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A study on foreign exchange reserves in India in the post liberalization ERA

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Abstract
India's economic reform since 1991 has been catalyst in shaping the performance of the economy. No doubt the economy has been brought to a higher growth trajectory, emerged as one of the fastest growing economies in the world and minimized many of the apparent inefficiencies that were persistent before the reform; however, it is overwhelmed by various socio-economic problems. This paper is primarily concerned with an analysis of the growth and trends in the foreign exchange reserves of India. It is based on secondary data and the data reliable for analysis are collected from handbook of statistics on Indian economy and the website of Reserve Bank of India. The study covers the period of 1991 to 2017. The collected data have been used for analysis with the help of compound growth rate. The analysis of the data reveals that foreign exchange reserves have significantly changed over the years. All the indicators noticed notable growth rate during the period under review. From the overall analysis showed that India holds adequate level of foreign exchange reserves.

Keywords: Economy, reform, reserve bank of India, compound growth rate, foreign exchange reserves

1. Introductions
In simplest terms foreign exchange reserves are the foreign currencies which are held by the central bank to support liabilities on the issued currency and also a way to influence the monetary policies of the country. It includes government securities, bonds, bank notes, bank deposits and treasury bills.
Regardless of the size of the economy almost all countries in the economy hold significant foreign exchange reserves and most of them being held in U.S dollars which is the most traded currency. Other currencies in reserves are British pound sterling, euro, Chinese Yuan, and Japanese Yen. Theorists believe that holding reserves in currencies which is not immediately connected to its own is best policy. China had the largest foreign exchange reserves $3520.4 billion in the year 2016.
The holding of forex is used to back the one's domestic currency. Countries who wish to have fixed exchange rate uses forex reserves as a tool of monetary policy. Central institution has ability to exert some control over exchange rates by retaining the option to shove reserves from another currency in to the market.

1.1 Components of Foreign Exchange Reserves
Special Drawing Rights
"The SDR is an international reserve asset, created by the IMF in 1969 to supplement its member countries' official reserves. In 2016, 204.1 billion SDRs (equivalent to about $285 billion) had been created and allocated to members. SDRs can be exchanged for freely usable currencies. The value of the SDR is based on a basket of five major currencies—the U.S. dollar, euro, the Chinese renminbi (RMB), the Japanese yen, and pound sterling.

1.1.1 The role of the SDR
The SDR was created by the IMF in 1969 as a supplementary international reserve asset, in the context of the Bretton Woods fixed exchange rate system. A country participating in this system needed official reserves government or central bank holdings of gold and widely accepted foreign currencies-that could be used to purchase its domestic currency in foreign exchange markets, as required to maintain its exchange rate.
But the international supply of two key reserve assets gold and the U.S. dollar proved inadequate for supporting the expansion of world trade and financial flows that was taking place.

Therefore, the international community decided to create a new international reserve asset under the auspices of the IMF.

1.2 Significance of the Study
Foreign Exchange Reserves accumulation has gained significance both for the welfare of the nation internally and internationally. The study has its implications beneficial to policymakers, various officials of government, investors both from domestic and abroad as well as Non-resident Indians, academicians and future researchers. The study possesses academic relevance in new theoretical and practical knowledge undoubtedly. In this light of its importance, an attempt on foreign exchange reserves has been undertaken with the specific objectives

2. Gold Reserves
Gold played a central role in the international monetary system until the collapse of the Bretton Woods system of fixed exchange rates in 1973. Since then, its role has diminished. But it remains an important asset in the reserve holdings of several countries, and the IMF is still one of the world's largest official holders of gold. In line with the new income model for the Fund agreed in April 2008, profits from limited gold sales were used to establish an endowment, and used to boost the IMF's concessional lending capacity to eligible low-income countries (LICs).
The IMF holds around 90.5 million ounces (2,814.1 metric tons) of gold at designated depositories. On the basis of historical cost, the IMF's total gold holdings are valued at SDR 3.2 billion (about $4.5 billion), but at current market prices, their value is about SDR 80.1 billion (about $112.7 billion). When the IMF was founded in 1944 it was decided that 25 percent of initial quota subscriptions and subsequent quota increases were to be paid in gold. This represents the largest source of the IMF's gold.

3. Importance of Foreign Exchange Reserves
Foreign exchange reserves increase the confidence in the monetary policies as well as exchange rate policies of the government. The capacity of the central bank to intervene in foreign exchange market and to control any adverse movement is enhanced. Also, the capacity to stabilize the forex rates to provide more favorable economic environment for the country is also enhanced.
During the crises forex reserves come to the rescue of any country and absorb the distress or shocks. Domestic currency gets backed by external assets and is good for equity market since the forex reserves are strong then people from different countries wants to invest in the country.

4. Objective of the study
- To understand the theoretical framework of forex reserves and their significance in the economic development.
- To statistically analyze the trends in the Forex Reserves of India.

5. Research Methodology
Data for the study is collected from Secondary sources. The study is based on published sources of data collected from journals, magazines, websites like i.e. www.rbi.org.in. Central Statistical Organization (CSO), Handbook of Statistics on the Indian economy were used. The data for this study was collected from the time period 2001 to 2015.

6. Results and Discussions
The regression statistics, for the growth of different policy periods, explains significant or insignificant levels of different growth rates of foreign exchange reserves in India for different policy periods.

Table 1: Regression Statistics of Foreign exchange reserves in India

	Coefficients	Standard Error	t Stat	P-value
Intercept	8.303286254	0.12261127	67.72041619	4.02803E-24
Time	0.364631521	0.044771306	8.144312876	1.2838E-07
D2	1.183317379	0.198427604	5.963471579	9.70401E-06
D2T	-0.26161416	0.048604638	-5.382493634	3.40786E-05
D3	-0.32559312	0.370290805	-0.879290332	0.390229351
D3T	-0.11292595	0.050765889	-2.224445528	0.038435206
D4	3.642281105	0.278453833	13.08037699	5.96154E-11
D4T	-0.33373646	0.046108056	-7.238137726	7.16777E-07

Source: RBI Handbook

The findings of the study clearly indicates that during the period of liberalization, the initial level of foreign exchange reserves of India was positive and it grew at 43.99%, which is statistically significant also, as P-value is less than 0.05 (5%). During the period of globalization, the level of foreign exchange reserves increased in comparison to liberalization, but the growth rate decreased drastically from 43.99% to 10.85%.

Table 2: Growth rate of Foreign exchange reserves for different policy periods

Policy Period	Intercept	ACGR (%)	About Growth Rate
Liberalization	8.303286254	43.99833074	Significant
Globalization	9.486603633	10.85106592	Significant
World recovery	8.303286254	28.62172766	Significant
Global Financial Crises	11.94556736	3.137726701	Significant

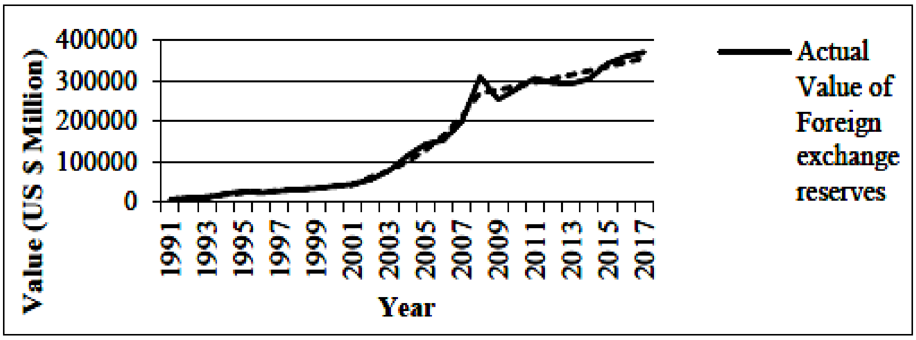
Source: RBI Handbook

This is a situation of "euphoria". Both the level of foreign exchange reserves and the growth rate are statistically significant. This means that globalization had a significant impact on the foreign exchange reserves of India. As far as the period of world recovery is concerned, it is observed that the level of foreign exchange reserves has not changed as compared to liberalization, as the value of D3 is not statistically significant. But the growth rate has decreased to 28.62% as compared to liberalization, which is statistically significant also. This implies that world recovery period had a significant impact on the growth rate of foreign exchange reserves in India. The period of global financial crises witnessed large amount of increase in the level of foreign exchange reserves in India in comparison to liberalization (intercept D4) and it is statistically significant also, but the growth rate has decreased drastically as compared to liberalization. This was mainly due to the outward flow of funds from India. India was less affected from the crises, as compared to other countries, due to increased level of foreign exchange reserves during the period of crises as compared to liberalization.

Table 3: Foreign Reserves in India Between 2001 to 2015

Year (End of March)	Gold	RTP	SDR	Foreign Currency Assets	Total
2001	127	29	0.11	1845	2001
2002	149	30	0.5	2491	2670
2003	168	32	0.19	3415	3615
2004	182	57	0.1	4662	4901
2005	197	63	0.2	5931	6191
2006	257	34	0.12	6473	6764
2007	296	20	0.08	8366	8682
2008	401	17	0.74	11960	12380
2009	488	50	0.06	12301	12839
2010	812	62	226	11497	12597
2011	1026	132	204	12249	13610
2012	1383	145	229	13305	15061
2013	1397	125	235	14126	15884
2014	1296	110	268	16609	18284
2015	1192	81	249	19855	21376

Source: RBI Handbook



Source: RBI Report

Fig 1: Growth Curve of Foreign exchange reserves

The growth curve clearly indicates that during the entire period of study (1991-2017), there was significant growth in the value of foreign exchange reserves in India. The figure 6.1 basically shows the upward trend in the differential growth of foreign exchange reserves between liberalization and other policy periods. During liberalization, there was growth in the value of foreign exchange reserves. As far as the globalization period is concerned, there was again significant growth in the value of foreign exchange reserves. This was mainly due to increasing FDI inflows into India.

The value of foreign exchange reserves declined during the period 2007-2009, due to global financial crises as can be seen in the figure 6.1. One of the reasons identified for decline in foreign exchange reserves during the above said period was outflow of FDIs and FIIs from India. Still, India was less affected from the global financial crises and soon observed rise in the foreign exchange reserves. India witnessed an upward trend in foreign exchange reserves 2009 and thereafter.

7. Conclusion

The paper has analyzed the impact of different policy periods on trends in foreign exchange reserves in India. The four policy periods, i.e., Liberalization, Globalization, World Recovery and Global Financial Crises are being considered for the analysis. The above analysis conclude that the level of foreign exchange reserves is statistically significant in all the policy periods except world recovery, and the growth rates are also significant in all the policy periods. The current paper can be of great use for the policy makers as it will help them to analyze the trends in foreign exchange reserves in India not only during various policy periods but also in predicting the future trends of the foreign exchange reserves. The present study has mainly concentrated on the trends in foreign exchange reserves during various policy periods. However, there are various factors like exports, FDIs, FIIs, ECBs, debt repayment etc. which also influence the level of foreign exchange reserves. Further researches can be undertaken in examining the impact of these factors influencing the level of foreign exchange reserves in India. Though the current paper has focused only on one country (India) leaving the scope for further research by doing comparative analysis for other emerging economies.

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