

THE FOREIGN EXCHANGE CRISIS  
& SOME REMEDIES

by

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OF all the problems facing this country today, in my judgment one problem which calls for immediate and urgent attention and solution is the problem of Foreign Exchange. It is not entirely a domestic problem. Whilst it has far-reaching implications on the general economy of the country in its various ramifications, it is a problem in which we are concerned with the world at large. Therefore this problem has a little touch of delicacy about it, particularly at this psychological moment and calls for a certain amount of restraint in handling it.

If you try to look at the genesis of this problem, I can assure you that it did not need an astrologer two years ago to forecast the crisis we are faced with today. Recently Mr. C. D. Deshmukh, the Ex-Finance Minister, observed in an article that as far back as April 1956, the problem had already arisen and that in his judgment we should have made efforts from then onwards to provide all the requisite resources to meet the situation.

You will be interested to know that in April 1956, when we embarked on the Second Five-Year Plan, we started with sterling reserves of Rs. 746 crores. Last week, according to the Reserve Bank's statement, our sterling balances had dropped to Rs. 200 crores. In the meantime, about the end of last year, we had to approach the International Monetary Fund for temporary assistance. As a member of I.M.F., India has been allotted a quota

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a ■ "People must come to accept private enterprise not as a necessary evil, but as an affirmative good."  
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—Eugene Black,  
President, World Bank

of \$400 million to be drawn in emergency with, of course, the previous approval of the International Monetary Fund, to tide over exchange difficulties. We were allowed to utilize \$200 million (about Rs. 95 crores). So, when I am referring to the balance of Rs. 200 crores last week, this sum of Rs. 95 crores is to be added to **Rs. 746** crores we had in April 1956. Apart from that, we had obtained from friendly countries during the current tenure of the Second Five-Year Plan about Rs. 826 crores of assistance committed although it may not have been actually used. We started the Second Five-Year Plan with a **carry-forward** of Rs. 108 crores in terms of foreign assistance which we were granted during the First Five-Year Plan, but which had remained unutilized till April 1956. That means that we had in all foreign assistance of **Rs. 934** crores including a carry-forward of Rs. 108 crores.

The genesis of the trouble lies in that there were very serious miscalculations and terrific under-estimates of the requirements of the foreign exchange resources to attain the targets which were laid down in the Second Five-Year Plan. Added to this, difficulties arose owing to the Suez crisis, rise in prices, increased freight and accelerated deliveries of certain capital goods which came in earlier than anticipated. All these combined together to land us into a perfect mess that we are in today.

I do not know if it is generally known to the public of India that from 1955 onwards the Commerce and Industry Ministry embarked on a lively spree of issuing import licences which aggregated to a figure of nearly Rs. 2,000 crores. I am unable to understand one charge which has been laid at the door of the Private Sector; and I am really surprised that a man of the knowledge and calibre of Mr. C. D. Deshmukh should have thought fit to repeat that charge in his recent statement. The charge is that our exchange difficulties, if not due entirely to the machinations of the **Private Sector**, were very largely aggravated by one sin

which the Private Sector committed, viz., their, to use Mr. Deshmukh's words, "intelligent anticipation" of exchange difficulty which the country was going to be confronted with and, therefore, they applied for and got licences for substantial amounts for import of capital goods and machinery from the Government. Those who prefer to make this charge forget the elementary fact of economic life in India today that without the previous consent and approval of the Government nobody is in a position to import any capital goods or machinery. Under the Industrial Control Act, in the first place, you have to **obtain** a licence which, through an elaborate procedure, goes to various Ministries. It is only when it is finally approved that anybody is in a position to order goods from abroad, receive them here and get the necessary exchange from Reserve Bank. Be that as it may, it is a solid fact that by this reckless and extravagant issue of licences from 1955 onwards, without any reference to the available resources and India's credit position to obtain potential resources, we have been landed into a situation where we are almost on the brink of international insolvency. It is a problem which has unfortunately not yet aroused sufficient interest throughout the country. The only good augury is that the incomprehensible complacency on the part of the authorities till recently is being replaced in the last few weeks by a greater awareness of what actually the country is going through. This lively awareness is evidenced by the representatives of the Finance Ministry going throughout the country and telling us that we have been faced with a crisis! Eighteen months ago, when some of us dared to tell the country that we were soon going to be faced with a man-made crisis, we were denounced as panic-mongers, if not unpatriotic. However, it is a happy augury that, even late though it is in the day, the authorities have fully realised the gravity of the situation and are straining their nerves to meet it:

There are various ways of meeting the situation.

The **situation** is very difficult; it is almost desperate. When you realise that we have still a little over Rs. 500 crores of commitments to meet before the end of the Second Five-Year Plan, that we have **Rs.** 200 crores lying with the Reserve Bank, and unless we are going to bargain for a situation where there will be no working funds left with the Reserve Bank for a country of this size, we must at least obtain Rs. **350** crores in the next two years.

One remedy which has been suggested in certain quarters is the devaluation of the Rupee. I for one am **not** yet convinced that it would be in the interest of the country in the context of the present situation to devalue the Rupee. At the same time, I must sound a note of warning that dogmatism on this issue is not going to help us to solve the situation. Whilst devaluation immediately will not be in the interest of the country, if the present adverse **balance** of payments position continues for a long period, it would be sheer folly to say today that devaluation can be ruled out for all time.

The other remedies are obvious remedies, and I am glad that the Government has started applying the brake, in a rather drastic way, to imports. Imports have been severely cut and very probably they may have to be cut still further by the end of the year. But restriction of imports is a double-edged weapon. It causes very serious repercussions on the economy of the country. One very bright feature in our economy for the last many years has been the increase in the tempo of industrial production. During the last few months, the tempo is gradually **slowing** down. And the full cumulative effect of restriction of imports will certainly lead to a further curtailment of the utilization of the installed industrial capacity of the country. Apart from other facts, a severe curtailment of imports will also lead to serious unemployment. If import houses which had licences of about Rs. **10 lakhs** twelve months ago are asked to work on a basis of an annual licence of Rs. 50,000, it is not business and, therefore, those

**import** houses must close down. So, one important **im-**plication of the restriction of imports, very highly justified though it is in the context of the situation, is that it must inevitably **affect** our development programmes by the reduction in the pace of industrial production.

The second remedy is to augment our exports. This reminds one of an old Gujarati proverb that when the house is on fire, we start digging a well. Exports, of course, must be increased; and every effort must be made **to** promote our exports. But here also one element\* fact which is being ignored by our authorities who have been terribly enthusiastic about promoting exports is that, as a result of the cumulative effect of various forces, **parti-**cularly of labour legislation in this country, India has become, by and large, a high-cost-producer. And, therefore, in most of the important commodities India is priced out today from world markets. Unfortunately, the level

of exports during the last six months has been considerably lower than what we had in the comparative period last year. If you consider the possibility of our exporting sugar, cement or some of the engineering products, you are immediately faced with the problem that our costs are absolutely out of parity with the prices obtainable in the world markets for these products. In a recent announcement, the Government said that it would be exporting 50,000 tons of sugar in the world markets.. I have discussed the problem with people who know something about sugar and they tell me that **50,000** tons of sugar which according to Indian prices is worth about Rs. **5½** crores will fetch in the world market today not more than **Rs. 3½** crores. Similarly with cement. Allowing for the heavy freight, export of cement from India to markets like East Africa and others is ruled out except at a substantial loss. So, India **having** become a high-cost producer, the possibilities of augmenting our exports to any substantial extent is only a hope not for the immediate future but over a long period of time.

What else are we left with? We are left **with** the sole hope of going to our friends abroad, explaining our situation to them, **and** asking for further assistance. There are, however, certain remedies which are also **within** our scope; but these remedies are only possible if we are prepared to shed our doctrinaire approach and **some** of our ideologies. If an effective approach is to be made to the friendly countries of the world, those countries, however kind and generous they may have been to us **in** the recent past, would certainly expect some things to happen in this country to give them a sort of an assurance that though things have gone wrong they will improve, and in future India will get on an even keel.

I am, therefore, suggesting two or three things which will enable us to approach countries abroad with a plea which may not fail. One such suggestion is bound to raise some controversy in the country. Although it would be futile to say that since Independence we have not made progress, that we have not many achievements to our credit, the two features on which we have failed—miserably failed—are the Food front and the Exchange position. Since we attained Independence, we have, spent as much as **Rs. 1,360** crores in purchasing the marginal supply of food. Out of this amount, fortunately due to the generous assistance of the U.S. Government, and some of the Colombo Plan countries, **Rs. 340 to 350** crores were paid for **through** their assistance. But we had a net draught on our foreign resources to the extent of **Rs. 1,000** crores in making food available to our growing population. Unless, therefore, the Government is prepared to take some energetic measures to ensure that at least in the years to come we may not be put to the necessity of using **up** our scarce and valuable foreign exchange resources in **purchasing** food, any plea that we may put forth to friendly countries would not be as effective as otherwise.

Secondly, although it is true that the present Government represents the vast majority of the voters in this

country, I believe a situation has arisen where if we want to make a real and effective impression abroad, the **Gov-**ernment of India ought to be more broad-based and not confined only to one political party. A situation has arisen where we want to pool all the available resources in the country and mainly the brain resources of the country. And, therefore, I feel that all the progressive elements in the country, whether they put on **Khaddar** or not, should be incorporated into a broad-based Government, which would make a better and more effective appeal to the countries abroad than the present Government **could** do.

I also believe that so far as mobilising our internal resources is concerned, we have not done everything that could be done or at least attempted on a large scale. India for many centuries has been known as the sink of precious metals. Although it is not possible to make a very accurate estimate of gold holdings in this country, I think it would not be very unsafe to surmise that India can claim today to possess at the internal prices something like **Rs. 3,000 to 3,500** crores worth of gold. I am fully conscious of the fact that a large part of this gold is not held in ingots, but must be held in the form of ornaments spread over millions of people over the country. But the Foreign Exchange situation is of such an imperative character that if we want to make an impression abroad, we should at least be in a position to tell them that we **have** made an earnest attempt to mobilise the gold resources of our country. I **have** had opportunities of discussing this problem recently with some highly placed people, and I have emphasised that a mere appeal will not produce results. A similar appeal was made some **years** ago, and it produced a few pairs of earrings and about a dozen gold rings. You have to take account of human nature and its weaknesses. And if an all-out, country-wide effort was made, and an offer was made, of course, added with emotional appeal, and if at-

tractive terms were offered to the holders of gold, I am not without hope that the attempt will succeed in producing substantial results. We have before us the experience of the French Government. On the model of French experience, if a proper scheme was drawn up, under which gold could be attracted, in the form of a 15 to 20 years' loan, repayable at such a price which would have relation to the price of gold at the time of repayment compared to the present price of gold, so that the holder of gold may have the assurance that the money which is returned to him by the Government at the time of repayment will put him in a position to replace the gold he has temporarily parted with, he would be better inclined to part with his gold. Here one important aspect of ideological approach creeps in. Under the French scheme, they decided to waive the penalty for anybody who had not previously disclosed his gold holding, and who under the French Law was subject to a penalty of 25% of the value of the gold. If a similar assurance was given to the holders of gold here that for non-disclosure of their gold holdings in the past they will not be penalised and further, that this loan will be free not only from income-tax, but also from estate duty, I think that there is a reasonable ground for believing that a substantial amount of gold lying inert today can be mobilised to the great use of the country in its present emergency. But I must repeat the warning that in order to put the Government in a position to expect a substantial response to the country-wide all-out efforts, all sections of the community in the country have to get together. And in order to make that possible, the first reservation to which I referred has to be fulfilled, viz., that the Government has to be sufficiently broad-based to ensure the co-operation of all progressive elements in the country who could all go on one platform and make their earnest attempt to persuade people to part with their gold to enable India to meet an emergency which I do not think throughout its history-it has ever been faced-with.

Based on a Speech by Mr. A. D. Shroff at the Rotary Club, Bombav, on July 29, 1958.

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