Institutional Determinants of Monetary Sovereignty: A Case Study

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I. INTRODUCTION

States' control over their domestic monetary and financial systems is a critical and generally underappreciated part of their sovereignty. In recent years, the literature on monetary sovereignty has emphasized how most states generally enjoy weak monetary sovereignty.[1] In her article *From Territorial to Monetary Sovereignty*,[2] Katharina Pistor argues forcefully, for example, that "if the question of sovereignty was tied not

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1. Katharina Pistor, *From Territorial to Monetary Sovereignty*, 18 THEORETICAL INQUIRIES IN L. 491 (2017).

2. *Id.*

to effective control over territory and people but to effective control over money, including state and private moneys, most states in this world would fail the test of sovereignty."[3] Pistor argues that only a very few countries—the U.S., the U.K., Canada, Japan, Switzerland, Australia, and China[4]—are "sovereign in monetary terms" and that these states are at the top of a hierarchical international monetary and financial system.

According to this account, only states that issue their own currencies can retain control over their monetary affairs.[5] States that issue their own currency may nonetheless effectively cede or lose control over their monetary and financial systems to the influence and impacts of private actors and financial markets. This is especially true where domestic monetary and financial policymaking is heavily dependent on external forces through capital flows or external debt denominated in foreign currencies. The consequences of such constraints on sovereignty are most apparent and dire during times of crisis, when states are unable to independently respond to systemic financial and economic vulnerabilities.[6] As Pistor writes: "Every crisis puts to a test the ability of states to rescue the domestic money system without recourse to external help. Some countries can help themselves and others can't. External help always comes with strings attached and constrains autonomous decision making." [7] At such times, "[o]nly countries that house intermediaries in the business of exporting money can maintain basic principles of democratic self-governance . . . ."[8]

This Article generally embraces but critically expands upon Pistor's account of monetary sovereignty by examining the case of India. While India is not among the countries that Pistor identifies as enjoying monetary sovereignty, its circumstances are quite different than those states she assigns to the periphery, or lower in the hierarchy, of the international monetary and financial system. India arguably retains more sovereignty in this regard than Pistor's account would ascribe to it. The claim here is not that India is unique in this regard, but rather, that it is illustrative. The case of India demonstrates that countries may not enjoy full monetary sovereignty but can reduce the extent of this vulnerability, maintain a robust degree of control over their monetary and financial

3. *Id.* at 493.
4. *Id.*
5. *Id.* at 492.
6. *Id.* at 497.
7. Katharina Pistor, *From Territorial to Monetary Sovereignty*, 18 THEORETICAL INQUIRIES IN L. 491, 494 (2017).
8. *Id.* at 516.

systems, and, thereby, insulate democratic self-governance. It also reflects the potential trade-offs in economic performance and social welfare that states may need to make to limit their integration with global monetary and financial systems.

As described in detail in Part III, below, India's economy was very controlled and insular in its first decades of independence. Since the 1990s, the country has embraced a wide range of gradually liberalizing reforms and has increasingly integrated its economy with the global economy.[9] Yet, it has deliberately and carefully maintained a significant amount of state control over its economy, including its monetary and financial systems. In particular, the country still heavily manages factors that generally erode a country's control over its monetary affairs—e.g., private money creation, cross-border capital flows, and levels of external debt.

While the country has opened its capital account in important ways in recent decades, it still actively manages a wide-ranging array of de jure and de facto limits on capital flows, both inward and outward.[10] Private external debt in India has been steadily increasing since the financial reforms of the 1990s, yet India has less external debt as a percentage of its gross domestic product (GDP) than many other emerging economies, and much of it is owed in rupees.[11] Furthermore, a large portion of that external debt is held in domestic bank accounts payable to non-resident Indians.[12] Relatively little of it is owed to other sovereigns or international financial institutions.[13] Its public external debt is not denominated in foreign currency.[14] Finally, India's sovereignty over private domestic money creation is quite robust, as elements of "shadow banking" ubiquitous in other jurisdictions are highly constrained there.[15]

India thus appears to enjoy a meaningful quantum of control over its monetary affairs, which in turn serves to help insulate its democratic self-governance. But at what cost? Maintaining or ceding monetary sovereignty involves trade-offs between control on the one hand and liberalization and integration with the global economy on the other. And

9. As a rough measure of integration over time, India's trade as a percentage of its GDP has gone from around ten percent in the 1970s to around twenty-five percent at the turn of the century and is now around forty-five percent. *See Trade (% of GDP)—India*, WORLD BANK GRP., https://data.worldbank.org/indicator/NE.TRD.GNFS.ZS?locations=IN.

10. *See infra* Part III.B.

11. *See infra* Part III.C.

12. *See infra* note 172 and accompanying text.

13. *See infra* Part III.C.

14. *See infra* note 201 and accompanying text.

15. *See infra* Part III.D.

these trade-offs have important implications for economic growth and social welfare.

Understanding various regulatory and macroeconomic policies in India as defining the extent of its monetary sovereignty provides a useful frame for evaluating the development of such policies to date and into the future. The direction of policymaking in the country has, across different governments, continued to be one of cautious, managed, and fitful liberalization. Policymakers have viewed such liberalization as a pathway for improving financial markets and increasing economic development in the country, thereby improving social welfare.[16] But it appears they have consistently weighed these benefits against those of maintaining a significant degree of state control over the economy.[17]

The policies that support India's sovereignty in this regard—the institutional determinants of its monetary sovereignty—have been credited with enabling the country to weather the global financial crisis of 2008-09 better than many other jurisdictions.[18] And they may have reserved for India more space for routine, non-crisis economic and financial policymaking. It is possible, however, that the generally cautious approach of government stewards of the domestic economic and its financial system has unnecessarily slowed the country's growth and development.[19] In particular, India's policies that help it maintain control over its monetary and financial affairs may have come at the cost of limiting the availability of financial resources in the country as well as the potentially disciplining force of external assessments. In other words, the degree of India's monetary and financial sovereignty at any particular point in time is a function of the balance among and between policies aimed at control, stability, and development. It is beyond the scope of this Article to assess these trade-offs or evaluate the country's economic policymaking. The goal instead is limited to observing that a balance is presumably being struck between monetary control and economic growth and to identifying some of the primary tools employed in striking that balance.

India's situation illustrates the array of institutional arrangements and governmental policies that determine a state's control over its monetary and financial affairs. This provides a useful framework for assessing where other states fall along a spectrum of monetary sovereignty. It also allows for an evaluation of the relative strength and

16. *See infra* Part III.A.
17. *See infra* Part IV.
18. *See infra* notes 56, 61 and notes 90, 112, 113 for accompanying text.
19. *See* discussion *infra* Part III.D.

vulnerability of monetary sovereignty and control in states that are perceived to be at the top of the monetary hierarchy. Thus, this analysis may provide a way forward to understanding a more complicated hierarchy of monetary sovereignty.

This Article proceeds as follows. Part II provides a brief overview of the concept of monetary sovereignty and describes the contemporary literature on the topic, including Pistor's contribution. Part III briefly surveys relevant aspects of India's economic and financial history and then examines some of the core policies that determine the degree of its control over domestic monetary and financial affairs: management of its capital account, the amount and composition of its public and private external debt, and the extent of domestic private money creation. The Article concludes by observing key applications and implications. Identifying and understanding the distinct determinants of India's control over monetary affairs can help inform recurring domestic debates over these policies by underscoring the trade-offs they necessarily involve and the potential stakes for democratic self-governance.

II. ON MONETARY SOVEREIGNTY

As Claus Zimmermann has noted, "[f]ew legal concepts have been subject to as little critical scrutiny over the past decades as that of monetary sovereignty."[20] To be sure, scholars and commentators have long understood that control over domestic money and monetary affairs is one of the baseline components of state sovereignty.[21] Yet the existence of sovereignty over monetary affairs has rarely found formal expression under international law. The first and probably still most authoritative formal recognition of monetary control as a part of sovereignty is the 1929 opinion by the Permanent Court of International Justice (PCIJ) in the

20. CLAUS D. ZIMMERMANN, *The Concept of Monetary Sovereignty Revisited*, 24 EUR. J. INT'L. L. 797, 798 (2013).

21. *Id.* at 799 ("Most authors, however, appear to approach monetary sovereignty as [a] purely positive, and static, concept, i.e., as a mere catalogue of state competences . . . ."); R.M. LASTRA, LEGAL FOUNDATIONS OF INTERNATIONAL MONETARY STABILITY 22-23 (2006); C. PROCTOR, MANN ON THE LEGAL ASPECT OF MONEY 500-01 (2005).

Serbian Loans Case,[22] which recognized that a state's authority over its currency is due the respect of other states under international law.[23]

If that authority has historically been recognized as a component of national sovereignty, however, much of the commentary on the subject concludes "that monetary sovereignty has become increasingly eroded, that it can be accepted only as 'a figure of speech,' and, even stronger, that it should be regarded as no more than a myth."[24] This erosion is deemed to be a product of numerous factors, including formal legal constraints and the growing power of market forces to influence or evade state authority, including the ability of privately created money to undermine state monetary control.[25]

The International Monetary Fund's (IMF) Articles of Agreement, the treaty creating the Fund, is both a manifestation of state sovereignty over monetary affairs and a significant formal limitation on that sovereignty. In the wake of extremely disruptive competitive currency devaluations before World War II, the initial state signatories to the Articles committed to a fixed exchange rate regime, which was a significant ceding of those states' sovereignty over their monetary affairs

22. *See* Zimmermann, *supra* note 20, at 799. Gianviti, *Current Legal Aspects of Monetary Sovereignty*, *in* CURRENT DEVELOPMENTS IN MONETARY AND FINANCIAL LAW iv, 3, at 4 (2005); Case Concerning the Payment of Various Serbian Loans Issued in France (Fr. v. Serb.), Judgment, 1929 P.C.I.J. (ser. A) No. 20-21, at 42-43 (July 12) In this case, payment of some pre-World War I Serbian bonds was to be made in gold francs; when payment was sought, French law had reduced the amount of gold in its francs, but provided that international loans would be paid per the value of the older gold francs. The PCIJ held that France had the ability to control the value and use of its own currency and thus determined that the bonds would be paid according to the higher value of the older francs.

23. Zimmerman, *supra* note 20, at 799. Zimmermann is here quoting F.A. Mann, who states: "To the power granted by municipal law there corresponds an international right, to the exercise of which other states cannot, as a rule, object."

24. *Id.* at 799-800; *See also* J. Lawrence Broz & Jeffry A. Frieden, *The Political Economy of Exchange Rates*, *in* OXFORD HANDBOOK OF POLITICAL ECONOMY 587 (Barry R. Weingast & Donald A. Wittman eds., 2006); Benjamin J. Cohen*, The International Monetary System: Diffusion and Ambiguity*, 84 INT'L AFF. 455, 465 (2008); W.M. CORDEN, TOO SENSATIONAL: ON THE CHOICE OF EXCHANGE RATE REGIMES (2004); BARRY EICHENGREEN, INTERNATIONAL MONETARY ARRANGEMENTS FOR THE 21ST CENTURY 89 (1994); Jeffry A. Frieden*, Globalization and Exchange Rate Policy*, *in* THE FUTURE OF GLOBALIZATION 344, 347 (Ernesto Zedillo ed., 2007); A.F. LOWENFELD, INTERNATIONAL ECONOMIC LAW 593-851 (2008); Robert A. Mundell, *Money and the Sovereignty of the State* (Int'l Econ. Ass'n, Conf. Paper, 1997), www-ceel.economia.unitn.it/events/monetary/mundell14.pdf, 5; BENN STEIL & MANUEL HINDS, MONEY, MARKETS, AND SOVEREIGNTY 33 (2009); LASTRA, *supra* note 21, at 16-17 (2006); PROCTOR, *supra* note 21, at 345 (2005); M.R. SHUSTER, THE PUBLIC INTERNATIONAL LAW OF MONEY 9 (1973).

25. Zimmerman, *supra* note 20, at 799-800.

and was understood as such at the time.[26] That exchange rate regime collapsed in the 1970s, and the Articles were amended to adopt a much more liberal exchange rate regime.[27] The Fund's Articles do not now proscribe any particular exchange rate regime or approach. Instead, members of the Fund now commit, among other things, to "undertake[] to collaborate with the Fund and other members to assure orderly exchange arrangements and to promote a stable system of exchange rates."[28] This commitment to help promote systemic or external stability includes a broader obligation of members to pursue financial policies that promote their own domestic stability.[29] While these obligations are broadly stated and arguably subject to weak enforcement, they are still properly understood as a nearly universal compromise of sovereignty in general and of monetary sovereignty in particular.[30]

Currency substitution, currency pegging, and currency and monetary union are voluntary formal limits on monetary sovereignty. [31] A primary motivation for adopting such policies is to reduce or eliminate exchange rate risk for cross-border transactions. Substitution and unions also reduce the costs of creating and managing a domestic currency. Full currency substitution involves adopting another state's currency and ceasing the use of a domestic currency, while pegging involves setting the value of a domestic currency to the value of a foreign currency, a combination of currencies, or some other value, often gold.[32] Approximately fifteen states have substituted currencies, and nearly fifty states have pegged their currencies to either the U.S. dollar or the euro.[33] Currency substitution and rigid pegging cede a state's authority and control over the most critical aspect of its monetary affairs—the value of

26. RICHARD W. EDWARDS, INTERNATIONAL MONETARY COLLABORATION 493 (1985).

27. Adam Feibelman, *Law in the Global Order: The IMF and Financial Regulation*, 49 NYU J. INT'L L. & POL. 687, 703-04 (2017).

28. IMF Articles of Agreement art. IV, § 1.

29. Feibelman, *Law in the Global Order*, *supra* note 27, at 704-705.

30. *See id.* at 705.

31. *See generally*, Alberto Giovannini and Bart Turtelboom, *Currency Substitution*, in HANDBOOK OF INTERNATIONAL MACROECONOMICS (F. van der Ploeg ed., Cambridge: Blackwell 1994); *see also*, Katharina Bucholz, *The Countries Relying on Foreign Currencies at Home*, STATISTA (Sep. 18, 2019), available at https://www.statista.com/chart/19398/substitution-currencies-or-pegging-their-currencies/?srsltid=AfmBOoq2lXiOFGHbZuLyfhi_rgWejBU6D9nUDsVp8TA9MMQyuog4jiyO.

32. *See* Bucholz, *supra* note 31.

33. *See* International Monetary Fund, *Annual Report on Exchange Arrangements and Exchange Restrictions 2023*, at 7 & 13 (Dec. 18, 2024), available at https://www.imf.org/en/publications/annual-report-on-exchange-arrangements-and-exchange-restrictions/issues/2024/12/19/annual-report-on-exchange-arrangements-and-exchange-restrictions-2023-541890.

its domestic currency—by essentially adopting a fixed exchange rate regime. Unlike the fixed exchange rate regime of the IMF's initial Articles, however, such substitution or pegging is done unilaterally by states that retain the full authority to reverse the policy or practice.[34]

Currency unions are formed when two or more states agree to adopt the same currency. Monetary unions, by comparison, involve more deeply coordinated monetary, fiscal, trade, and financial policymaking.[35] A monetary union therefore requires ceding some degree of monetary control and authority to institutions and actors outside of the state itself. In the case of European Monetary Union, for example, each member of the Union has adopted the euro as its currency, and the European Central Bank conducts monetary and exchange rate policy for the Union.[36] Members maintain direct control over their own fiscal policies, but they are bound by agreement to limits on domestic budget deficits and borrowing, among other things.[37] While states can in theory exit monetary unions as they can reverse other monetary and exchange rate policies, there are huge practical hurdles to doing so, to the extent that such an option may often not be feasible.[38]

Not surprisingly, the emergence of the European Monetary Union in the early 1990s spurred a wave of attention to the topic of monetary sovereignty. The prevailing view among writers at that time was that accession to such a union was a nearly total abdication by each member of its monetary sovereignty, and that the creation of the European Monetary Union reflected the declining significance of monetary sovereignty in general. Responding to this, some writers advanced a concept of monetary sovereignty consistent with even comprehensive and institutionalized monetary union. As Zimmermann asked, "does this undeniable erosion of the formerly exclusive character of certain state competences really imply, as is being claimed in much of the existing literature, that monetary sovereignty as a legal concept has itself become

34. *See id.*

35. Zimmerman, *supra* note 20, at 803; *see also* Adam Feibelman, *Europe and the Future of International Monetary Law*, 22 TRANSNAT'L L. & CONTEMP. PROBS. 101, 120 (2013).

36. *Id.* at 120.

37. *Id*.

38. *See, e.g*., Platon Monokroussos, *GRexit and Why It Will Not Happen: Catastrophic for Greece and Destabilizing for the Euro* (Working Paper, 2016), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2616278, 5; *see also* Jens Dammann, *The Right to Leave the Eurozone*, 48 TEX. INT'L L.J. 125, 126, 130 (2012) (arguing that members of the eurozone have a formal right to withdraw from the monetary union and that under some circumstances it may be reasonable for a member to do so).

outdated?"[39] According to him, "[s]uch cooperation under evolving economic constraints does not amount to ringing the death knell for the concept of monetary sovereignty. Instead, it may be more appropriate to regard such a joint exercise of monetary sovereignty as reflecting a special form of cooperative sovereignty . . . ."[40]

If persuasive, this concept of monetary sovereignty is yet strikingly thin. Against this background, Pistor's account is, in some respects, a relatively robust conception of monetary sovereignty, at least for the states that still have it. From this perspective, her account can be understood as rescuing something of the notion of monetary sovereignty. Yet Pistor also embraces much of the contemporary view about the erosion of monetary sovereignty, finding as she does that most states simply do not possess it,[41] including all of the states in the Eurozone. According to her, most countries with domestic currencies nonetheless do not enjoy monetary sovereignty because they have formally ceded it, because privately created money (domestic or foreign) becomes "inextricably intertwined" with official money instruments,[42] or because they "incur most of their own debt in foreign currency, which they do not control"[43] and which may be costly for the state to access for itself or on behalf of private domestic interests.[44]

Regarding formal voluntary constraints on sovereignty like joining a monetary union or accepting the obligations of membership in the IMF, Pistor agrees that this voluntary delegation can be an expression of sovereignty, not a ceding, but only if it "does not preempt self-governance about core issues of statehood."[45] Pistor does not specify these core issues of statehood. Under normal circumstances, it seems, they may or may not be implicated or constrained by a lack of control over monetary affairs.[46]

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39. Zimmermann, *supra* note 20, at 800.

40. *Id.* at 812. "[T]o the extent that agreeing to such transfers is what provides the state's population with a maximum of monetary and financial stability under contemporary economic constraints, it appears appropriate to analyse the underlying transfer of sovereign powers not as a surrender of monetary sovereignty, but as its effective exercise under contemporary economic constraints." *Id.* at 817.

41. Pistor, *supra* note 2.

42. *Id.* at 492, 493, 507.

43. *Id.* at 493.

44. *Id.*

45. *Id.* at 513.

46. "Countries on the receiving end of capital flows, the private moneys issued and disseminated under laws they don't control, are largely helpless. They surrender democratic self-governance much earlier than in a crisis situation when they are forced to seek outside help." *Id.* at 516. Pistor also argues, "In fact, the very operation of the money system is anathema to democratic self-governance. Deliberation based on shared normative commitments enshrined in

In times of financial crisis, however, underlying constraints on monetary affairs, whether they are voluntarily adopted or imposed by other countries or private markets, are revealed as consequential vulnerabilities. As Pistor writes:

> Every crisis puts to a test the ability of states to rescue the domestic money system without recourse to external help. Some countries can help themselves and others can't. External help always comes with strings attached and constrains autonomous decision making . . . .[47] It is an inherently hierarchical system that links assets, intermediaries, and countries in ways that predetermine winners and losers in times of crisis.[48]

Thus, for example, "financial assets, or moneys, produced under the laws of one sovereign can wreak havoc on the territory of another . . . . [States] need not have delegated sovereignty consciously; all they have to do is to open their borders to free capital flows."[49]

And the stakes are high. States that cannot rescue their domestic monetary and financial systems inevitably cede crucial aspects of sovereignty and self-governance. They become dependent on financial rescue or support from other states or international institutions, and those external actors inevitably influence the modes of rescue and recovery. Often, such support involves formal or informal conditions touching upon a wide range of domestic policies.[50] Even if such conditionality is developed in concert with domestic leaders, it can—and often does—override the conventional processes of domestic policymaking. At the very least, in such circumstances, foreign actors heavily influence decisions with profound domestic social and political consequences.[51]

"The best safeguard against such a predicament," Pistor says, "is to practice monetary autarchy, an isolationist stance that is not very attractive. Neither, however, is the prospect of being pushed to the periphery of a system controlled by others who will further entrench their

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constitutional law is at the heart of democratic decision making. Money operates according to different rules: competition, hierarchy, and power." *Id.*

47. *Id.* at 494.

48. *Id.* at 495.

49. *Id.* at 501, 516. Pistor notes, "Countries on the periphery are beholden to private money and can at most hope for a helping hand from countries at the apex of the system. Yet only those whose stability may pose a threat for monetary sovereigns can rely on this help." *Id.* at 517.

50. NGAIRE WOODS, THE GLOBALIZERS: THE IMF, THE WORLD BANK AND THEIR BORROWERS 79 (Cornell Univ. Press 2006).

51. *Id.*; INTERNATIONAL MONETARY FUND, *2018 Review of Program Design and Conditionality* 3, 7 (2019), available at https://www.imf.org/en/Publications/Policy-Papers/Issues/2019/05/20/2018-Review-of-Program-Design-and-Conditionality-46910.

position at the top with every future crisis."[52] While that statement suggests only two equally unappealing options, Pistor does acknowledge that states might retain some degree of sovereignty through reducing private domestic money making[53] and through limiting foreign capital flows.[54] But she highlights the challenges for such intermediate approaches for states on the periphery of the global monetary and financial systems.[55]

The balance of this Article explores the space between these two polar choices and argues that the case of India demonstrates that there is, in fact, a spectrum of monetary sovereignty. The existence of this spectrum both supports and complicates Pistor's account of hierarchy within the global financial and monetary systems. It reflects that the degree of a state's degree of control over its monetary affairs can to some extent be a shifting quotient. This quotient depends on both domestic and external factors, determined largely by a state's external debt, exchange rates, exposures to capital flows, and the scope of domestic private money creation. And these factors are in turn determined by an array of institutional arrangements, laws, and policies.

III. ASSESSING INDIA'S MONETARY SOVEREIGNTY

This part describes how India has limited and managed its exposure to most factors that can undermine domestic control over monetary affairs since it gained independence from Great Britain. Part III.A provides a broad overview of overarching themes in the country's macroeconomic steering and its general approach to integration with the global financial and monetary systems.

The balance of Part III describes India's policies and practices related to external indebtedness, cross-border capital flows, exchange rate policy, and domestic private money creation. In India, as elsewhere, these policies are inevitably interrelated. As with other emerging economies, in India these policies have been directed at navigating the "impossible trinity," i.e., the idea that an economy cannot simultaneously have an

52. Pistor, *supra* note 2, at 517.

53. *Id.* at 499 ("Insulating the making of money from direct state control, however, is only part of the story. The other part is ensuring that the production of money is not taken over by the private sector, which invariably will seek full conversion into public money.").

54. *Id.* ("States can impose capital controls for inbound or outbound capital flows, but they are difficult to police and have been largely abandoned when fixed exchange regimes were replaced by floating ones.").

55. *Id.*

independent monetary policy, free cross-border capital flows, and a fixed or highly stable exchange rate, but rather that only two of these are possible at a time.[56] This trilemma poses challenges of strategy, economic theory, and institutional capacity.[57] Broadly speaking, policymakers in India have met these challenges in recent decades with cautious and fitful liberalization.

A. Background

1. Historical Trends

India's current landscape of macroeconomic policies is a product of gradual evolution over the years since it became an independent nation in 1947. At that point, the country had relatively few externally oriented economic policies. During the first decades of independence, reflecting the influence of the Soviet model, India had a "mixed economy model and planned development strategy."[58] Economic planning was pursuant to five-year plans; early five-year plans tended heavily toward "self-sustaining growth" and self-reliance.[59] As was true in many developing economies at the time, India pursued policies of import substitution, domestic resource mobilization,[60] and "export pessimism."[61] In sum, in its first decades of independence, India was largely a closed economy.[62]

Partly as a result of such policies, India faced consistent difficulty in obtaining and retaining foreign exchange through this period.[63] Furthermore, by the 1970s, its approach to import substitution was becoming untenable, leading to import liberalization.[64] A historic drought

56. *See* Y.V. REDDY, INDIA AND THE GLOBAL FINANCIAL CRISIS: MANAGING MONEY AND FINANCE 26 (Anthem Press 2009). Robert Mundell and Marcus Fleming first articulated the underlying basis of the trilemma. *See* Robert A. Mundell*, Capital Mobility and Stabilization Policy Under Fixed and Flexible Exchange Rates*, 29 CAN. J. ECON. & POL. SCI., 475 (1963); J. Marcus Fleming, *Domestic Financial Policies Under Fixed and Floating Exchange Rates*, 9 IMF STAFF PAPERS 369 (1962).

57. *See discussion infra* Part III.A.2.

58. REDDY, *supra* note 56, at 97.

59. *Id.* at 45.

60. *Id.* at 44.

61. *Id.*; John Echeverri-Gent*, India's Response to the Global Financial Crisis: From Quick Rebound to Protracted Slowdown*, *in* UNEXPECTED OUTCOMES: HOW EMERGING ECONOMIES SURVIVES THE GLOBAL FINANCIAL CRISIS 84 (CAROL WISE et al. eds., Brookings 2015).

62. REDDY, *supra* note 56, at 45.

63. *Id.* at 44.

64. *Id.* at 97. *See also* VIJAY JOSHI & I.M.D. LITTLE, INDIA: MACROECONOMICS AND POLITICAL ECONOMY, 1964-1991 (World Bank, 1994) available at https://documents.worldbank.org/en/publication/documents-reports/documentdetail/259451468772490617/india-macroeconomics

and the oil shock of the late 1970s exacerbated both problems, precipitating a general crisis.[65] A full-blown foreign exchange crisis was averted only because the country was able to draw upon foreign reserves it had accumulated.[66] But, in 1981, in order to finance its recovery from this crisis, India sought and obtained support from the IMF.[67]

Emerging from the crisis of 1979-81, the country enjoyed a period of robust growth.[68] But this growth was due in part to reforms that also led to fiscal and trade deficits and rising short-term external debt.[69] These structural problems, a rigid and dysfunctional financial system,[70] and the emergence of coalition politics[71] set the stage for a greater crisis in the early 1990s.[72]

In a dramatic period for the country, fiscal and trade deficits as well as high levels of external borrowing led to the depletion of foreign exchange reserves and, eventually, a sharp depreciation in the value of the rupee.[73] The country came perilously near defaulting on external obligations. In 1991, the crisis culminated in another financial support program with the IMF and loans from foreign banks secured by the country's gold reserves, which had to be secretly airlifted to Europe.[74] The recovery from this crisis involved some of the most significant financial reforms that the country had introduced up to that point and which formed the foundation of subsequent and contemporary financial and monetary policies. These included the beginning of a shift to a market-based

-and-political-economy-1964-1991, 50-51; *see also* Ankit Mital, *The Long Road to the 1991 Economic Crisis*, MINT (July 8, 2016), available at https://www.livemint.com/Sundayapp/E0rCYXfJyjWd2qsENV3KOO/The-long-road-to-the-1991-economic-crisis.html, 3.

65. REDDY, *supra* note 56, at 97. "[A] relatively closed economy does not provide immunity from a foreign exchange crisis." *Id.* at 45.

66. Mital, *supra* note 64.

67. *Id.*

68. REDDY, *supra* note 56, at 97.

69. *Id.* at 98.

70. *Id.*

71. John Echeverri-Gent, *Political Economy of India's Fiscal and Financial Reforms* 1 (CREDPR, STAN., Working Paper No. 105, 2001), available at https://kingcenter.stanford.edu/sites/g/files/sbiybj16611/files/media/file/105wp_0.pdf.

72. REDDY, *supra* note 56, at 97.

73. *See generally*, Shankar Acharya, *India: Crisis, Reforms and Growth in the Nineties*, (Stan. Ctr. for Int'l Dev., Working Paper No. 139, 2002), available at https://kingcenter.stanford.edu/sites/g/files/sbiybj16611/files/media/file/139wp_0.
pdf.

74. Vinay Pandey, *4 Reforms That Pulled India Back After It Ran Out of Money in 1991*, THE ECONOMIC TIMES (July 21, 2016), https://economictimes.indiatimes.com/news/economy/policy/4-reforms-that-pulled-india-back-after-it-ran-out-of-money-in-1991/articleshow/53308703.cms?from=mdr.

exchange rate, the elimination of most industrial licensing requirements, a significant relaxation of rules against foreign investment in various industries, and some meaningful disinvestment by the government from public sector entities.[75] These reforms and adjustments are widely viewed as having been successful and, especially, as having provided conditions for a subsequent period of robust and sustained growth.[76] Notably, however, these reforms were very controversial at the time, with vocal opponents criticizing them as being directed by foreign lenders and undermining India's autonomy.[77]

Since the early 1990s, economic reforms have continued gradually, with a trend of cautious liberalization and slowly increasing integration with the global economy.[78] These have included evolution in policies related to financial regulation,[79] monetary policy,[80] capital controls,[81] the exchange rate,[82] and trade.[83] The early 1990s also saw the rise of administrative agencies, which enjoyed some degree of independence,[84] privatization of some state-owned enterprises and further state disinvestment,[85] and the beginnings of a domestic capital market.[86]

The period between the crisis and reforms of the early 1990s and the global financial crisis beginning in 2008 was generally one of growth and stability in India.[87] And by the time of the global financial crisis of 2008,

75. *Id.* at 3-4. Other reforms included the reduction of the fiscal deficit through, inter alia, new taxes, the adoption of some important global banking practices, the reduction of some custom duties, the creation of a new national stock exchange, and moderate liberalizing of interest rates. *Id.* at 5-6. *See also* Atul Kohli, *Politics of Economic Growth in India, 1980-2005: Part II: The 1990s and Beyond*, ECON. & POL. WEEKLY, 1361 (Apr. 8, 2008) (noting that the reforms related to "external economic relations" were discontinuous from previous reforms), available at https://www.princeton.edu/~kohli/docs/PEGI_PartII.pdf.

76. *Id.* at 18-24.

77. *See, e.g.*, Kulwindar Singh, *Foreign Direct Investment: A Critical Analysis of FDI from 1991-2005*, CENTRE FOR CIV. SOC'Y, NEW DELHI, 3-5 (2005), available at https://ccs.in/sites/default/files/2022-10/Foreign%20Direct%20Investment%20A%20Critical%20Analysis%20of%20FDI%20from%201991-2005.pdf; Kohli, *supra* note 75, at 1363.

78. *See* Echeverri-Gent, *supra* note 61.

79. REDDY, *supra* note 56, at 16-17, 109-11.

80. Echeverri-Gent, *supra* note 61, at 78 ("At the beginning of the 1990s, India lacked the policy instruments needed to implement modern monetary policy.").

81. REDDY, *supra* note 56, at 1-2.

82. *Id.* at 201.

83. *Id.* at 46-47.

84. Echeverri-Gent, *supra* note 71, at 6.

85. *Id.* at 7.

86. *Id.* at 13.

87. Acharya, *supra* note 73, at 6-10 (discussing improvements in trade, external debt, and foreign reserve levels); REDDY, *supra* note 56, at 46.

the country had liberalized many aspects of its economy, increased its integration with global financial systems, and expanded its international trade to the extent that policymakers could boast that the country had emerged "as a significant player in the world economy."[88] As one telling indicator, the country's trade to GDP ratio rose from sixteen percent in 1990 to fifty-five percent in 2012.[89]

Yet, by global standards, India was still a relatively closed economy at the onset of the global financial crisis. The state's control over the economy and the country's relative insularity from the global economy was evident in India's experience of that crisis and its policy response.[90] The country weathered the crisis without severe domestic economic and financial disruption and, most notably, without needing to obtain external assistance.[91]

In the years since the global crisis, India has continued this slow if steady process of liberalization and integration.[92] In this period, attracting inward foreign investment has become a primary policy goal and focus of much popular attention. Current Prime Minister Narendra Modi explicitly campaigned in 2014 on a promise to elevate the country's World Bank *Doing Business* ranking.[93] Domestic actors have also increased outward foreign investment in this period.

The country has continued to reform its regulation of the banking sector by, among other things, allowing more foreign investment in the sector[94] and has adopted various reforms to improve credit markets, especially by facilitating debt enforcement and collection.[95] It has also gradually liberalized domestic rules regarding international trade "to enable domestic firms to restructure and spread the costs of adjustments over time."[96] Since the 2008 crisis, this has involved a greater focus on

88. *Id.* at 1.

89. Echeverri-Gent, *supra* note 61, at 84.

90. *See* Echeverri-Gent, *supra* note 61, at 74-75 ("At first glance, India's response to the global financial crisis appears to be one of the most successful responses . . ."); *see also* REDDY, *supra* note 56, at 210-11.

91. *See infra* at notes 112-114.

92. REDDY, *supra* note 56, at 2, 47-48.

93. Adam Feibelman, *Legal Shock or False Start? The Uncertain Future of India's New Consumer Insolvency and Bankruptcy Regime*, 93 AM. BANKR. L.J. 429, n.212 (2019).

94. *See* Sharat Kumar & A Srija, *Foreign Direct Investment in India in the Post-1991 Period*, *in* THE INDIAN ECONOMY SINCE 1991: ECONOMIC REFORMS AND PERFORMANCE 270 (B.A. Prakash ed., PEARSON, 2012).

95. *See* Insolvency and Bankruptcy Code, Act No. 31 of 2016; Sick Industrial Companies (Special Provisions) Act (SICA), Act No. 1 of 1986; Echeverri-Gent, *supra* note 61, at 77.

96. REDDY, *supra* note 56, at 46, 90; Echeverri-Gent, *supra* note 61, at 84.

developing trade ties across Asia.[97] But India's integration has been a somewhat ambivalent and complicated project. During the COVID-19 pandemic, for example, in response in part to a growing trade deficit, the government launched a broad Atmanirbhar Bharat (Self-Reliant India) policy, featuring the slogan "Make in India."[98]

In sum, India's economy has evolved dramatically in the years since its independence, developing a more market-based and globally integrated economy as well as a more liberalized financial system. But its economy still stands out as relatively insulated, partially integrated, and largely controlled.[99] As described below in subparts III.B-D, this has been largely by design and has been the subject of ongoing debate within the country.

2. Monetary (and other Macro) Policymaking

The express objectives of the Reserve Bank of India's (RBI) conduct of monetary policy are price stability and growth,[100] but policymakers are also charged to "keep in mind the considerations of exchange rate stability and financial stability in pursuing the basic objectives."[101] The RBI generally pursued an expansionary monetary policy after the crisis of 2008-09[102] marked by lower interest rates.[103] Like other emerging economies, India had to navigate the effects of similarly expansionary policies in larger economies after the crisis, which tended to push capital flows toward emerging economies. In the wake of the COVID-19 pandemic, India, like other countries, faced rising inflation, and the RBI raised rates to address it.[104] In light of recent and recurring crises, policymakers in India have grown increasingly concerned about stability

97. Echeverri-Gent, *supra* note 61, at 84 (describing India's "Look East" policy during global financial crisis).

98. *Towards a Genuine Atmanirbhar Bharat*, DECCAN HERALD (Sep. 28, 2025), available at https://www.deccanherald.com/opinion/towards-a-genuine-atmanirbhar-bharat-3746334.

99. *See, e.g.*, Kohli, *supra* note 75, at 1363 (noting the "steady but relatively slow-paced integration of [the] Indian economy with the global economy, a trend that has pretty well continued into the present period").

100. REDDY, *supra* note 56, at 200.

101. *Id.* at 195.

102. Echeverri-Gent, *supra* note 61, at 76.

103. REDDY, *supra* note 56, at 205.

104. *See, e.g.*, Mohit Kumar Shrivastav et al., *Navigating Post-COVID Inflationary Pressures: A Systematic Review of India's Monetary Policy Framework and Its Economic Impact*, INT'L J. RSCH. AND INNOVATION SOC. SCI. (2025), available at https://rsisinternational.org/journals/ijriss/articles/navigating-post-covid-inflationary-pressures-a-systematic-review-of-indias-monetary-policy-framework-and-its-economic-impact/.

of its monetary and financial systems,[105] and the RBI has been more consistently counter-cyclical than the banks of many other large and developing economies.[106]

As Y.V. Reddy, a former governor of the Reserve Bank of India, has observed, "the conduct of monetary policy depends on a number of factors that are unique to a country and to the context."[107] Such factors include the structural aspects of the economy and institutions, as well as the extent of the economy's openness.[108] As noted above, the potential impact of transnational factors in the conduct of monetary policy is widely understood to result in a trilemma: An economy cannot have a fixed or very stable exchange rate, an open capital account, *and* an independent monetary policy.[109] It is fair to say that policymakers in India have responded to this trilemma over time by adjusting approaches to each of the three components. Until the 1990s, the country was committed to relatively strict exchange rate stability, pegging the rupee to foreign currencies.[110] This, in turn, depended on fairly rigid capital controls, discussed below. Beginning in the mid-1990s, the country adopted a market-based exchange rate, but intervened in markets to maintain stability, as policymakers balanced this exchange rate policy with independence in steering interest rates.[111] During the global financial crisis, the rupee faced a sharp depreciation,[112] which the RBI was able to manage by, among other things, injecting liquidity into the economy[113] and providing a rupee-dollar swap facility without support from the Federal Reserve.[114] The rupee began appreciating again in 2009-10 with return of inward portfolio investment.[115] After the 2008-09 crisis, policymakers have generally avoided direct efforts to maintain a targeted

105. REDDY, *supra* note 56, at 201.

106. *Id.* at 26.

107. *Id.* at 205-07.

108. *Id.* at 207.

109. *Id.* at 197. Consider, for example, a country that wanted to allow relatively free capital flows while maintaining a fixed or very stable exchange rate. It would presumably need to dedicate monetary policy to supporting the exchange rate. If it wanted to direct monetary policy to other goals, it would need to allow more flexibility in the exchange rate or control capital flows (the latter of which would help maintain a stable exchange rate).

110. Echeverri-Gent, *supra* note 61, at 81.

111. REDDY, *supra* note 56, at 103, 107-08, 197, 202, 207-10.

112. Echeverri-Gent, *supra* note 61, at 82.

113. *Id.* at 85.

114. Press Release, Reserve Bank of India, Rupee-Dollar Swap Facility for FPIs in G-Securities, CDs, CPs, etc. (Sep. 18, 2008), available at https://www.rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=19416.

115. Echeverri-Gent, *supra* note 61, at 82.

exchange rate.[116] As the follow section discusses, this approach has depended in part on managing cross-border capital flows.

B. Capital Flows, Controls

India has employed extensive controls on the flow of capital in and out of the country throughout its existence as an independent state.[117] The country joined the IMF and its post-war fixed exchange rate system in 1945, two years before its independence. At that time, capital controls were a regular feature of financial systems around the globe and were understood as a natural component of a fixed exchange rate regime.[118]

Over the last four or five decades, as cross-border capital flows have become an essential and defining feature of the international financial and monetary systems, capital controls have been a topic of great interest and debate across the globe.[119] Conventional views and practice regarding capital controls have changed dramatically since the end of World War II, especially since the 1970s, when the fixed exchange rate system collapsed and many states adopted floating exchange rate regimes. The period between then and the financial crisis of 2008-09 saw a growing, if not universal, consensus among scholars and policymakers that exchange rates should be set by the market, that capital controls were ineffective and inefficient, and that developing economies would benefit from opening their capital accounts to the maximum extent possible.[120]

The global financial crisis dramatically highlighted the risks and vulnerabilities associated with some types of capital flows, especially those most susceptible to volatility. During the crisis and in the post-crisis period, many states adopted policies to manage cross-border capital flows to avoid and resolve domestic financial crises.[121] This experience led to a

116. Reddy, s*upra* note 56, at 112; Rajeswari Sengupta and Bhargavi Zaveri Shah, *Why RBI's Attempts to Control the Rupee Can Have Adverse Consequences*, THE INDIAN EXPRESS (Aug. 24, 2024, 10:47 AM), https://indianexpress.com/article/opinion/columns/why-rbis-attempts-to-control-the-rupee-can-have-adverse-consequences-9529975/.

117. Radhika Pandey et al., *Motivations for Capital Controls and Their Effectiveness* 9, (NAT'L INST. OF PUB. FIN. AND POL'Y NEW DELHI, Working Paper No. 168, 2016).

118. *See* Adam Feibelman, *The IMF and Regulation of Cross-Border Capital Flows*, 15 CHI. J. INT'L L. 409, 416 (2015).

119. *Id.* at 416-22.

120. Pandey et al., *supra* note 117, at 4.

121. Kevin P. Gallagher, *Regaining Control? Capital Controls and the Global Financial Crisis, in* THE CONSEQUENCES OF THE GLOBAL FINANCIAL CRISIS: THE RHETORIC OF FREEDOM AND REGULATION (Wyn Grant & Graham K. Wilson eds., 2012); Feibelman, *The IMF and Regulation of Cross-Border Capital Flows*, *supra* note 118; Annamaria de Crescenzio & Etienne Lepers, *Extreme Capital Flow Episodes from the Global Financial Crisis to COVID-19*, OECD Working Papers on International Investment 2021/05, available at https://www.oecd.org/content/dam/

broad reconsideration by scholars and policymakers of capital control measures and an emerging new consensus that, under some circumstances, such policies can be useful tools for promoting financial stability.[122]

Although India has relaxed its management of capital flows to a significant extent over recent decades, it continues to heavily regulate its capital account by contemporary standards.[123] According to Reddy, "management of the capital account has become an important element of public policy in India"[124] and, in his view, has had a beneficial effect on the country's financial system and its economy.[125] As discussed in the section above, managing cross-border flows is an important lever for India's policymakers in maintaining exchange rate stability and in conducting monetary policy.[126]

The current system of controls and management is largely the product of reforms that began in earnest in the 1990s.[127] The country's capital controls include sectoral limits, regulation of the process of foreign

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oecd/en/publications/reports/2021/07/extreme-capital-flow-episodes-from-the-global-financial-crisis-to-covid-19_a4983e26/d557b9c4-en.pdf.

122. Pandey et al., *supra* note 117, at 4 ("After the 2008 crisis, there was fresh interest in the possibility that capital controls could be a useful part of the policy toolkit." (citing Jonathan D. Ostry et al., *Capital Controls: When and Why?*, 59 IMF ECON. REV. 562 (2011)); Jonathan D. Ostry et al., *Tools for Managing Financial-Stability Risks from Capital Inflows*, 88 J. INT'L ECON. 407 (2012); Int'l Monetary Fund, *The Liberalization and Management of Capital Flows—An Institutional View* (Policy Paper, 2012).

123. "Unlike all developed countries and many EMEs, the overall capital controls system [in India] was never dismantled." Pandey et al., *supra* note 117, at 8; Illa Patnaik & Ajay Shah, *Did the Indian Capital Controls Work as a Tool of Macroeconomic Policy?*, 60 IMF ECON. REV. 439-64 (2012); Ajay Shah & Ila Patnaik, *India's Experience with Capital Flows: The Elusive Quest for a Sustainable Current Account Deficit in Capital Controls and Capital Flows*, *in* EMERGING ECONOMIES: POLICIES, PRACTICES, AND CONSEQUENCES 609-43 (Sebastian Edwards ed., U. Chi. Press 2007); R. Mohan and M. Kapur, *Managing the Impossible Trinity: Volatile Capital Flows and Indian Monetary Policy* (Stan. Ctr. for Int'l Dev., Working Paper No. 401, 2009).

124. REDDY, *supra* note 56, at 284.

125. *Id.*

126. *Id.* at 43. Notably, however, the country did not utilize controls to limit substantial outflows during the early months of the COVID-19 pandemic, relying on central bank intervention in currency markets instead. *See* Ila Patnaik & Radhika Pandey, *Why IMF Evaluators Want India-Style Capital Controls to be Adopted Around the World*, THE PRINT, Oct. 23, 2020, available at https://theprint.in/ilanomics/why-imf-evaluators-want-india-style-capital-controls-to-be-adopted-around-the-world/529127/ (noting that "[i]n the past, [India] has used capital controls to manage the 'impossible trinity'").

127. "From the early 1990s onwards, a process of capital account liberalisation has taken place, though parametric changes in the capital controls system." Radhika Pandey et al., *supra* note 117, at 8; *see also* REDDY, *supra* note 56, at 1-2.

direct investment, limits on foreign holdings of Indian government bonds, regulation of gold imports, regulation of commercial external borrowing, and limits on interest paid on foreign bank deposit accounts (generally held by non-resident Indians).[128] These controls and others represent "a large complex system with rules that are tailored to the asset class, investor type, recipient type, transaction magnitude, etc. . . . encoded into thousands of pages of law [and] administered by a team of over 10,000 officials."[129]

There has been an observable hierarchy in India's approaches to capital flows.[130] The basic policy framework has generally sought to increase capital inflows with a cautious approach to outflows, including outward direct investment by domestic firms and individuals. As is common globally, foreign direct investment has been favored over other types of transactions, especially short-term external debt.[131]

The framework of controls now allows full convertibility for current account transactions (like payments for imports and exports) and "authorized" capital flows inward and outward, including portfolio investments by foreign institutional investors.[132] The framework for foreign direct investment has generally evolved from a system of broad prohibitions to one of gradually fewer prohibitions and a scheme of automatic and non-automatic allowance of inward direct investment.[133] Investments that are not prohibited but not automatically allowed must navigate an often cumbersome governmental approval process. Over time, an increasing number of types of direct investment have been automatically allowed.[134]

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128. Pandey et al., *supra* note 117, at 8. The Securities and Exchange Board of India has recently proposed to relax various rules that apply to foreign portfolio investors that invest exclusively in Indian government bonds. *See* SEBI, *Consultation Paper on Proposal to Facilitate Relaxation in Regulatory Compliances for FPI Applicants Investing only in Indian Government Bonds* (May 13, 2025), available at https://www.sebi.gov.in/reports-and-statistics/reports/may-2025/consultation-paper-on-proposal-to-facilitate-relaxation-in-regulatory-compliances-for-fpi-applicants-investing-only-in-indian-government-bonds_93906.html.

129. Pandey et al., *supra* note 117, at 8; REDDY, *supra* note 56, at 33; Ila Patnaik et al., *Foreign Currency Borrowing by Indian Firms: Towards a New Policy Framework*, NAT'L INST. OF PUB. FIN. & POL'Y NEW DELHI No.167, 3-4 (2016).

130. REDDY, *supra* note 56, at 90.

131. *Id.* at 108-09.

132. *Id.* at 90, 275-82.

133. *Id.* at 90.

134. *See* Press Release, Indian Ministry of Commerce and Industry, India Records USD 81.04 Billion FDI Inflow in FY 2024-25 (May 27, 2025), available at https://www.pib.gov.in/PressReleasePage.aspx?PRID=2131716#:~:text=This%20constitutes%20nearly%2070%25%20of,confidence%20in%20India's%20economic%20resilience.

The volume of inward capital flows to India has significantly increased since the 1990s,[135] yet the level of de jure capital controls is relatively high compared to other emerging markets and "cumulative engagement with global financial markets, as measured by the sum of its gross stock of external assets and liabilities as a ratio of GDP," has been relatively low.[136] Furthermore, while the evolution of capital controls in India since the 1990s has generally been one of gradual liberalization over time,[137] the system has not moved inexorably in that direction. Since the 1990s, it has sometimes loosened up enforcement or de jure restrictions on capital flows and sometimes tightened them to manage its capital account.[138] The system is operated by a sizable bureaucracy which effectively implements and modulates policy, making the restrictions on capital flows harder to evade than in other jurisdictions.[139] As Pandey et al. observe, "[t]he administrative infrastructure for the controls is well established: the RBI has autonomy on foreign exchange management, and it is able to provide notification of changes with immediate effect via circulars and later issue regulatory amendments. Further, RBI actions on capital controls take place quite frequently."[140]

While most of the recent literature on capital controls has focused on their impact on financial and monetary stability,[141] Panday et al. find that, for Indian policymakers, "the prime motivation is exchange rate policy and not systemic risk regulation."[142] Whatever the motivation, they also find that

> the evidence is mixed regarding the extent to which capital controls are able to deliver on the objectives of macroeconomic policy.[143] . . . Our

135. Echeverri-Gent, *supra* note 61, at 79.

136. *Id.*

137. Amadou N. Sy, *Capital Account Convertibility and Risk Management in India* (Int'l Monetary Fund, Working Paper No. 251, 2007).

138. Pandey et al., *supra* note 117, at 3 ("Further, Indian policy makers have modified the capital control framework frequently to address concerns about the exchange rate, country risk perception and other issues.").

139. "Several researchers have argued that capital controls may be particularly effective in a country like India with the legal and administrative machinery to implement controls." *Id.*

140. *Id.* at 3, 14; REDDY, *supra* note 56, at 27.

141. *See generally*, Feibelman, *The IMF and Regulation of Cross-Border Capital Flows*, *supra* note 118; *see also*, Inga Rademacher, *Central Banks, Monetary Stability, and the Varieties of Capital Control Liberalization*, SOCIO-ECON. REV. 1 (2024), available at https://doi.org/10.1093/ser/mwae077.

142. Pandey et al., *supra* note 117, at 3.

143. *Id.* at 35; Nicolas E. Magud et al., *Capital Controls: Myth and Reality—A Portfolio Balance Approach* (Nat'l Bureau of Econ. Rsch., Working Paper No. 16805, 2011); Bernardo S. de M. Carvalho & Márcio G.P. Garcia, *Ineffective Controls on Capital Inflows Under*

> results suggest that there was no significant impact of the capital control actions, either on the exchange rate or on measures connected with systemic risk.[144]

While domestic policymakers continue to have confidence in the utility of the regime,[145] much of the recent academic study and commentary on India's capital control framework has similarly criticized the general approach for being "not . . . effective in permitting safe activities while reducing systemic risk." [146]

C. External Debt

External debt is a distinct and crucial factor affecting exchange rate and financial stability. A country's external debt generally refers to both public and private debt—debt owed to foreign creditors by domestic government entities and private firms, respectively.[147] Borrowing from creditors abroad generally increases the pool of capital available for domestic commercial and financial activities and for financing public expenditures. External debt also arises from financing imports. Thus, creditors are institutional, individual, and official, and the instruments of external debt are heterogeneous, including loans, trade credit, and debt securities.[148]

External debt can dilute or undermine a state's control over domestic monetary affairs, and it can do so in a variety of ways.[149] Most obviously, it involves financial claims by entities beyond the jurisdiction of the borrower's state.[150] It adds to the overall public and private debt stock within the country and to the amount, and often the volatility,[151] of cross-border capital flows. In many circumstances, such debts are owed in a foreign currency, which can impact the exchange rate and generate

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Sophisticated Financial Markets: Brazil in the Nineties, in FINANCIAL MARKETS VOLATILITY AND PERFORMANCE IN EMERGING MARKETS 29-96 (Sebastian Edwards and Márcio G. P. Garcia eds., U. Chi. Press 2008); Gurnain Pasricha et al., *Domestic and Multilateral Effects of Capital Controls in Emerging Markets* (Nat'l Bureau of Econ. Rsch., Working Paper No. 20822, 2015).

144. Pandey et al., *supra* note 117, at 4, 34.

145. REDDY, *supra* note 56, at 284.

146. Patnaik et al., *supra* note 129, at 5.

147. Artuto C. Porzecanski, *Borrowing and Debt: How Do Sovereigns Get Into Trouble?*, *in* SOVEREIGN DEBT MANAGEMENT 309 (ROSA LASTRA & LEE BUCHHEIT EDS., 2014).

148. Gene Frieda, *Sovereign Debt Markets, in* SOVEREIGN DEBT MANAGEMENT 295(Rosa Lastra & Lee Bucheit eds., 2014).

149. *See generally*, Anna Gelpern & Brad Setser, *Domestic and External Debt: The Doomed Quest for Equal Treatmen*t, 35 GEO. J. INT'L L. 795 (2007).

150. *Id.* at 796.

151. *See supra* note 121.

significant exchange rate risks to borrowers and, through them, to the government.[152]

Furthermore, the distinction between public and private external debt can effectively collapse, especially in times of crisis if, for example, private external debt fuels a currency crisis or a domestic banking crisis, which may require public support through recapitalization or otherwise.[153] Regional debt crises, some fueled by foreign currency denominated debt, have flared regularly since the 1990s, including crises in Latin America, Asia, and Europe.[154]

Notably, in the years after the global financial crisis of 2008-09, when interest rates in the largest economies had been historically low, it was much easier for many countries that previously borrowed heavily in foreign currencies to borrow in their local currencies.[155] As a result, in recent years there has been general growth of domestic currency debt and a decline in the overall cost of sovereign borrowing.[156]

In considering the impact of external debt on states' control over their economies, it is important to appreciate the significant influence of credit ratings agencies have on states' economic and financial policymaking.[157] Ratings on states' public bonds and sovereigns' separate credit ratings are not only critical for the marketability of those securities, but they also impact the terms and availability of commercial external lending and the appeal of the country for foreign investors in general.[158] Thus, states must be ever attentive to the potential consequences of

152. *See* Gelpern & Setser, *supra* note 149, at 796.

153. REDDY, *supra* note 56, at 43.

154. *See, e.g.*, Daniel Marx et al., *Sovereign Debt and the Debt Crisis in Emerging Countries: The Experience of the 1990s*, *in* CHRIS JOCHNICK & FRASER A. PRESTON, EDS., SOVEREIGN DEBT AT THE CROSSROADS: CHALLENGES AND PROPOSALS FOR RESOLVING THE THIRD WORLD DEBT CRISIS (Oxford Univ. Press 2006).

155. Frieda, *supra* note 148, at 293-94, 304-05.

156. *Id.* at 288-90.

157. Richard Cantor & Frank Packer, *Determinants and Impact of Sovereign Credit Ratings*, 6 J. FIXED INC. 76 (1996); Marwan Elkhoury, *Credit Rating Agencies and Their Potential Impact on Developing Countries in* COMPENDIUM ON DEBT SUSTAINABILITY AND DEVELOPMENT, 165-90, 176 (United Nations 2009); Sydney Maki et al., *India's Outlook Cut to Negative by Moody's*, BLOOMBERG (Nov. 7, 2019, 4:07 PM), https://www.bloomberg.com/news/articles/2019-11-07/india-s-outlook-to-negative-by-moody-s-as-growth-risks-mount; Colin Scott, *Private Regulation of the Public Sector: A Neglected Facet of Contemporary Governance,* 29 J. L. & SOC. 56 (2002); Robert H Sifon-Arevalo et al., *Sovereigns: Sovereign Rating Methodology*, S&P GLOBAL (June 4, 2025), https://www.spglobal.com/ratings/es/regulatory/article/-/view/sourceId/10221157.

158. Elkhourey, *supra* note 157, at 2-3, 8-9.

downgrades of their bonds and their own sovereign credit rating,[159] which would negatively affect the cost of borrowing and access to credit for the state, its governmental subunits, and its domestic private firms.[160] From the rating agencies' perspective,

> [i]t is reasonable to assume that orthodox policies focusing on the reduction of inflation and government budget deficits are favoured. There is a risk, therefore, that in order to avoid rating downgrades, borrowing countries adopt policies that address the short-term concerns of portfolio investors, even when they are in conflict with long-term development needs.[161]

In other words, ratings agencies influence states' economic policymaking, subtly and sometimes dramatically, directly and indirectly. This should be understood as a concrete example of how private market actors can effectively circumscribe states' control over their monetary and financial systems.[162] Relatedly, it is now routine for institutional and other sophisticated creditors to purchase protection from credit loss to both public and private borrowers in the form of credit default swaps. As a result, the movement in prices of credit default swaps has become an important source of information and influence along with formal credit ratings.[163]

Under normal circumstances, the sustainability of public and external indebtedness is primarily a function of economic growth and fiscal discipline, although both can become unsustainable because of unexpected shocks to the domestic economy.[164] At some point, the overall amount of a state's indebtedness itself becomes a threat to sustainability and, therefore, a distinct concern for policymakers and markets.[165] And the sustainability of external indebtedness in particular is often also a function of the cost and availability of foreign currency. Countries can reduce vulnerability to high levels of external debt by accumulating

159. "As a result, even some sovereigns that do not intend to issue cross-border debt in the immediate future are seeking credit ratings from CRAs." *Id.* at 9.

160. *Id.* at 11; Cantor & Packer, *supra* note 157, at 38.

161. Elkhourey, *supra* note 157, at 11.

162. *See* Kangle Zhang, Not Equal: Towards an International Law of Finance (2020) (Ph.D. dissertation, University of Helsinki).

163. Frieda, *supra* note 148, at nn. 14-15, 298-99, 307.

164. Porzecanski, *supra* note 147, at 309-12.

165. High levels of private indebtedness—whether owed to domestic or external creditors—can represent a public vulnerability because private debt crises often evolve into government debt crises, largely through the fulcrum of the domestic banking sector. *See generally*, Anna Gelpern, *Banks and Governments: Aerial View* (GEO. U. L. CTR. 2013).

foreign reserves,[166] although doing so has macroeconomic trade-offs.[167] Given these different factors, there are various ways to measure the sustainability of a country's debt and its vulnerability to debt crises.[168]

As of March 2025, India's total external debt was $736.3 billion, which represented 19.1 percent of the country's GDP.[169] Of that, 54.2 percent was U.S. dollar-denominated and 31.1 percent was denominated in Indian rupees.[170] The dollar-denominated debt represented mostly commercial debt.[171] Commercial debt—including commercial loans and bonds, bank borrowing, and foreign portfolio investments in debt instruments—was also the largest component of total external debt (39.6 percent), followed by domestic bank accounts of non-resident Indians (22.4 percent).[172] Formal external sovereign debt was $168.4 billion (13.3 percent).[173] Of the total external debt, $134 billion was short-term debt (18.3 percent of all external debt and 20.1 percent of foreign reserves).[174] The country's foreign exchange reserves have been robust since the 1990s;[175] they are currently enough to cover over 90 percent of its total external debt.[176]

1. External Commercial Debt

India's corporate debt markets have been relatively slow to develop and fall far short of providing the credit needs of domestic firms.[177] Thus, larger firms have increasingly turned to foreign lenders, which in turn slows the development of the domestic financial system as financial assets

166. Frieda, *supra* note 148, at 303.

167. *Id.* at 303.

168. Porzecanski, *supra* note 147, at 322-23 (noting that foreign debt to exports has become a less important measure of debt sustainability, owing in part to the decline in importance of the distinction between domestic and foreign debt).

169. *India's External Debt: A Status Report, 2024-25*, GOV. OF INDIA, MINISTRY OF FIN., at xii, available at https://dea.gov.in/files/external_debt_documents/Ex%20Debt%20Report%20 2024-25_Final.pdf.

170. *Id.* Other significant amounts of debt were borrowed in yen (6.2%), IMF special drawing rights (4.6%) and the euro (3.2%). *Id.*

171. Patnaik et al., *supra* note 129, at 3. The term ECB (external commercial borrowings) has a specific meaning in the context of Indian regulations on borrowing from abroad, and is different from the term "foreign currency borrowing" in several respects." Patnaik et al., *supra* note 129, at 3-4, n 1.

172. *India's External Debt: A Status Report, 2024-25*, *supra* note 169, at 8-9.

173. *Id.* at 7.

174. *Id.* at 4.

175. REDDY, *supra* note 56, chpt. 18.

176. *India's External Debt: A Status Report, 2024-25*, *supra* note 169, at 4.

177. Echeverri-Gent, *supra* note 61, at 77.

are effectively exported.[178] Under the existing legal framework, Indian firms generally borrow abroad in foreign currency, including through trade credit, and incur rupee-denominated external debt by issuing bonds available to foreign investors.[179] The amount of India's external foreign currency borrowing, which is attributable mostly to commercial debt, has increased significantly over the last two decades.[180] Notably, however, this increase in external and foreign currency borrowing has been limited to a relatively small set of the largest and well-performing commercial firms in the country.[181]

This increase has exacerbated systemic vulnerabilities as was revealed during the global financial crisis of 2008-09.[182] In the years leading up to that crisis, "a large share of India's corporate debt market moved offshore."[183] Firms then had to return to the domestic credit market when global credit markets dried up in the crisis, creating stress on the domestic markets.[184] In that way, "[t]he growing exposure of Indian firms to foreign debt created a channel through which the [crisis] affected India."[185]

Even in peacetime, the increase in foreign currency borrowing by commercial firms puts pressure on exchange rate management. In India, as elsewhere, monetary policy that targets exchange rate stability provides some protection for firms that are most exposed to a depreciation of the rupee.[186] But moral hazard can complicate this effort if borrowers rely on exchange rate stability when borrowing in foreign currency and fail to hedge currency risk as a result. Such unhedged currency risk, if widespread, can lead to build up of risks in the financial and monetary systems.[187] To address this, if indirectly, bank regulators generally require "[c]apital and provisioning requirements for [banks with] exposures to entities with unhedged foreign currency exposure."[188]

178. *Id.*

179. Patnaik et al., *supra* note 129, at 5-8; *India Bonds*, CBONDS, http://cbonds.com/countries/India-bond (last visited Sep. 15, 2025).

180. Patnaik et al., *supra* note 129, at 3, 8-9.

181. "One can immediately see that less than 10 percent of the firms in that year's sample have documented FCB." *Id.* at 12-13.

182. *Id.* at 3.

183. Echeverri-Gent, *supra* note 61, at 79, n. 9.

184. *Id.* at 77.

185. *Id.* at 79.

186. "One goal of managing the exchange rate is the "avoidance of sovereign debt through commercial borrowings." REDDY, *supra* note 56, at 46.

187. Patnaik et al., *supra* note 129, at 2-3.

188. *Id.* at 8.

2. External Public Debt

Not only is public debt a smaller portion of India's external debt than commercial and foreign-held bank accounts, external public debt is a rather small portion of all of the country's overall public debt.[189] India's total public debt has been roughly eighty-three percent of its GDP in recent years, spiking to ninety percent as a result of the pandemic.[190] This reflects a significant if sustainable overall debt burden.[191] But according to Reddy, "the structure of public debt displays characteristics that make [India] less vulnerable than other countries with similar debt magnitudes."[192]

Until the 1990s, the RBI essentially provided money to the central government by purchasing government debt when necessary, effectively monetizing government debt.[193] In the 1990s, the government began a general process of "delinking" public debt and its monetization by the RBI.[194] Now, the largest components of the country's public debt are debt securities of the central government and the subordinate states. The total national government debt in India was approximately $3.16 trillion in 2024.[195] The central government has approximately $1.3 trillion in outstanding securities,[196] and the states have approximately $755 billion, more than governmental subunits in many other emerging economies.[197] There is a very small amount of municipal bond debt, although that may

189. Anneesha Chitgupi et al., *Who Lends to the Indian State?* (XKDR, Working Paper No. 34, 2024).

190. International Monetary Fund, *General Government Gross Debt to GDP*, available at https://www.imf.org/external/datamapper/GGXWDG_NGDP@WEO/OEMDC/ADVEC/WEOWORLD/IND; *India's Public Debt Ratio to Jump to 90 Per Cent Because of COVID-19*: *IMF*, ECON. TIMES (Oct. 14, 2020, 5:51 PM), https://economictimes.indiatimes.com/news/economy/indicators/indias-public-debt-ratio-to-jump-to-90-per-cent-because-of-covid-19-imf/articleshow/78661641.cms?from=md.

191. REDDY, *supra* note 56, at 106-107.

192. *Id.* at 50.

193. *Id.* at 91.

194. *Id.* at 104.

195. *See* Aaron O'Neill, *India: National Debt from 2020 to 2030*, STATISTA (May 26, 2025), https://www.statista.com/statistics/531619/national-debt-of-india/; *see also* Reserve Bank of India, https://www.rbi.org.in/Scripts/FAQView.aspx?Id=79 (last visited Oct. 13, 2025).

196. Reserve Bank of India, https://rbidocs.rbi.org.in/rdocs/Content/PDFs/OS_GS_L2014.PDF (last visited Oct. 13, 2025); Ira Drugal, *India's Integration with Global Bond Markets: A Tale of Two Ideas*, NDTV PROFIT (Jan. 7, 2020, 8:02 AM), https://www.ndtvprofit.com/opinion/indias-integration-with-global-bond-markets-a-tale-of-two-ideas.

197. Reserve Bank of India, *Frequently Asked Questions*, https://www.rbi.org.in/Scripts/FAQView.aspx?Id=79 (last visited Oct. 13, 2025).

be poised to increase somewhat.[198] The number of municipal bond issuances have nearly doubled in the last couple of years,[199] with the total amount of municipal bond debt currently around $382 million.[200]

Notably, most of the country's public debt is local currency-denominated and most is held by domestic entities.[201] Again, while India's has over $2 trillion in outstanding government securities, its external sovereign debt is just under $170 billion.[202] State governments are not authorized to borrow externally.[203] Borrowing has increased and become increasingly more important for states within the Indian federal system.[204] In 2017, the states ceded most of their taxing powers to the central government to receive a portion of revenues from a new national sales tax.[205] But the recent pandemic revealed cracks in this arrangement as the states received less from the central government than they expected,[206] forcing them to add significantly to their existing stock of debt.

198. *See* Adam Feibelman & Bhargavi Zaveri-Shah, *The Case for a Municipal Bankruptcy Law in India*, *in* INSOLVENCY AND BANKRUPTCY BOARD OF INDIA, QUINQUENNIAL OF INSOLVENCY AND BANKRUPTCY CODE (2021), available at https://ibbi.gov.in/uploads/whatsnew/1d8b31fc65f7ac6f09a973be8f12f868.pdf.

199. *Municipal Bond Statistics*, SEC. AND EXCH. BD. OF INDIA, available at https://www.sebi.gov.in/statistics/municipalbonds.html.

200. *Id.*

201. *Status Paper on Government Debt (FY21)*, INDIA MINISTRY OF FIN., at 15, 16-17, available at https://dea.gov.in/files/public_debt_management_documents/Status_Paper_on_Government_Debt_for_2021_22.pdf ("Government securities are primarily held by domestic institutional investors."); Chitgupti et al., *supra* note 189 at 34 (noting that only five percent of lending to the state in India is from voluntary sources, describing the balance as financial repression); Vatsal Nahata, *Who Finances India's Public Debt: Key Policy Implications*, FIN. EXPRESS (May 21, 2023), available at https://www.financialexpress.com/market/who-finances-indias-public-debt-key-policy-implications-3093997/. As noted above, the government has proposed new guidelines aimed to continue expanding foreign portfolio investments in government securities. *See supra* note 128.

202. *See supra* note 171; *see also Status Paper on Government Debt (FY21)*, *supra* note 201, at 48-49.

203. *Status Paper on Government Debt (FY21)*, *supra* note 201, at 6.

204. *See, e.g.*, Radhika Pandey et al., *Understanding States' Debt and Bond Markets* (Nat'l Inst. of Pub. Fin. & Pol., Working Paper No. 410, 2024), available at https://nipfp.org.in/media/medialibrary/2024/06/WP__410_2024.pdf.

205. "The states gave up the bulk of their tax-making powers to the federal government in 2017 in return for a share of revenue from a nationwide sales tax." Anirban Nag & Shruti Srivastava, *Investors Shun Indian State Bonds as Lockdown Slashes Revenue*, BLOOMBERG (Apr. 29, 2020, 5:00 PM), https://www.bloomberg.com/news/articles/2020-04-29/investors-shun-indian-state-bonds-as-lockdown-slashes-revenue; Echeverri-Gent, *supra* note 71, at 9-12 (discussing the fiscal relationship between India's central government and its states).

206. Nag & Srivastava, *supra* note 205.

The RBI manages public debt for both the federal government and states[207] to avoid volatility.[208] One aspect of this role is the management of states' exposure to currency risk.[209] But the link is still limited because relatively little of India's external central government debt is in foreign currency, and especially because the central government's bonds have been exclusively rupee denominated.

Interestingly, India's central government proposed in 2019 to issue around $10 billion in its first dollar-denominated bonds.[210] Shortly after the announcement, however, this plan was scrapped, and India did not issue the bonds.[211] The particular reasons for this change in plan remain a matter of speculation. But it is possible to understand the deliberations in India over issuing foreign currency bonds as a concrete illustration of the broader balance policymakers try to strike between engagement and integration with international financial markets and maintaining a relatively high degree of control over domestic monetary and financial affairs.

D. Private Money

As discussed above, financial instruments created outside of the formal banking and monetary system and subject to limited state control and management can be an important factor in reducing a state's control over its financial and monetary systems. The scope of this private financial activity corresponds in many respects to what is frequently described as "shadow banking."[212] Such private money inevitably impacts the routine conduct of monetary policy since holders of privately-created money will inevitably seek to convert it to "state money" in times of crisis,[213] it can also represent a major factor of vulnerability to systemic instability.

The role of privately created money—either foreign or domestic—in India's economy has increased in recent years with the country's

207. REDDY, *supra* note 56, at 105.

208. *Id.* at 107.

209. *Id.* at 106, 111.

210. *See* Mitu Gulati & Mark Weidemaier, *India to Issue Its First Foreign Currency Sovereign Bond?*, CREDIT SLIPS: SOVEREIGN DEBT (July 27, 2019, 9:50 AM), https://www.creditslips.org/creditslips/2019/07/india-to-issue-its-first-foreign-currency-sovereign-bond.html.

211. *Status Paper on Government Debt (FY21)*, *supra* note 201, at 6 ("There is no sovereign borrowing from international capital markets.").

212. *See, e.g.*, Pistor, *supra* note 2 (citing Tobias Adrian & Hyun Song Shin, *The Shadow Banking System: Implications for Financial Regulation* (Staff Report, Fed. Reserve Bank of N.Y., Working Paper No. 382, 2009).

213. *See supra* notes 42-44.

gradual liberalization of the domestic financial system. Yet it is still relatively modest. The amount of foreign-created private money in India is limited in large part through the operation of capital controls, as discussed above.[214] Private money creation and financial innovation within the country is limited both in scope and variety. As explained below, the country's financial system is generally bank-heavy, and most commercial finance is conducted by formally regulated institutions, although a significant amount of smaller scale commercial finance in the country is informal—especially trade credit and small unregulated loans.[215]

The financial activities of non-bank financial institutions (NBFIs) are sometimes described as shadow banking in India.[216] They form a sector that has faced crises and episodes of instability in recent years.[217] But these activities represent only a narrow portion of shadow banking as that activity is conventionally understood outside of India, especially since the global financial crisis.[218] These institutions, though not banks by definition, provide basic financial products and are regulated by the RBI, which is also the banking regulator. And, in any event, the sector is modest compared to the banking sector.[219] Along with commercial banks, NBFIs, the informal sector, and microfinance institutions, institutional participants in the domestic market for money instruments include

214. *See supra* Part III.B.

215. *See, e.g.*, Ira N. Gang et al., *Finance, Gender, and Entrepreneurship: India's Informal Sector Firms*, 58 J. DEV. STUDS. 1383 (2022).

216. Viral V. Acharya et al., *The Growth of a Shadow Banking System in Emerging Markets: Evidence from India*, 39 J. INT'L MON. & FIN. 207, 208 (2013), available at https://pages.stern.nyu.edu/~sternfin/vacharya/public_html/pdfs/NBFC_Paper.pdf (noting that "NBFCs in India appear to be substitutes for direct lending by banks in the non-urban parts of the Indian economy"); Sashi Sivramkrishna et al., *Shadow Banking in India,: Nature, Trends, Concerns and Policy Interventions*, 12 REV. ECON. BUS. STUDS. 29 (2019), available at https://www.ceeol.com/search/article-detail?id=1240629; Arvind Awasthi & Siddharth Shukla, *Growth of Non-Banking Financial Sector in India: Trends and Determinants,* 65 J. GOKHALE INST. POL & ECON. 247 (2023), available at https://gipe.ac.in/wp-content/uploads/2023/10/Artha-Vijnana_September-2023_compressed.pdf#page=41.

217. *See* Awasthi & Shukla, *supra* note 216, at 248; Sivramkrishna et al., *supra* note 216.

218. Shachindra Nath, *India's NBFCs, Wrongly Called Shadow Banks, Need the Government's Backing*, QUARTZ, https://qz.com/india/1658264/ilfs-dhfl-other-nbfcs-need-nirmala-sitharamans-budget-help/ (last updated July 20, 2022).

219. Financial Stability Board, *Global Monitoring Report on Non-Bank Financial Intermediation*, at 54 (2024), available at https://www.fsb.org/uploads/P161224.pdf. In 2019, the sector represented $42 billion in assets. *See Why India's Troubled Shadow Banks Spook the Market*, BLOOMBERG (July 1, 2019), https://www.bloomberg.com/news/articles/2019-07-02/why-india-s-troubled-shadow-banks-spook-the-market-quicktake.

insurance companies, some large corporate firms, and state governments.[220]

Activities that generate important private money instruments around the globe are scarce or effectively non-existent in the country. While there is a growing number of money market mutual funds in the country, for example, the size of these combined is still relatively modest.[221] Securitization is discouraged by regulators, with significant limitations imposed for securitization of real estate loans.[222] Credit default swaps have been slowly introduced into the economy but are still relatively rare. To increase liquidity in the domestic corporate bond market, the Securities and Exchange Board of India recently moved to allow mutual funds to sell credit default swaps under some circumstances.[223] Previously, mutual funds were only allowed to buy credit default swaps, and they are still only allowed to do so to hedge actual risk in their portfolios.[224]

Similarly, a domestic derivatives market has emerged in recent years, especially for hedging currency risk, but that market is "shallow and illiquid" and Indian firms generally do not have access to foreign derivatives market (even to hedge currency risks).[225] The Reserve Bank of India has recently adopted some reforms to expand the domestic

220. Golaka C. Nath & Raja N. Aparna, *Indian Money Markey Dynamics*, CCIL MONTHLY RAKSHITRA NO. Feb. 2012 7-14 (2012), available at https://mpra.ub.uni-muenchen.de/38994/; *The Indian Money Market*, INDIABONDS (Oct. 31, 2024), available at https://www.indiabonds.com/bonduni/blogs/the-indian-money-market/.

221. *Funds Mobilised and Total Assets—According to Investment Objectives*, SEC. AND EXCH. BD. OF INDIA, available at https://www.sebi.gov.in/statistics/mutual-fund/mf-investment-objectives.html.

222. Echeverri-Gent, *supra* note 61, at 83. India's National Housing Bank recently created a residential mortgage-backed securitisation company to serve as "a commercially sustainable market intermediary to facilitate the growth and development of Residential Mortgage-Backed Securitisation (RMBS) market in the country." Press Release, Indian Ministry of Finance, RDCL, A Residential Mortgage-Backed Securitisation (RMBS) Company Set up by NHB Receives Certificate of Registration to Commence Operations, from RBI (Jan. 27, 2025), available at https://www.pib.gov.in/PressReleasePage.aspx?PRID=2096815.

223. Securities and Exchange Board of India, *Flexibility in Participation of Mutual Funds in Credit Default Swaps*, Circular No.: SEBI/HO/IMD/PoD2/P/CIR/2024/125 (Sep. 20, 2024), available at https://www.sebi.gov.in/legal/circulars/sep-2024/flexibility-in-participation-of-mutual-funds-in-credit-default-swaps-cds-_86871.html.

224. *Id.*

225. *See, e.g.*, Ajay Shah, *The Journey of Indian Finance*, *in* THE CAMBRIDGE ECONOMIC HISTORY OF MODERN SOUTH ASIA at 20 (Latika Chaudhary et al. eds., Cambridge U. Press 2026), available at https://ideas.repec.org/p/anf/wpaper/25.html#download ("A wide variety of rational trades such as short selling or derivatives trading are proscribed or banned."); Patnaik et al., *supra* note 129, at 4-5.

market for foreign exchange derivatives to expand the ability of residents to hedge against exchange rate risks.[226]

IV. CONCLUSION AND IMPLICATIONS

Through an array of interrelated policies, India has managed over the last three decades to significantly expand its engagement with the global economy and international monetary and financial systems. In this time, the country's cross-border trade has expanded significantly. Much more foreign investment is allowed in the country through a variety of pathways—both portfolio investment and direct investment, and in many sectors that were previously off-limits to foreigners, including the financial sector. Outward foreign investment by Indian firms has also increased significantly. In general, the country's financial sector is considerably more open, complex, and connected to the rest of the world than it was in the early 1990s.

Yet these capital flows are relatively modest compared to other emerging markets. They are actively managed by regulators in part to promote financial and monetary stability, and apparently as an integral part of exchange rate policy as well.

Policymakers in India continue to retain a great degree of control over other critical levers of its domestic economy. Relatively little of the country's public debt is held abroad, limiting its overall financial exposure to foreign interests, and its risk of exchange rate instability is greatly reduced by almost entirely avoiding public borrowing in foreign currencies. Developments and innovations that have become familiar features of the international financial system, especially the various types of shadow banking, have been slow to develop or avoided altogether in the country. Thus, the potential threat of domestic private money to India's control over its monetary affairs is substantially contained.

In sum, the country remains somewhere near the middle of the spectrum between the command economy of its founding and the model of a market economy embraced by the Washington consensus of recent decades. And it appears that policymakers have, over time, through an array of distinct but related institutional arrangements, deliberately chosen

226. *See* Reserve Bank of India, *Master Direction—Risk Management and Inter-Bank Dealings*, FMRD Master Direction No. 1/2016-17 (Sep. 22, 2025), available at https://www.rbi.org.in/scripts/BS_ViewMasDirections.aspx?id=10485; Veena Sivaramakrishnan, *Decoding the Liberalized FX OTC Derivatives Framework in India*, SHARDUL AMARCHAND MANGALDAS INSIGHTS (Jan. 13, 2025), available at https://www.amsshardul.com/insight/decoding-the-liberalized-fx-otc-derivatives-framework-in-india/.

this place on the spectrum. The country's approach is a somewhat stable equilibrium of very gradual liberalization and partial integration.

Taken separately, the country's regime of capital controls, its exchange rate policy, the amount and structure of its external debt, and the scope of domestic private money creation each present a set of particular policy challenges and opportunities. But together, they largely determine the overall extent of India's engagement with global monetary and financial systems and the scope of the state's ability to exercise control and authority over its economy.

Having avoided or limited many of the determinants that can undermine domestic control over monetary affairs, India thus appears to possess a significant degree of monetary sovereignty in the Pistorian sense. The country retains a great deal of power to direct and insulate its monetary and financial system and, thereby, its real economy. Since the beginning of the reform era in the 1990s, it has not needed to seek outside financial assistance, and it would take a dramatic shock to its economy to force it do so in the foreseeable future. It is fair to assume that this posture has at least helped the country preserve the degree of autonomy and democratic self-governance it enjoys. This at least somewhat complicates the notion of a hierarchy in international monetary affairs. India provides at least one example of a state that is not as subordinate as Pistor's account would suggest, yet not itself able to directly influence the fortunes of others.

More control over monetary affairs is not necessarily better. As noted above, many states that once enjoyed broad monetary sovereignty have voluntarily ceded or delegated it to supranational institutions, as have members of the euro zone. Or they have ceded it informally through channels of financial and monetary integration. States have been largely, if not primarily, motivated in these actions by the promise of an economic and financial trade-off.

That India has retained a meaningful degree of this component of sovereignty is a product of steady policymaking over decades, a broad consensus within bounds of disagreement. The gradual evolution of approaches to financial and monetary "modernization" in that country appears to have been constantly balanced against a strong concern about maintaining state autonomy, limiting vulnerability to foreign states, foreign institutions, and all private actors. While it is often tempting to see

in India an inexorable trend toward openness and engagement, there is a strong countervailing tug.[227]

This tug is a product of various factors, perhaps including fundamental aspects of the country's political economy, inertia, and limits imposed by state capacity. To at least some extent, however, India's approach should also be understood as a deliberate set of choices with a common aim of preserving a degree of autonomy or control over financial and monetary affairs in a global system that offers many ways to cede these things. Understanding the core policies that shape India's monetary system as determinants of its degree of monetary sovereignty can help sharpen or reframe ongoing domestic debates over these policies. Focusing on such policies as determinants of monetary control more generally can also help identify sources of vulnerability in economies that are thought to be at the top of the international monetary hierarchy, a topic for future study.

227. *See, e.g.*, Shah, *supra* note 225, at 1 ("While there is isomorphic mimicry with many things that look like a financial system [in India], officials retain substantial control over how finance works. In a functional perspective, Indian finance today resembles the environment of the 1980s more than meets the eye.").