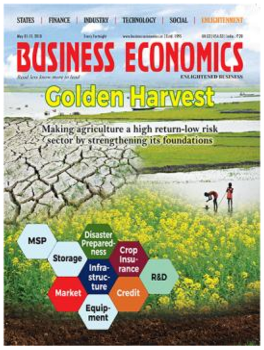

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Deteriorating India's international net investment position

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It is now recognized that trade deficit and current account deficits would widen if the government and the monetary authorities did not give up their stand-off position; and they should do much more beyond offering band-aid solutions. Their efforts to attract more inflows of capital of short term variety have proved futile.

Although India's think tank Niti Aayog's vice chairman Rajiv Kumar made a statement in August that he was not worried about falling rupee but he was more concerned with widening trade deficit, it is now widely obvious that depreciation of Indian currency has made the imports more expensive and exports have not expanded to bridge the current account deficit.

The current account deficit of 1.9% of GDP in fiscal year 2017-18 is likely to be up to 2.8% in 2018-19, which would only intensify further pressure on exchange rate

Declining reserves

The landed value of imports of the petroleum crude has gone up in terms of rupees. The price of oil has always been denominated in US dollar. If the crude oil price goes up in dollar terms we have the effects of two whammies. International reserves are also going down from $ 426 billion, registered as a historical record for India in April, has declined in August to about $399 billion. Of course, there is another reason as well. The Reserve Bank of India (RBI) has also sold dollars to reduce the volatility in encage rate fluctuations, as it does not target any specific level of exchange rate, nominal or real.

About 80% of India's crude requirements are met by imports; the demand is inelastic with respect to price of the crude; and nearly 50% of India's total imports are the crude.

Price of crude is now feared to touch $100 per barrel soon, since Organization of Petroleum Exporting Countries (OPEC) made it clear it would not raise output in the face of a likely shortage. The rise in the oil price beyond $70/barrel is generally considered as a dangerous level. It is estimated that every $10 increase in price in oil would raise trade and current account deficit in the balance of payment accounts by $ 9 billion, which is around 0.3 percent of gross domestic product. If it touches $90/barrel, the current account deficit would reach 3.6% of GDP, which is presently around 2.4% having risen from 1.9% of GDP in March 2018?

Certainly the prediction that the crude price would touch $100/barrel has explosive consequences on Indian economy.

Net International investment position

Can we blame all the ills on oil price and other external factors alone?

How about our own faults? Are they not relevant?

Certainly, there are some policy errors. We made poor judgments. We neglected one major source of external earnings: promoting and diversifying exports. We left to one single source to finance trade and current account deficits in the balance of payments. It was all because India presented an attractive destination for earning higher returns. The private and institutional investors overseas poured in their funds in emerging economies, including India, since the 2008 financial crisis days when the advanced countries kept low rates of interest.

Once the recessionary conditions faded and advanced economies, notably the US, recovered and with normalization of interest and pronouncements by the US Federal Reserve Board indicating that there would be a series of interest rates in 2018, the single source on which India has depended all these years stress on dried up, India was rudely shaken.

Dependency on hot moneys

The single source dependency, the portfolio investment inflows, which are of short time (less than a year) and known to be fickle, lived up to their reputation. The hot moneys are of "easy come and easy go type".

During the good times, their inflows led to appreciation of nominal exchange rate. Now, their outflows have landed the rupee in trouble. The rupee plunged to near Rs 73/dollar mark on September 18.All because of foreigners' poor perceptions of the current Indian economy: Indian inflation touching 5% in June; rising current account deficit; depreciating currency and related risks; and above all, the likelihood of the US interest rate going further up; and India could not be perceived any longer as a safe haven for short term investments.

Furthermore, the boast that our policy makers made that India can handle the situation any time with record level of $426 billion of April ; that the Indian rupee was already overvalued because of past capital inflows and the falling rupee to a natural value is inevitable, gave rise to the impression the trend in falling rupee would continue and the government and monetary authorities would not intervene! There was also an additional boast that Indian exports would now become more attractive with further depreciation and rescue the economy.

Depreciation of the rupee is part of global currency crisis caused by US- China trade war threats, which have now become real as some tariffs imposed by US on Chinese goods have come into effect. Almost all Asian currencies have depreciated, although by not as the same percentage level. Indian exports are not significantly become attractive as the authorities claimed. Our exports are not as diversified as those of China.

Record outflows

In the meanwhile, the outflows of hot moneys have been on the rise. The latest data released by National Securities Depository Limited (NSDL) and duly reported by *Deccan Herald* on September 20, 2018, show the withdrawal by foreign portfolio investors from India's equity and debt markets amounted to Rs 51. 591 crores in nine months (January to September 2018) is the highest. The withdrawal by such enormous outflows is now a record.

The 2008 crisis following the collapse of the Lehman Brothers led to an outflow of Rs 41, 216 crores. Certainly, the current crisis is far more damaging. The fall of the rupee to Rs 72.98 on September 2018 dollar is not surprising. Experts say the rupee may touch Rs 75/dollar by year end.

Net International Investment Position

That brings us to discuss India's international investment position (IIP).

Overseas investors create assets for them in the form of shares, bonds, deposits and physical assets. So too, foreign banks, governments and agencies when lending to India come to acquire assets. They become liabilities for India. Similarly, investments by Indian counterparts by way of equity and loans to foreigners result in creation of assets for the country.

The Table 1 shows the liabilities of India is greater than the assets owned in India by foreigners. The net IIP is the difference between assets and liabilities.

Table 1: India's Net Investment Position (US$ Billion)

Year	Trade	Current A/C	International	Net Investment
	Balance	Balance	Reserves	Position
2000-01	-12.5	-2.7	42.3	NA
2004-05	-33.7	-2.5	141.4	-41.8
2008-09	-119.5	-27.9	252.0	-51.2
2009-10	-118.2	-38.8	279.9	-158.4

2010-11	-127.2	-47.9	304.8	-218.9
2011-12	-189.7	-78.2	294.4	-249.5
2012-13	-195.7	-87.8	292.1	-307.3
2013-14	-147.6	-32.3	304.2	-331.6
2014-15	-144.9	-26.8	341.7	-364.2
2015-16	-130.0	-22.1	360.8	-361.0
2016-17	-112.4	-14.3	370.0	-388.5
2017-18	-160.4	-48.7	424.5	-420.3

The net IIP has been all along negative and is also rising.

Table 2 shows the ratio of assets to liabilities

Table 2 : International Assets and Liabilities ($ billion) and Ratio

	2014-15	**2015-16**	**2016-17**	**2017-18**
Total Assets	522.4	550.3	569.9	632.8
Total Liabilities	887	911.8	958.4	1053.1
FDI	265.4	293.4	342.6	379.4
Portfolio Investment	233.6	225	238.4	272.2
Reserves	341.6	360.2	370	424.5
Net investment position	-364.6	-361.5	-388.5	-420.3
Assets/Liabilities Ratio	0.59	0.60	0.59	0.60

The ratio of assets to liabilities hovers around 60 percent. That is, assets fall short of liabilities.

We know the reasons. The whimsical and unreliable hot moneys cannot be depended upon.

The only solid way open to India is promotion of exports. Dr Arvind Panagariya, a former vice chairman of Niti Aayog made a suggestion two months ago That was for setting up a task force for devising ways and strategies for promoting exports. His suggestion is timely and it deserves all consideration.

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