



Current Account Deficit

For Prelims: Current account deficit (CAD), Fiscal Deficit, Government Budgeting, Foreign Exchange Reserves

For Mains: Issues Related to CAD, Recent Status of India's CAD.

Why in News?

Recently, the government released data showing that **India's exports and imports decreased by 6.59% and 3.63%**, respectively, in January 2023, there are indications that the country's **current account deficit (CAD)** will moderate despite the global slowdown triggered by the rising inflation and interest rates.

- The moderation in CAD is expected to be aided by the fall in commodity prices, rising workers remittances and services exports, and abatement of selling pressure by foreign investors.

What is the Current Account Deficit?

- **About:**
 - **Current account deficit (CAD)** is when the value of a **country's imports of goods and services is greater than its exports.**
 - **CAD and fiscal deficit** together make up twin deficits that can impact the stock market and investors.
 - **Fiscal Deficit is the gap between the government's expenditure requirements and its receipts.** This equals the money the government needs to borrow during the year.
- **Implication:**
 - The CAD is significant because it affects the **economy, stock markets, and people's investments.**
 - **A lower CAD can boost investor sentiment** and make the country's currency more attractive to investors.
 - A surplus in the **current account** indicates that **money is flowing into the country,** which can **boost foreign exchange reserves** and the **value of the local currency.**
- **Recent Status of India's CAD:**
 - The CAD for the first half of 2022-23 was **3.3% of GDP**, but the situation improved in Quarter 3:2022-23 due to **lower commodity prices and moderated imports.**
- **Negative Effects of CAD on Economy:**
 - **Weaker Currency:** When a country's imports exceed its exports, it can cause a **decrease in demand for its currency,** leading to a weaker currency value (depreciation).
 - This can **make imports more expensive,** leading to higher inflation and a reduction in purchasing power.
 - **Debt Accumulation:** If a country is unable to finance its current account deficit with foreign investment, it may need to borrow to cover the gap.
 - This can lead to an **increase in debt levels, which can further harm the**

economy.

How India can Moderate Current Account Deficit?

- **Encourage Exports:** Increasing exports is one of the most effective ways to reduce CAD.
 - The government can provide incentives for **export-oriented industries**, **streamline export procedures and regulations**, and negotiate better trade agreements with other countries.
- **Promote Import Substitution:** Encouraging domestic production of goods that are currently being imported can help to reduce the trade deficit.
 - This can be **achieved by providing incentives for domestic manufacturers** and by imposing tariffs or import duties on certain goods.
- **Improve Productivity and Competitiveness:** Improving the productivity and competitiveness of the domestic economy can help to increase exports and reduce the trade deficit.
 - This can be achieved through various measures such as **investments in infrastructure, technology, and education**.

Conclusion

The reduction in CAD in January 2023, driven by a fall in imports, is seen as a positive sign by experts, but it needs to be sustained over many more months to alleviate concerns about the country's external account. **Maintaining a healthy CAD is important for the value of the currency** and the overall health of the economy.

UPSC Civil Services, Previous Year Question (PYQ)

Q1. Consider the following actions which the Government can take: (2011)

1. Devaluing the domestic currency.
2. Reduction in the export subsidy.
3. Adopting suitable policies which attract greater FDI and more funds from FII's.

Which of the above action/actions can help in reducing the current account deficit?

- (a) 1 and 2
- (b) 2 and 3
- (c) 3 only
- (d) 1 and 3

Ans: (d)

Q2. With reference to Balance of Payments, which of the following constitutes/constitute the Current Account? (2014)

1. Balance of trade
2. Foreign assets
3. Balance of invisibles
4. Special Drawing Rights

Select the correct answer using the code given below:

- (a) 1 only
- (b) 2 and 3
- (c) 1 and 3
- (d) 1, 2 and 4

Ans: (c)

Source:IE

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