Storm Clouds over India's Balance of Payments*

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India's current account deficit for the second quarter (July-September) of 2022-23 has reached a massive $36.4 billion which is 4.4 per cent of the gross domestic product, higher than at any time in the last nine years. It is only in October-December 2012 that the absolute level of the current deficit had been $32.6 billion which was 6.7 per cent of the GDP.

By contrast the current account deficit had been $18.2 billion in the first quarter of 2022-23 or 2.2 per cent of GDP, and $9.7 billion or 1.3 per cent of GDP in the second quarter of 2021-22, i.e., exactly a year ago. In other words compared to the first quarter itself there has been a doubling of the current account deficit as a percentage of GDP which is a whopping increase; compared to the second quarter a year ago the increase in GDP percentage is more than three times.

Quite apart from the sheer size of the current account deficit, there are at least three reasons why the balance of payments is a cause for serious concern. First, the reason for the increase in the current account deficit, by as much as $18. 2 billion compared to the previous quarter, is an increase in merchandise trade deficit, that is, in the excess of imports over exports of goods. The merchandise trade deficit increased by over $20 billion, from $63 billion to $ 83.5 billion, between the first and the second quarters. According to the Reserve Bank of India this increase was for two reasons: first, the increase in oil prices that has occurred in the wake of the Ukraine war and pushed up our import bill; and, second, the lacklustre performance of our exports because of the slowing down of the world economy. Economic commentators in the media have adduced other factors, like the weak rupee and the revival of domestic demand, for the widening of the merchandise trade deficit, but these are erroneous assertions: a weak rupee should, if anything, improve rather worsen the trade deficit; and the revival of demand has not been so pronounced as to widen the deficit so much, since the GDP growth itself which is the primary source of income has been low.

The problem with the factors identified by the RBI is that they are not going to go away soon. The Ukraine war is not just a conflict between two countries over some bilateral issues. It has to do with the shape that imperialism will have in the future and therefore has a decisive significance; because of this imperialism will resist any easy and amicable solution to the war. Likewise, the inflation that had made an appearance even before the war but has now become exceedingly serious in the metropolitan economies as a consequence of it, is being sought to be combated through the creation of recession and unemployment; this again will be a long drawn-out affair. It follows therefore that the merchandise trade balance will continue to remain as adverse as in the second quarter of 2022-23 for quite some time.

The second cause for concern is that this merchandise trade deficit has occurred in the midst of a sharp decline in the exchange rate of the rupee amounting to as much as 10 per cent over the calendar year 2022. Normally, an exchange rate depreciation is supposed to improve the trade balance. Such an improvement of course takes time, so that the simultaneous occurrence of a worsening of the trade balance and an exchange

rate depreciation should not be a matter of surprise. But the persistence of a large deficit invariably creates expectations of an exchange rate depreciation, which in turn give rise to an actual exchange rate depreciation by causing financial outflows. Since neither of the factors mentioned by the RBI as underlying the widening trade deficit at present, is going to be affected by any exchange rate depreciation, its impact on the deficit will be marginal even after sufficient time has elapsed, in which case we are entering a period of free-fall for the rupee. It is already being called one of the weakest currencies in Asia, but this state of affairs is going to persist, perpetuating inflation in the country through the cost-push effect emanating from imported inputs.

It may be thought that India's large foreign exchange reserves should prevent such a free fall of the rupee, but even the current fall has occurred despite nearly a hundred billion dollars being spent by the RBI in its efforts to stabilise the rupee. In the second quarter of 2022-23 itself there was a $25 billion decline in reserves. The depletion of reserves therefore cannot prevent a fall in the rupee; what is more, as the level of reserves declines, speculation against the rupee will escalate, making matters even worse. It follows therefore that despite our large reserves India's balance of payments have become a serious cause for concern.

The third reason why the balance of payments situation portends ill for the economy is as follows: the yawning merchandise trade deficit has occurred in a situation of low GDP growth. The first quarter (April-June) GDP growth in 2022-23 over the corresponding quarter of 2021-22 had been 13.5 per cent, reflecting recovery from a Covid-induced trough. But the second quarter growth has been just 6.3 per cent compared to the second quarter of 2021-22. The growth in gross value added (GVA) in the second quarter, which measures the actual increase in production, ignoring the effects of tax changes that GDP incorporates, was even lower, just 5.6 per cent. The reason for the slowdown in growth was a slowing down of the manufacturing sector which was not an episodic development but a persisting one (People's Democracy, December 25). India's creeping industrial stagnation in short is pulling down its GDP growth rate, and the rise in merchandise trade deficit has occurred despite this growth slowdown.

The rise in trade deficit will almost certainly entail a further rise in the interest rates in India. This will be done keeping several objectives in mind: for attracting global capital for financing the deficit; for reducing the deficit by curtailing domestic demand; and for curbing the inflation unleashed by a declining rupee. Neoliberal capitalism has just this one instrument, which creates recession and unemployment, for combating multiple economic woes and it is going to be used vigorously in the coming days. That however will only worsen the growth rate of GDP and accentuate unemployment and distress in the economy. The fact that the yawning merchandise trade deficit is occurring not because of any pronounced boom in the economy but rather in the midst of a creeping industrial stagnation, therefore augurs ill for the economy.

Some may argue that there is nothing new in the current situation, that in 2012-13 the country had faced a similar predicament when the tapering off of bond purchases by the Federal Reserve Board of the United States, indicating a tightening of US monetary policy, had caused a similar widening of the merchandise trade deficit (as mentioned earlier) and a fall in the rupee; but that, while heralding a period of

economic difficulties for the country, had not precipitated any insurmountable crisis. Why should a similar situation be a matter of such serious concern now?

There is a fundamental difference between then and now. The world economy is currently afflicted by high inflation unlike then, because of which there is a general rise in interest rates everywhere and the entire world economy is going into a precipitate recession. At that time the RBI had responded to the situation by raising India's interest rate, while other countries were not increasing rates, which was why the RBI's response succeeded in preventing a crisis. But now, a rise in the interest rate by the RBI simply would not work because all capitalist countries are raising interest rates; this general rise in interest rates will bring about a world recession and hence keep our merchandise trade deficit high for quite some time, thereby precipitating a continuing economic crisis in India as suggested above.

All this is indicative of the cul-de-sac that neoliberal capitalism has run into, and the severe challenge to the hegemony of western imperialism that has emerged. World capitalism in short is currently in a state which creates new possibilities of transcending it. But if instead of seizing such an opportunity our economy remains stuck within a regime of neoliberal capitalism, and seeks to overcome its predicament merely by resorting to bailouts through borrowing, then that will only accentuate in future the economic crisis which the country is facing at present.

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