SUBJECT- INDIAN ECONOMY (Generic IVth)

CHAPTER – 27

TRADE POLICY OF GOVERNEMENT OF INDIA

Topics for Today's Class (21/04/2020)

- **Foreign trade and economic growth in India**
- **The Liberalization Policy - 1985-91** (Pre Independence Policy)
- **Developments in Trade Policy since July, 1991**

FOREIGN TRADE AND ECONOMIC GROWTH IN INDIA:

Introduction: Theoretically, the relationship between foreign trade and economic growth can be a positive, a negative and an elective one. The positive view has been held by the classical and neo-classical economists. According to them foreign trade is, "an engine of economic growth". On the other hand, structuralists believe that international trade has an actually operated to the detriment of the poor countries causing deterioration in their terms of trade. In between the two extreme positions lies the elective view, which incorporates some elements of each of the opposing viewpoints.

Foreign Trade Policy and Development in lndia –

During the last four decades lndia followed the policy of industrialization through import substitution. The adoption of import substitution (IS) strategy of development was influenced by the consideration of 'size' factor and also because of 'export pessimism'. The Mahalonobis Model of development adopted in the Second Five Year Plan visualized no role for international trade in economic growth. It was based on the assumption of a relatively closed economy. In subsequent plan periods, lndia became highly 'controlled' and an 'isolated' economy having the very high rates of effective protection, in the range of 100 to 200 percent or even more. This led to very inefficient domestic industries and heavy prices for domestic consumers. The heavy protection and subsidies to industry led to excessive capital intensity and relatively little labour absorption and thus generally aggravating the unemployment and under-employment problems. In India, import substitution has been the problem of under-employment. In lndia import substitution has been come too far.

The formation of trade-policy in lndia has been mainly dictated by the size of the country. Generally, it is believed that foreign trade does not occupy an important role to play in case of large countries like U.S.A., China etc. The average propensity to import in case of Large countries is relatively small as compared to small countries.

The large countries have sufficient natural resources and very extensive domestic market and hence, they are not dependent on foreign trade for the sale of their products. As a result of this, lndia till 1965 did not assign any role to trade-policy for achieving growth and equity.

In June 1966, Government of lndia devalued its currency to overcome its adverse balance of payment situation. According to some economists, Like Jagadish Bhagwati, it was an attempt to introduce liberalization in Indian economy. However, it was a very 'mild' or 'partial' liberalization in which no other reforms were undertaken in trade and exchange rate policies. The liberalization episode can be defined as an extensive use of the price mechanism that would reduce the anti - exports bias of the trade regimes. The distortions in the economy should be minimized if not fully abolished. The trade liberalization should outward and inward orientation are two sides of the same coin that serve to show whether the policy emphasis is put on the domestic markets or on international trade.

In the Third Plan period, some attempts were made to promote the exports, but still the trade policy was highly restrictive and controlled. There were severe restrictions on trade and exchange rates. A renewed emphasis was placed on export promotion with the sharp widening if trade deficits followings the two oil shocks of 1973 and 1978-79. In 1978, the Alexander Committee gave a dimension to import - export policy in India by a number of innovative suggestions. The committee recommended that protection through licensing system couldn't be continued definitely and that there is a merit in exposing Indian industry to competitive environment so that it leans the skills of efficient production and management for cost reduction and improvement in quality of product.

The Alexander Committee introduced the elements of trade-liberalization and globalization in our export import policy in 1978, although, despite liberalization in import and industrial policies, the desired improvement in efficiency of industry did not take place.

Abid Hussain Committee:

Due to failure of the Alexander Committee, in achieving its objectives, the Government appointed in July 1984, a high-powered under the chairmanship of Shri Abid Hussajn, then secretary to the Ministry of Commerce, to go into the details of the framework of the Import-Export policy and suggest measures for rationalization and improvement in the policy wherever necessary. The trade policy of 1985-86 has been developed on the basis of 'Abid Hussian Committee'. The main objectives of the Import-Export policy were as follows:

1, To import continuity and stability in Import-Export policy;

2. To facilitate production through 'earner access' to 'imported inputs';

3. To expand the base for export promotion;

4. To promote efficient import substitution;

5. To reduce licensing, streamline procedures and decentralize decision-making.

The Liberalization Policy - 1985-91 (Pre Independence Policy):-

The liberalization policy has focused on two aspects:

(1) Foreign Capital, and

(2) Trade Policy.

(1) Foreign Capital: The industrial policy provides increased opportunities for foreign investment with a view to take advantage if technology transfers, marketing expertise and introduction of modern managerial techniques. It is also intended to promote a much-needed shift in the composition of external private capital inflows towards equity away from debt - creating flows. The following measures have been announced in this regard:

(a) Automatic approval will be given for direct foreign investment up to 51 percent foreign equity ownership in a wide range of industries. Earlier all foreign investment was generally Limited to 40 percent.

(b) To promote access to international markets, majority foreign equity holdings up to 51 percent equity will be allowed for trading companies, those primarily engaged in export activities.

(2) Trade Policy: For several decades, trade policy in India has been formulated in a system of administrative controls and licenses. As a result, the country has a bewildering number and variety of lists appendices and license. This system has led to delays, waste, inefficiency and corruption. Human intervention - described as discretion - at every stage, has stifled enterprise and spawned arbitrariness.

The first and major attempt of liberalization was done by the Rajiv Gandhi Government during the mid-eighties from 1985-86 to 1989-90, the exports surged forward and the period witnessed a record average annual growth of 17 percent in dollar terms. Unfortunately and unaccountably, this had declined to 9 percent in 1990-91 and to only 4.4 percent in April 1991. The Government, therefore, decided that while all essential imports like palm oil and edible oil would be protected, all other imports would also be linked to exports by enlarging and liberalizing the replenishment licensing system.

As part of our country's strategy to promote the international integration of our economy, it is necessary to phase out the excessive and often indiscriminate protection provided to industry which weakened the incentive to develop a vibrant export sector. An important element of the strategy will be a transition from a regime of quantitative restrictions to price-based system. Our medium-term objective is to progressively eliminate licenses and qualitative restrictions especially for capital goods and raw materials, so that these could increasingly be placed on Open General License (OGL)

Developments in Trade Policy since July, 1991:

In 1990-91 the Indian economy experienced the adverse balance of payment crisis with the outbreak of Gulf-War. In order to solve the BOP problem and other structural rigidities, the Government in July 1991 implemented strong comprehensive trade and exchange rate reforms. The Government has realized the importance of trade liberalization and globalization. The purpose of this study is to analyze these measures in detail, therefore, we would just make a reference of the Export-Import Policy from 1991-92 to 1996-97.

The principle objectives of this policy are as under:

1. TO establish the framework for globalization of India's foreign trade;

2. To eliminate or minimize quantitative, licensing and other discretionary controls in the framework of India's foreign trade;

3. To simplify and streamline the procedures governing exports and imports;

4. To promote efficient and internationally competitive import substitution and self-reliance under a deregulated framework for foreign trade;

5. To promote the productivity, modernization and competitiveness of Indian industry and a deregulated framework for foreign trade;

6. To augment India's exports by facilitating access to raw materials, intermediaries, components, consumables and capital goods from international market.

According to this policy, exports and imports are allowed freely subject to regulation by Negative List of Exports or a Negative List of Imports. The number of items in the two lists has been reduced to the minimum. In addition to this the Liberalized Exchange Rate Management System (LERMS) has been introduced from March I, 1992, and the rupee has been made partially convertible for all approved external transactions. The discussion of all these trade policies changes establish a fact that the Government of India, is fully committed to the policy of liberalization and globalization of the Indian economy in order to make it competitive and productive.

Further, the trade policy that was earlier characterized only by short-term changes to combat exigencies was turned into a long-term consistent policy. But it also raised an important related issue regarding the probable impact on the trends in exports and imports of such changes

The five year Export and Import policy (EXIM Policy) undergoes modifications in the form of changes in the licensing policies, alterations in the list of items subjected to various trade restrictions, and procedural changes every year. The modifications to the Exim Policy declared by the Ministry of Commerce on April 1, 2000 and April 1, 2001 is very much in tune with the requirements of the WTO panel ruling about Quantitative Restrictions (QRs). This also marks India's another decisive step towards liberalization and export-induced growth.

The existing **Export Processing Zones** (EPZs) are to be converted into **Special Economic Zones** (SEZs). The SEZs will be treated as being outside the customs territory of the country and have special tax breaks. In order to boost the exports, the deregulation policy promoted in the country. A scheme is evolved for granting special assistance to the state governments on the basis of export performance and export related infrastructure. Various steps have been taken in rationalization of export promotion schemes like (i) Export Promotion of Capital Goods Scheme, (ii) Duty Exemption Scheme, (iii) Duty Entitlement Passbook Scheme, (iv) Rationalization of Deemed Export Scheme and (v) Sector specific rationalization involving Gems and Jewellery, Silk, Leather Handicrafts and Garments, Drugs etc. On the import side, the QRs on 714 tariff Lines have been removed. The Special Import License (SIL) list was abolished in April 2001.

The amendments of the Exim policy made during April 2001 further gave importance to the boosting up of the exports. This was mainly done with the view to compensate with the Liberalization of the imports. The highlights of the policy included creation of market access initiative, introduction of the new chapter on Special Economic Zones, extension of Annual Advance License Facility for deemed export and the intermediate supplies, extension of the validity of the duty free Replenishment Certificate Scheme and the procedural simplifications. It gave special importance to the agricultural sector through the creation of the Agricultural Export Zones wherein the state governments may identify product specific Agri-Export Zone for end to end development for export of development products from geographically contiguous areas.

Further, Quantitative Restrictions were removed on 111 items at 8-digit Level, Tariff policy revised within the bound rates, the customs duties have been enhanced on tea, coffee, copra, coconut and desiccated coconut from 35 percent to 70 percent and on crude edibie oils, the rates range from 45 percent to 75 percent and 85 percent. The EXlM Policy Schemes like Duty Exemption Scheme and the Export Promotion Capital Goods Scheme are being made applicable to the agricultural sector.