Indian Economy · GS - III

How would the recent phenomena of protectionism and currency manipulations in world trade affect macroeconomic stability of India?

EXAM YEAR	PAPER	SUBJECT
2018	GS - III	Indian Economy

MARKS	WORD LIMIT
15	~250 words

Answer Hint

Trade barriers; export competitiveness; exchange-rate volatility; current account deficit; inflation; capital flows; multilateral trade cooperation

Model Answer

Introduction

Protectionism involves restricting imports through tariffs, quotas or domestic-content requirements, while currency manipulation refers to policies intended to influence exchange rates for economic advantage. Both can disrupt India's macroeconomic stability.

Impact of Protectionism

1. **Exports and employment:** Tariffs imposed by trading partners can reduce demand for Indian goods, affecting sectors such as textiles, pharmaceuticals and engineering.
2. **Global supply chains:** Trade restrictions disrupt intermediate-goods supplies and raise production costs.
3. **Retaliation:** Countermeasures can intensify trade conflicts and weaken global demand.
4. **Domestic industry:** Selective protection may support infant industries, but prolonged protection can reduce competition and efficiency.

Impact of Currency Manipulation

1. **Export competitiveness:** An artificially undervalued trading partner's currency may make its goods cheaper relative to Indian products.
2. **Trade balance:** Cheaper imports may widen India's trade deficit, although the overall effect depends on demand elasticities and domestic production.
3. **Inflation:** Rupee depreciation raises the domestic cost of imported crude oil, fertilisers and electronics.
4. **Capital flows:** Exchange-rate uncertainty can increase risk premiums and discourage investment.
5. **External debt:** Depreciation raises the rupee cost of servicing foreign-currency debt.

Macroeconomic Consequences

These developments can increase inflationary pressures, widen the current account deficit, create volatility in financial markets and complicate monetary policy. However, a weaker rupee may also support exports and remittances.

Way Forward

India should diversify export markets, strengthen domestic manufacturing, improve logistics, maintain adequate foreign-exchange reserves and use exchange-rate flexibility alongside prudent macroeconomic management. It should also pursue rules-based trade through the WTO.

Conclusion

Protectionism and currency disputes pose risks to growth and external stability. Competitiveness, diversified trade and sound macroeconomic policies offer a more sustainable response than indiscriminate retaliation.

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