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RESEARCH ARTICLE

IMPACT OF SINKING RUPEE ON INDIA'S FOREIGN TRADE(THREATS TO EXCHANGE RATE FLUCTUATIONS)

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Abstract

This study investigates the impact of rupee-dollar variations on the Indian economy. The economic conditions brought about by the rupee's decline against the dollar demonstrate that there has been a significant detrimental impact of this price fluctuation on several industries. Any country's export competitiveness and the value of its local currencies in terms of other currencies have a complex relationship. If the exported goods rely heavily on imported resources, this relationship will become more complicated. The Indian rupee has lost value numerous times during the past year, reaching a high of 80.064 to the dollar in July 2022. The Indian economy, which already had a significant budget and current account imbalance, was negatively impacted by exchange rate pressure. The Indian government made numerous difficult decisions to follow it again on the path. This essay discusses several difficulties brought on by these fluctuations as well as actions taken by the government and central bank to make them effective.

Introduction:-

The exchange rate between two currencies is the price at which one currency will be exchanged for another. The phrase "forex rate" or "foreign exchange rate" is frequently used. It is the rate of exchange between the currencies of two distinct countries. The forward exchange rate is the currency rate that is now stated but for which delivery and payment settlement will occur at a specific future period. The market-based exchange rate will change each time the value of one of the two-component currencies changes. The value of a currency typically increases when demand exceeds supply. The Indian Rupee and the British Pound were correlated from 1950 to 1973. On September 24, 1975, ties between the Indian rupee and the pound sterling were cut, severing the link between the two currencies. In India, a float exchange system was implemented. As a result, the effective exchange rate of the rupee was determined on a managed, floating basis and linked to a "basket of currencies" with India's trading partners. In 1993, the Liberalized Currency Rate System (LERMS) was replaced with the Unified Exchange Rate System, a market-based exchange rate system. The RBI did not, however, give up its ability to act in the market and manage the value of the rupee.

Since the early 1990s, India has implemented several economic changes, notably the liberalization of foreign capital inflows. The Bretton Woods system's collapse in 1971 marked the beginning of floating exchange rate systems in numerous countries, and the foreign exchange market has since expanded to become the largest market in the world. The main reforms that received attention were the expansion and strengthening of the foreign currency market and

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the liberalization of exchange control. The market dynamics that control the exchange rates are based on the supply and demand for these currencies. A currency's value decreases when supply outpaces demand.

The Indian rupee, the country's currency now, is constantly falling, wreaking havoc on the economy. Because they are typical in most countries, currency fluctuations are an intrinsic component of the floating exchange rate system. This exchange rate mechanism, commonly known as the forex or foreign exchange rate, determines the price at which one currency will be exchanged for another. Many fundamental and technological factors influence the rate. Understanding the concept of exchange rate and currency fluctuation and evaluating the variables that contributed to the rupee's decline against the dollar are the main objectives of this study. Talking about the several strict measures the Indian government has taken to strengthen the rupee.

Literature Review:-

Lily et .al (2022) found that Exposure to exchange rates does impact corporate value. Two significant discoveries are revealed when the DFR market beta is included in the exchange rate exposure model. First, there has been a marked rise in the number of businesses vulnerable to fluctuations in currency rates, particularly in Indonesia, Thailand, Sri Lanka, and Vietnam. Second, more businesses in the sample nations will be exposed to multiple bilateral exchange rate risks. The results show that alternative explanations for the exchange rate exposure conundrum may include market features like thin trading. Asymmetric analysis should also be included in future studies as a potential substitute explanation for exchange rate exposure.

Mukhopadhyay A. (2021) examined that before the pandemic, there was a noticeable dearth of investment and consumption demand; COVID-19 accentuated those trends. Therefore, from this point forward, demand creation through direct government fiscal intervention will be a significant component of India's economic recovery.

Das et al. (2020), by using the Jaya optimization approach and Extreme Learning Machines, created a hybridized intelligent machine learning-based currency exchange forecasting model (ELMs). This model can accurately forecast the exchange rates of the US dollar (USD) to the euro over a range of periods, from one day to one month in advance, based on statistical measures, technical indicators, and a combination of the two.

AnubhaDhasmana claims that India provides a unique setting for analyzing the consequences of exchange rate fluctuations. Before the Balance of Payments crisis in 1991, the Indian Rupee was tied to a basket of currencies that included the US Dollar as the main currency. The foreign payment crisis of 1991 forced the Reserve Bank of India (RBI) to implement a series of market-focused adjustments in the financial sector, and in March 1993, it changed from a fixed to a market-based exchange rate regime. The implementation of current account convertibility in August 1994, the gradual liberalization of the capital account, and other trade and financial liberalization initiatives all contributed to an increase in overall foreign exchange market turnover. An increase in Indian Rupee volatility has directly resulted from these adjustments. In light of this, the RBI's exchange rate management strategy has been designed to avoid speculative attacks and maintain orderly circumstances in the foreign exchange market without establishing a precise exchange rate goal.

According to **Ravindra Dhokla**, a Member of the Monetary Policy Committee, the Indian Rupee has recently declined significantly against the US Dollar. The pace of decline is noticeably slower when measured in terms of trade-weighted Nominal Effective Exchange Rate because other currencies have also declined against the US Dollar. The decrease in NEER affects headline inflation. Therefore, its impact on inflation will likely not be huge**.**

Background of India's exchange rate policies

India provides a unique case study for analyzing the effects of exchange rate fluctuations. Before the Balance of Payments crisis in 1991, the Indian Rupee was tied to a basket of currencies that included the US Dollar as the main currency. The foreign payment crisis of 1991 forced the Reserve Bank of India (RBI) to implement market-focused modifications in the financial sector and shift the paradigm from a fixed to a market-based exchange rate system in March 1993. A rise in total turnover in the foreign exchange market of more than 150% (from $73.2 billion in 1996 to $130 billion in 2002-2003, and then to $1,100 billion in 2011-2012) was caused by the establishment of the current account convertibility in August 1994, the gradual liberalization of the capital account, along with other trade and financial liberalization measures.

In light of this, the RBI's exchange rate management strategy has been designed to avoid speculative attacks and maintain orderly circumstances in the foreign exchange market without establishing a precise exchange rate goal. To accomplish this, the RBI has used a variety of instruments, including currency sales and purchases in both the spot and forward segments of the foreign exchange market, adjustments to domestic liquidity using the Bank Rate, Cash Reserve Ratio (CRR), Repo rate, etc., and monetary sterilization using specialized instruments. As a result, asymmetry amid bouts of appreciation and depreciation has been a fascinating aspect of RBI's activity. In addition, RBI has been actively participating in the foreign exchange market by purchasing foreign currency during the rupee's appreciation.

Objectives of the Study:-

1) To comprehend the idea of currency and exchange rate fluctuation.
2) To comprehend the reasons for the rupee's depreciation against the dollar.
3) To research the true effects of the rupee's decline on the Indian economy
4) To support the rupee, the government and RBI have implemented a number of severe restrictions.
5) To give viable solutions to solve the issue

Table 1:- Concept of Currency Appreciation And Depreciation.

Impact on	Rupee depreciation occurs when the value of a rupee falls in relation to the dollar (for instance, when US$-INR moves from Rs.75 to Rs.80).	Rupee APPRECIATES when the rupee's value rises relative to the USD(For example, when US$-INR moves from Rs80 /- to Rs 75/-
Importers	Imports become expensive as we must pay an additional Rs. 5 for every USD. Imports increase in price.	Imports become more affordable as we spend Rs. 5 less for every USD imported.
Exporters	Exporters will earn more money. For every dollar exported, the exporter will also receive an additional Rs. 5. EXPORTERS GET MORE PAY	Less money will be made by exporters. The exporter will now receive Rs. 5 less for every dollar exported. EXPORTERS GET LESS PAY
Indian Who Wish to Go on Holidays Abroad and for Education	The cost of this trip will increase since tourists must pay an additional Rs. 5 for every dollar they spend outside of India. The cost of vacation and educational packages will increase.	The cost of the journey is reduced by Rs3 for each USD the traveller intends to spend abroad. There will be less expensive vacation and education packages.

Sinking Rupee as a big danger to Economy

The current state of affairs is endangering the economy from the inside and the outside. If it cannot arrest the rupee's decline, India could experience its most significant financial crisis. The central bank must decide how to deploy its meager reserves while maintaining investor confidence. The table highlights the constant reduction of the Indian rupee with the US dollar (RBI exchange rate data).

Table 2:- Exchange Rate INR/ USD.

2006 (April)	2007 (April)	2008 (April)	2009 (April)	2010 (April)	2011 (April)	2011 (Aug.)	2011 (Dec.)	2012 (April)	2012 (Aug.)	2012 (Dec.)
45.15	41.04	39.85	49.96	44.64	44.52	45.249	54.235	51.659	55.989	54.629

2013 (April)	2013 (Aug.)	2013 (Dec)	2014 (April)	2014 (Aug.)	2014 (Dec.)	2015 (April)	2015 (Aug.)	2015 (Dec.)	2016 (April)	2017 (Jan.)
54.626	61.819	62.102	60.262	61.058	62.652	64.402	65.22	67.043	66.666	68.322

2017 (Aug)	2018 (Jan.)	2018 (Aug)	2019 (July)	2019 (Nov.)	2020 (Jan.)	2020 (April)	2021 (March)
63.6458	63.2965	74.3407	68.374	72.1512	70.7246	76.97	72.29

2021 (Dec.)	2022 (Jan.)	2022 (July)
76.3125	73.8102	80.064

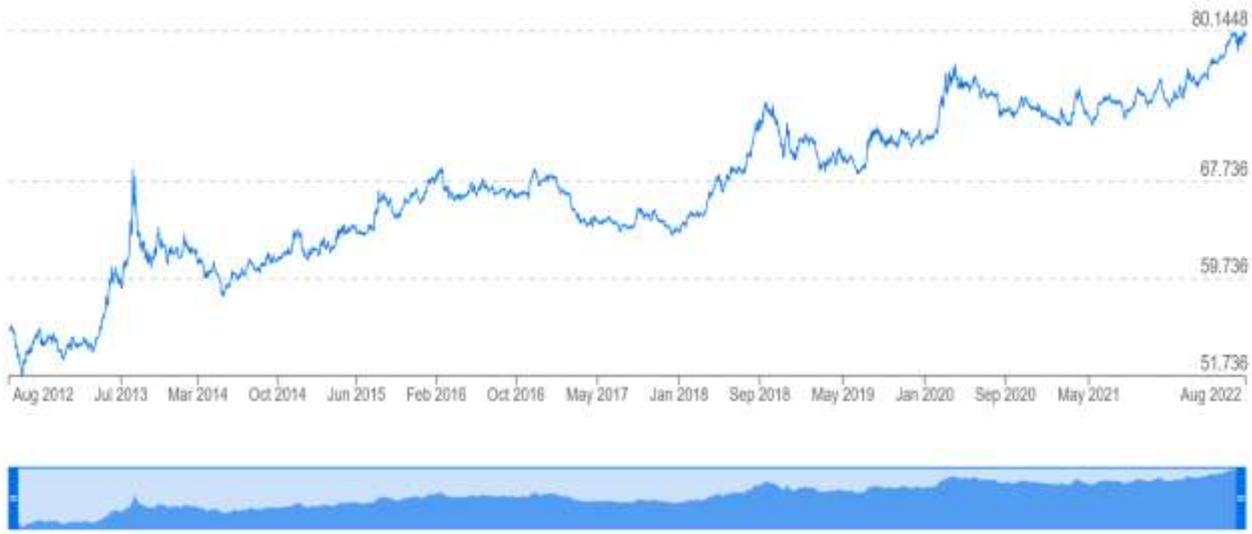

Fig.1:- INR per 1 USD Source: www.xe.com/currencycharts/?from=USD&to=INR&view=10Y.

The severe crisis that hit the economy and attracted the attention of the RBI and the Indian government was brought on by several factors. Here are a few of the reasons. First, currency depreciation can be caused by various factors, including economic, political, and unethical behavior, although some require more concentration and objective study than others.

Dollar on a Strong Position in the global Market:
The enormous strength of the Dollar Index is the primary cause of the rupee's decline. However, due to US equities' record-breaking performance and the labor market improvement, investors are more optimistic about the future of the US economy.

Recession in the Euro Zone:
The recession in the Eurozone is also impacting the rupee. Due to the Euro crisis, which has been affecting the global economy for the past few months, investors are focusing on buying dollars and selling euros. As a result, the rupee exchange rate will be under pressure to fall if there is any currency exportation or reduction in investment.

PThe pressure increasing Current Account Deficit:
A declining currency will make an export-heavy nation happier. On the other hand, India does not profit from this since a substantial portion of its imports is made up of crude oil and gold. Moreover, one of India's leading commercial partners, the eurozone, is experiencing a severe economic crisis. The decreased demand, has dramatically damaged Indian exports

Speculations from Exporter and Importer side:
Speculations in the markets are a significant factor in the rupee's decline. An unexpected spike in dollar rates caused importers to start scrambling for dollars to cover their positions, which increased the demand for dollars even more. On the other hand, exporters continued to hang onto their dollar reserves as they bet the rupee would continue to decline. The combination of the two causes led to an increase in the demand for dollars and a decrease in the value of the rupee.

Unattractive Indian Market:
A reliable source of dollars entering the Indian market is foreign institutional investors (FIIs). However, a recent survey shows India's FII participation in developing markets has significantly reduced. Other factors contributing to this lack of attractiveness are strict political policies.

Interest Rate Difference:
Higher accurate interest rates often entice foreign investment, but the RBI is under increasing pressure to lower the policy rates as GDP slows. Foreign investors prefer to avoid investing in such circumstances. This has an additional impact on India's capital account movements and puts pressure on the rupee to depreciate.

Challenges faced by the Forex Reserves of the Indian Government:
RBI can buy Indian Rupees and sell foreign exchange reserves, increasing demand for the currency. However, using up vast amounts of forex reserves to stop depreciation runs the danger of deteriorating trust in the economy's capacity to satisfy even short-term external obligations.

Make SavingsAppealing- Easing Capital Controls:
The RBI can move to increase the supply of foreign currency by increasing market activity to strengthen the rupee. The RBI may increase the FII investment cap for governmental and corporate debt instruments. As a result, long-term FDI debt funds might be persuaded to invest in infrastructure. The external commercial borrowing ceiling can be increased to allow for more considerable ECB borrowings.

Raise the cost of maintaining and repaying foreign debt:
A significant negative effect of the rupee's depreciation is that it will make it more difficult for the Indian government and businesses that have raised dollar-denominated debt to service and repay their international debt. This is because most international loans with dollar terms will immediately result in a weight of expensive short-term debts.

Effect of Covid 19 on Foreign Trade of India
With a 21-day total lockdown, the Indian government has quickly taken action to contain the coronavirus. However, the immediate effect of this epidemic will be a decline in economic growth and disruption of India's import and export markets due to reduced access to its vital international supply chains.

There was a global slowdown because China was the outbreak's first epicenter. An estimated 50 billion dollars in exports will be lost in global value chains in 2020 if China's exports decline by 2%. China is India's primary import source, making up 14.2% of total imports from the rest of the world, valued at USD 68.1 billion in 2019. Chemicals, textiles and apparel, automotive, and metals and metal products are the industries most impacted by the spillover effects of the disruption in Chinese supplies, with a potential cost to India's exports of over USD 348 million. According to projections, the textile and garment industries will take a blow of USD 129 million, followed by the chemicals industry.COVID-19’s direct effect on India’s exportations

The COVID-19 report gives Indian firms the most exposure in the textile, apparel, and transportation sectors, making up around 18% of the country's total exports. The main three exports from India—fuels, chemicals, and stone and glass—represent more than 40% of its overall exports and exhibit moderate sensitivity. The industries that are less dependent on export markets, including those that produce vegetables, polymers, rubber, cattle, food products, etc., have the lowest exposure risks.

Table 3:- Potential impact of COVID-19 on trade.

Potential Impact on Sector	India's Exports (USD Billion)	Export Product Share (%)
Fuels	48.6	15.1
Chemicals	44.6	13.8
Stone and Glass	43.1	13.4
Textiles and Clothing	37.0	11.5
Mach and Elec	32.2	10.0
Metals	26.6	8.3
Transportation	24.3	7.6
Vegetable	18.0	5.6
Plastic or Rubber	11.0	3.4
Animal	10.6	3.3
Food Products	6.8	2.1
Miscellaneous	6.4	2.0
Minerals	3.9	1.2
Hides and Skins	3.3	1.0
Footwear	3.1	1.0
Wood	2.7	0.8

Notes: High Moderate Low

Source: World Bank WITS, 2019; Moody's analytics

Impact of the Ukraine War on India's Foreign Trade

Besides the pharmaceutical and sunflower oil refining industries, Russia and Ukraine account for a relatively tiny portion of India's international trade. Thus we might not be significantly impacted. However, the escalating price of crude oil could harm India's foreign trade.

Data analysis reveals that neither Russia nor Ukraine are big trading partners. India imported $2.14 billion and $1.98 billion worth of goods from Ukraine in FY 2022 and the first nine months of FY 2023, respectively, as shown in Table 1. These account for about 0.54 and 0.45 percent of all imports into India, respectively. Russia contributed 1.39 percent and 1.56 percent, or $5.49 billion and $6.89 billion, respectively, of India's total imports in FY 2022 and the first nine months of FY 2023. However, these two countries are modest export partners for India once more. India supplied commodities to Ukraine for $450 million in FY 2022 and $372 million in the first nine months of FY 2023.

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Table 4:- India's Trade with Ukraine and Russia.

	Ukraine		Russia	
	FY2022	**9MFY2023**	**FY2022**	**9MFY2023**
Imports (US$ Mn)	2,139.86	1,980.11	5,485.75	6,893.57
Share (%)	**0.54**	**0.45**	**1.39**	**1.56**
Exports (US$ Mn)	450.97	372.23	2,655.52	2,546.74
Share (%)	**0.15**	**0.12**	**0.91**	**0.83**
Total (US$ Mn)	**2,591.37**	**2,352.79**	**8,142.66**	**9,441.87**
Share (%)	**0.38**	**0.32**	**1.19**	**1.27**

Source: DGCI&S

Further investigation of both countries' import and export figures provides researchers with an intriguing picture. India acquired 1.74 million tonnes and 0.97 million tonnes of crude sunflower oil in 2022 and 2023, respectively. Ukraine is the source of a disproportionately significant amount of India's imports of crude sunflower oil. India acquired 2.2 million tonnes and 1.4 million tonnes of crude sunflower oil in 2022 and 2023, respectively. Thus, in FY 2022, Ukraine accounted for 80% of all imported crude sunflower oil; in FY 2023's first nine months, this ratio fell to 72%. India's dependence on Ukraine has barely decreased, while its imports of crude sunflower oil from Argentina climbed from 6.3 million tonnes by a factor of two.

Policy Implications

These findings offer some crucial insights for policymakers attempting to determine how exchange rate changes affect the real economy. First off, as the import cost channel predominates in the short run, a real depreciation is likely to have a short-term negative influence on the firm's output growth. Real depreciation has a more significant impact than genuine appreciation, and the impact is asymmetrical.

Suggestions and Recommendations:-

The government should take action to ease the limitations on portfolio investment in the Indian market, signaling its intention to maintain foreign inflows to promote FDI and establish a favorable environment for economic growth.

·Banks should not be allowed to hold exclusive positions in currency futures or options.

·Making India a desirable travel destination with long-term diversity is the best way to do this, as attracting sufficient foreign inflows is the key to finding a solution.

·Another strategy to address this issue is to liberalize FDI ceilings while reducing administrative burdens and putting in place the necessary infrastructure to make doing business simple.

1. Plans for issuing sovereign bonds should be launched regularly. The rupee's standing on the international market will improve.
2. It is important to successfully execute significant policy reforms, such as the Goods and Services Tax (GST), the Direct Tax Code (DTC), FDI in retail and aviation, the Companies Bill, and fuel decontrol.
3. Government policies ought to be made public to set a target range for rupee volatility.

Conclusion:-

A nation's pride, as well as several indices of economic growth, are affected when the value of its currency declines. The rupee devaluation includes decreased foreign investment, increasing external debt pressure, and growing prices for India's oil and fertilizer subsidies. The main benefit of rupee depreciation is the improvement of the current account deficit due to export stimulation and import deterrence. However, despite this year's considerable growth in exports and sales, Indian businesses are still experiencing significant foreign exchange losses due to the weakening of the rupee. The total profitability of these businesses suffers as a result. For a nation like India, imports are essential for trade. This decline has been attributed to the bleak prognosis for the global economy, increasing inflation, a growing current account deficit, and FII outflows. RBI has responded with timely involvement by occasionally offering dollars. However, investors favor the USD as a haven currency during global unrest. RBI can loosen capital regulations to entice investment by raising the FII investment limit on corporate and government debt instruments and introducing more excellent caps in ECBs. The government can produce a stable political and economic climate. The future of the INR will be primarily influenced by the forecast for the global economy and the Eurozone. With the efforts taken by the central bank, a reverse trend is anticipated for the rupee's future, but it will only have a short-term effect.

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