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External sector scenario of India in pre and post COVID era

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Abstract
This study examines the External Sector scenario of the Indian economy in the pre and post COVID era, with an emphasis on trade dynamics, capital flows, and currency rate volatility. This study used secondary data from various sources, such as the Reserve Bank of India, World Bank database, MoSPI, Export Import Data Bank (Annual), Trade Statistics, and Ministry of Commerce and Industry. This study found that the covid-19 pandemic did not affect the Indian economy but also affected the world economy. This study found that in the first five months of 2020, the worldwide volume of goods trade decreased by 20% compared with the same period in 2019. This reduction was more abrupt than it was during the global financial crisis. This study concludes that in recent years, global economic growth has been impacted by geopolitical conflicts and nationalism, and increasing India's exports of goods and services would be more challenging than previously. To turn this difficulty into an opportunity, both the business and public sectors should prioritize product safety, quality consciousness, and policy stability.

Keywords: External sector, Indian economy, COVID-19 impact

Introduction

Competition in global marketplaces promotes efficiency and growth, while preferential market access motivates enterprises to explore export markets. External balance is determined by the natural interaction of optimizing behavior between domestic and foreign agents. An external balance indicates the need for policy interventions. Annachhatre, M. & Gore, M. (2021) [1].

Over the past 20 years, India's economy has become more integrated through trade and financial flows. The COVID-19 pandemic has resulted in decreased world trade, reduced goods prices, and rigidity external financing situations, affecting several countries' current accounts and currencies. In the first five months of 2020, the worldwide volume of goods trade decreased by 20% compared with the same period in 2019. This reduction was more abrupt than it was during the global financial crisis. During the pandemic, India’s changing nature of global trade witnessed decreased exports of diamonds, jewelry, engineering goods, textiles, and allied products, while exports of medications, pharmaceuticals, software, and agricultural products increased. On the other hand, during the pandemic, India received a surplus on the current account balance after 17 years gaps.

Significant FDI and FPI inflows help to keep the capital account balance stable. Foreign currency reserves reached an all-time high of $586.1 billion on January 8, 2021. The RBI's forex market interventions have successfully decreased volatility and one-sided appreciation of the rupee. Export promotion measures include the Production Linked Incentive (PLI) Scheme, Remission of Duties and Taxes on Exported Products (RoDTEP), better trade logistics infrastructure, and digital initiatives. Since the COVID-19 epidemic, the global economy has faced a number of shocks, including the Russia-Ukraine conflict, Middle East developments, and the Red Sea problem.

These events have caused supply disruptions to various commodities and a significant increase in inflation in many nations. India's foreign sector remains strong, despite geopolitical challenges and high prices. Although merchandise exports declined due to weaker demand from major trading partners, service exports remained strong, reducing the overall trade deficit from USD 121.6 billion in FY23 to USD 78.1 billion in FY24. Lower costs for imported commodities, notably crude oil, are also observed. In FY24, India received USD 44.1 billion in net foreign portfolio investment (FPI), which was fueled by solid economic growth, a stable business environment, and increased investor confidence. In the future, growth is likely to be driven by changes in India's export basket, enhanced trade infrastructure, increasing quality consciousness, product safety in the private sector, and a stable policy environment. International Trade has boosted the economic progress of India. Over time, efforts to improve trade have led to a large increase in the share of products and services in the GDP. This is illustrated in Figure 1.

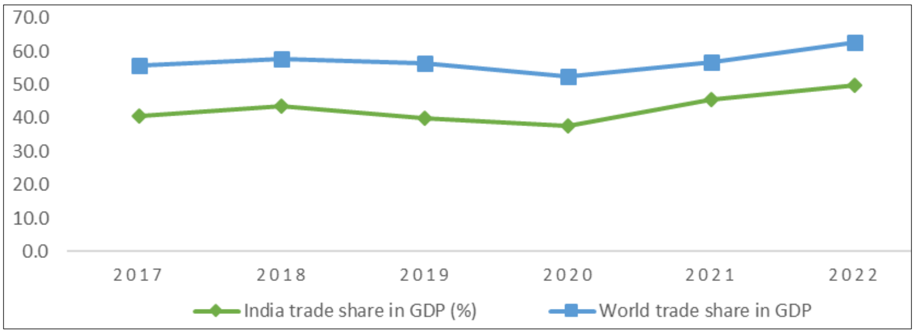

Fig 1: Total Trade as a Percenatge of GDP

Figure 1 shows India's trade share in GDP with World's share in GDP for the period 2017–2022. This figure highlights that in 2017 India's trade share was 40.7 % of its GDP while World trade share was 55.8% of GDP. During the Covid-19 period, both India's trade share as well world's trade declined. In 2020, India's trade share was 37.8% while world's trade share was 52.4%. however, due to consist efforts trade share revived again and increased after the pandemic. In 2022, India's trade share increased to 50% whereas world's trade share rose to 62.6%. This shows that India's trade has been, meeting up with global levels.

India's Merchandise Trade Performance

India's merchandise exports have grown on a continuous basis for nearly three years, beginning in FY17. However, in FY20, the economy slowed, caused by the External Sector outbreak of the world's pandemic, which put a brake to this trend. FY22 represented a major turnaround. A similar pattern has been observed in merchandise imports. This shown below in figure 2.

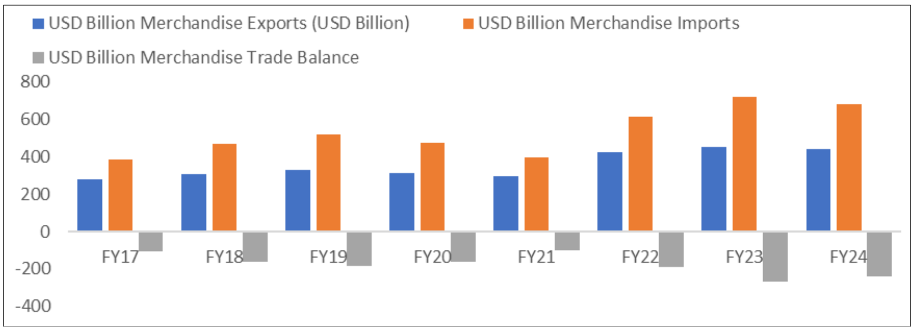

Fig 2: FY 18 India's merchandise exports

Figure 2 shows that in FY 18 India's merchandise exports crossed 300 bn USD but due to pandemic it reduced to 291 bn USD. Similarly, India's merchandise imports were 465 bn USD in FY 18 while in FY 21 it declined to 394 bn USD. In recent years, merchandise exports and imports contracted in FY24 compared to FY23 due to slowdown in our largest trading partners, effect of contractionary monetary policy by many nations to curb inflation etc.

India's Services Trade Performance

India is presently the world's seventh-largest service exporter, up from 24th in 2001. India is ranked second in the world for telecommunications, computer, and information services exports, and sixth overall. In terms of exports, the country ranks eighth in other business services, tenth in transportation, and fourteenth in travel. The RBI notes that India's BOP position has been strengthened by continuous rise in services exports, which have helped offset the country's merchandise trade deficit.

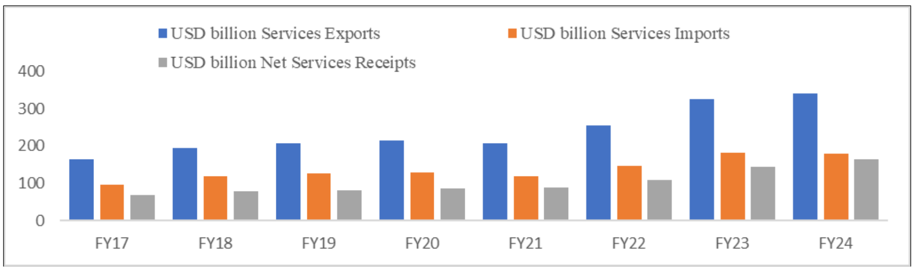

Fig 3: India's Services Trade Performance

Figure 3 shows India's rising services exports and imports as well as net services receipts. Services exports growing since FY 17, from 164 bn USD to 341 bn USD in 2024 but it slowed down during the pandemic i.e., 206 bn USD in FY 21. Similarly, services imports rising since FY 17 from 95 bn USD to 178 bn USD but declined due to pandemic in FY 21 i.e., 117 bn USD.

Composition and Direction of India's Trade

An examination of the composition of foreign trade enables us to analyses the progress and rate and speed of structural changes operating in the country. if we find that a country export finished goods, machinery and capital equipment but imports raw material and food grains, we can safely conclude that it has reached a high level of development. On the other hand, if a country imports capital equipment and machinery but exports primary commodities, we can conclude that country is an underdeveloped one. In 2017, India's major imports was Petroleum, Crude & products, electronic goods, Pearls, precious & Semi-precious stones, Gold and Machinery, electrical & non-electrical etc. whereas its exports include Engineering Goods, Gems & Jewellery, Petroleum Products, Organic & Inorganic Chemicals, Drugs & Pharmaceuticals etc. Organic & Inorganic Chemicals, in 2020-21, India's major imports was Petroleum, Crude & products, electronic goods, Gold, Machinery, electrical & non-electrical, Organic & Inorganic Chemicals etc. while its exports composite the same commodity as in 2017-18.

In 2023-24, India's principal imports include Petroleum, Crude & products, electronic goods, Machinery, electrical & non-electrical, Medicinal & Pharmaceutical products, Coal, Coke & Briquettes, etc. while its exports constitute while its exports include Organic & Inorganic Chemicals, Petroleum Products, Gems & Jewellery, Organic & Inorganic Chemicals, Drugs & Pharmaceuticals etc.

Direction of trade means from which country India imports and to which countries it exports its product. In 2017 India top five trading partner was USA, UAE, Hong Kong, China, Germany in terms of its exports whereas its five-trading partner from which India import was China, USA, UAE, Saudi Arabia and Switzerland.

In 2023-23, India's top five exporting countries involve USA, UAE, China, Singapore and Saudi Arabia while its top five importing countries include China, Russia, UAE, USA and Saudi Arabia. This highlights that there is no major change in India's trading partner since 2017 except Russia includes in top five in 2023-24.

Foreign Investment Flows

Foreign Direct Investment (FDI) as an investment targeted at gaining a long-term interest in a firm operating outside of the investor's country. In this sense, the word "long-term" differentiates FDI from portfolio investment, which is short-term and entails a large turnover of securities. It differs from other types of investment, such as portfolio investing, in that it seeks long-term interest as well as some level of influence or control. Governments frequently favor FDI because it can bring capital, technology, and knowledge that can help to economic growth and development in the host country (Shaikh *et al*., 2024) [2].

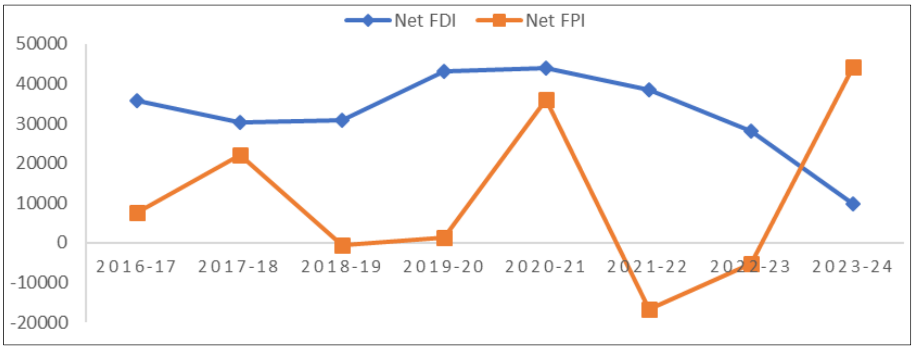

Fig 4: India's Foreign Investment Flows

Figure 4 shows Net FDI inflows declined from USD 35.6 billion during FY17 to USD 9.7 billion in FY24. Net inflows decreased due to increased repatriation and disinvestment because of profitable exits. FY 2020-21, net capital flows were moderate at US$ 16.5 billion compared to US$ 40.0 billion in FY 2019-20. This was primarily due to net repayments of external commercial borrowings (ECBs) and a drop in bank capital. Net foreign investment increased to US$ 31.4 billion in FY 2020-21, compared to US$ 28.7 billion in the same time last year. In recent years, there is a decline in net FDI inflows. In 2023-24, Net FDI declined to 9 bn USD from 27 bn USD in 2022-23. This is due to increased interest rates in industrialized nations and enticing exit opportunities from India's thriving stock market. India received Highest FDI equity inflows from Singapore (26.5%), followed by Mauritius (17.9%), USA and Netherlands (11%), Japan (7%), UAE (6.5%) etc. Net FPI inflows decreased in 2022-23 period but increased significantly in 2023 -24 crossed 44 bn USD.

Exchange Rate

The exchange rate is the price of one currency compared to another. The exchange rate has a tremendous impact on the global economy, influencing everything from international trade and investment to people's daily costs of living around the world. This rate reflects the relative demand and supply of different currencies and is influenced by a number of economic factors, including inflation, interest rates, and trade balances.

Figure 5 highlights depreciation of Indian rupees against USD since 2017. In 2017, Rupee/USD exchange rate was Rupees 65/USD, it increased to Rupees 65/USD in 2020. Rupee depreciated further to INR 82 against US dollar in 2023. According to Economic Survey 2024, Rupee experienced lowest volatility in FY 24.

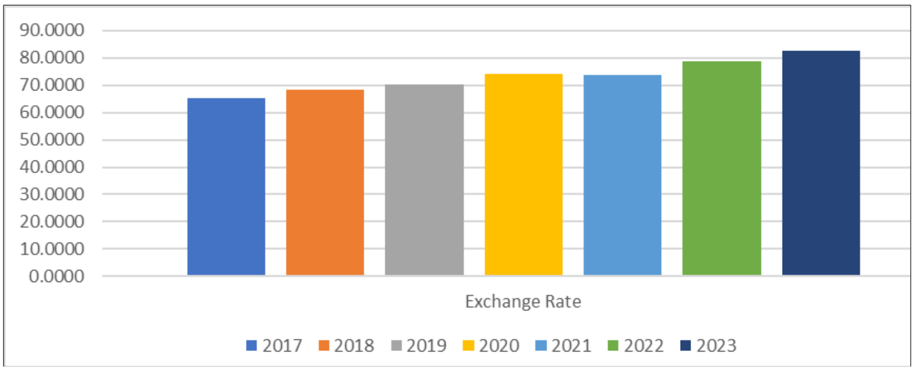

Fig 5: Exchange Rate

In FY24, the Rupee/USD exchange rate ranged between ₹82-83.5/USD, with only a 2.9% depreciation. In FY24, the rupee declined by 6.9% against the pound sterling and 6.8% against the euro. However, it increased by 3.5% against the Japanese Yen over the period.

The rupee's relative stability, despite a stronger US currency and higher US government yields, shows the Indian economy's strong macroeconomic fundamentals, financial stability, and improved external position. In the future, strong foreign inflows and modest trade deficits are projected to keep the rupee in a healthy range.

The Indian rupee exchange rate is determined by the market. The RBI supervises the foreign exchange market to maintain order and prevent excessive volatility in the Indian rupee. It has stabilized foreign exchange markets and reduced INR volatility. The government recently announced initiatives to diversify and grow forex funding sources to reduce exchange rate volatility and global spillovers.

Conclusion

This study examined India's external sector scenario in pre and post COVID-19. This study concludes that during pandemic India's share in GDP decreased from 40% in 2017 to 37% in 2020 but as the pandemic period end it increased 50% in 2022. This show that India is moving away from pandemic period. Before the pandemic period, India's trade deficit was 181 bn USD it decreased to 161 bn USD due to decreased in imports as well as exports but imports decreased more than exports India received trade surplus after 17 years gap period due to pandemic. In recent years, India's foreign sector faces downside risks due to ongoing geopolitical tensions and policy uncertainty such as decreased in demand from major trading partners, increase in trade costs, goods price volatility etc. India must focus on increasing its competitiveness in a variety of product categories. India has the potential to become a major global supplier of agricultural commodities. Strengthening regional trade linkages and expanding markets for Indian goods might minimize global demand volatility.

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