



## RUPEE DEPRECIATION - GS III MAINS

**Q.** The Indian rupee depreciation affects many sectors and the economy. Discuss the impacts of depreciation on Indian economy. (10 marks, 150 words)

**News:** *Rate of rupee depreciation coming down: Piyush Goyal*

### What's in the news?

- Commerce and Industry Minister Piyush Goyal said the rate of rupee depreciation has come down and expressed hope that after 8-10 years, it will start appreciating against US dollar, helping the Indian economy to grow at a faster pace.

### Key takeaways:

- Unlike in the past, Goyal said, the Reserve Bank of India and the finance ministry are working together to push the growth of the country.
- The government has taken a series of measures to boost economic growth and now India has become the fifth largest economy of the world.
- Rupee has stabilised now, otherwise it used to depreciate at a rate of 3-3.5 per cent annually,

### Depreciation:

- In the foreign exchange market, it is a situation when **domestic currency loses its value in front of foreign currency.**
- In the floating exchange rate regimes, the value of a country's currency is determined by the market forces of demand and supply.
- A currency depreciates with respect to foreign currency when the supply of currency in the market increases while its demand falls.

### Reasons for Currency Depreciation:

- **Declining exports** leads to a fall in export revenues and thus the demand for a country's currency reduces and it depreciates.
- A **large increase in imports** due to increased demand for imported goods can weaken the exchange rate due to the net outflow of currency.

### Recent Factors Boosting Rupee Depreciation:

#### 1. Trade deficit growth:

- The increase in imports, particularly due to rising oil prices, has led to India's trade deficit reaching a record high.



## 2. Policy differences between central banks:

- The Fed's low interest rates and optimistic economic outlook have strengthened the US dollar, diverging US and Indian central banks' policies.

## 3. Reserve accumulation:

- The Reserve Bank of India (RBI) has been actively purchasing US dollars to build reserves and prepare for potential future turbulence.

## 4. Capital exodus and market uncertainties:

- The benchmark stock index, S&P BSE Sensex, has declined by almost 10% from its peak, driven by capital outflows.
- Concerns regarding the Omicron variant and geopolitical tensions have also contributed to market uncertainties.

## 5. Global factors:

- Various global factors, including the conflict between Russia and Ukraine, rising crude oil prices and tightening global financial conditions, have played a role in the depreciation of the Indian rupee.

## Impacts of Rupee Depreciation:

### Positive Impact:

- Theoretically, a weaker rupee should boost India's exports. However, in the current global uncertainty and weak demand scenario, higher exports may not materialize.

### Negative Impact:

- Risk of imported inflation
- Challenges for interest rate management
- Increased cost of imports
- Adverse impact on oil and gas industry
- Inflationary pressure
- Impact on various sectors.

## Role of Reserve Bank of India (RBI):

The RBI plays a crucial role in managing currency volatility and supporting the rupee. Some steps taken by the RBI include

- Monitoring foreign currency markets and intervening when necessary.
- Relaxing restrictions on foreign ownership of government bonds and increasing borrowing limits for businesses to attract foreign currency inflows.
- Proposing rupee settlement methods to reduce the demand for US dollars in international trade.

## Measures to Address Rupee Depreciation:

- Encouraging foreign investment
- Relaxing foreign investment caps
- Selling foreign currency reserves



- Promoting industrial growth
- Export promotion and import reduction
- Rationalizing foreign currency expenditure
- Attracting NRI investments.

## WAY FORWARD:

### 1. Inclusion of Indian Corporations in Global Indices:

- Promoting the inclusion of large-cap companies in global indices can offset foreign portfolio outflows and enhance foreign investments.

### 2. Entry into Bond Indices:

- Expediting India's entry into bond indices can attract foreign inflows and positively impact interest rates.

### 3. Adequate Forex Reserves Management:

- Maintaining a comfortable level of foreign exchange reserves and employing timely interventions to control volatility can safeguard the rupee's value.

### 4. Fiscal Discipline and Inflation Control:

- The government should focus on limiting borrowing, while the RBI concentrates on inflation control as mandated by law.

### 5. Enhancing Export Competitiveness:

- Improving infrastructure, logistics, and export incentives to make Indian exports more competitive.

The Indian rupee depreciation affects many sectors and the economy. Imported inflation and trade deficits can hinder export competitiveness. Long-term stability requires fiscal discipline and inflation control. India's resilient economy may improve the rupee's outlook, but careful monitoring and proactive measures are needed to overcome the challenges.