A Rethink on India's Foreign Trade Policy

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Over the last decade, India's foreign trade – exports and imports – has undergone a significant transformation both in terms of composition of commodities and direction. However, foreign trade expanded over the period with dominance of import growth vis-à-vis exports resulting in widening of the negative trade balance. The trade policy announced on 27 August 2009, in the backdrop of the economic crisis, kept the short-term objective of arresting and reversing the declining trend of exports and sought to provide additional support to those sectors badly hit by the recession in the developed world. Accordingly a policy objective of achieving an annual export growth of 15% with an annual export target of $200 billion by March 2011 was set, and in the three years up to 2014, the country was expected to come back on the high export-growth path of around 25% per annum (Government of India 2009). Unfortunately, the growth target set for the years after 2012 turned out to be too ambitious as exports declined sharply in financial year (FY) 2012-13. It is also recognised that in a fast-growing economy a rapid increase in exports is the only option available to maintain the current account deficit at reasonable levels (Government of India 2011).

Against this backdrop, this note primarily attempts to review the developments in India's trade over the last decade vis-à-vis global trends. Secondly, the note analyses the changing composition and direction of India's exports and imports (in terms of $). One significant feature has been that India's exports never kept pace with imports during the high trade-growth phase. After analysing possible reasons, the note finally attempts to bring out some strategic steps that might be needed to correct the growing trade imbalance.

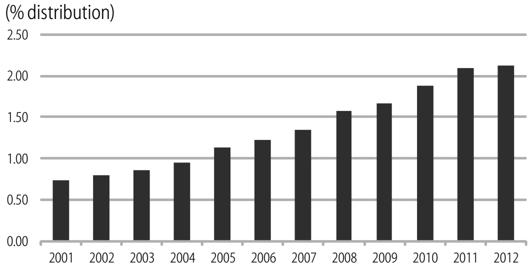
1 India's Place in Global Trade

India was one of the fastest growing economies in the last decade, its merchandise-trade growth expanded more or less in tandem with global trade. India's trade over the period showed remarkable increases, as its share in world trade went up from 0.80% in 2002 to 2.13% in 2013 (Chart 1). But unlike its east Asian counterparts, India's merchandise trade grew mainly due to increased imports than that of exports. As a result, the trade deficit accelerated from a near balance in 2000-01 to as high as $191.7 billion in 2012-13 (Chart 2, p 138).

1.1 Elasticity of Trade to GDP

An attempt has been made to work out crude elasticities of trade to gross domestic product (GDP) over the period 2002 to 2012 for India and the world (Table 1). It is generally observed that India's elasticity was significantly lower compared to world trade during the whole of the period – both during the pre-crisis period as well as the post-crisis periods. It is therefore the higher growth of GDP in India vis-à-vis that of the world, which has helped India's share in world trade grow over the decade. But, since the crisis of 2008, not only has India's trade elasticity come down significantly to 1.9 from 3.8 in the pre-crisis period, the real GDP growth is also converging more or less to the world's GDP growth rate (Chart 3, p 138). Looking at both, lower GDP growth and lower elasticity of trade to GDP, the trade outlook for the near term is indeed bleak and requires some special attention and strategic policy direction.

Chart 1: Share of India's Total Trade to World's Total Trade* (% distribution)



* in terms of $ Million.
Source: United Nations Conference on Trade and Development (UNCTAD).

2 Direction and Composition

Both in terms of direction and composition of commodities, India's trade still remains highly skewed despite some diversification seen in the last few years. This is reflected in the concentration of trade with a few countries, and in a few commodity groups. This tendency is evident both with respect to exports and imports. This makes India's trade vulnerable. The trade policy objective of diversification is yet to be achieved. Apart from this, what is also evident is the widening trade imbalance, which is biased towards imports rather than exports.

2.1 Direction of India's Trade

Direction of trade data reveals that India's trading partners are about 230 countries globally. But, of these, more than 60% of trade volume (in $) is with 23 countries. Among these 23 countries, India depends on only four countries, viz, United Arab Emirates (UAE), China, US and Saudi Arabia, for more than 51% of trade. Such an overdependence makes India's trade performance vulnerable to any changes that take place in these few countries.

Table 1: Crude Elasticities of Trade to Real GDP Growth (Average growth rate per annum %)

Period	Trade		GDP (Constant 2005 US$)		Crude Elasticities@	
	India	World	India	World	India	World
2002-08	30.4	16.4	8.0	3.3	3.8	5.0
2009-12	13.4	4.7	7.1	1.7	1.9	2.8
2002-12	23.6	11.7	7.7	2.7	3.1	4.4

@ Average growth in Trade/Average real GDP growth.
Data Source: World Bank and United Nations Conference on Trade and Development (UNCTAD).

India has been consistently maintaining trade deficits with most of the top trading partners. In terms of trade volume, the top 10 countries in order of importance in 2012-13 were: the UAE, China, the US, Saudi Arabia, Switzerland, Germany, Singapore, Hong Kong, Indonesia and Japan, accounting for 48% of total trade. India had a negative trade balance with six of these countries, viz, China, Saudi Arabia,

Chart 2: Trend in India's Export, Imports and Trade Balance ($ Million)

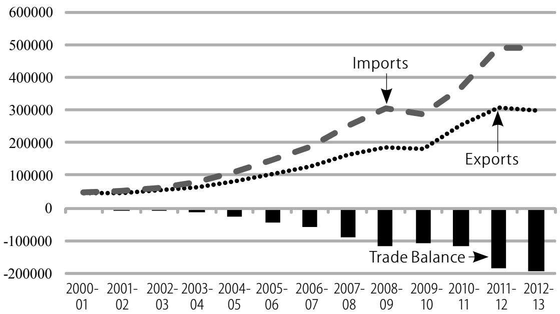
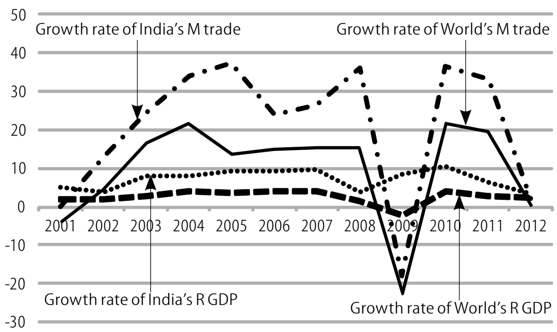


Chart 3: Trade Growth of India and World along with Real GDP Growth (constant 2005 $) **of India and World** (%)



Switzerland, Germany, Indonesia and Japan, far in excess of the positive balance with the remaining four countries. Among the top 23 countries accounting for about 60% of total trade volume, India's trade balance remained negative along with as many as 14 countries (EPW 2013). China has emerged as one of the important trading partners of India over the years, but the benefits are skewed towards China. In the first five months of 2013, India's trade deficit with China is reported to have increased by 34% to reach $12 billion.

Exports have no doubt become more diversified in terms of trading partners with a shift from developed economies to-wards developing ones, with China becoming one of the top three trading partners. Directional changes in exports were also seen clearly in the post-crisis period. India's exports to Europe, America, and Commonwealth of Independent States and Baltic shrunk after the economic slowdown hit in the year 2008. On the other hand, India's exports to Asian and African countries went up after the crisis. India has thus shifted focus from traditional markets in European and American countries to Asian countries.

The highest and most drastic shift in the direction of India's imports was seen from Asia, which was 29.22% in total imports in 2002-03, which increased to reach 60% of India's total imports in the year 2012-13. India's imports from north-east Asian countries (consisting of China, Japan and Hong Kong) have consistently remained higher with about 12% share. Decline in imports from Europe (from European Union countries) has been seen in the post-crisis period. Imports from America also bettered on account of augmented import from Latin American countries, while imports from North America came down after the crisis.

2.2 Composition of India's Trade

Exports: Compositional changes in India's export basket have been taking place over the years. A gradual shift in India's manufacturing exports was seen from labour-intensive sectors like textiles, leather and manufacturing, handicrafts, and carpets, to capital and skill-intensive sectors. Share of primary products in India's exports fell over the years from 15.90% in FY 2000-01 to 14.20% in FY 2012-13 (Table 2, p 138).

Table 2: Share of Export of Principal Commodities Group (%)

Commodity	2000-01	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
Primary products	15.90	15.60	13.50	13.70	12.00	13.40	14.20
Plantation	1.48	0.60	0.58	0.59	0.56	0.59	0.58
Agri and allied products	8.80	8.31	7.84	7.06	6.91	8.96	10.61
Marine products	3.16	1.06	0.83	1.17	1.04	1.13	1.15
Ores and minerals	2.62	5.61	4.26	4.88	3.45	2.75	1.85
Manufactured products	83.00	84.60	86.50	86.30	88.00	86.60	85.80
Leather and mnfrs	4.41	2.15	1.94	1.88	1.56	1.57	1.62
Gems and jewellery	16.75	12.07	15.33	16.27	16.13	14.67	14.45
Sports goods	0.15	0.08	0.08	0.08	0.07	0.07	0.07
Chemicals and related products	14.01	13.72	12.99	13.66	12.29	12.87	14.15
Engineering goods	12.87	20.68	21.85	18.21	19.84	19.14	18.89
Electronic goods	2.54	2.15	3.87	3.15	3.30	3.06	2.81
Projects goods	0.06	0.09	0.08	0.06	0.03	0.03	0.05
Textiles	24.26	11.33	10.43	10.71	9.24	8.89	8.78
Handicrafts	1.50	0.31	0.16	0.13	0.10	0.09	0.07
Carpets	1.32	0.58	0.42	0.41	0.41	0.28	0.33
Cotton raw incl waste	0.11	1.36	0.35	1.15	1.16	1.41	1.22
Petroleum products	4.29	17.42	14.87	15.77	16.52	18.32	19.98
Unclassified exports	1.66	2.49	4.13	4.83	7.40	6.18	3.39
Total	100	100	100	100	100	100	100

Data Source: DGCIS, Kolkata.

Contribution of the top-10 commodities was on an average at 62%, for the period starting from 2003-04 up to 2012-13. Petroleum (crude and products), gems and jewellery, transport equipment, machinery and instruments, and electronics goods are among the top-10 commodities. Export of gems and jewellery increased steadily in value terms. Export of petroleum also grew consistently but for a dip recorded in FY 2008-09. Transport equipment was the persistent performer among this group. Rather, most of the commodities in this band improved performance each year except in 2008-09, when impact of crisis surfaced leading to a moderation in exports.

About 58% to 60% of India's export earnings are generated from four commodity groups, viz, garment, gems and jewellery, engineering goods, and petroleum products. The share of engineering goods which reached 21.85% in 2008-09 dipped to 18.9% in 2012-13. The share of gems and jewellery came down to around 14% from 17%. The jewellery industry is an import-based industry and hence sufficient credit in foreign currency is a must for easy and continued availability of raw diamond. Export of readymade garments saw a substantial fall during the period. The share of readymade garments dipped to 4.3% from about 12.5% mainly due to competition from China, Bangladesh, Turkey and Vietnam. This sector is labour-intensive and offers maximum scope for export and employment growth.

Imports: India is a net importer of crude for its energy needs and has faced rising petroleum imports. In recent times, global oil prices are more or less stable, but India's petroleum bills have gone up mainly due to an increase in demand for petroleum in volume terms.

Presently, the share of petroleum import is about 35% of total imports. Similarly, the import of hi-tech capital good imports whose share now is about 18% may also go up. This is unavoidable for a developing economy. But, the share of gold import which was averaging at about 7% of total imports jumped to about

11.5% in the last couple of years (Table 3). As a result import bill increased from $4 billion to $58 billion between 2000-01 and 2011-12.

3 Strategic Rethink

Since India is facing a widening trade deficit with major trading partners, bilateral trade negotiations should emphasise some element of reciprocity. Now, the position seems to be one-sided favouring the partner's interests more than India's.

Manufacturing exports have the lion's share in total exports over the years. It constituted 85% of the total merchandise exports in FY 2003-04 which increased over the period to 86% in 2012-13. The manufacturing sector has sustained its share but growth somehow looks restricted.

As noted by Kumar and Gupta (2008), the lack of a focused approach in identifying, sustaining and building the country's competitive advantage, the concentration of exports in low value categories and relatively poor inflow of foreign direct investment (FDI), especially in export-oriented industries are responsible for the relatively weak performance of India's manufacturing exports.

Exports have shifted towards technology-intensive-manufacturing exports with an increased share of engineering goods, petroleum products, chemical and related products from labour-intensive traditional sectors like textiles, gems and jewellery, leather, jute, carpets and handicrafts. There is scope to im-prove efficiency of these sectors which can contribute to enhance their share in manufacturing exports. Boosting exports of these sectors has the added advantage of increasing employment as these are labour-intensive industries. These sectors are facing peculiar problems. These include securing availability of raw material and alternative markets for gems and jewellery, corporatisation and compliance of environmental standards for leather, technology upgrades for improved productivity, balance between the domestic and export requirements for jute and ways and means to handle variations in international demand for carpets and handicrafts.

If we want to enhance our performance in these traditional sectors we need to tide over existing shortcomings by ensuring adequate availability of raw material, skill development, manufacturing parks/clusters, tapping potential markets, appropriate brand promotion, providing financial/fiscal incentives, capacity building for export, continuation of existing schemes, etc.

Micro, small and medium enterprises (MSMEs) have made substantial contributions to the Indian economy, and exports from this sector have been accorded high priority in India's export promotion strategy. The sector faces a number of problems such as low levels of technology and innovation, inadequate access to concessional credit, poor marketing, and branding, packaging and complicated government procedures. Addressing these problems is expected to improve their production capability and exports. Emphasis of the strategy is on skill development and training, standardisation and quality, access to affordable credit, impetus for innovation, and brand building.

The share of MSMEs in total exports is spread across different product segments. In case of items like textiles, leather goods, processed food, engineering goods, and gems and jewellery, export performance has been commendable over the years. Sectors like sports goods are almost 100% export-oriented. In view of this, export promotion from MSME sector has been accorded high priority in India's export promotion strategy which includes simplification of procedures, incentives for higher production of exports, preferential treatment to MSMEs in market development fund, simplification of duty drawback rules, higher value addition, skill development and training, thrust on standardisation and quality, access to affordable credit, impetus for innovation, etc, would be essential elements of the strategy (Government of India 2011).

Table 3: Share of Imports of Principal Commodities Group (%)

Commodity Group	2000-01	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
A) Bulk Imports	41.82	44.62	45.58	42.92	40.60	43.63	46.35
of which: Petroleum Crude and Products	31.32	31.70	30.84	30.22	28.66	31.67	34.43
B) Pearls, Precious and Semi-Precious Stones	9.62	3.16	5.53	5.65	9.36	5.76	4.59
C) Machinery	8.22	18.00	13.50	12.55	11.20	10.58	9.89
D) Project Goods	1.50	0.51	1.05	1.63	1.66	1.79	1.33
E) Others	38.84	33.71	34.34	37.24	37.17	38.24	37.83
of which: Gold and Silver	9.28	7.05	7.39	10.33	11.52	12.59	11.34
Total	100	100	100	100	100	100	100

Data Source: DGCIS, Kolkata.

The focus on gold and oil alone to restrict imports tends to obscure other important impediments which are also structural and policy-induced. India has the third largest coal reserves in the world, yet it has imported substantial quantity of coal for internal consumption and thus share of coal and coke in total import rose from about 2.2% to 3.4% between 2000-01 and 2012-13. Similarly, one-third of fertiliser consumption is imported as there was inadequate production capacity within India. Share of fertiliser in total imports is still about 2%. India is also among the larger edible-oil-consuming countries, but it still imports edible oil from countries like Malaysia and Indonesia for domestic consumption. The ban on iron ore mining in several states has meant that steel producers have to import ore. The share of metalliferrous ores and products in imports doubled to 3% during the period. Similarly, the shares of import of many conspicuous consumption goods are also increasing.

Thus, the faster growth of imports is getting more and more skewed in favour of gold and avoidable imports of some commodities and luxury items. Such items cover more than 25% of India's import bill. Import substitution in several commodities should be explored.

To conclude, after the eruption of the sub-prime crisis in the US which was followed by the European crisis it was inevitable to change our focus towards non-traditional markets to keep our exports alive, which have taken a major hit after the crisis and still remained shaky. There is a dire need to scale up exports in the wake of unabated and inevitable high imports.

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