Chapter-2

A Theoretical Overview:

Indian Economy, Globalization and Foreign Exchange Reserves

2.1. Introduction

India achieved its independence from the British Raj in 1947. From then on, the country was faced with several challenges – social, economic, socio-political and many others. We opted for a mixed economy along with the state-led industrialization strategy. Specifically, there was an emphasis laid on import substitution. While this policy failed to foster much economic growth, it did set the ground for industrialization in India.

The early part of the 90’s decade was particularly a difficult one. Because of the crisis of balance of payments, India was pushed to a situation of default repayment of its debts. The policy makers reacted by carrying out wide-ranging outward-looking economic reforms. Distrusting market forces and restrictive trade policies started being perceived as hurdles to good growth. There was a clear move from the regime of the state to one that was a little more market-friendly, though this move was gradual. Abolition of the license system for establishing businesses and creating capacities deregulated industry. Furthermore, the abolition of quantitative restrictions and tariffs liberalized the trade regime. There was also a conscious promotion of foreign investment with initiatives such as permitting current account convertibility and allowing foreign exchange rates to be determined by market forces. The numerous reform policies have largely been moving towards making maximum use of the potential advantages of the globalization. There have been quite a few achievements along with some adverse consequences as well. The economic growth of India has moved to about 7.3 per cent during the period between 2000 and 2008.\(^65\) Much improvement has also been recorded by way of indicators like balance of payments and foreign exchange reserves. There has also been a lot of progress with regard to balance of payments as well as the foreign exchange reserves. In fact, the last two decades have

been particularly good in terms of the spread of telecommunication and information technology. There were some serious concerns during the post reform period. Basically, there has been quite an increased in the regional inequalities. Additionally, some of the western and southern states registered a healthy growth rate, higher than others. Secondly, some inter-personal inequalities coupled with rural-urban disparities are also increasingly growing. Thirdly, poverty is reducing at a certain pace too. Ultimately, the positive changes in different measures of the non-income welfare measures education and health in the span of the post reform period that would dip much below the improvement that has been achieved in the economic context.

It is a fact that economic reforms that were started in the 90’s signified a huge growth potential in India. With regard to this, it seems sensible to integrate India with the overall globe since it offers opportunities and challenges. Despite this, the policy initiatives would not be sustainable if there is a disproportionate burden on even a few sections of people in some parts of the country. Therefore, monitoring not just the macro indicators such as growth, balance of payments and foreign exchange reserves, etc., but also the indicators reflecting rising distributional issues is important.

2.2. Indian Economy: Trend and Pattern of Growth

The optimal sustainable degree at which an economy can develop without leading to an increase in the rate of inflation is the probable degree of development of an economy. The probable growth rate is ascertained by the development in the economy’s industrious ability which consecutively relies on the progress in inputs (labour, capital, land, etc.) and technology. An economy may also develop more than the probable rate for a limited period but that would initiate inflationary forces. If the progress is less than the probable rate it is likely that the unemployment rate in the economy is increasing. (Ambani, 2005)66

India has been noted as a large and comparatively slow and poor as a developing country. After the attainment of independence in the year 1947, the economic policies of India offered the government with the basic role in terms of promoting development

in the economic field. The size of India dictates its federal structure that are the provisions led by the Constitution (which are ratified in the year 1950), and attained subsequent evolution offering central government with the dominant position added by the India’s constituent units (that are States and Union Territories). The leaders of India aspire indigenous version related to Fabian socialism, added by government being the benevolent guardian that leavened smattering aspects of Gandhian influences for smallness, rural traditions and self-sufficiency.

Economic growth of India got reasonable in 1970s and averaged within 3 and 4 per cent/year. However, it is not considered as rapid way to diminish count of poor people, nor towards comfortable deal with strains related to the process of governing country with notable substantial linguistic, religious and ethnic diversity added by economic inequalities. Still, India is capable enough to preserve unity and its political system made of parliamentary democracy still prevails. However, the noted political stability gets accompanied by evolution of economic system that gets riddled by the increase in the rigidities as well as inefficiencies or so-called ‘license-quota-permit raj’.

In the year 1980s, influences of fresh ideology and observation attained from faster growth in various East Asian economies made India policymakers attempt changes in the governmental role of Indian economic development. This was added by the modes of liberalization in the regime of trade, there was the loosening of controls over domestic industrial aspects added by the investment promotion attained in the modern technologies from telecommunications. Growth of Indian economy got accelerated by 5 per cent and the same was at the cost of imbalances in the macro economy (fiscal as well as current deficits’ account) that worsened the starting phase of 1990s due to the collapse of Soviet Union that turns up as the major trading partner and relevant turmoil in Middle East.

In the year 1991, India faced diversified balance in the crisis of payments and this turned up as the occasion meant for the substantial advance for the structure of the economic reforms, which are attempted. There are some major steps attained for trade liberalization to reduce tariffs as well as conversion of the quantitative restrictions towards tariffs, added by the sweeping away of huge restrictions of segment over domestic investment of the industry. Two notable changes of early 1990s
symbolize/encapsulate ‘economic reform’ within India. The Soviet Union collapse in the year 1991 and stellar of the growth performance is related to China that is after world economy added by market initiation with reforms during 1980s. This got two notable developments as per reform in India during 1990s, and the same got distinguished from the temporary aspects as per earlier payment balance crisis in the year 1966.

The way to reduce governmental role is directly controlling functionalities of the market work with added implications. It has been noted that sectors like telecommunications and finance demand for newer regulatory format as per the environment where the bureaucrats no longer creating discretionary judgments as per case-by-case format. This must get strengthened by indirect and direct impacts related to technological change in these kinds of sectors. Moreover, removal of control over industrial investment cannot solve India’s slow growth problem, yet gets complemented by the mode of restructuring functionalities of labour market, added by the improvement of institutional and physical infrastructure. Attainments of these aims were hampered in understandable pressures of interest group and there are constrained aspects led by higher level of fiscal deficit by the government. High fiscal deficit remains traceable towards the subsidies of interest group and interaction nature between the state and central governments.

Aggregate mode of performance statistics got an incomplete mode of economic reform that has got sectors like agriculture that still gets shackled by inefficient mode of public procurement. This is added by system of distribution added by severe input related to market distortions, where the industry gets hampered by small scale reservations as well as inefficient finance with the financial sector dominating indirect and direct public. This is towards the control of investible resources, added by the rigidities of labor market hampering whole organization (as against informal) economic segment. Trade liberalization and foreign investment – aspect of ‘globalization’ as per reforms of India gets assistance in some areas. However, this is not sufficient towards the promotion of widespread competitiveness or the way to rectify/overcome poor Indian infrastructure. Therefore, agenda for economic reform in India is lengthy and complicated.
There is also the complication noted during 1990s and is the substantial increase attained in regional inequality. As inequalities gets widened within respective states (as coast as well as urban areas from Gujarat and Maharashtra as against the interior rural regions); the basic emphasis is over widening disparities among the states. This gets noted as natural action and offers political size and importance of government with states that are indirect and direct channels towards numerous transfers related to central government. This paper thus aims in examining interaction over the agenda of key reformation pieces and federal structures of India in terms of reducing and managing inter-state inequalities. This is in reference to situation that has some aspects related to economic reform added by larger forces of global economy with increased regional inequalities in India.

The potential rate of growth of an economy is the maximum sustainable rate at which an economy can grow without causing a rise in the rate of inflation. The potential growth rate is determined by the growth in the economy’s productive capacity which, in turn, depends on the growth in inputs (labour, capital, land, etc.) and technology. An economy can grow above the potential rate for some time but that will trigger rising inflationary pressures. Growing below the potential rate will imply a rise in the rate of unemployment. (Farrell et al., 2004)67

On account of the international predicament, the development rate of the Indian economy dropped down to 6.8 per cent p.a. from the earlier rate of nearly 9 per cent p.a. during 2003-2008. The development rate increased to 6.8 per cent during 2008-09, which further improved to 8.9 per cent during the initial half of 2010-11 (Yergin and Stanislaw, 2002)68. The question which arises here is that does the strong rate denote that the economy is further going back to its earlier path of growing at nearly 9 per cent p.a.? This further depends on what would be the extant probable development rate. (Shukla, 2001)69

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The most preferred technique to estimate the probable rate of growth of an economy is the HP filter technique, as put forth by Hodrick and Prescott (1980)\textsuperscript{70}. The figure 1 below displays the probable growth rates for the Indian economy by employing the quarterly figures from Q1 1996-97 to Q2 2010-11. As can be seen in the figure, the probable growth rate of the Indian economy has reached a little more than 8.5 per cent in the mid-2000s from approximately 5.5 per cent during the later 1990s (Spilimbergo et al., 2008)\textsuperscript{71}. After the mid-2000s, the probable rate has reduced and due to the international predicament, the rate has become 7.5 per cent and less. \textsuperscript{72}

There was a rude drop in the savings and investment rates in the economy after the international predicament: the savings rate actually reduced to approximately 33 per cent during 2008-09 and 2009-10 from around 37 per cent of GDP during 2007-08. The same period saw the investment rate lower to 35.5 per cent from around 38 per cent of GDP. Thus the reduction in the probable growth rate in the Indian economy is somewhat mirrored by the decline in the savings and investment rates. (Hoque and Yusop, 2010)\textsuperscript{73}

The economy developed by 8.9 per cent during the initial half of the present fiscal year and this figure is more than the probable rate. This is also the fallout of the perseverance of inflationary strain on the Indian economy. (Choong et al., 2005)\textsuperscript{74}


\textsuperscript{72} http://articles.economictimes.indiatimes.com/2012-07-30/news/32924166_1_export-growth-services-wto-report


Figure 1: Growth Rate of Indian Economy: Actual Vs. Potential
Q1 1997-98 to Q2 2010-11

Source: Constructed based on data from CSO.

2.2.1. Balance of Payments in Indian Economy

The numerical account which methodically sums up the monetary transactions of an economy in contrast to the remainder of the world for a particular time frame is referred to be the Balance of Payments. (Dipendra, 2001)\(^75\)

Thus the balance of payments in India is a methodical account of the global monetary transactions of Indian residents with the remaining world in view of goods, services, unreciprocated transfers and transfers of capital. The term residents include both nationals and non-nationals who live in India (Kandil & Morsy, 2010)\(^76\). Generally

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foreign students, tourists, foreign diplomatic officers and global organisations are not regarded to be residents but embassy officials and the armed forces of the nation, working overseas are considered to be residents despite their actual location.

The balance of payments of India displayed in this segment have been obtained majorly from the Exchange Control Records and the primary data on majority of the official transactions, not directed through the banking mediums are got from the Government agencies and the Reserve Bank of India. The Reserve Bank of India from time to time makes available the corrected/latest data via its Press Bulletin depending on this data obtained. The RBI monthly Bulletin and RBI’s website (www.rbi.org.in) are correct/modify the data available. With reference from July 1996, R.B.I. has altered the design of the Balance of Payments. The modified series in the novel form has been provided for the year 2000-01 to 2009-10.

The Fifth Edition of the Balance of Payment Manual identifies BoP as comprising of the current account, capital account, mistakes and certain omissions, as well as alterations in forex reserves. As part of the current account of the BoP, it has also classified transactions into merchandise (comprising of exports and imports) and invisibles. Further on, invisibles are classified as: Services that include travel, transport facilities, insurance, government which is not a part in any other document (GNIE), as well as miscellaneous. Components of miscellaneous services include communications, construction, financial, software, news agency, royalties, and management along with other business services. Income is another aspect of invisibles while the third aspect of invisibles includes transfers (grants, gifts, remittances, and so on). These do not have any *quid pro quo* (*"this for that"* in Latin) to most often means a more-or-less equal exchange or substitution of goods or services.

As part of capital account, it is possible to classify capital inflow by way of the instrument – which may be debt or equity and maturity - which may short-term or long-term. Capital account comprises of mainly foreign investment, loans, as well as banking capital. Further on, foreign investment comprises of foreign direct investment (FDI) along with portfolio investment which consists of foreign institutional investors (FIIs) while American depository receipts or global depository receipts (ADRs/GDRs) signifying non-debt liabilities. Loans are forms of borrowings to be repaid at a later
date in time generally along with a pre-determined rate of interest. Loans are in the form of external assistance, external commercial borrowings [ECB], as well as trade credit. It also includes banking capital along with non-resident (NRI) deposits in the form of debt liabilities.

The performance of BoP developments in the year 2010-11 were in the form of higher exports, imports, invisibles, trade, CAD as well as capital flows in complete absolute terms in comparison with the previous fiscal year 2009-10. There was adequate growth in exports as well as imports to the extent of 37.3% and 26.8% respectively over the previous year. There was a dip in the trade deficit by 10.5% in 2010-11 over the previous year. Despite this, as an element of the Gross Domestic Product (GDP), it marked 7.8% in 2010-11 as against 8.7 % in the previous year. There was also some amount of improvement in net invisible balances of about 5.8% over the previous year. The CAD increased to the extent of US$ 45.9 billion in the year 2010-11 over the previous year’s US$ 38.2 billion. It however improved very minimally as a ratio of the GDP to 2.7% in 2010-11 over the previous year’s 2.8%. The net capital flows in the range of US$ 62.0 billion in 2010-11 were up by 20.1% as compared to 2009-10’s figure of US$ 51.6 billion. This could be attributed majorly to higher inflows under the ECBs, external assistance, short-term trade credit, NRI deposits, as well as the bank capital. The year 2010-11 showed a CAD of US$ 45.9 billion which the capital account surplus of US$ 62.0 billion financed and which ended as accumulation to the already present foreign exchange reserves of US$ 13.1 billion (US$ 13.4 billion in 2009-10).

The first half of 2011-12 (H1 April-September 2011) witnessed a higher CAD in absolute terms surpassed its coordinate in the corresponding period of the previous year. This was largely because of a higher trade deficit. Additionally, the net capital flows in absolute terms was also more in the first half of the year 2011-12 as compared to the corresponding period of the previous year.

**Current Account**

**Merchandise Trade**

Exports surpassed the US$ 200 billion mark for the first time in 2010-11, which also registered a 37.3% growth from the previous year 2009-10’s figure of US$ 182.4
billion when it exported US$ 250.5 billion. Exports of goods were mostly engineering goods, petroleum products, gems and jewellery, as well as chemical and such other products. Along with better exports, there was also a change in the nature of exports in the sense that there was more export quantum of higher value-added engineering and petroleum products that the previously labour-intensive manufacturing kinds. Additionally, the fact that developing countries are turning into our favourite and largest export market in recent times has also been a relatively new development.

As in exports, there was also a good growth in imports of about 26.8% that brought in US$ 381.1 billion in 2010-11 over the previous year’s US$ 300.6 billion. Imports of oil upped by 19.3% in 2010-11 (against a dip of 7% the previous year) thereby accounting to about 28.1% of the entire imports (30.2% in the year 2009-10). The rise in imports was topped by petroleum and such products as well as pearls and semi-precious stones. The chapter on International Trade contains a detailed analysis.

There was an increase of about 10.5% in the trade deficit to US$ 130.6 billion as against the previous year’s US$ 118.2 billion. This was due to more increase in the imports as compared to exports after a commendable domestic performance in 2010-11. The trade deficit however worked its way from 8.7% in 2009-10 to a better 7.8% in 2010-11 on account of a greater increase in the GDP at market prices vis-à-vis the trade deficit.

India’s CAD widened during the H1 period of 2011-12 indicating the effect of the growth asymmetry between India and rest of the globe. The growth of exports and imports picked up in 2010-11 and went on into the first half of 2011-12.

In the H1 of 2011-12, US exports improved from US$ 107.3 billion in the H1 period of 2010-11 to about US$ 150.9 billion, touching a growth pattern of about 40.6% as against the 30% in the H1 of 2010-11 over the corresponding period in the previous year. There was much buoyancy in exports of goods like engineering and petroleum items. An encouraging and supportive government policy with much focus on the diversification of higher value-added products in sectors like engineering and petroleum sectors brought about resilience in the performance of exports. Exports are also effectively supported by trade policy with the help of schemes like the Focus
Market Scheme (FMS), Focus Product Scheme (FPS), and Duty Entitlement Passbook Scheme (DEPB).

Furthermore imports to the tune of US$ 236.7 showed an improvement of about 34.3% in the H1 of 2011-12 as compared to the 27.3% that was registered in the H1 of the previous year. Consistently rising prices of crude oil accompanied by increasing prices of gold and silver have also resulted in creating import bill in the H1 phase of 2011-12.

Trade deficit also expanded by about 24.5% to the amount of US$ 85.8 billion (9.4% of the GDP) in the H1 period of 2011-12, as against US$ 68.9 (8.9 % of the GDP) in the H1 phase of the year 2010-11. This occurred despite the higher exports as against that of imports in the H1 phase of 2011-12.

**Invisibles**

The invisibles account of the BoP shows the total effect of transactions that are relevant to international trade in the services along with the income of non-resident assets and liabilities, labour and property as well as cross-border transfers, largely remittances of workers.

The year 2010-11 showed a major increase in exports as well as imports of services. Exports of services moved up by 38.4% and touched US$ 132.9 billion from the US$ 96.0 in the previous year. There was also an increase of 113.3% in business services which touched US$ 24.8 billion from the US$ 11.3 billion in 2009-10 while financial services moved up by 75.7% from US$ 3.7 billion in 2009-10. There was also a rise seen in receipts of software services, largely by way of better efficiency and movement into diversified export destinations. There was also an increase in software receipts of about 11.7% in 2010-11 (that pegged at 7.3 % the previous year) which translated into US$ 55.5 billion, accounting for 41.8 per cent of total service receipts. These were 12.4 per cent of total current receipts. The Net service exports moved up from 36.0 billion in 2009-10, registering 35.5 per cent increase over the previous year to US$ 48.8 billion in 2010-11.
An increase on private transfer receipts took place as well. These comprised mainly of remittances from Indians working overseas. The increase was by about 3.7% touching US$ 55.6 billion in 2010-11 from US$ 53.6 billion 2009-10. About 12.4% of the current receipts (that was 15.5% the previous year) were taken by private transfer receipts. There was also a reasonable increase in other categories of receipts (transportation, insurance, communication, and GNIE).

Invisible payments saw an increase of 36.2 per cent from US$ 83.4 billion in 2009-10 to US$ 113.6 billion in 2010-11. There was a 36.2% growth in invisible payments which overtook the 21.3% growth mark the previous year. It further increased which was largely attributed to business services, financial services, travel, and investment income. Despite the surplus because of service-sector exports being higher in 2010-11, growth in net receipts on account of transfers was still moderate while the net outflow of investment income increased during the same period. Therefore, the net invisible balance (receipts minus payments) registered 5.5% increase to US$ 84.6 billion in 2010-11 compared to the previous year’s US$ 80.0 billion. As a proportion of GDP, net invisible balance declined from 5.9 per cent in 2009-10 to 5.0 per cent in 2010-11. At this level, the invisible surplus financed 64.8 per cent of trade deficit as against 67.7 per cent during 2009-10.

As part of the H1 in 2011-12, there was an increase of about 17.4% in the invisible receipts which moved to US$ 106.0 billion as against the US$ 90.3 billion in the corresponding period of the previous year. Services, transfers, and income which are the broad categories of invisibles registered good increase. There was also adequate growth in services exports which were around 17.1% in the period H1 of 2011-12 as compared to the 32.7% in the corresponding H1 of the previous year. As for the growth in imports, it was abnormally lower at 1.0% in the H1 of 2011-12 as opposed to 48.3% in the H1 of the previous year. With regard to the net basis, there was an increase in services surplus to the tune of US$ 31.1 billion in H1 of 2011-12 from US$ 21.5 billion in the corresponding period of the previous year. A decline in investment income receipts by 3.8 per cent was also seen when it touched US$ 4.2 billion during H1 of 2011-12, while payments amounted to US$ 13.6 billion (US$ 12.2 billion a year earlier). Transfer receipts comprise largely of personal transfers moved up to US$ 32.3 billion in the H1 of 2011-12 that was about US$ 27.2 billion the previous year.
An increase of 3.9% was seen in terms of invisible payments in the H1 phase of 2011-12 which touched US$ 53.0 billion over the previous year’s US$ 51.0 billion in the same period. There was also a 34.6% shoot-up in the net invisibles balance (receipts minus payments) which helped it touch US$ 52.9 billion (5.8 per cent of GDP) in H1 of 2011-12 from the previous year’s US$ 39.3 billion (5.1 per cent of GDP). At this point, the invisibles surplus financed about 62.0% of the trade deficit during the phase H1 of 2011, as against 57.0% in the previous year’s corresponding period.

There was a marginal decrease in the goods and services deficit (i.e. trade balance plus services) when it slipped from US$ 82.2 (6.0% of the GDP) in 2009-10 to US$ 81.8 billion (4.9 per cent of GDP) during 2010-11. The fiscal 2011-12 witnessed its widening to US$ 54.7 billion around the H1 as against US$ 47.4 billion during the previous year’s corresponding period by way of an increase in the trade deficit. Yet, as a ratio of GDP, it dipped marginally to 6.0% in 2011-12 (up to H1 period) from 6.1% in the previous year (up to H1 period)

**Current Account Balance**

There was an increase in the CAD from the previous year’s US$ 38.2 billion to US$ 45.9 billion in 2010-11. This occurred in spite of the improvement in net invisibles, largely because of higher trade deficit. Yet, as an element of the GDP, the CAD worked upward marginally to 2.7% in 2010-11 as compared to 2.8 per cent in the previous year.

There was also an increase in the CAD to US$ 32.8 billion in H1 of 2011-12, as against US$ 29.6 billion during the corresponding period of the previous year. This occurred largely because of a higher trade deficit. In its role as a proportion of the GDP, it was marginally lower at 3.6% in the H1 of 2011-12 as compared to 3.8% in the corresponding H1 of the previous year.

The latest data from the Ministry of Commerce states that, exports achieved a 23.5% growth in terms of US$ 242.8 billion during April 2011-January 2012, as against the US$ 196.6 billion that was achieved in the same period during the previous year. Imports also clocked a 29.4% growth and marked US$ 391.5 billion during April 2011-
January 2012 over the figure of US$ 302.6 billion made in the corresponding period of the previous year. As such, trade deficit upped by 40.3% to US$ 148.7 billion in the period April 2011-January 2012 as against the US$ 106 billion made in the period from April 2010-January 2011.

Capital Account

It is possible to classify capital inflows by way of: instrument (debt or equity) and maturity (short-term or long term). The major elements of capital account are foreign investment, loans, and banking capital. Foreign investment includes foreign direct investment (FDI) while portfolio investment signifies non-debt liabilities. Loans (external assistance, ECBs, and trade credit) and banking capital such as NRI deposits are debt liabilities. FDI is preferred over portfolio flows, in India, since FDI flows tend to be more stable than portfolio and other kinds of capital flows. Also, rupee-denominated debt is more preferable than foreign currency debt while medium-term and long-term debt is preferred over short-term debts.

International capital flow can be explained by push and pull factors. Push factors are factors that operate from the outside of an economy and inter alia include parameters like low interest rates, sufficient liquidity, slow rate of growth, or lack of investment opportunities in advanced economies. As for pull factors, these include robust economic performance and improved investment climate that take place because of economic reforms in emerging economies and are internal to an economy.

In 2010-11, both gross inflows of US$ 499.4 billion and outflows of US$ 437.4 billion under the capital account were higher than gross inflows of US$ 345.8 billion and outflows of US$ 294.1 billion in the preceding year. Capital inflows in net terms had increased by 20.2% to US$ 62.0 billion (3.7 per cent of GDP) in 2010-11 as compared to US$ 51.6 billion (3.8 per cent of GDP) in 2009-10 largely because of trade credit and loans (ECBs and banking capital).

The Non-debt flow or foreign investment- FDI and portfolio investment (ADRs/GDRs & FIIs) on a net basis declined by 21.4% from US$ 50.4 billion in 2009-10 to US$ 39.7 billion in the following year. This dip in foreign investment was further offset by the
debt flows components of loans and banking capital which shot up by 130.3% touching US$ 33.4 billion in 2010-11 from the previous year’s US$ 14.5 billion.

There was also a decline trend seen in the inward FDI flow whereas there was an upward trend seen in the outward FDI in 2010-11 as compared to the previous year’s figures. Inward FDI dipped from US$ 33.1 billion in 2009-10 to US$ 25.9 billion in 2010-11. The decline according to sector occurred largely due to lower FDI inflows that took place under manufacturing, financial services, electricity, and construction. The largest element of FDI inflows to India on the basis of countries, that investment that came through Mauritius was the biggest element of the FDI inflows to India in 2010-11 then followed by Singapore and the Netherlands. There was also an increase in the outward FDI which moved from US$ 15.1 billion in 2009-10 to US$ 16.5 billion in the subsequent year - 2010-11. A lower inward FDI and increase in the outward FDI, net FDI (inward less outward) to India stood substantially lower at US$ 9.4 billion during 2010-11 from the previous year’s US$ 18.0 billion.

Furthermore, the Net portfolio investment flow went through a slight decline US$ 32.4 billion in 2009-10 to US$ 30.3 billion in the next year. The reason for this was because of a dip in ADRs/GDRs to US$ 2.0 billion in 2010-11 from US$ 3.3 billion in the previous year. This development occurred despite the FII inflows indicated a marginal increase to US$ 29.4 billion in 2010-11 from US$ 29.0 billion in 2009-10.

There were also other categories of capital flows, such as the debt flows of ECBs, banking capital, and short-term credit which increased significantly in 2010-11. The Net ECB inflow also stepped up majorly to the extent of US$ 12.5 billion in 2010-11 as compared to the previous year’s US$ 2.0 billion. Likewise, there was also a spurt in the short-term trade credit. This moved from US$ 7.6 billion in 2009-10 to US$ 11 billion in 2010-11, pointing towards substantial domestic economic performance. Furthermore, there was also an increase in the external assistance increased from US$ 2.9 billion in 2009-10 to US$ 4.9 billion in the next year.

There was improvement in the capital account surplus which moved up by 20.1% touching US$ 62.0 billion during 2010-11 from US$ 51.6 billion in the previous year. Yet, as a part of the GDP, it slipped a little bit to 3.7% in 2010-11 from 3.8% in the
previous year. The Net accretion to reserves (on BoP basis) in 2010-11 registered US$ 13.1 billion, which stayed static at roughly the same score as in the previous year (US$ 13.4 billion). The fiscal year 2011-12 (up to H1), indicated that under the capital account both, there were gross inflows of US$ 244.2 billion and outflows of US$ 203.1 billion were higher than the gross inflows of US$ 207.5 billion and outflows of US$ 168.5 billion during the same period a year ago. With regard to net terms, there was a moderate increase in capital inflows which moved to US$ 41.1 billion in H1 of 2011-12 as compared to the figures of US$ 39.0 billion recorded in the H1 of the previous year.

Despite the net FDI being higher at US$ 12.3 billion in the H1 of 2011-12 as against US$ 7 billion in H1 in the previous year, there was still a decline in the net portfolio investment from US$ 23.8 billion to US$ 1.3 billion in the same period. The reason for this decline was a huge beating that FII flows took and dipped to US$ 0.9 billion in 2011-12 (up to H1) as against US$ 22.3 billion in H1 of the previous year. There were also other capital flows, including ECBs and banking capital, also substantially increased. Net capital inflow as an element of GDP showed reasonable moderation from 5.0% in H1 of 2010-11 to 4.5 per cent in H1 of 2011-12. The Net accretion to reserves (on BoP basis) during H1 of 2011-12 was lesser at US$ 5.7 billion as against the US$ 7 billion in the H1 of the previous year which happened largely because of the widening of the CAD.

According to the latest information on capital inflows, it was seen that FDI inflows were US$ 35.3 billion in the period of April-December 2011 (as against US$ 16.0 billion in the corresponding period of the previous year). There was also major and sharp decline in the portfolio inflows to US$ 3.3 billion in the period of April-December 2011 from US$ 31.3 billion in the previous year. This reflected uncertainty and risks involved in the global economy because of the euro zone crisis.

India’s Foreign Exchange Reserves

India’s foreign exchange reserves are made up of foreign currency assets (FCA), gold, special drawing rights (SDRs), and reserve tranche position (RTP) in the International Monetary Fund (IMF). When the Reserve Bank of India (RBI) intervenes in the foreign exchange market in order to straighten out the volatile exchange rate behaviour, foreign
exchange reserves are levelled. Another reason for this is also the activity of the US$ with world currencies. It is possible to accumulate foreign exchange at a time when one notices an absorption of too much of forex flows on the part of the RBI via an interaction in foreign exchange market, aid receipts, and interest receipts and funding from the International Bank for Reconstruction and Development (IBRD), Asian Development Bank (ADB), International Development Association (IDA), etc.

FCAs are maintained in major currencies like the US dollar, euro, pound sterling, Australian dollar, and Japanese yen. The US$ as well as the euro are intervention currencies; but these reserves are denominated and are also expressed in the US dollar only, which is the international numeraire. The level of reserves dips when the US$ appreciates against major international currencies and vice versa. Safety and liquidity can be seen as the guiding principles of foreign exchange reserves management in India with return optimization being embedded strategy within this framework.

India’s foreign exchange reserves began from a level of US$ 5.8 billion around the March 1991, and has slowly and steadily risen to a level of US$ 25.2 billion by the end March 1995, US$ 38.0 billion by end March 2000, US$ 113.0 billion by end March 2004, and US$ 199.2 billion by end March 2007. Foreign exchange reserves were around US$ 314.6 billion around the end of May 2008, before decreasing to US$ 252.0 billion at the end of March 2009. This decrease in reserves in the year 2008-09 was an outcome of the fallout of the global crisis and strengthening of the US dollar with regard to other international currencies. In the period of 2009-10 witnessed an upward trend in the foreign exchange reserves which rose to US$ 279.1 billion by the end of March 2010. This was due to the evaluation gain on account of the depreciation of the US$ with regard to important international currencies too. In the fiscal year 2010-11, foreign exchange reserves showed an increasing trend and touched US$ 304.8 billion around the end of March 2011, increased by about US$ 25.7 billion from the US$ 279.1 billion level at the same time in the previous year. From the sum increase in reserves, US$ 12.6 billion was because of the evaluation gains that happened out of depreciation of the US dollar against major currencies and the balance US$ 13.1 billion was on BoP basis.
The current fiscal year, when seen on a monthly basis, reflect certain trends in the foreign exchange reserves. These have touched a record high level of US$ 322.0 billion around the end August 2011. But, there was a dip seen to about US$ 311.5 billion around the end September 2011 before peaking to US$ 316.2 billion at end October 2011. Further on, there was also a decline seen in November and December 2011. By December 2011, they stood at US$ 296.7 billion, showing a dip of US$ 8.1 billion from US$ 304.8 billion at end March 2011. This dip in reserves has been caused to an extent because of the interference of the RBI in order to control the slide of the rupee against the US dollar. This level of reserves provides about eight months of import cover as well.

2.2.2. Foreign Exchange Markets in India – a brief background

The forex market in the country began properly about 30 years when in the year 1978; the state permitted banks to swap forex among them. These days more than 70 per cent of the swapping in forex usually happens among the banks. The market has over 90 permitted people who exchange money and usually emerge protected and secure once trading finishes. Trade is managed by the Foreign Exchange Dealers Association of India (FEDAI), a self managed group of traders. From 2001 onwards, clearance and settling jobs in the forex area are mainly done by the Clearing Corporation of India Limited (CCIL) which handles dealings of close to 3.5 billion US dollars per day about 80 per cent of the complete dealings.

The liberalizing event has greatly increased the forex area in the nation by permitting banks as well as corporations more room to hold and swap forex. The Sodhani Committee of 1994 had suggested more freedom for banking establishments which were involved, permitting them to establish their own trade boundaries, interest extent on FCNR accumulations and the application of derived aspects.

The expansion of the forex area during the recent past has been particularly striking. During the past five years from 2000-01 to 2005-06, the trading volume in the forex area (such as exchanges, futures and future negations) has become the thrice, expanding
at a compound annual rate of more than 25 per cent\textsuperscript{77}. Among the banks, foreign exchange trading has gone to make up a large share (more than 77 per cent) of the gross trading during this time, even if there is a pattern for that amount. (A reason for this domination is a consequence of counting twice because buying and selling are individually joined and one dealing between banks causes buying and also a selling entry) This keeps in trend with international trends.

During the March of 2006, roughly half or 48 per cent of the dealings were spot trading, while exchange dealings, (mainly repeat buying deals based on a single deal-stable or future- clubbed with a lengthier gestation future deal in the opposite way) made up 34 per cent and future and future negations constituted 11 per cent and 7 per cent each. Roughly a two-third fraction of all dealings put to rupee at one end.

In 2004, as per the third survey of the year of forex and derivation markets performed by the Bank for International Settlements (BIS (2005a)), the Indian Rupee was at the 20\textsuperscript{th} spot amongst all sorts of money values in the sense of appearing by one side of all forex dealings across the world and its stake had increased thrice compared with 1998.

Being a hub for forex swapping steps, India has the 23\textsuperscript{rd} rank amongst all nations which were done by the BIS studies in 2004 and made up 0.3 per cent of the global revenue. Trade occupies a relative and moderate proportion in the country and 11 banking establishments make up more than 75 per cent of the trade that was examined according to the BIS study, 2004.\textsuperscript{78}

\subsection*{2.2.3. Level of Forex Reserves in India}

The India method to establish the sufficiency of foreign exchange is in the process of development, in recent times, particularly with the release of the important Report of the High Level Committee on Balance of Payments and also Governor Jalan’s explanation of the clubbing of international volatility, local conditions and country safety requirements in establishing the liquidation which could be hazardous and hence

\textsuperscript{78} ibid
testing the reserve sufficiency. There is a need to give certain evidence with regard to a few of the markers of reserve sufficiency outlined here and there are no comments made about sufficiency as such.

The forex reserves have three components—gold, special drawing rights, forex possessions. On the third of May, 2002, out of the US $ 55.6 billion of gross holdings, forex possessions made up the largest stake with US $ 52.5 billion. Gold could make up only US $ 3 billion. During July 1991, the Reserve Bank of India decided as a short term measure and through the reserve handling mechanism, to give gold to get loans. The holding of gold is very important in holdings handling when there are financial troubles. From then onwards, gold has had an inactive part is reserve handling.

The degree of forex reserve has gradually gone up from US$ 5.8 billion in the end of March, 1991 to US$ 54.1 billion in the end of March 2002 and increased even more to US$ 55.6 billion on May 3, 2002. The conventional weighing of trade based markers of reserve sufficiency or the import coverage (described as 12 times the division of holdings and import revenues) reduced to 21 days of imports by the conclusion of December 1990 and then went up to 11.5 months during the concluding part of March, 2002.

With regard to financial markers, the per centage of net forex possessions of the Reserve Bank of India to money that the public had greatly went up from 15 per cent during 1991 to 109 per cent during the end part of March, 2002. The ration of NFA to wide money had gone up more than 6 times and stood at 18 per cent from 3 per cent.79

The debt linked markers of reserve sufficiency revealed a great deal of betterment during the 1990s. The ratio of limited duration borrowings (or payment commitments to last at least a year) to forex holdings had greatly reduced from 147 per cent during the end part of March, 1991 to 8 per cent during the end part of March, 2001. The share of uncertain money movement described to also factor in total portfolio movements and limited duration borrowing has reduced from 147 per cent in the year 1991 to 58.5 per cent during the end part of March, 2001. Making up a component of the maintainable

outside borrowing status, the limited duration borrowing constituent has reduced from 10 per cent during the end part of March, 1991 to 3 per cent during the end part of March, 2001. Also the extent of borrowing service payouts comparative to present receiving has reduced from 35 per cent in 1991 to 16 per cent in 2001.

2.2.4. Foreign Exchange Reserve: Trends in India

India’s business money hazard has gone up a great deal during the last few years, with FDI inside the nation greatly surpassing investments by Indian origin firms outside. A study of the country’s overall global investment status(IIP) shows that the total commitments of the nation are gradually increasing and tends to be far more than the cover afforded by the nation’s forex possessions.

The IIP is a brief of the condition of outside economic advantages and commitments of a nation. IIP information encompasses dealing by the Reserve Bank of India, the government, banking institutions and businesses.

The Net IIP is the brief of the outside economic advantages excluding the brief of the outside economic commitments. It is a statement of the distinction between what the economy possesses and what it needs to pay off. As per most recent information by the Reserve Bank of India, corporate houses have net commitments worth $437 billion in terms of IIP post adjustments during the end of December during 2010 as opposed to a forex protection f $279 billion in the same time. This implies that the country’s economic commitments greatly surpass the security of the foreign exchange holdings. On the other hand, China achieved a net asset status of $1.8 trillion with regard to its IIP in the year 2009. Our country’s net liability status in terms of IIP has been gradually increasing as time passes and surpassing the increase of forex holdings. A host of issues, for instance the greater investments by outsiders in the country and burgeoning dependence on outside commercial debt by Indian firms have resulted in economic disadvantages increasing quicker than advantages.
This is a cause for the Reserve Bank of India being uneasy with more rise in the outside commercial debt threshold of $30 billion which is allowed to Indian firms. Corporate houses have been trying to increase this threshold considering outside borrowings tend to be less expensive compared with local borrowings. However, foreign commitments increased during 2010 because firms took more loans to take advantage of the easier availing of cheap finances from outside.

The less official field or business field interaction with the risks linked with money has gone up during the past few years with a burgeoning net liability status as opposed to non those who do not stay.

Outside entitlement to Indian possessions in terms of Indian rupees are a lot more compare to Indian resident entitlement entities abroad in terms of foreign exchange, the RBI commented in its report.

The net commitments of the business industry increased from an amount of $160 billion to $437 billion from March 31, 2004 and March 31, 2010. Thus, the nation’s net outside commitments, (gross outside commitments which included dealings by the Reserve Bank of India, banking and business institutions excluding foreign exchange holdings) have gone up from $47 billion to $158 billion during the said time. The country’s forex holdings were $297.3 billion during December, 2010 an increase from $279.1 billion in March. It had to be recognised that the forex holdings had assisted and protected the country from an adverse effect of the global financial troubles. In comparison with several Western countries, our country has been comparatively less impacted by the international economic crisis that took place in 2008-09 and that caused several highly developed nations to experience a turndown. India had the fourth biggest forex possessions at $297.3 billion during December end 2010. Simultaneously, the forex possessions of Japan and Russia were $1.12 trillion and $479.4 billion each. Our neighbour China's forex holdings were $2.45 trillion during June, 2010.

As per the study, the nation’s holdings basically consisted of portfolio investments which were relatively susceptible to abrupt halts and turnarounds and loan from outside. The country’s forex holdings have gone up through the years from just about $80

5.8 billion during March, 1991. The holdings touched a pinnacle of $ 314.6 billion during the end of May, 2008 before reducing to $ 252 billion during the end of March, 2009.

The reduction in holdings during 2008-09 was product of the result of the international financial problems and the boosting of the US dollar in comparison to the foreign currency, the survey said.

Regarding the aspect of possessing multiple choices of a previously organized credit line, the study observed that this kind of a choice was needed but not enough since international investors often looked at the size of forex balances as an important input in implementing investing choices, it said.\textsuperscript{81}

2.3. Impact of Foreign Exchange Reserves on Balance of Payments

Foreign exchange reserves of India is inclusive of various external assets that are very much available and eventually are controlled by RBI in terms of meeting payment balance in financing needs, intervening exchange markets in order to stem volatility in reference to the exchange rate led by Rupee along with various related purposes. In current scenario, the foreign exchange reserves of India are actually comprise of assets of foreign currency initiated by RBI, SDRs, gold and RTP in IMF. In reference to India, SDRs are considered under government books and thus are not integral to assets of foreign currency under RBI, yet remains as a component to foreign exchange reserves. There is the inclusion of RTP in foreign exchange reserves from the 2\textsuperscript{nd} of April, 2004 in accordance to most relevant international practices. Change marked in reserves is subject to serve financing item within Indian BoP. Entire balance (that is the summation of current account balance, errors & omissions and capital account balance) are interrelated to the change marked in reserves under opposite sign. In a way, the net credit or debit status in entire balance gets matched through opposite entry under reserves for denoting an increase under reserves (or the debit) added by the possibility of declination in reserves (or the credit).

\textsuperscript{81} ibid
Movement in reserves has been well extracted from reserves’ stock. This particular stock is comprised of both ‘real’ kinds of changes under reserves added by valuation effects. Assets of foreign currency related to RBI, has been expressed through US dollars, and it is comprised of other kinds of hard currencies like Euro, Yen, Sterling, etc. Thus, the rates of cross-currency exchange for these currencies can affect stock related to foreign currency assets under RBI, that are eventually expressed through the valuation assessed under US dollars. For gold, aspect of valuation is rising continuously due to changes in international prices related to gold. As gold reserves are subject to get valued at the rate of 90 per cent of average market price of London during the month, yet developments in SDR/ exchange rate of US$ are affecting SDR holdings valuation and RTP. The way BoP records under actual changes in reserves, respective valuation lays effect in stock that got removed. Effect of valuation works out through the derivative differences among reserves’ stock by the end of reference period that gets expressed through current exchange rate added by same stock which is expressed under exchange rate, which is subject to prevail in beginning of reference period.

Gold (here, the monetary gold) has been marked as an asset that is owned by RBI and has been further interpreted to remain 9995/9999 pure. All kinds of transactions related to gold happen between RBI and relevant counterparts, like central banks of some other countries, or among RBI and IMF or the international monetary organisations. The value of gold is considered as reserve asset without any outstanding financial mode of liability. As noted by extant practice, for purchase/sale of gold by RBI from places different from central bank/international organisation; the terms of acquisition or sale gets recorded as export (or credit)/import (or debit) in terms of goods in current account added by contra debit/credit entries in reserve account or monetary gold. BPM, still insist on the fact that transactions of gold with non-resident kinds of entities need to get captured by BoP (here should not be any recorded transaction under BoP, in case counterparty gets identified as resident). Thus, as gold gets acquired through RBI from government, it never gets recorded and so in case of India's BoP; whilst they were recorded primitively under the process of “non-monetary gold” (or credit) in terms of the merchandise with contra entry (or debit) under respective monetary gold (or reserves).
In case of RTP from subscription for quota increase in IMF, 25 per cent gets quota paid in terms of hard currency being integral to RTP as in India's BoP turns up as debit entry in contrast to “IMF Quota” along with credit entry or (decrease in assets) in terms of foreign currency reserves (which is either under foreign currency assets, RBI/SDR holdings, as per relevant instance. It is an approach that never change level related to foreign exchange reserves since the loss of reserves, in terms of under assets of foreign currency or SDR holdings, turns up as a fully offset through relevant increase in reserve position under IMF as latter turns up to be a part of foreign exchange reserves. Rest 75 per cent of Indian quota gets paid through the non-negotiable as well as non-interest modes of bearing government related securities through the way of depositing the same in IMF Account No. 1 meant for RBI that was hereby declared as debit entry in contrast to “IMF quota” added by the contra entry in terms of “miscellaneous or other capital receipts”. Thus the entry made in contrast to IMF quota (or debit) depicted the whole amount of the quota increase paid to the IMF (both the foreign currency component and the rupee securities issued in favour of the IMF for the domestic currency component related to quota subscription) added by contra entry (or credit) in (i) “reserves” (foreign currency component), (ii) “Miscellaneous or other capital receipts” (rupee securities as issued by IMF) in order to declare the liabilities to IMF have added by securities which are owned by IMF yet are held in India.

Rupee securities as has been led by IMF are considered in terms of both liabilities and assets. This kind of approach has been pursued in conformity of earlier guidelines declared in IMF. Still, as declared under latest edition in Manual (BPM6), component of domestic currency of IMF quota payment that has been paid either under domestic currency or for securities is never entailed in reference to the impact led by BoP/IIP as per net basis, as these securities are declared as liabilities and assets. Thus component of domestic currency under IMF quota payment is never made visible in BoP statistics of India.

SDRs’ allocation led by IMF for India has been included in terms of credit entry under “other capital” related to Indian capital account where BoP is considered to show increase liabilities of India towards IMF, along with counter debit entry under SDR holdings led in reserve assets offering increase in foreign exchange reserves of India.
In the initial stage of current decade, India has been designated by IMF as ‘creditor country’ under the regulation of Financial Transaction Plan (or FTP). This is because, India attained surplus BoP status. By this scheme, domestic currency or (securities) initiated by IMF in terms of quota subscription converted in foreign currency, offering share of foreign currency component (or RTP) that increased the corresponding declination under the share related to component of domestic currency quota, without attaining any kind of alteration for total quota subscription by interrogated country. Participation in FTP enabled IMF for holdings of rupee under the contribution of Indian quota with hard currency. Contribution has been forwarded by India towards FTP by payment offered to IMF by hard currency and through debiting Government account related to amount equivalent to rupee that gets realised through in-cashing rupee securities offered to IMF previously for quota payment. Consequently, increase of reserve tranche status is marked with IMF under equivalent declination of assets of foreign currency related to RBI, in reference to unaltered level of foreign exchange. Still, the component of rupee to IMF quota subscription decreases in correspondence to the increased share of relevant hard currency in total quota subscription. All these entries are relevantly reversed in the instance where India received contributions IMF under the completion its participation under scheme that has been borrowed from countries and repaid loans to IMF.

2.4. Indian Economy and Globalisation

Globalisation is clearly the phenomenon that has slowly shrunk the globe in more ways than one. It opened up the doors of countries and welcomed a new era of business by doing away with hurdles by way of rules or regulations that would restrict trade and investment between nations. The underlying idea in globalization is to improve economic strength by way of competitiveness, in order to develop the economy and society simultaneously. We must also understand that there are some misconceptions about this phenomenon and learn to identify these.

As a phenomenon, globalization has been going on for centuries now. The benefits of tea were known throughout China and people regularly sipped tea. When this custom spread to different parts of the world, the entire world wanted tea from China. This is how tea started being exported from China to hundreds of places across the globe.
Globalisation as a concept needs to be explored in terms of time and its impact. And, therefore it is not a very easy thing to define globalization in so many words or describe it as being good or bad. It is, however, important that the globalization process be perceived from a point of view that is not restricted to simply liberalization and privatisation, something which most people tend to.

Despite both the terms being part of business vocabulary, they are distinctly different concepts. While globalization is not restricted by time, liberalization and privatization can be, subject to rules and regulations of the respective country or countries involved. All these processes are inter-related since globalization as a concept exists in the space between the two ends – liberalization and privatization.

This extract intends to study the reality and the lack of it in order to clarify certain misconceptions and thereby improve peoples’ knowledge of the strong potential globalization has. Yet, it has been far from an easy task with regard to India.

India’s relationship with globalization started with its economic reforms in 1991, after having gone through an import substitution strategy for almost four decades. During this period, the public sector worked its way to pump up growth in the economy, gearing it to register better economic growth. Sadly, it did not deliver results as expected. The idea is not to criticize the policies since it seemed to be the need of the hour at that point in time. From 1991, India has shown reasonable and consistent economic growth with other macroeconomic sectors showing positive progress as well. However, the essential sentiment of India’s economic progress could be described as ‘uneasy’ or ‘a comparative failure’.

Several nations have been on the part of export-led growth, mostly the East and South-East Asian countries. South Korea is an excellent example in a country rising from zilch to a healthy level of economic prosperity. Both the countries, India and South Korea achieved their independence in 1947 and started off with relatively similar economic conditions, having even similar per capita income. Though both the countries commenced their independent journey with an import substitution growth strategy,
South Korea got on to the export-centric route to foster better growth in its weak economy.

This country’s performance speaks for itself. About thirty years ago, South Korea was in line with several poorer countries of the African and Asian sub-continent in terms of its gross domestic product (GDP). This is in stark contrast to its present figure of a phenomenal ($13,478) which is seven times of that of India, seven times of that of India ($2,077), 13 times of North Korea’s GDP, and comparable to the lesser economies of the Europe. Moreover, South Korea has assumed its responsibility as a member of Organisation for Economic Co-operation and Development (OECD), also regarded as the rich nations’ club.

China is also a case in point. People of China opted for the globalization process around the end of the 70’s decade by practising liberalization in their own economy. China is today regarded as an important and developed nation and is soon poised to be a part of the World Trade Organization.

Sanjay Baru, Editor of the *The Financial Express* and himself a well-regarded journalist says, “What’s the bottom line? There has certainly been much competition and better fuelled growth over the past twenty years or so. But, the economy still needs a stronger nudge to ascend on to a path of better growth for it to be able to match the performance of its East and South-East Asian neighbours. Investment is an important requirement at this point in time.

Though investment changes quite a few equations, it has to be effective in generating employment and also using it to create wealth. It is futile to linger on the argument of whether the 90s were a better decade than its predecessor or not. It would be more worthwhile to achieve an average growth rate of 8 per cent in the initial period of the new century.

This segment also seeks to create more knowledge in the layperson about what globalization really is and how it impacts the people of India. It also works towards building a kind of constituency for economic reforms rather than taking a negative thought process and looking for drawbacks in the globalization process, India would do
better in working out hard core solutions for its progress. As Indians, we will have to opt for a path in a particular direction, the one that will lead us to make globalization bring a better tomorrow especially for the poor.

Indian economy faced severe crisis during July 1991, due to the instance when foreign currency reserves plummeted for nearly $1 billion; fiscal deficit turned high and become unsustainable; there was the up roaring of inflation with the annual rate assessed as 17 per cent\(^2\); NRIs and had foreign investors lost relevant confidence over Indian Economy. The Indian capital flew out and closed towards defaulting loans. Added by bottlenecks inside home, there are many unforeseeable changes that were swept away in terms of economies in Western as well as Eastern Europe, Latin America, South East Asia and elsewhere, during the same time span. All these economic compulsions considered within the country and abroad and declared for complete overhauling of Indian economic policies.

2.4.1. Impact led by Globalization

Globalization in terms of national economy has been noted as many. Aspects of globalization have intensified modes of interdependence added by competition among economies in global market. All these economic kinds of reforms are yielded with following benefits: (Rachman, 2008)\(^3\)

Impact of globalization over India had got favourable benefits in reference to overall economic growth rate. It has been marked as an improvement in Indian growth rate since 1970’s being just 3 per cent as against twice the GDP in countries such as Indonesia, Brazil, Korea and Mexico. India’s estimated average annual growth rate got doubled during 80s till 5.9 per cent, yet remained lower than Korea, China and Indonesia. Growth of Indian GDP improved its global position. Eventually the position

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of India in global economy improved from 8th position (1991) to 4th position (2001); when GDP got estimated over purchasing power as per parity. (Fischer, 2006)\textsuperscript{84}

From 1991 to 92; reforms program of Rao listed the growth of Indian economy by 0.9 per cent. Still, the GDP growth consequently accelerated to the level of 5.3 per cent during 1992-93, and further to 6.2 per cent during 1993-94. Growth rate above 8 per cent was attained during 2003-04. GDP of India grew with the rate declared in following graph from independence. (Henry and Sasson, 2008)\textsuperscript{85}

Figure 2: India GDP Annual Growth Rate

India - Growing Economy


(1) **Increased Foreign Trade:** India’s share in world trade has increased because of the many foreign trade policies that have been opted for, by way of globalization. While the country had only about 0.53 per cent of the world trade in 1990-91, it shifted to 0.60 per cent around 1995-96 and then to 1.0 per cent around 2005-06.

(2) **Increase in Foreign Investment:** Because of the globalization process, not just foreign investment but also foreign portfolio has increased considerably.

   a) **Foreign Direct Investment:** Foreign Direct Investment is the investment that foreign companies make so as to create fully-owned companies in a foreign country that they will be able to manage or buy shares of, to be able to manage such companies. One of the major characteristics of FDI or Foreign direct Investment is that the management of the native companies is in the hands of foreign companies or new companies are established in India by foreign companies. The foreign investor, being the one to take the risks is the one who is solely responsible for the profit or loss of such a company.

   b) **Portfolio Investment** – In regard to portfolio investment, foreign companies or foreign institutional investor (FIIs) purchase shares or debentures of native companies though the management and control stays with the native company itself. Foreign investment in India has shown significant improvement. The beginning of the 90’s saw total foreign investment (FDI and Portfolio Investment) of about US$ 103 million. By 2005-06, this amount had increased to US$ 20,155 million. India experienced a huge balance of payments and saw a major improvement in its foreign exchange reserves because of the substantial increase in the foreign investment.

(3) **Increase in Foreign Collaboration:** Collaboration of foreign companies with several Indian companies is a very good outcome of the globalization process. Collaboration agreements could be technical collaboration, financial collaboration or even a combination of the two. Foreign technology is provided by the foreign companies in financial collaborations. One sees several foreign
companies establishing several enterprises in India as collaborations with Indian companies.

(4) Increase in Foreign Exchange Reserves- Because of the Indian economy’s globalization, there has also been a substantial increase in the foreign exchange reserves. The foreign exchange reserves of India were in the range of about Rs 4,388 cr. in 1991 which shot up to Rs 7,96,000 cr. (US$ 185.1 billion). This goes to show how foreign exchange reserves of India have increased 181 times.

(5) Expansion of Market: Globalization has not just widened the market size but has also helped Indian business units expand their reach across the globe. MNCs today are not at the mercy of national boundaries and work well with companies such as Infosys, Tata Consultancy, Wipro, Tata Steel have a strong presence in many countries all over the world.

(6) Technological Development: One of the other advantages of globalisation is that it has facilitated the inflow of foreign technology, which is not just much superior to that of Indian companies but is more advanced as well. Indian business units are sure to use this modern technology and benefit greatly from it as well.

(7) Brand Development: Globalisation has helped branded goods to reach places far and wide. Today, people are able to exercise their choice of using branded goods in not just durable goods but also with regard to daily use products such as soaps, cold-drinks, tooth-paste, garments, food grains, and so on. Indian consumers typically like to use foreign and branded items. This has further helped in developing brands as well as their quality.

(8) Development of Service Sector: The service sector has also benefited greatly from globalization. The entry of foreign companies has pushed indigenous companies to step up their levels of service and quality too. One notices this trend in several sectors like telecommunications, insurance, banking. Mobile phones that were practically non-existent a couple of decades back are today very cheap and popular in India.
(9) Increase in Employment: Globalization has fuelled employment opportunities greatly. Foreign companies have established their production facilities and trading network in India. This activity has improved employment chances for Indians, e.g. many Indians are presently employed in foreign insurance companies, mobile companies, etc.

(10) Reduction in Brain Drain: Because of the globalization phenomenon, many multinational corporations have set up their business units in India. These corporations offer attractive salary packages and excellent working conditions in addition to lucrative perks to efficient, skilled Indian engineers, managers, professionals, etc. When Indians are being offered such employment opportunities and packages in their own country, why would they want to leave the country? Naturally, the brain drain has reduced

(11) Improvement in Standard of Living: The advantages of globalization having percolated down the layers of society are showing results with the standard of living of Indian population improving.

Globalisation has thus resulted in reduced prices of different products especially like electronic items like television, A.C., mobile phones, refrigerator, etc. now middle-income group also uses these luxury products. Joint ventures are therefore formed between two or more parties to undertake economic activity together. The parties mutually decide to come together and form a new and combined entity by both contributing equity. Naturally, they share the revenues, expenses, and control of the enterprise in terms of their individual hold. The venture can be for one specific project only, or a continuing business relationship such as the Fuji Xerox joint venture. As against this, a strategic alliance does not involve any kind of equity stake by the participants and is a much lighter arrangement.

2.4.2. Structure of Indian Economy

Globalization increased GDP added by the growth in various sectors with lots of changed aspects. Earlier maximum portion of GDP in economy generated from primary
sector, yet the current service industry got devoted with maximum portion of GDP. Service sectors turned up as growth driver in the economy added by the contribution offered more than 57 per cent of GDP. (Winters et al., 2004)\textsuperscript{86}

India has been ranked as 18\textsuperscript{th} position among international exporters of services added by a share of 1.3 per cent in international exports. Service sectors have been expected to offer benefit from on-going liberalization related to foreign investment regime within the sector. ITES-BPO and Software sectors recorded exponential growth in the current years. GDP growth rate included major sectors in economy as follows -

**Table 2: Structure of the Economy (GDP in Percentage)**

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**Source:** Reserve Bank of India Annual Report (1999-2011)

**Inflows of Foreign Direct Investment**

There is an increase in FDI from US$100 million during 1990-91 to US$ 5536 million during 2004-5. Detailed foreign investment inflow is noted as below: (Frankel., 2006)\textsuperscript{87}

Current account deficit is subject to get hovered at the rate less than 1 per cent of GDP in current years. Strength of external sector got reflected under sizeable accumulation related to foreign exchange reserves of India by including foreign currency assets, SDRs, gold and reserve position along with IMF reaching US$ 141.5 billion by 31\textsuperscript{st} March, 2005. The total assessment has been declared as US$1 billion within 1990–91 with payments crises under balance. Composition of debt got favourable.


Figure 3: Foreign Direct investment inflows (in US$ Million)

![Bar chart showing foreign direct investment inflows in US$ Million]


There was short-term debt that got amounted for 3.5 per cent from total external debt added by concessional debt amounting till 36.5 per cent of total debt. Burden of external debt turned up sustainable as per the range of indebtedness measures. Both the determined debt service payments in terms of being proportionate to current receipts and external ratio of debt-to-GDP fell steadily in 1990s, and in the current position, it is about 17 per cent and 22 per cent, respectively. ((Das, 2008a)\(^8\))

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