

# THE RUPEE PROBLEM

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Banking, NPAs and RBI

The rupee, which is currently the worst-performing currency in Asia, is finally receiving some help from the authorities. The Union government, after a meeting with Reserve Bank of India Governor Urjit Patel, on Friday [announced a list of measures to arrest the sharp decline in the currency](#), which has lost about 12% of its value since the beginning of the year. These include steps to curb the import of non-essential goods and encourage the export of domestic goods, which will help in addressing the country's burgeoning current account deficit that hit a five-year high in July. Other steps such as removing restrictions on foreign portfolio investments and encouraging Indian borrowers to issue rupee-denominated 'masala bonds' were also announced to facilitate the inflow of dollars and de-risk the economy from fluctuations in the exchange rate. Further, the term limit imposed on borrowings of manufacturing companies is to be shortened further in order to curb dollar demand. The response to the move from the markets will need to be carefully tracked. Even before the official announcement on Friday, the rupee witnessed some recovery against the dollar amidst hopes of favourable government intervention, while stocks and bonds also recovered.

## A brief history of the rupee

These steps to strengthen the rupee in the short term are welcome, given the large-scale outflow of capital from emerging markets to the West. These *ad hoc* steps to avoid an immediate crisis in the external sector, however, should not deflect attention from the more fundamental reasons behind the decline of the rupee. India has been unable to boost exports over the years for various reasons. At the same time, it has been unsuccessful in finding sustainable domestic sources of energy to address the over-reliance on oil imports. This has meant that the rise in the price of oil has traditionally exerted tremendous stress on the current account deficit and the currency, as is happening now. The government needs to think of a long-term plan to boost exports, preferably through steps that remove policy barriers that are impeding the growth of export-oriented sectors, in order to find a sustainable solution to the problem of the weakening rupee. The depreciating rupee is also a symptom of persistently higher domestic inflation in India over many decades. For example, in line with vastly different inflation rates in India and the U.S., the rupee has lost about 60% of its value in the last 10 years against the dollar. So this problem cannot be addressed without drastic changes in the style of monetary policy conducted by the RBI, which is an unlikely proposition. Until then, the best that can be hoped for is a steady drop in the value of the rupee without any drastic shocks to the economy.

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