

# THE EXTERNAL SECTOR

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*with C. J. Batliwalla\**

The economic and financial developments taking place during our years in the external sector of the Indian economy set the context for the three chapters which comprise this part. To a greater extent than the other chapters of this volume whose approach is primarily Bank-centred, the next three chapters present a survey of the relevant developments in India's external economic policies and financial diplomacy, and an account of the Bank's role in relation to them. However, a note of caution is in order here. The wider history presented in these pages is based on materials at the Bank and those in public archives. Therefore, these chapters do not purport to offer a comprehensive, much less definitive, history of developments in India's external sector.

The opening chapter of this part (chapter 15) deals largely with issues of reserve utilization and management arising from India's membership of the sterling area and the restrictions arising therefrom. Some new material has become available to researchers after the last volume of the Bank's history saw the light of day nearly three decades ago. For this reason and in the interests of expository convenience, the chapter also gives a brief background account of sterling balance negotiations which took place in the years immediately preceding those covered by this volume. The restrictions Britain

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\*Chapters 15–17 and appendixes F and G have been written with C.J. Batliwalla, to whom I am grateful for painstaking research and attention to matters of fact and detail. She is the sole author of Appendix E.

imposed on India's use of its wartime sterling acquisitions were progressively relaxed at the same time as the latter were liquidated to finance the early stages of the second plan, and India's efforts to come to terms with the challenges posed by the likely and actual restoration of sterling convertibility are also documented here. Finally, the external outlook during these years was influenced by the effects on Indian trade of Britain's 'dollar shortage' problem, and a certain nervousness which surfaced from time to time about the stability of the sterling. The Indian evaluation of these factors and discussions at the Bank about the exchange rate policy India should adopt in the event of prolonged instability in the international currency markets are also covered briefly in the opening chapter.

Chapter 16 is devoted to an account of India's efforts to mobilize external resources to meet the longer-term financing needs of the second and third plans, the short-term balance of pressures to which the Indian economy was subject during these years, and the manner in which the Bank and the government sought to cope with them.

The third and final chapter in this part picks up the financing story from about 1963, when there was a perceptible deterioration in India's aid environment. The strain on the country's external finances during the next four years was worsened by the effects of severe droughts and a freeze in western aid. The resulting crisis led to the rupee's controversial devaluation in June 1966 and the inauguration of significant external sector reforms some of which had later to be rolled back or reversed because of the aid environment continuing to be adverse. Chapter 17 thus concludes with an account of the devaluation and its immediate aftermath.

There are three appendixes (E, F, and G) at the end of the book, relating to this part of the volume. The first describes the administration of exchange control in India during our period. The second discusses the country's role in negotiating quota increases at the International Monetary Fund, while the third offers a brief account of the working of India's bilateral trade agreements with the erstwhile Soviet Union and the centrally planned economies of eastern Europe.