INDIA'S BALANCE OF PAYMENTS PROBLEM

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"Free Enterprise was born with man and shall survive as long as man survives."

— A. D. Shroff
1899-1965
Founder-President
Forum of Free Enterprise

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By

JIBAN K. MUKHOPADHYAY*

I. PROLOGUE

India's difficult balance of payments (BOP) situation has by and large continued to remain an ongoing phenomenon. Not only during the early phase of India's Five Year Plans but also after almost four decades of our planning experience, the overall BOP position has continued to remain under strain.

The current BOP situation is rather grim and is being widely discussed at various official and non-official reports. Ministers and senior government officials describe it to be "very difficult", while at the same time they pronounce their ritual "pledge" to resolve the problem. International Monetary Fund (IMF) have been tirelessly warning us about the serious consequences of the difficult BOP situation and offering their very own suggestions to reform the economy. Various experts and analysts "foresee" that India is in danger of getting caught in an "external debt trap". Newspapers and magazines regularly carry screaming headlines on the "worsening of India's foreign trade deficit" or the impending danger of our "foreign exchange crisis".

Amidst these animated discussions, which at times travel from one extreme to the other, reality often becomes a victim. It is therefore important to understand this perpetually difficult BOP situation in an objective and dispassionate manner.

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* The author is an Economist attached to Tata Services Ltd. The views expressed in the booklet are his personal and not those of the Company..

Balance of Payments Defined: Before proceeding further, it is necessary to keep in mind the definitions of terms generally used in connection with the BOP. The overall BOP of a country is reflected in what is called its net 'current account' which is made up of (i) visible trade in merchandise (i.e. foreign trade deficit or surplus) and (ii) invisible trade (i.e. excess or shortfall of income from services such as banking, insurance, tourism, transportation, investment etc. over expenditure on similar services). A surplus on the current account indicates the net amount a country has earned in its external transactions, as a deficit is a measure of the amount the country has spent in excess of its earnings from international transactions.

When we talk about balance of payments problem or the foreign exchange shortage or "crisis" (the latter in fact reflects the strain on the overall BOP situation), one should usually refer to the current account deficit, which is a more wholistic concept and not just the trade deficit alone, which is a part of the whole. We have experienced in the past that the high trade deficit may also to some extent get neutralised by the net invisible receipts.

II THE BACKGROUND: THE INWARD-LOOKING POLICY

A vast developing country like India, or for that matter any country, has to import various goods and services for the ongoing demands and aspirations of its economic development. It also needs to export certain goods and services, which it can produce based on its given resource endowments and comparative advantage, to pay for its imports as well as repayment of external debt. External borrowing is needed mainly because of the shortage of foreign exchange resources, caused primarily due to a gap between the high expenditure on imports and the low earning from exports of goods and services.

In retrospect, it appears that a highly inward-looking and one-sided external trade policy was adopted at the time of the inception of our Five Year Plans and allowed to be continued for long. The cornerstone of this inward-looking external trade policy was the strategy of import substitution, adopted with the noble objective of attaining self-reliance of the economy. In the process, export as a dynamic sector was, until recently, virtually ignored and external trade policy was made equivalent to a very protective, rigid and regimented import policy. With higher imports, necessitated by the growing economic development programmes, and lacklusture performance of exports, India merrily continued to borrow from international financial institutions like the World Bank. For example, a large portion of the International Development Assistance (IDA) fund of the W.B. was made available to India at a nominal service charge of 0.75% plus a commitment fee of 0.5% and with a long maturity period as high as 35 years. A total assistance of about US $24 billion (bn) was made available to India from 1951-52 to 1986-87; out of which IDA funds, coming in since 1961, was as high as 58%. This type of concessional external assistance helped us to get foreign exchange resources for our development programmes. This soft option at the same time made us very complacent with respect to exports. We did not feel the urge to adopt the hard option of increasing exports. It would have been easier to increase our exports in the 1960s when the world economy in general and the economies of the developed countries in particular experienced high rate of growth. But we missed the bus.

The external trade policy during First Five Year Plan (1951-52 to 1955-56) was made under the comfortable influence of the accumulated surplus sterling balance and there was no great worry for meeting the foreign exchange needs of the Plan.

The formulation of the Second Five Year Plan (1956-57 to 1960-61) was dominated by an overwhelming "export pessimism". The planners in their wisdom thought that significant foreign exchange earnings from exports were not possible in the short run, since there were not too many items, apart from tea, jute and cotton piece goods, to be pushed in the world market. As such, the opportunity of adopting a dynamic external trade policy was abandoned. The Second Five Year Plan document declared, albeit with good intentions, that

"while every effort has to be made to promote exports of new items and to develop and diversify the markets for the country's major exports".

But instead of formulating an aggressive export policy, it merely hoped that

"...it is only after industrialisation has proceeded some way that increased production at home will be reflected in larger export earnings".

The hope, needless to say, was not materialised. We have continued with a policy of import-substitution in basic intermediates and capital goods sectors for attaining the objective of self-reliance. In doing so we were loaded with inefficient and economically non-viable projects in several cases, which, ironically, were also highly import-intensive.

Subsequently, during the Third and Fourth Five Year Plan periods (1961-62 to 1965-66 and 1969-70 to 1973-74 respectively) some recognition had to be given to increased export earnings for financing growing imports and debt repayment obligations. Some export promotion measures were announced in a stop-go and piecemeal fashion for increasing exports. However, this emphasis on exports was mainly in the nature of corrective measures. It was not a decided shift of policy in favour of a strategically aggressive export drive.

The Fifth Five Year Plan (1974-75 to 1978-79, terminated in 1977-78) made a feeble attempt towards expansion of exports of some manufacturers like engineering goods, garments, leather goods, marine products etc.

More or less the similar trend of ignoring the exports sector continued during Sixth Five Year Plan (1980-81 to 1984-85), with relatively more emphasis on "efficient" and not just any, import-substitution strategy.

The early years of the Sixth Plan were the period of the post second oil shock (in 1979-80), the impact of which was more severe than that of the first oil shock. This provided a cushion to our balance of payments problem. The foreign exchange reserves increased and Government was at a loss about how to utilise it since rupee resources were so scarce for converting these foreign exchange resources!

However, immediately after the second oil shock India's balance of payments position sharply deteriorated. This was mainly due to higher oil import bill and very slow incremental growth in our narrow-based exports. The current account deficit rose ten fold within two years from Rs.234 crores in 1979-80 to Rs.2,317 crores in 1981-82, the second year of the Sixth Plan. To meet this critical balance of payments situation India had to approach the International Monetary Fund (IMF) and obtained Rs.274 crores under the Compensatory Financing Facility, Rs.545 crores from the IMF Trust Fund in 1980-81 and also negotiated an Extended Fund Facility (EFF) to the tune of SDR 5 bn. in November 1981, of which SDR 3.9 bn. was finally utilised as balance of payments position started improving to some extent from 1982-83.

The inflow of foreign exchange support from the IMF and increased crude oil production from the Bombay High, which became economically viable because of higher oil price, helped the balance of payments position to some extent. Total crude oil production of India increased by almost 2.5 times from 10.5 million tonnes in 1980-81 to 25 million tonnes in 1983-84, causing a reduction in oil imports. Yet the volume of exports during the Sixth Plan increased by a mere 3% per year against the plan target of 9% while the relatively higher growth in imports including contingency imports was required for the economy. Despite the on-going emphasis on import-substitution, the very low growth in exports reflected a lack of serious export promotion strategy.

Under the circumstances, the need for increasing exports in a more dynamic way to pay for growing imports and debt repayment obligation was emphasised in the Seventh Five Year Plan (1985-86 to 1989-90). For attaining the objective of higher growth in exports several export promotion measures were introduced for the first time in a serious way.

The external trade policy thus was highly inward-looking. No wonder that India featured in the category of "Strongly Inward Oriented" countries in a study of 41 developing member countries of the World Bank during 1963-85.

India's export performance suffered during this period due to lack of suitable promotional policy to such an extent that our balance of payments position remained almost persistently vulnerable. Neither the strategy of import substitution could help the situation by substantial reduction in imports over the years, nor the reliance on the proposed development strategy of basic, heavy and capital goods industries of the Second Plan helped realise the objective of the desired growth of export diversification and competitiveness in the latter years. The external trade policy remained tucked to rigid import restrictive policy for the sake of socalled self-reliance via protection and import-substitution.

Besides, though the country adopted a highly centralised planning system, yet in determining the target of national economic growth rates of any of our plans, no interlinking or integration was made with respect to the growth of exports. That is to say, if we are supposed to achieve a particular annual rate of growth of our GNP in a particular plan, it was not determined how much of this growth should come from exports. Target setting for exports were separately, perhaps artificially done. Exports were treated as a residual sector.

Sharp Fall in India's Share in World Exports: It is no wonder therefore that the plight of India's external sector looks frustrating when compared with some other late coming Asian Countries. They followed a "Strongly Outward Oriented" policy during 1963-85. The Four Tigers (South Korea, Hong Kong, Singapore and Taiwan) have pursued an aggressive export-led policy and managed to make a massive penetration in the world market. The share of the Four Tigers in the world exports spectacularly increased from little over 2% in 1971 to 7.2% in 1987. Of late China has also made its presence felt very spectacularly in the world export market; its share moved up from 0.7% in 1971 to 1.6% of world exports in 1987.

As against this, India's share in the world exports steadily declined from almost 3% in 1938 to 1.1% in 1960, to 0.7% in 1970, and further to 0.54% in 1975 and remained stagnant at the level of less than 0.5% during the eight years.

Growth-Led Policy of Exports: While on this, I must hasten to add that I do not imply by this comparative performance statistics that India should have adopted, or should adopt in the foreseeable future, an aggressive policy of "export-led" growth of the type followed by the Four Tigers. For a vast poor and unemployment ridden country like India it is neither possible, nor it is desirable to adopt a policy of export-led growth. But certainly the growth in exports should have progressively supplemented the national economic growth. Unfortunately, that did not happen. India's exports remained stagnant at the level of around 5% of GNP for almost a decade as against 35% (in recent years) for South Korea. If our exports could double within the next five years to raise its share of GNP to 10%, our share in the world exports may be just one per cent. Achieving this objective will be no easy task. The point here is that even with the 10% share in GNP, exports will certainly not "lead" our economic growth.

However, on this issue I am generally in agreement with what the Abid Hussain Committee (1985) had very sensibly suggested:

"In an economy such as India, the route to a quantum jump in exports, which is now necessary to attain the objective of self-reliance, lies in growth-led exports. Therefore production for export must constitute an integral part of domestic production. As this integration would take some time to materialise, in the interim, we are suggesting a regime on export promotion policies which would overcome the constraints on export performance." (Emphasis added).

III. RECENT CHANGES: PRAGMATIC LIBERALISATION

The Liberalisation of Import Policy: The flag-ship of the inward-looking foreign trade policy of India was in fact the restricted import control policy, which was devised for conserving foreign exchange, promoting import substitution and providing protection to indigenous industry.

The import control policy was perhaps most stringent during the Second Plan period because of acute foreign exchange crisis. This, more or less, continued till 1974-75. Although import restriction may help conserve foreign exchange in the short run, it has been experienced that they hurt the long term growth of exports and foreign exchange earnings. Understanding of this reality has at last led to the liberalisation of the import policy.

For the first time, the procedural rigidities of the import policy was liberalised to some extent in 1975-76 following an improvement in the foreign exchange position, thanks to increased remittances from Indian workers mainly from the Middle East. Then, the Janta Government not only continued with the liberal imports policy, but also cleared quite a few cob-webs of controls and regulations particularly in 1978-79, which more or less continued till the early 1980s. This trend of liberalisation, indeed very desirable as it was, even more vigorously continued in the import policies for 1985-88 as well as 1988-91. The main objectives of the latest import policy (1988-91) have been stated to be: to stimulate industrial growth and promote exports by providing easy access to essential imported capital goods, raw materials and components so as to help modernisation, technology upgradation and making industry progressively competitive. The policy also aimed at promoting efficient import-substitution, self-reliance and further rationalisation and simplification of procedural matter.

There also have been some concern about increasing imports in the face of the country's difficult balance of payments position. It may be mentioned in this connection that imports will increase along with the higher growth of industrial production and overall economy. An expert calculation suggests that for one per cent real growth of Indian economy, about 1.5% real growth in imports is required. This implies that despite long years of emphasis on import-substitution, Indian economy still remains considerably import-dependent. As such, the increase in imports are largely because of the growing needs of the economy for domestic production and exports. Any abrupt reduction in developmental imports will certainly disrupt the national economy.

Finally, it needs to be appreciated that whatever "liberalisation" has been introduced in the imports policy was so far in the nature of procedural de-bottlenecking alone. The policy has not been "liberalised" in the right sense of the term. A large number of consumer goods are banned from imports (vide Schedule I of the Import Control Order, 1955). Besides, heavy customs duties are imposed on large number of items whose import procedure has been liberalised. The total earnings of Government from customs duties has been estimated to be as high as Rs.17,880 crores, or 35% of total tax revenue in 1989-90 (budget estimate).

Dr. Abid Hussain has eloquently discussed this point, which the critics of the liberal import policy may just consider:

"India today probably has the most highly protective trade regime among major trading nations in the world, with a mean nominal tariff of over 120 per cent (after accounting for major exemptions) as compared with about 90 per cent for China, Bangladesh and Pakistan and between 20 to 40 per cent in most other countries..."

The Export Promotion Strategy: That the export earning should finance a larger and larger proportion of our imports and debt repayment obligations was at last realised during the mid 1980s. The Abid Hussain Committee, to which a reference has already been made, and several other expert bodies and representations from trade and industry made signal contribution towards the consolidation of this perception. The prospect of increasing debt service burden from the middle of 1980s, particularly because of bunching of IMF repayment schedule coupled with not so very rosy prospect for net concessional foreign assistance also have prompted the drive towards export promotion. Finally, since the mid-1980s a multifaceted package of export-promotion measures have been adopted as a high priority strategy for augmenting foreign exchange resources.

A host of measures in the area of licensing, fiscal as well as supply and reinforcement of infrastructure facilities have been introduced for building and sustaining a dynamic export effort. For example, action plans on 14 thrust commodities of exports have been prepared, Cash Compensatory Scheme (CCS) and Duty Drawback Scheme have been extended and streamlined for hundreds of items, a MODVAT Scheme has been introduced for minimising incidence on imports on a number of items, 100% exemption of export profit under section 80 HHC of income-tax has been announced, concessional customs duties have been allowed for major export thrust industries, export credit has been eased etc. Exchange rate of the rupee also has been, and is being, appropriately adjusted downwards vis-a-vis major foreign currency. All this has already created a favourable environment for ushering in the era of positive exports culture. Responses from trade and industry also have been warm. The Reserve Bank of India and the leading commercial banks also have come forward to help the exporters.

IV. CURRENT BOP SITUATION: DIFFICULT, BUT NOT CRITICAL

Thanks to the pragmatic and liberal policies, streaks of silver linings seem to have appeared on the horizon. The question now is whether it will be sustained, grow and blossom into prosperity making India resolve its chronic BOP difficulty by earning more foreign exchange resources from the export of goods and services so as to pay for the required imports and meet heavy debt repayment obligations.

Bright Spots in Merchandise Trade: India's exports increased by about 29% to Rs.20,281 crores in 1988-89 (15.5% in terms of US dollar), 26.4% in 1987-88 and 14.3% in 1986-87. The average rate of growth in exports in the last three years comes to 23% in terms of rupee value. The real rate of growth measured in terms of volume has been high at about 12% per year on an average during this three year period. This is spectacularly high when compared with the rate of growth in the years prior to 1986-87.

Imports in 1988-89 increased by almost 24% to Rs.27,693 crores (11% in terms of US dollar) from about 11% growth in 1987-88 and 3% in 1986-87. The average rate of growth in imports during these three years has been 12.4% per year. As a result of lower growth in imports, the ratio of exports and imports improved from 55% in 1985-86 to 73% in 1988-89.

The deficit trade balance recorded Rs.7,412 crores in 1988-89 as against the projection of Rs.9,500 to Rs.10,000 crores made by several experts/institutions. The trade deficit in 1987-88 was Rs.6,658 (Rs.754 crores higher than the figure of 1988-89), Rs.7,749 crores in 1986-87 and a very high figure of Rs.8,763 crores in 1985-86. In terms of US dollars the growth in trade deficit in 1988-89 over 1987-88 was very marginal, only 0.2%, and in terms of SDR it in fact declined by 0.5%. As a percentage of GNP also it is about 1.9% in 1988-89, declined from a high 3.4% in 1985-86, 2.7% in 1986-87 and 2% in 1987-88.

Some other encouraging factors of India's emerging exports are:

(i) the share of exports in GNP has increased from 4.7% in 1985-86 to 6.1% in 1988-89.

(ii) the share of manufacturing exports has increased from 69% in 1985-86 to 79% in 1988-89.

(iii) the growth of exports is contributed in the recent years by a group of items [e.g. gems and jewellery, textiles (garments and cotton fabrics), engineering goods, chemicals, leather and marine products] compared with the past experience when growth in exports was largely contributed by one or two items e.g. crude oil in 1983-84 and 1984-85.

(iv) the ongoing devaluation of the rupee vis-a-vis US dollar and other hard currencies together with export promotion measures have helped the growth of exports, while the former has also added to the cost of imports; hence is the need for reduction in "avoidable" imports like some items of steel and metals etc. for which sufficient capacities have already been created and edible oils. Some items like fertilizers and cement have already gone out of the list of bulk imports. Capital goods imports have increased in 1986-87 and 1987-88, but its rate of growth has come down in 1988-89.

In the area of imports, the relatively high growth in 1988-89 as was largely contributed by certain essential bulk imports like edible oils, food-grains, pulses etc. totalling about Rs.2,000 crores necessitated because of the drought in 1987. The import of crude oil and petroleum products was also high at 25 million tonnes in 1988-89 as against 22.6 million tonnes in 1987-88. The price of crude oil in 1988-89 was also slightly higher than it was in the previous year. This will be even higher in 1988-89 since the domestic production of crude oil has been stagnating and consumption increasing. Therefore, the growth in imports should not be contributed to procedural liberalisation of the import policy as it is often done by the committed critics of liberalisation policy.

Being encouraged by the spectacular growth in exports in recent years, Ministry of Commerce is likely to fix a target of exports in the range of Rs.27,000 crores to Rs.30,000 crores (an increase of 33% to 48% over 1988-89) for the year 1989-90. A 15% real rate of growth of exports per year may be set up during the Eighth Plan period. Some industry spokesmen think that a target of about 100% increase in exports in 1989-90 over 1988-89 should be possible, if better infrastructure facilities like power, transport, telecommunications facilities etc. are provided and smooth implementation of liberalisation policies are carried out. This optimism of the Indian exporters may appear to be high, but it certainly symbolises a spectacular and encouraging growth of export culture. There is also now a better government industry interface as regards exports for earning foreign exchange.

A Challenging Task: Though all these are very encouraging bright spots, for sustaining a dynamic and gainful growth in exports in the medium and long terms a further liberalisation towards reconstruction of the Indian economy will be urgently required so as to make our exports competitive in terms of price and quality. The need for increasing export-competitiveness has become more urgent also because of growing protectionist policies in developed countries as reflected (i) in the recent "naming" of India by the USA under the clauses "Super 301" and "Special 301" of the omnibus US Trade Act, 1988 and (ii) the prospect of an integrated Europe by 1992. The United Europe may eventually turn into a "Fortress Europe", which may create added difficulty for exports from the third world countries like India.

Disquieting Trends in Invisible Receipts: In the area of invisibles, the remittances from Indian workers abroad reached a high figure of Rs.2,800 crores in 1985-86. In the following years it marginally declined. However, the remittances receipt marginally increased in 1987-88, perhaps to an estimated figure of Rs.2,500 crores. In 1988-89, these remittances are likely to remain more or less the same.

As regards tourists arrival, although there was a modest increase of 7.2% in 1988 over 1987 (assuming all tourists including those from Bangladesh, Pakistan etc.) as against 2.3% increase in 1987, there was a significant fall in tourist arrivals from high spending US and Western European countries. The actual foreign exchange earning figure for 1988-89 is not available. The previously "anticipated figure" of Rs.2,103 crores (11.3% increase over 1987-88) is still being used in official sources for 1988-89.

Tourism in India has high potentiality not only to earn net foreign exchange resources since its import content is very small as compared with merchandise exports but also to provide employment as it is highly labour-intensive. Though a beginning has been made to exploit its potentiality, but it has to go a long way.

The overall net invisibles receipt was Rs.4,311 crores in 1980-81, a very high increase from Rs.(-)27 crores in 1970-71. It declined to Rs.3,630 crores in 1985-86 and further to Rs.3,524 crores in 1986-87, the latest year for which the data is available. Net invisible receipts financed only 36% of our trade deficit in 1987-88, 38% in 1986-87 as compared with 57% in 1984-85 and as much as 72% in 1980-81. However, based on our emerging exports, somewhat better prospect for higher foreign exchange earnings from project and consultancy exports and private remittances in the wake of the restoration of construction activities in the Gulf after the cessation of Iran-Iraq war as well as in other developing countries where India's technological competence has relevance; better prospect for tourism etc., a recent study has visualised Rs.10,000 crores worth of net invisible receipts by 1994-95.

Repayment of External Debt: According to Government, the total debt on medium and long term loans was Rs.55,000 crores at the end of 1987-88. But according to the Institute of International Finance (IIF) it was around Rs.75,000 crores. This figure is higher because of the inclusion of both short term loans and non-resident Indian (NRI) deposits in foreign currencies in Indian banks. While calculating total debts, Government more or less follows the World Bank practice where the NRI deposits are excluded. According to Government's calculation the debt service ratio, expressed in terms of our current foreign exchange earnings (i.e. merchandise exports plus earnings from invisibles) increased from 12.1% in 1984-85 to 24% in 1987-88 and to around 26% in 1988-89, (30% according to the IIF), largely due to bunching of repayments to the IMF.

Total debt servicing (repayment and interest) has increased steadily from Rs.2,422 crores in 1984-85 to Rs.5,950 crores in 1987-88 and further to the peak of Rs.6,900 crores in 1988-89 before falling since 1989-90. This was because the repayment to the IMF has already reached its peak in 1988-89 and would fall in 1989-90 onwards. Therefore, it is likely that the debt service ratio also should gradually fall.

This implies that an external debt-trap is not in close sight. However, we may walk into it because of our traditional habit of over consumption, say, utilisation of foreign exchange resources in projects not requiring any foreign exchange at all (e.g. municipal projects, road building etc.)'

The Current Account: The overall current deficit increased in 1987-88 by 7.9% to Rs.6,293 crores against Rs.5,830 crores in 1989-90. It has been tentatively estimated to be around Rs.7,500 crores. But the current account balance as share of GNP has been mercifully on the decline viz., 2.3% in 1986-87, 2% In 1987-88 and about 1.9% in both 1987-88 and 1988-89.

Foreign Exchange Reserves: Reflecting the strain on the overall balance of payments situation, foreign exchange reserves (excluding gold and SDRs) came down to Rs.6,610 crores as on end March, 1989 providing import cover for 2.9 months compared with Rs.7,290 crores at the end of March 1988, providing 3.9 months of import cover. The position is likely to improve in 1989-90 as the rate of growth in imports are likely to go down and rate of growth in exports are likely to go up. Exports have already increased by a spectacular 38% in April-May 1989 over April-May 1988 and imports by 17%. This is a very hopeful sign, though only time will tell whether these rates will be maintained.

The large inflow of NRI deposits with Indian banks provided considerable cushion to our balance of payments. From just over Rs.1,000 crores at the end of 1980-81, these deposits have grown phenomenally to Rs.13,000 crores at end Dec. 1988. It must be noted, however, that even as these deposits lend support to our foreign exchange reserves, technically speaking they constitute India's liabilities in as much they are repatriable on demand.

External Assistance: The gap in our BOP as reflected in the net current account deficit needs to be covered. We have been habitually trying to bridge our external account by taking recourse to external assistance, foreign debt in popular parlance.

The Aid India consortium has recently pledged \$6.7 billion for 1989-90, a marginal increase of 6.3% from \$6.3 billion pledged in 1988-89, and \$5.4 billion committed in 1987-88. Out of this, the concessional aid (i.e. IDA and certain other small credits from various world bodies) constituted 60% in 1989-90, 62% in 1988-89 and 61% in 1987-88. These figures imply that the concessional aid components have been stagnating in the recent years. Gone are those socalled happy days when India used to enjoy about 40% of the total IDA funds until the early 1980s. Presently about 30% of the IDA funds are shared between India and China.

Besides, our receipt of foreign aid in the total inflow of foreign resources declined from 96.4% in 1980-81 to 43% in 1985-86, but fortunately increased to 76.1% in 1987-88. Mercifully, there is also a massive amount of unutilised aid of about Rs.28,000 crores as on March 1989. Plans for speedy utilisation of this amount will also help the flow of foreign funds.

Due to the recent drying up of concessional assistance, India has been compelled to borrow more from foreign commercial banks, who are only too eager to lend money to India, for bridging the uncovered gap in our BOP. India's credit worthiness has remained very high and there never was any default in the past. Approvals for these borrowings therefore have increased to Rs.2,654 crores in 1987-88 (Rs.1,700 crores in 1985-86 and Rs.1,396 crores in 1986-87) and are likely to go further up in 1989-90. Funds are being raised in foreign currencies like the Yen, DM and Swiss Franc.

There is nothing wrong in raising finances abroad particularly because these are known to have been obtained on terms more favourable than what the domestic market could have offered. The risk with the borrowings from abroad is that the liability of the Indian borrower keeps going up with the steady depreciation of the rupee vis-a-vis international currencies.

But continuous dependence on either concessional or any other type of borrowing do not represent a healthy state of economy which is living beyond its own means. Incidentally, the same is more devastatingly true for the internal borrowing, which has gone upto an astronomical figure of Rs.2.4 lakh crore as on end March 1989-90 for which Rs.17,000 crores are to be paid as interest in 1989-90 alone! Unless radical steps are urgently taken in the fiscal areas the "internal debt trap" (i.e. a situation may soon arise when the interest burden alone in any given year may exceed all new loans incurred in that year) is a more probable danger than the external debt trap. The two problems however are inter-linked and reflect the adoption of the perverse philosophy of the ancient Indian sage, Charvaka.

The issue of going again to the IMF for any of its various "repurchase" (i.e. borrowing) facilities also needs a mention. There is technically nothing wrong in going to the IMF under rare and pressing circumstances and not habitually. Besides, going to the IMF creates a strong resentment because of the IMF conditionalities which are looked upon as infringement of national sovereignty. We have already utilised many repurchase facilities of the IMF in the past as already mentioned before. Going again to the IMF will not indicate prudent management of the economy. And then, if we are to borrow more heavily in the future from the foreign commercial banks to repay these new IMF and/or other debt obligations, it will not be at all a desirable situation.

It can be reasonably hoped that a "critical situation like the above will be averted particularly because of our emerging exports and other foreign exchange earnings from invisibles, moderately increasing foreign direct investment including NRI direct investment (NRI bonds however are yet to receive great response), rapidly growing NRI deposits, the scope for speedier utilisation of unutilised foreign aid as well as by taking recourse to limiting "avoidable imports".

V. EPILOGUE

The prime support to our balance of payments problems therefore has to come from exports. However, for a dynamic, gainful and sustained growth in exports, an imaginative export policy needs to be evolved as an integral part of our economic planning system. While the degree of economic liberalisation needs to be accelerated with its implementations made more effective and smooth for increasing competition, export promotion strategy will have to be continued in a more straight forward and simplified manner to provide a more useful and strategic support to our export drive in the medium term. A long term policy for increasing foreign exchange earnings from invisibles like tourism also will be required. At the same time, the efficient import substitution needs to be carried out in right earnest in such areas, where it is economically viable. Further encouragement to foreign direct investment also needs to be carefully examined.

Among the major factors which raise our cost of production are high taxes and levies and periodic increases in administered prices of products of which the public sector units are virtually monopoly producers. The responsibility of restraining cost escalations thus rest to a large extent on the Government and their corporations. In this regard, there is a strong case for the continuation of the liberalisation policy together with privatisation of selected public sector units.

The views expressed in this booklet are not necessarily those of the Forum of Free Enterprise.

"People must come to accept private enterprise not as a necessary evil, but as an affirmative good."

— **Eugene Black**

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