

India's New Foreign Trade Policy Pluses and Minuses

BISWAJIT DHAR

Despite some steps in the right direction, the new policy has several limitations. This article makes a case for looking at them anew.

The long-awaited foreign trade policy (FTP) of the National Democratic Alliance (NDA) government evoked much interest both because it was the first comprehensive statement on the government's priorities in the external sector, and also, perhaps more importantly, it would show if the present government has set its sights differently from the United Progressive Alliance (UPA) government.

It was the UPA government that tabled the first FTP in 2004, replacing the export–import policy. This seemed to suggest a change in the thinking of the

policymakers—they had finally understood that it was necessary to move beyond export–import procedures and incentives for improving foreign trade performance, and that it was imperative for FTP to consider policies for improving production efficiencies and reducing transaction costs. In other words, FTP had to extend beyond the decision-making confines of the Department of Commerce, and the department had to develop a broader framework that provided the scope for coordinating with a number of administrative ministries to make the foreign trade sector more vibrant. But despite tabling two five-year FTPs, the UPA government did little to change the orientation of policy-making in trade.

The NDA government has attempted a new approach in its FTP by tabling two documents. While the main document follows the UPA government's practice of

Biswajit Dhar (bisjit@gmail.com) teaches at the Centre for Economic Studies and Planning, Jawaharlal Nehru University, New Delhi.

detailing export–import procedures, the new government has made a detailed foreign trade policy statement (FTPS) that articulates its overall thinking on the external sector, covering two key dimensions. First, the policy statement spells out the government’s strategy for addressing some of the structural and institutional issues that are relevant for improving the performance of the foreign trade sector. Second, the government has given some idea about its thinking on the ways in which it would make trade and economic integration agreements with major trade partners work better for Indian enterprises. The second dimension is important because India has concluded a number of economic integration agreements with trade partners over the past decade, but most of them have not delivered the expected results.

‘Whole-of-Government’ Approach

It must be said to the credit of the Department of Commerce that it recognises that “foreign trade policy can neither be formulated nor implemented by any one department in isolation” and that “a ‘whole-of-government’ approach will be required.” The FTPS speaks of a “major path-breaking” initiatives that the department has taken “to mainstream State and Union Territory (UT) Governments and various departments and ministries of the Government of India in the process of international trade.” Yet, another reflection of a possible change in thinking in the commerce department is an important statement made in the FTPS—“the biggest challenges that India’s foreign trade faces today are from within the country.” To meet these challenges, the FTPS underlines the need for “Setting Our House in Order.”

There is no doubt that bold print of the FTP shows a welcome departure from past thinking. The proposed involvement of other departments and ministries of the central government as well as state and union territory governments, and the recognition of “behind-the-border” constraints faced while engaging in foreign trade should be regarded as steps in the right direction. However, the details of this strategy

spelt out in the FTPS have several limitations, and there is a strong case for looking at them anew.

The “whole-of-government approach” lists the possible areas of engagement with state and union territory governments, but is silent about the manner in which departments and ministries of the central government would be involved in supporting conduct of foreign trade. As for states and union territory governments, the FTPS mentions that they “can play a crucial role in promoting exports and rationalising non-essential imports.” This statement is quite intriguing since governments in member-countries of the World Trade Organization (WTO) have little policy space to either promote exports or restrict “non-essential imports.” One of the key objectives of the WTO is to minimise government interference in the conduct of foreign trade and, therefore, members are not allowed to provide subsidies and other incentives for promoting exports. As for “rationalising non-essential imports” (appears to be a euphemism for “restricting imports”), it should be pointed out that state and union territory governments do not have any instruments for doing so. Imports can only be restricted by using customs duties, which can only be imposed by the central government. Further, India had the right to restrict imports of “non-essential” products using quantitative restrictions because of a weak balance of payments (BoP) situation, which it did until 2000. However, this right had to be given up in 2001 after a WTO Dispute Settlement Panel ruled that India no longer faced BoP problems and therefore had no basis to continue with these restrictions.

The other dimensions of involving state and union territory governments that are listed in the FTPS are essentially statements of intent. These include assistance that the Department of Commerce is providing state and union territory governments to prepare export strategies and set up an “Export Promotion Mission to provide an institutional framework to work with State Governments to boost India’s exports.” It is not entirely clear from the FTPS how these initiatives will give the necessary

impetus to state and union territory governments to participate more vigorously in export promotion.

Three Issues Highlighted

What are the steps that the FTPS suggests for “setting our domestic house in order?” It suggests this can be done by addressing three sets of issues. The first is to make better use of telecommunications and information technology (IT) infrastructure, especially the internet, in trade transactions. The second is to remove the anomalies caused by the “absence of a uniform system of indirect taxation in India.” The existing system, according to the FTPS, prevents exporters from getting “a rebate or drawback on all indirect taxes paid on the exported product and the inputs that went into its production, significantly inflating the final price of the exported product and making it less price competitive”. And the third is the “liberalisation, rationalisation and simplification of labour laws.” The FTPS insists,

Recent initiatives by the Central Government and some State Governments ...must be taken to their logical conclusion in order to make Indian labour more productive and efficient, which will, in turn, contribute to enhancing the global competitiveness of India’s products.

Given the huge burden of inefficiencies that plague the domestic manufacturing sector, which often begin at the shop-floor, the three areas identified by the FTPS seem to convey yet again that the policy-makers are not fully cognisant with what it takes to make India a globally competitive production hub. What is really needed is actualising the “whole-of-government” approach, which can provide a comprehensive view about the needs of the manufacturing sector for enhancing its competitiveness. This approach, which was a feature of policies adopted by most of the successful countries in East Asia, is

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essential for repositioning Indian industry on the world stage.

SEZ Failure

Special economic zones (SEZs) are another area where successive governments have ignored the steps necessary to make them function effectively. Although the FTPS says that exports from SEZs increased significantly from Rs 22,000 crore in 2005–06 to Rs 4,94,077 crore in 2013–14, there is a facet of these zones that the government needs to consider. Since the notification of rules under the SEZ Act in 2006, 435 SEZ had been formally approved by the Board of Approvals until March 2015. Of these approved SEZs, 189 have been functional. Importantly, all but 20 of these SEZs were established before 2010 and only three after 2013. The past few years have also witnessed a spate of cancellations of the approvals granted for setting up SEZs. Since July 2014, approvals for 82 SEZs have been withdrawn by the Board of Approvals. India's experience with SEZs thus seems to be at considerable variance with that of China, where SEZs have contributed immensely to the country's export growth over the past several decades. One possible way forward for the Government of India would be to understand the process countries such as China follow for establishing of successful SEZs and consider applying good practices wherever they are possible under Indian conditions.

Regional Trade Agreements

As mentioned, the FTPS provides an account of the Government of India's position on its economic integration agreements with partner countries. The commerce and industries minister has commented on more than one occasion that these agreements have not been particularly beneficial to India's interests and that they must be comprehensively reviewed. Perhaps in the continuation of this position, the FTPS indicates that two sets of initiatives should be taken—one, to make these agreements work better for Indian enterprises through focused programmes; and two, to explore opportunities in countries where India has a relatively small footprint, including through economic integration agreements.

The South Asian Free Trade Agreement (SAFTA), one of the older free trade agreements that India is a party to, has remained largely dormant. The government has proposed reinvigorating SAFTA by building regional value chains in several sectors that are of considerable interest to the countries in the region, which include textiles, engineering goods, chemicals, pharmaceuticals, auto components, and plastic and leather products. Successful implementation of this proposal would go a long way towards furthering the cause of South Asian regional integration.

India's free trade agreement with the Association of Southeast Asian Nations (ASEAN), which has been operational since 2009, has not brought the desired benefits. The present government has therefore proposed reworking the contours of its engagement with its eastern neighbours by focusing on trade integration with the CLMV (Cambodia, Lao PDR, Myanmar and Vietnam) countries. As a part of this strategy, it has decided to support the development of manufacturing hubs by the Indian private sector in these countries.

The government has indicated that it will actively consider enhancing India's economic engagements with the African region by assisting countries there to develop their productive capacities in both agriculture and manufacturing. Such a programme would not only complement the development cooperation initiatives that were taken by the UPA government, but also enable these initiatives to yield better results.

Although the FTPS is an important statement of the government's intent to improve the performance of the foreign trade sector, the results are not likely to be delivered if the operational framework is not made functionally more robust. There are a number of weaknesses in the proposed framework that were alluded to in an earlier discussion, and the government would need to address them. There is a greater urgency for so doing because the FTPS sets an ambitious target of increasing India's exports of merchandise and services to \$900 billion by 2019–20, which would raise the country's share in world exports to 3.5% from the 2% it is now.

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