupee devaluation in the last one year clearly shows the identical experiences that were took place in the year 1966 and 1991. From the last 45 years since 1966, the inadequate returns from the value of exports have been the major worrying concern for the declining rupee value. One of the very few services sectors, which has benefited from the declining Indian rupee is the ITES. Due to majority of the foreign projects currently under process are based on USA, the exchange rate has benefited the IT companies to gain hedge in the last two quarters due to the change in the exchange rate.

Table No.1: Exchange rate of Indian Rupee

DAILY EXCHANGE RATE OF THE INDIAN RUPEE (Rupees per unit of foreign currency)				
Date	**US Dollar**	**Pound Sterling**	**Euro**	**Japanese Yen**
30-Aug-2013	66.5742	103.3431	88.1605	67.8300
31-Aug-2012	55.7215	87.9508	69.6555	71.0400
30-Aug-2011	46.0190	75.4251	66.6958	59.9800
31-Aug-2010	47.0800	72.6350	59.5000	55.9600
31-Aug-2009	48.8800	79.2052	69.7000	52.7000
29-Aug-2008	43.7900	80.0500	64.5600	40.1400

Source: RBI report on exchange rates (period between 2008-2013)

From table no.1, it is evident that with in a period of 6 years, the value of rupee has declined from Rs.43 per dollar to Rs.66 by the end of 30th August, 2013. Rupee has achieved 10.6% decline in the past 5 years. The conversion rate of Pound sterling has increased from 80rs. to 103 Rs. The declining conversion rates for Euro and Japanese Yen are 7.5% and 14% respectively.

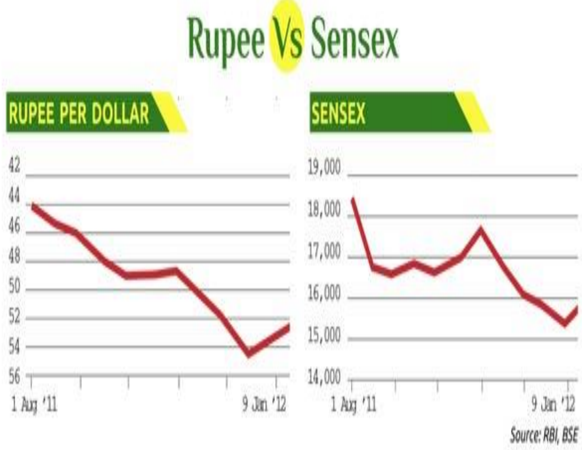
VI. IMPACT OF RUPEE DEVALUATION ON INDIAN ECONOMY

According to the report of ASSOCHAM, the average monthly expenditure of the Indians in the last 6 months has increased from initial 15% to 20%. The rise of petroleum and Diesel has been the major cause for the increase in the spending pattern rate. From the observations through primary data sources which have been collected from the opinions of experts in financial services, banking, ITES and Insurance professions, the following observations are made with regard to the causes for the declining of rupee value.

A) DECLINING OF RUPEE VALUE ON SENSEX

The declining rupee value especially started to emerge at a great speed in the year 2011. The report of RBI and BSE Sensex with reference to the impact of rupee devaluation on financial services with special reference to Sensex has clearly shown that from the select period of 1st August 2011 to 9th January, 2012, the declining of rupee value per dollar has shown the same downward trend in the movement of Sensex curve. When the rupee value has declined from 44 rupees to 56 rupees per dollar, the Sensex has shown its downward trend from 18,000 point approximately to just more than 16,500 points. The comparison is clearly showing the evidence of rupee depreciation on the fall of Sensex.

Figure 1: comparison of Rupee and Sensex curve



Source: Statistics of rupee value from the report of RBI, And the sensex results are gathered from BSE(Bombay Stock Exchange)

B) IMPACT ON FINANCIAL SERVICES

The rupee devaluation has especially affected the growth of all the sectors of Indian economy. Especially, its impact on financial services is evident. Table No. shows the difference in the grows of all the sectors in general and financial services in particular.

Table 2: comparative study on statistics for first quarter (2012-13, 2013-14)

S.No.	Name of the sector	Quarter 1 results 2012-13	Quarter 1 results 2013-14	Difference in growth rate (%)
1	Agriculture, forestry and fishing	2.9	**2.7**	**-.3**
2	Mining & quarrying	0.4	**-2.8**	**-3.2**
3	Electricity, gas & water supply	6.2	**3.7**	**-2.5**
4	Construction	7	**2.8**	**-4.2**
5	Trade hotels, transport & communication	6.1	**3.9**	**-2.2**
6	Financing, insurance, real estate & business services	9.3	**8.9**	**-0.4**
10	Community, social & personal services	8.9	**9.4**	**+0.5**
11	Overall statistics	5.4	**4.4**	**-1.0**

Source: Report of Ministry of statistics on First quarter results

The statistics clearly specifying that except in the community, social & personal services, remaining all sectors have shown negative growth. In agricultural sector, the growth has declined to 2.7%. In mining, construction, electricity, gas & water supply, it has shown high margin of negative growth. For financing, insurance, real estate & business services, the period rupee devaluation especially in the past one year has shown its impact with negative growth rate. Overall statistics are also clearly specifying that there is a decline in the growth.

C) PERSISTENT INFLATION

Right from the year 1969 to 2013, the nation has reported fluctuating inflation rate. The highest is recorded in 1974 with 34.6% and it has shown lowest of -11.3% in the year 1976. Further, the nation has recorded 5.79% rate of inflation by the month of July, 2013(Report by Ministry of Commerce & Industry). The inflation is especially shown increasing due to falling of rupee. The increasing inflation has adversely affecting right from grocery items, vegetables to all the manufactured goods and Fuel and power segment. The overall price in all the goods specified in the basket of whole sales goods by Government of India shows the failure of a common man's purchasing power.

D) DECLINING FINANCIAL GROWTH

The reports of RBI for the current year have clearly shown that the balance of payments surplus has reached to 3.83 billion dollars which is compared with a deficit of 12.8 billion dollar a year in the beginning of the year. The rising Current Account Deficit (CAD) has shown high worrying concerns for the nation. As the rupee value got declined, the value of CAD has grown to 4.8% by the end of August, 2013.

The rising CAD is mainly based on the lessening of exports and rising imports especially for Gold and Crude Oil. The value of Gold has shown reverse price growth especially in India due to declining rupee value. The value of Gold accounted as much as 11% of imports (as per the report of RBI,2012-13). Further, heavy dependence on imports, i.e., 78% from other countries has shown clearly about the over consumption of crude oil in India. Due to heavy dependence on foreign countries, the declining rupee and growth of economy has shown adverse effects on the value of imports. The margin between exports (1652.02 billion rupees)and imports (i.e., 2342.13 billion rupees) by the end of August, 2013 is clearly depicting the picture of deficit. All together, these financial indicators and statistics are clearly showing the adverse affects on economic growth of India.

VII. REBOUNDING STRATEGIES

From the observations and analysis from various sources which include the opinion of the experts, RBI reports and sources from the economic advisory report to Government of India, the following rebounding strategies are suggested.

A) CHANGE IN THE PATTERN OF POLICY BY RBI

Table No.4 shows the present reserves at RBI with reference to foreign currency, Special drawing rights (SDRs), Gold and other valuable assets.

Table No.4: Assets under RBI as on 30th August, 2013

Period	Foreign Currency Assets		Gold		Reserve Trench Position		SDRs			Total	
	(Rupees Billion)	(US Dollar Million)	(Rupees Billion)	(US Dollar Million)	(Rupees Billion)	(US Dollar Million)	(SDRs Million)	(Rupees Billion)	(US Dollar Million)	(Rupees Billion)	(US Dollar Million)
30-Aug-2013	16470.60	247402	1446.30	21724	132.50	1990	14435	291.20	4375	18340.60	275492
31-Aug-2012	14354.60	257620	1462.10	26239	123.10	2209	14435	244.80	4393	16184.60	290462
26-Aug-2011	13179.27	286195	1119.40	25349	137.72	2991	2884	213.69	4640	14650.08	319175
27-Aug-2010	12026.54	256648	895.64	19278	90.67	1935	-	233.41	4981	13246.26	282842
28-Aug-2009	12731.75	260523	465.76	9671	65.84	1347	-	235.60	4821	13498.95	276362
29-Aug-2008	12529.04	286117	380.64	8692	21.73	496	-	0.16	4	12931.57	295309
31-Aug-2007	9073.01	221509	281.86	6881	18.66	455	-	0.09	2	9373.62	228847

Report: RBI report on Foreign exchange reserves (period considered 2007-2013)

From Table no. 4 , it is to observe that RBI is fortunate to maintain high procurement of foreign currency. Further, the gold reserve from the period of 31st August, 2007 to 30th August, 2013, it is to observe that the RBI has procured 4 times of gold in a period 6 years. The recent decisions of RBI to exchange excess reserves of Gold and Foreign currency will provide sufficient growth to the Indian currency. Thought the effort provides short term growth, yet it is mostly needed strategy to be adopted.

B) USING FOREX RESERVES

As Table No.4 clearly indicates about the Forex reserves, liquidating the excess Forex reserves to a certain extent will provide the opportunity to regain the strength to the value of Indian currency. Further, the strategic decisions by both RBI and Ministry of Finance with regard to liquidate Forex reserves will also encourage foreign investors to keep a close view on the economic adjustments made by the government.

C) LIBERALIZATION IN CAPITAL FLOW AND CONTROL

The recent decision of Government to extend the capital flow in various financial services including liberalization of private banking entry in banking sector, increasing limit of FDI from 26% to 49% in insurance sector will greatly help the nation to attract FDI and FIIs. Further, the decisions regarding 100% FDIs in retail and other services will greatly provide the timely help to regain the momentum of Indian currency value.

D) CREATING AWARENESS AND ADMINISTRATIVE DECISIONS ON IMPORTS

The major drawback for the increasing of imports is largely due to excessive imports of gold and crude oil. Ensuring and awaking the people with regard to limited usage of petrol, diesel and other crude oil components will help the nation to achieve sustainability. As per the annual report of Ministry of Petroleum for the period 2011-12, there is a huge scope for energy generation through alternative sources including coal, lignite, thermal and Natural Gas. Achieving technological success right from procurement to production will help to reduce the heavy dependence on imports. Further, the present rate of import duty at 10% and extending upto 15% will greatly help to reduce the heavy imports in India. Further, encouraging the awareness about the limited consumption of gold and gold ornaments will also provide a great contribution to lessen the value of imports.

VIII. FINDINGS & SUGGESTIONS

The declining value of Indian rupee has been significant with the predictions showing worse for the next 6 months due to lower growth rate in all sectors and worrying concerns of global economic growth. The short term measures from RBI and statements of ruling government will temporarily restrict the decline. Due to short term strategies and actions, the long term survival of Indian rupee is still on the cards. The lessening value of denomination especially in comparison with US dollar, British pound sterling and Euro currency, the sectors depending on foreign projects will have to face a deep crisis in coming days. The rising inflation due to the devaluation of rupee will show its verse effects on the purchasing capacity of the people and in turn the production and GDP rate will further decline. Effective planning and implementation of both short term and long term policies and practices by RBI, government and the awareness of the people with reference to limited consumption of gold and other imports will help the rupee to regain the strength in comparison with other countries' value of currency.

Stronger organizational risk culture both by regulatory and the government would help improving risk management Liberalized decision implementation of FDI inflows, enhanced FII limits in government and corporate bonds will be the available options to make remedial measures on Rupee decline and improving Indian economy.

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