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Vivek Saingar, student of International Medical Institute, Kursk State Medical University, Kursk, Russia

Email: viveksaingar2708@gmail.com

Science tutor: Vlasova Olga Vladimirovna, head of Economics and Management department of Kursk State Medical University

## EFFECT OF CURRENCY DEVALUATION ON SMALL AND MEDIUM FIRMS IN INDIA

**Abstract:** currency devaluation can have significant impacts on small and medium-sized enterprises (SMEs) in India. This study examines how currency devaluation affects these firms, focusing on aspects such as purchasing power, export-import dynamics, business profits, and financial stability.

**Keywords:** SMEs, purchasing power, export-import dynamics, India

Вивек Сайнгар, студент Международного медицинского института Курского государственного медицинского университета, Курск, Россия

Электронная почта: viveksaingar2708@gmail.com

Научный руководитель: Власова Ольга Владимировна, и.о.заведующего кафедрой экономики и менеджмента ФГБОУ ВО «Курский государственный медицинский университет

## ВЛИЯНИЕ ДЕВАЛЬВАЦИИ ВАЛЮТЫ НА МАЛЫЕ И СРЕДНИЕ ФИРМЫ В ИНДИИ

**Аннотация:** девальвация валюты может оказать значительное влияние на малые и средние предприятия (МСП) в Индии. В этом исследовании рассматривается, как девальвация валюты влияет на бизнес, уделяя особое

внимание таким аспектам, как покупательная способность, динамика экспорта и импорта, прибыль и финансовая стабильность.

Ключевые слова: малые и средние предприятия, покупательная способность, динамика экспорта и импорта, Индия

Imagine a seesaw with your import pricing on one side and your export prices on the other. Devaluation of currency is comparable to someone abruptly shifting their weight on a seesaw. The small and medium-sized enterprises (SMEs) in India may find this transition challenging. The process by which the government reduces a nation's currency's value in relation to other currencies is known as currency devaluation. Consider this: the rupee has lost value if one US dollar was worth 70 Indian rupees, and it is now worth 80. As a result, while Indian enterprises must pay much more for imported raw materials, foreign purchasers may find Indian products more affordable.

The most evident and often shocking effect of devaluation is the rise in the cost of imported raw materials. All companies are impacted by this effect, but manufacturing and processing industries that heavily rely on imported components are most affected. Examine a graph that shows the percentage increase in manufacturing costs on the y-axis and the percentage of devaluation on the x-axis to demonstrate this effect. A high rising curve indicates a direct link. Let's examine one specific instance, the textile industry, which plays a significant role in the Indian economy. A 10% devaluation of the rupee directly raises the price of the final product, possibly increasing the cost of imported chemicals, dyes, and specialized equipment [1].

Currency devaluation fundamentally alters the competitive landscape for small and medium enterprises (SMEs) engaged in export activities. When the local currency weakens against foreign currencies, Indian SMEs often experience an immediate rise in their export competitiveness, as their goods become relatively cheaper for international buyers. This phenomenon can stimulate demand abroad, potentially leading to increased export volumes. However, the benefits are countered by rising import costs, particularly for SMEs that rely on foreign raw materials and components, which can strain profitability and operational viability. As highlighted in research

related to other emerging markets, such as Nigeria, SMEs must adapt by employing strategies focused on local sourcing and effective cost management to cushion the adverse effects of currency fluctuations on their operational effectiveness. Thus, the net impact of currency devaluation on export competitiveness is nuanced, necessitating a careful balance between leveraging new opportunities and mitigating inherent risk. SMEs form an integral part of the Indian economy, which represents 30% of its GDP and 48% of exports while employing over 110 million individuals. Despite such apparently enviable statistics, businesses at the lower level are not bereft of issues related to inadequate credit facilities, obsolete technology, and regulatory challenges, among others. An example of such external factors that businesses face is the devaluation of currency, which will negatively impact their profitability and competitive positioning in the global scenario [1,2].

This document explores how currency devaluation affects Indian SMEs and presents strategies and policy recommendations to mitigate its impact.

Currency devaluation significantly influences the pricing of Indian goods in international markets, particularly affecting small and medium enterprises (SMEs). When the Indian rupee loses value against other currencies, the cost of Indian exports decreases, making them more competitively priced abroad. This situation boosts demand, as foreign buyers can purchase goods at a lower cost compared to those from countries with stronger currencies. However, the benefits of this scenario can be offset by the rising costs of imported raw materials and components, which SMEs often rely on to produce their products. As highlighted in various studies, such a disparity leads to challenges in maintaining profit margins and sustaining operational viability ((Gulati et al.); (Chadha et al.)). Consequently, while currency devaluation may initially enhance the competitiveness of Indian goods internationally, the resultant fluctuations in input costs can ultimately complicate the economic landscape for SMEs in India [1,2,3].

Currency devaluation, or the decline of the Indian Rupee's value, is influenced by:

1. Global Economic Trends: Recessions or crises prompt capital flight from emerging markets, weakening the Rupee.

2. Trade Deficits: India's persistent import-export imbalance creates demand for foreign currencies.

3. Inflation: Relatively higher inflation than that of trading partners depreciates the Rupee.

4. Policy and Political Uncertainty: Instability shakes off investors' confidence and thus creates capital outflows

Added to this are increasing oil prices, a strong US Dollar, and foreign investor withdrawals-which all make life hard for SMEs dependent upon either imported raw materials or foreign credits [1,2,3,4].

#### Key Challenges of the SMEs

##### 1. High Rising Cost of Imports

Devaluation increases the price of imported raw materials, machinery, and technology that SMEs rely on. For example:

A 10% Rupee devaluation raises the cost of production for manufacturers importing components such as steel or electronics.

SMEs, in most cases, cannot pass these costs on to customers, and hence their profit margins are squeezed.

Imported machinery or software becomes too expensive, thereby reducing productivity and innovation.

##### 2. Costlier Foreign Credit

Devaluation increases the cost of servicing loans in foreign currencies. SMEs may face:

Higher interest rates or more stringent lending terms by foreign creditors.

Inability to finance new machinery or technology.

##### 3. Pressure on Profit Margin

Lower profits mean reduced operational budgets, which delay expansions and investments in innovation. For example, manufacturers who are compelled to use

cheaper alternatives may compromise on quality and hence risk their long-term competitiveness.

#### 4. Global Market Challenges

Although a weak Rupee is supposed to make Indian exports cheap, SMEs dependent on imported inputs find it difficult to gain from the price advantage due to the increase in import costs. Fluctuating currency values also complicate the issue of long-term contracts across borders.

The government of India and the Reserve Bank of India have prepared various schemes to support SMEs during currency fluctuations. Some of these are discussed below:

##### 1. Financial Assistance

Interest rate subvention and credit guarantee schemes like ECLGS help SMEs maintain liquidity.

Platforms like TReDS ensure timely receivables from corporate buyers.

##### 2. Export Promotion

The enhanced incentives and market access initiatives are inducing SMEs to ramp up their exports.

The support for participation in international trade fairs helps them increase visibility in global markets.

##### 3. Skill Development

Training programs on forex management and international trade practices help make currency risks manageable for SMEs.

##### 4. Buy Locally, Source Locally

The PLI Scheme provides for incentives for manufacturing in the country itself, thus making reliance on costly imports unnecessary.

#### Case Studies: Thriving Strategies in Devaluation Times

##### 1. Tech Innovator-Bangalore

Due to higher import cost of software, the SME refocused on the export markets, dynamic pricing, and negotiated Rupee-based contracts with service providers. This has resulted in an increase in international clients by 40% within one year.

## 2. Auto Parts Manufacturer (Pune)

The company reduced its dependence on imports by buying 70% of the materials locally and investing in R&D. Improved processes and innovative designs helped maintain profit margins despite a 15% increase in cost.

## 3. Organic Spice Exporter, Kerala

This SME leveraged a weak Rupee to expand into new markets in Eastern Europe and Australia. Revenue increased by 30% due to hedging strategies and premium product offerings.

### Recommendations for Policymakers

The government could help SMEs tide over the currency devaluation by:

#### 1. Improving Financial Support

Streamline credit facilities such as ECLGS and make forex hedging instruments available at subsidized rates.

#### 2. Exports

Targeted incentives and simplification of access to foreign markets for SMEs.

#### 3. Skills

Initiate forex and trade management training programs in vernacular languages.

#### 4. Local Supply Chains

Tax exemptions and subsidies to SMEs that use domestic sourcing solutions.

#### 5. Awareness

An online single window with up-to-the-minute information on currency trends, government schemes, and trade opportunities.

The impact of increased import costs on the operational expenses of small and medium enterprises

The rising import costs, exacerbated by currency devaluation, pose significant challenges for small and medium enterprises (SMEs) in India, particularly in their operational expenses. As the Indian rupee depreciates, the price of imported raw materials and components escalates, directly impacting the cost structure of SMEs that rely on these inputs for production. Increased expenses diminish profitability, forcing businesses to either absorb the costs or pass them on to consumers, potentially leading

to reduced demand. This situation is further complicated by the fact that many SMEs lack the financial resilience to weather such economic fluctuations. Moreover, the pressing need for cost control becomes paramount; SMEs may need to consider local sourcing of materials to mitigate the impact of higher import prices, a strategy reflected in the successes of SMEs in other economies facing similar challenges. Ultimately, without strategic adaptations, SMEs risk compromising their competitive position in the market.

Long-term Strategies:

Deepening India's macroeconomic stability will decrease its currency volatility.

Invest in infrastructure to cut down on logistics costs and move towards competitiveness.

Creation of an innovation ecosystem to help SMEs develop high-value, low price-sensitive products [5].

In conclusion, the devaluation of currency presents a complex landscape for small and medium enterprises (SMEs) in India, impacting their operations and growth trajectories in multifaceted ways. While a weaker currency can enhance export competitiveness by making Indian goods more affordable in international markets, it simultaneously raises the cost of imported raw materials and technology, thereby straining operational budgets. The dual nature of these effects necessitates that SMEs adopt adaptive strategies to mitigate the adverse impacts while capitalizing on potential export opportunities. Furthermore, government support and well-structured policies are crucial in cushioning SMEs against the immediate financial volatility associated with currency fluctuations. Ultimately, the resilience of SMEs in the context of currency devaluation will hinge on their ability to navigate these challenges through innovation, financial planning, and strategic partnerships, which are essential for sustaining their contributions to Indian economic development. While Indian SMEs do face serious problems arising out of currency devaluation, an outcome of increasing costs to global market instability, with proactive strategies, innovation, and strong government support, the SMEs will not only survive but also thrive during such times.

By building resilience and adaptability, India can make sure that its SME sector will keep on contributing as a major driving force towards its economic growth.

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