The Official D&I Newsletter

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Words of Visionaries

Module: Financial Dooms that Shook the World

At Dreamers & Innovators, the ongoing module: "**Financial Dooms that Shook the World**" is an ambitious endeavour to help young Dreamers comprehend the technicality prerequisite to understanding national and international economies. The module aspires to build awareness of economical concepts along with coursing through three historically significant financial crises. The overall aim is to build the knowledge & skill which shall help the Dreamers to analyse the current circumstances of the Pandemic and predict where we are headed economically.

This week's newsletter showcases the ideas of four promising Dreamers: Aryan, Aditya, Manek and Ananya, who provide you with a surgical analysis of the causes of India's BoP Crisis of 1991, and the drastic measure taken.

Dreamers & Innovators is a knowledge and skill-building platform for 21st century learners. We aspire, design and execute interactive learning experiences where global knowledge relevant to today and tomorrow is brought to young Dreamers. At D&I, 21st century skills are honed, confident communication is developed and independent, informed opinions are nourished.

Studying Causes of Grave Fiscal Deficit

Aryan Bansal
14 years

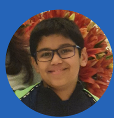
India, in the year 1991, faced an economic crisis during which inflation rose upwards by 17%, the food prices rose by 20% and the GDP throughout the 1980s was as low as 3.3%. Some events led to this crisis.

At the time of independenc, the prime minister, Jawahar Lal Nehru, inspired by Soviets, formulated policies that were inclined to socialism. However, this brought about an era we today call the License Raj. Businessmen faced a hard time just getting a license to register their businesses. Furthermore, private businesses that included oil, power, telecom and heavy machinery were banned. To add, the ongoing wars left the government in need of funds for Defense expenditure. During the time of consultation and meeting, India suddenly had political instability. Rajiv Gandhi withdrew his support from Chandra Shekhar's government. Taking note that IMF couldn't grant a loan to 2 governments of India to handle the economic crisis, a non-settled government just made things worse. To settle a government, Lok Sabha elections were held. Sadly, shortly after, Rajiv Gandhi was assassinated.

In 1991, one of the major suppliers of oil, Iraq, went to war with Kuwait. Since the government needed funds for the war they increased the oil prices, mainly leading our government to spend more on oil imports.

The Indian Ministry of Finance and RBI officials chose to ask the International Monetary Fund for a loan. During this time, the Cold War had recently ended. India was in cooperation with the Soviet Union which was USA's enemy. This affected the loan as the USA wouldn't grant a loan to one of its rival's allies easily.

Tough Times, Tough Measures



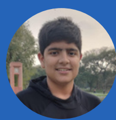
Aditya Verma
13 years

The BoP economic crisis of 1991 was one of the most devastating economic crises that India has suffered. The trade deficit increased from Rs. 12,400 crore in 1989-90 to Rs. 16,900 crore in 1990-91. The current account deficit increased from Rs. 11,350 crore in 1989-90 to Rs. 17,350 crore in 1990-91.

There were several reasons for this ranging from the Iraq-Kuwaiti War in the Middle East, which resulted in oil imports prices increasing exponentially and trade deficit value skyrocketing, all the way up to political instability caused due to the formation of 3 separate coalition governments; loss of investors' confidence in India due to economic instability; worst of all, the slow growth of important trading partners like the US. India's foreign exchange reserves were at USD 1.2 billion in January 1991 and depleted by half by June, an amount barely enough to cover roughly three weeks of essential imports. India was only weeks away from defaulting on its external balance of payment obligations.

The Government of India's immediate response was to secure an emergency loan of USD 2.2 billion from the International Monetary Fund by pledging 67 tons of India's gold reserves as collateral. The Reserve Bank of India had to airlift 47 tons of gold to the Bank of England and 20 tons of gold to the Union Bank of Switzerland to raise USD 600 million. These moves helped tide over the balance of payment crisis temporarily and kick-started P V Narasimha Rao's economic reform process.

Narrating India's BoP Crisis



Manek Mehra
13 years

It was a scary sight to see, the world's largest democracy, India, was now out of money. Only a week's supply to feed 830 million people. This isn't out of a movie, this isn't fiction, this is history. The situation mentioned above was happening in 1991. Let's take a look at what actually led to this horror.
During 1947 and after, India underwent many events which led to this horrific situation. First of all, there were the wars with our neighbouring countries, China and Pakistan, two very powerful countries with massive armies. There were the first Kashmir War right after independence from 1947 - 48, the Sino Indian war of 1962, the Indo-Pak war of 1965, the Sino India war of 1967, the Indo-Pak war of 1971.

There were many other factors as well which led to India's bankruptcy. There were many droughts during this time period especially in 1965 and 1966, where India's primary activity, agriculture, took a turn for the worse. The food prices were said to have risen up to 20%, the inflation by 17% and the GDP during this period was as low as 3.3%. Which meant India now had to export food which cost a lot from the country's budget. There was also another big reason. Political instability was a common sight to see. Most terms didn't last more than three years and the prime ministers kept changing. Each prime minister had a different plan or approach towards improving the standards of living in India.

Now, imagine, with so many different plans already working from the last leadership, would it be possible to even get one of these plans accomplished? These are some of the events that led to the turmoil in the Indian economy in 1991.

A Loan or a Drastic Step?

Ananya Jalan
14 years

The Balance of Payments Crisis of 1991 was one of the worst issues that the Indian economy has ever faced. Many events like the Iraq-Kuwait War leading to a hike in the prices of oil and the end of the Cold War with US coming out as the ideological victor had put India in an awful situation.

The inflation rate had risen year-on-year after Independence touching an all-time high of 20% on consumable goods and 17% on durable goods. The tax laws were not resulting in any positive hope. After the collapse of the Soviet Union, with their ally lost, foreign trading too had become a hapless avenue for India. To add on top, the failure in the agricultural sector imposed the burden of subsidising agriculture and increased expenditure on food imports.

India's forex reserves took a huge dip and resulted in a major deficit. To prevent an even more negative outcome, India took a loan of 1.8 billion dollars from the International Monetary Fund.

Before granting the loan, the IMF imposed three conditions. First, to liberalise the country's economy. Second, to allow international brands and companies into India. Third, to devalue the Rupee by 20% against the US Dollar. After accepting these conditions India was able to gain a temporary support which led to recovery.