

International Trade

7

CHAPTER

External trade growth collapsed in different countries in the tumultuous recession-ridden years of 2008 and 2009. The fall in trade, which was steeper than the decline in real GDP, was arrested in 2010, with trade growth recovering faster than real GDP growth. The recovery in trade growth has been made possible, in part, by the fiscal stimulus imparted by the governments and the low base of the preceding years. However, the extent of recovery differs substantially across countries and world trade remains below its pre-crisis level. India, which weathered the global crisis well, seems poised to be among the few countries to surpass the earlier peak and even reach or surpass the pre crisis trends in trade.

WORLD TRADE

7.2 The sudden and sharp decline in world trade from US \$ 16 trillion in 2008 to US\$ 12.4 trillion in 2009 was followed by an impressive recovery in 2010. World trade reached US\$ 7.03 trillion in the first half of 2010, with a value growth of 24 per cent. World trade volumes which fell by an unprecedented 10.7 per cent in 2009 have quickly recovered with a growth of 12 per cent in 2010 as per the International Monetary Fund's (IMF), World Economic Outlook (WEO), January 2011 (Table 7.1).

While this recovery is partially due to the base effect, the pickup in world output from the negative territory of (-) 0.6 per cent in 2009 to a positive 5.0 per cent in 2010 backed by the fiscal stimulus of different countries helped. As stated by the IMF, world trade remains below its pre-crisis trend and for some economies, particularly those hit by a banking crisis, it remains below pre-crisis levels. Growth in trade volumes of emerging and developing economies in 2010 was more robust than that of advanced economies, just as the fall in 2009 had been less severe.

Table 7.1 : Trends in growth in trade volumes

(per cent change)

	2009	2010	Projections	
			2011	2012
World Trade Volume (goods and services)	-10.7	12.0	7.1	6.8
Imports				
Advanced Economies	-12.4	11.1	5.5	5.2
Emerging and Developing Economies	-8.0	13.8	9.3	9.2
Exports				
Advanced Economies	-11.9	11.4	6.2	5.8
Emerging and Developing Economies	-7.5	12.8	9.2	8.8

Source : IMF, World Economic Outlook, January 2011

7.3 Growth in world trade volume is expected to moderate in 2011 and 2012 to 7.1 per cent and 6.8 per cent respectively, as per IMF projections. However, the trade growth in emerging and developing economies is expected to be more robust than that in the advanced economies in 2011 and 2012.

Trade Credit: International Scenario

7.4 While the global economic crisis adversely affected international trade, on the supply side there is enough evidence to suggest that the financial crisis might have reduced the availability of trade credit. This could have resulted in a decline in the volume of trade that would otherwise have taken place even with the demand shock. Thus the shortage in trade credit might have deepened and prolonged the recession. Nearly 90 per cent of world trade reportedly depends on some form of trade finance or insurance, with the total size of this market estimated at between US\$ 10 to 12 trillion in 2008. The World Trade Organization (WTO) has estimated a shortage in trade finance liquidity to the tune of US\$ 25 billion as a fallout of the economic recession, whereas the World Bank estimated that the shortage in trade finance accounted for 10 to 15 per cent of the decline in trade.

7.5 A recent National Bureau of Economic Research (NBER) study provides new evidence that adverse credit conditions were an important channel through which the global economic and financial crisis affected trade volumes. Taking the case of the US market, the study states that countries with higher inter-bank rates and thus tighter credit availability exported less to the USA. Thus not only the fall in US demand, but even the credit tightening in the US, resulting in higher cost of trade financing for firms exporting to the US, could have posed a bigger challenge in countries with high cost of credit.

7.6 A study undertaken by the Organization for Economic Cooperation and Development (OECD) in June 2010 shows a differentiated picture in terms of the impact of trade finance on pre- and post-crisis trade, pointing to a threshold effect. The study highlights that availability of trade finance seems to have a limited impact on exports under 'normal' circumstances, i.e. outside crisis periods. However, an IMF-BAFT (Bankers' Association for Finance and Trade) survey in March 2010 is of the view that the drop in global demand was the most important reason for the decline in trade, followed by reduced

trade financing. An International Chamber of Commerce (ICC) survey of mid-2010 covering 161 banks located in 75 countries indicates that the costs of trade finance remain substantially higher than they were in the pre-crisis period, raising questions concerning affordability for exporters.

7.7 According to an April 2010 report by the Group of 20 (G-20) Trade Finance Experts Group, through the second half of 2009 and the first quarter of 2010, there is evidence that short-term trade finance markets have generally improved. Average prices for letters of credit in large emerging economies have fallen from 150-250 basis points (bps) a year ago to 70-150 bps, and the markets in many advanced economies are quickly returning to normalcy. However, this recovery has not been universal and several regions have markets that remain stressed, especially in Africa. Market sources cite that international or large pan-African banks continue to charge 200 to 320 bps to endorse a letter of credit in countries regarded as having a lower risk in Africa. Low-income countries in Asia and Central America seem to be in a better situation. In these areas, liquidity has returned to near normal, but there is still a market gap resulting from the general deterioration in the credit-worthiness of traders, coupled with greater risk aversion of commercial banks. An interesting development is a potentially long-lasting shift towards structured trade finance. The financial crisis brought a heightened sensitivity to risk, which has led to an increase in the relative demand for intermediated trade finance over traditional open account financing. In fact, recent estimates indicate that the level of intermediated (bank-supported) trade finance in 2009 surpassed that of open account transactions, reversing a long-term trend towards open account financing.

7.8 The G-20, in its Communiqué issued during the Seoul Summit (November 2010) has reiterated the need for enhancing the availability of trade finance in developing countries, particularly the low-income countries. In this regard, the G-20 Ministers have agreed to monitor and assess trade finance programmes in support of developing countries and to evaluate the impact of regulatory regimes on trade finance. The G-20 Trade Finance Expert Group, together with the WTO Experts Group on Trade Finance and OECD Export Credit Group, are mandated with assessing the current need for trade finance in low-income countries, and, if a gap is identified, will develop and support measures to increase its availability in low-income countries.

7.9 BAFT-IFSA (the merged entity of BAFT and International Financial Services Association) announced the Master Partnership Agreement (MPA) in June 2008 for mitigating the trade finance risk. The MPA is an industry standard for use by banks and their counter parties around the globe to facilitate the buying and selling of country and bank trade finance related risk. It is designed to simplify the exchange of documentation, reduce legal costs, increase efficiency, and promote trade.

7.10 Multilateral organizations have introduced several supportive measures to stimulate availability of trade finance. More than 850 foreign trade transactions for the total amount of \$550 million were supported by the European Bank for Reconstruction and Development's (EBRD) Trade Facilitation Programme (TFP) in 2009, providing additional benefits to the trade finance market. The Asian Development Bank's (ADB) Trade Finance Facilitation Programme (TFFP) exposure limit was increased to US\$ 1 billion. In 2009, the TFFP supported US\$2 billion in trade, an increase of over 300 per cent compared to 2008. Under its Global Trade Finance Programme, the International Finance Corporation (IFC) issued US\$3.46 billion in guarantees in financial year 2010, a 44 per cent increase over the previous year.

7.11 Pre-export financing and loans backed by export credit agencies have played a major role in 2010 trade finance markets. National governments across the globe devised strategies on war footing to support trade finance activities, some of them through the respective export credit agencies or developmental institutions (see Box 7.1).

Trade Credit: Indian scenario

7.12 In the wake of the global crisis and the problems being faced by exporters, the Reserve Bank of India (RBI) had reduced the interest rate ceiling to 250 bps below the benchmark prime lending rate (BPLR) on pre-shipment rupee export credit up to 270 days and post-shipment rupee export credit up to 180 days. This facility was available up to 30 June, 2010. In addition, the Government of India in its Union Budget for 2010-11 extended interest rate subvention of 2 per cent on pre and post shipment rupee export credit for certain employment-oriented export sectors such as handicrafts, carpets, handlooms, and small and medium enterprises up to 31 March 2011. On 9 August 2010, the interest rate subvention scheme was further extended to leather and leather manufacturers, jute manufacturing including floor covering, engineering goods, and textiles for the

Box 7.1 : Response to Trade Credit Crunch in Select Countries

The policy responses of some select countries related to trade credit were as follows:

- The US-Exim (Export-Import) Bank announced a programme for providing US\$ 4 billion in new short-term trade finance facilities and US\$ 8 billion in medium- and long-term trade finance facilities to support export of US goods to emerging markets. Similarly, China, through the China-Exim Bank, provided short-, medium-, and long-term trade finance facilities for export of Chinese goods and services to emerging markets.
- The Federal Reserve, USA announced currency swap facilities with the European Central Bank and central banks in various countries to keep the foreign currency liquidity in the international financial system.
- The UK Government announced plans to guarantee as much as £20 billion of bank loans to small and medium companies ensuring flow of credit.
- Germany announced a financial-sector rescue package of \$ 480 billion (US \$ 672 billion), to secure confidence in and liquidity into the banking system.
- The Central Bank of Russia announced schemes to lend to commercial banks without requisite collateral for up to six months. In addition, the Central Bank granted a credit line of US\$ 50 billion to Vnesheconombank until the end of 2009.
- The Government of Hong Kong SAR has proposed extending the maximum guarantee period for working capital loan for small and medium enterprises (SMEs) from two years to five years.
- The Japanese Government announced US \$1.0 billion trade finance facilitation initiative, to be developed in close cooperation with the IFC and ADB.
- Banco Nacional de Desenvolvimento Economico e Social (BNDES), the export credit agency of Brazil announced R\$ 6 billion working capital credit facilities for Brazilian companies.
- The Brazilian Central Bank auctioned US\$ 1 billion to banks (who will use it for trade credit lines) with repurchase clauses.
- Colombia and Venezuela jointly pledged US\$ 100 million each for creation of a special fund in order to boost cross-border trade between the two countries.

period from 1 April 2010 to March 31, 2011. With the introduction of a base rate, the lending rates charged on rupee export credit were deregulated with effect from 1 July 2010. However, the RBI has stipulated that banks may reduce the interest rate chargeable as per the base rate in the sectors specified above by the subvention available, even if the interest rate charged to exporters goes below the base rate, subject to a ceiling of 7 per cent.

7.13 As a result of difficult financing conditions prevailing in the international credit markets and increased risk aversion of the lending counterparties, the gross inflow of short-term trade credit to India during 2008-09 was lower than in 2007-08. The gross inflows of short-term trade credit reached US\$ 41.8 billion during 2008-09, while repayments (outflows of short-term trade credit) stood at US\$ 43.8 billion, resulting in a net outflow of US\$ 2.0 billion during 2008-09. Thus financing of short-term trade credit did not pose much of a problem in India. However, the situation changed in 2009-10 with short-term trade credit inflows increasing by 27.5 per cent to US\$ 53.3 billion, while short-term trade credit outflows increased only marginally by 4.5 per cent to US\$ 45.7 billion, thereby resulting in a net inflow of US\$ 7.6 billion. This trend became further pronounced in financial year 2010-11. Short-term trade credit to India recorded a large net inflow of US\$ 6.7 billion in H1 of 2010-11 (as against a marginal net outflow of US\$ 0.05 billion during H1 of 2009-10) in line with the increase in imports associated with strong domestic economic activity and improved conditions in the global financial markets. After the negative growth, as on 27 March 2009, export credit grew moderately as on 26 March 2010. This trend continued with export credit growth at 11.3 per cent as on 31 December 2010. However export credit as a percentage of net banking credit fell by 0.9 percentage points from 5.5 per cent as on 28 March 2008 to 4.6 per cent on 27 March 2009 and 4.1 per cent as on 31 December 2010 (see Table 7.2).

7.14 The various policy initiatives taken by the RBI through a hike in the all-in-cost ceiling for improving the trade credit mechanism, enhancement of the limit on overseas borrowings by banks, extending the line of credit as well as swap facility to Exim Bank, have helped in easing the pressure on trade financing. This is further corroborated by the increase in share of short-term trade credit (both inflows and outflows) in overall gross capital flows— while share of inflows increased from 10.9 per cent in 2007-08 to

Table 7.2 : Export Credit

Outstanding as on	Export Credit (₹ Crore)	Variations (Per Cent)	Export credit as per cent of NBC
24 March 2000	39,118	9.0	9.8
23 March 2001	43,321	10.7	9.3
22 March 2002	42,978	-0.8	8.0
21 March 2003	49,202	14.5	7.4
19 March 2004	57,687	17.2	7.6
18 March 2005	69,059	19.7	6.3
31 March 2006	86,207	24.8	5.7
30 March 2007	104,926	21.7	5.4
28 March 2008	129,983	23.9	5.5
27 March 2009	128,940	-0.8	4.6
26 March 2010	138,143	7.1	4.3
31 December 2010*	153,794	11.3	4.1

Source: Reserve Bank of India (RBI).

Notes:

* Variation over the figure as on 26 March 2010.

NBC—net banking credit.

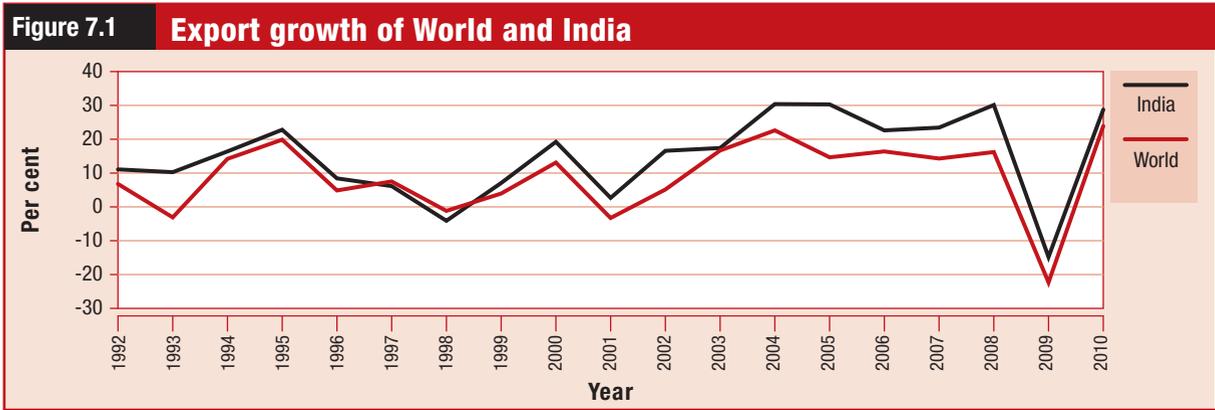
Data up to March 2004 relate to select banks accounting for 90 per cent of bank credit. Data 18 March 2005 onwards, pertain to all scheduled banks excluding regional rural banks (RRBs) availing of export credit refinance from the RBI.

15.6 per cent in 2009-10, share in outflows increased from 9.6 per cent to 15.8 per cent during the same period.

INDIA'S MERCHANDISE TRADE

7.15 India's trade growth (in US dollar terms) has been robust at 20 per cent plus since 2002-03. While India's trade growth has a strong correlation with world trade growth, it has been significantly higher than world trade growth particularly in two time periods, first just following the 1990 reforms and second after 2003 (see Figure 7.1).

7.16 Unlike many other countries, the global recession only slightly jolted the continued upward growth in India's export sector with exports rising at a reasonable rate of 13.6 per cent in 2008-09. The compound annual growth rate (CAGR) for India's merchandise exports for the five-year period 2004-05 to 2008-09 increased to 22 per cent from the 14 per cent of the preceding five-year period. However, in 2009-10 export growth was negative at (-)3.5 per cent, partly reflecting the effect of global recession and partly the higher base effect due to lagged export data of 2008-09. Despite this negative growth, India's ranking in the leading exporters in merchandise trade



Source: IMF & WTO

Note: Data for 2010 is only for three quarters

which slipped marginally from 26th in 2007 to 27th in 2008 improved to 21st in 2009.

7.17 However, this reasonably good overall picture for the whole year hides some of the difficulties through which the export sector went in the 12 crisis ridden months. In the case of India, the rebound in export growth from the second half of 2009-10 early 2010-11 was as sharp as the earlier fall, partly reflecting the low base and partly global trends (see Figure 7.2). Some deft handling by the Government on the export front also lessened the pain for the exporters in these trying months.

7.18 Though export growth decelerated from July to November 2010 after high spurts from February 2010 to June 2010, cumulative export growth in April-December 2010-11 was good at 29.5 per cent with

cumulative exports reaching US \$ 164.7 billion during this period. Current indications are that India will not only achieve the target of US\$ 200 billion but surpass it in 2010-11.

7.19 Export growth in dollar terms decelerated in 2008-09 while in rupee terms it exhibited an opposite movement reflecting the direct effect of the high depreciation of the rupee by 12.5 per cent. In 2009-10, while export growth in dollar terms was negative, in rupee terms it showed a very marginal increase due to the marginal depreciation of the rupee by 3.1 per cent. In 2010-11 (April-December), export growth was robust both in dollar and rupee terms, the latter being slightly less due to the appreciation of the rupee by 5.0 per cent (Figure 7.3). Import growth movements in dollar and rupee terms exhibited similar movements during the same period (Figure 7.4).



Source: Based on Directorate General of Commercial Intelligence and Statistics (DGCI&S) data.

Table 7.3 : Trade Performance : Volume and Unit Values

(Annual per cent change)

	Exports				Imports				Terms of Trade	
	Value		Volume	Unit Value	Value		Volume	Unit Value	Net	Income
	Rupee terms	US\$ terms			Rupee terms	US\$ terms				
2001-02	2.7	-1.6	0.8	1.0	6.2	1.7	4.0	2.8	-2.1	-1.3
2002-03	22.1	20.3	19.0	2.9	21.2	19.4	5.8	14.3	-9.8	7.4
2003-04	15.0	21.1	7.3	7.5	20.8	27.3	17.4	3.1	3.6	11.2
2004-05	27.9	30.8	11.2	14.9	39.5	42.7	17.2	18.9	-3.5	7.3
2005-06	21.6	23.4	15.1	6.1	31.8	33.8	16.0	14.0	-6.0	8.2
2006-07	25.3	22.6	10.2	13.7	27.3	24.5	9.8	15.1	-1.3	8.8
2007-08	14.7	29.0	7.9	5.1	20.4	35.5	14.1	1.9	2.6	10.7
2008-09	28.2	13.6	9.0	16.9	35.8	20.7	20.2	13.8	2.5	11.7
2009-10	0.6	-3.5	-1.1	1.0	-0.8	-5.0	9.9	-10.0	12.3	11.0
2010-11*	23.4	29.5	-	-	13.6	19.0	-	-	-	-

Source: Computed from DGCI&S data.

Note: * April-December 2010.

Volume and unit value index of exports and imports are with new base (1999-2000=100)

7.20 The deceleration in export growth in rupee terms in 2009-10 was not only due to the large deceleration of growth in unit values to 1.0 per cent compared to 16.9 per cent in 2008-09 but also due to actual decline in quantum by 1.1 per cent

compared to the 9 per cent growth in 2008-09. This was mainly due to the negative growth in both volume and unit values of manufactured goods. Export volume of food and food articles like rice, coffee, spices, and oilseed cake also fell (though their unit values

Figure 7.3 Export growth and exchange rate changes

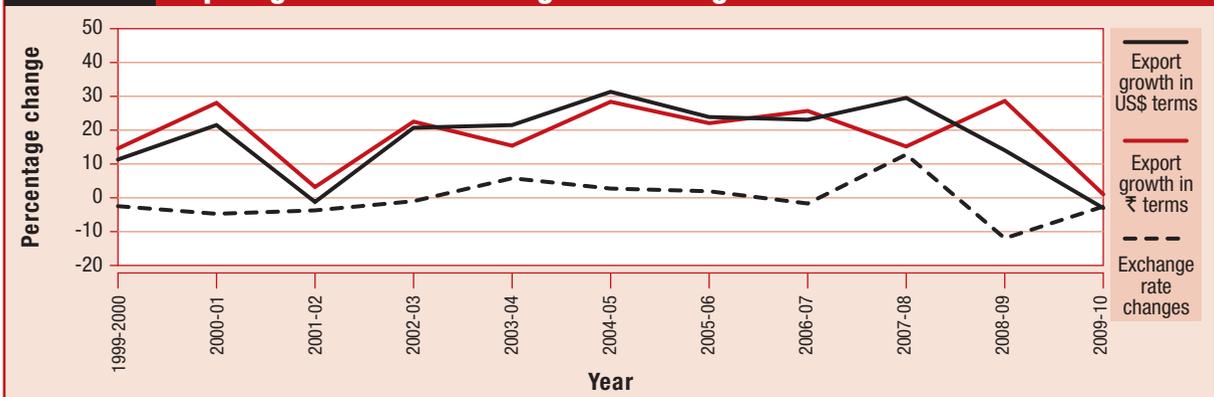
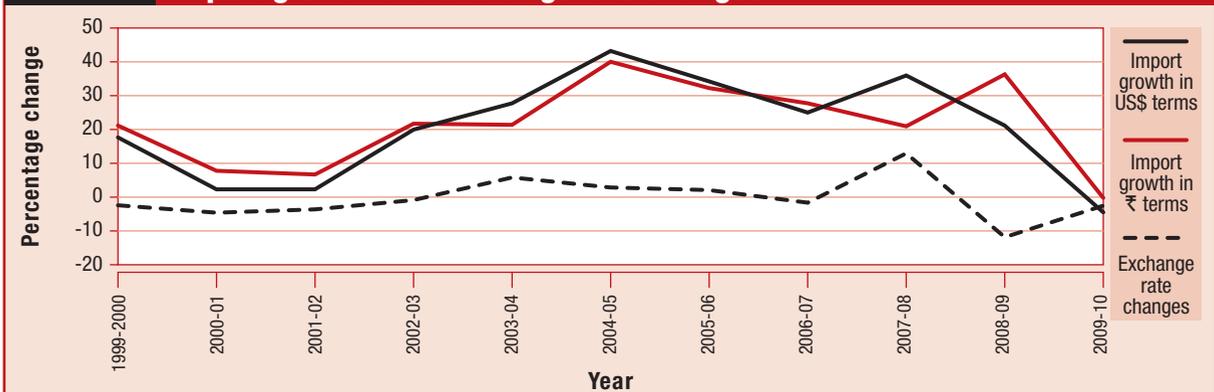


Figure 7.4 Import growth and exchange rate changes



Source: Based on DGCI&S and RBI data.

increased) mainly due to supply constraints and policy interventions like ban on exports in the case of non-basmati rice.

7.21 A dissection of the export quantum indices region-wise, shows that the negative quantum growth for the first time in the decade was due to the negative quantum growth for almost all the regions, except the South African Development Community, Asia-Pacific Economic Cooperation, and the European Union. In particular, the (-) 8.0 per cent growth for the Association of South East Asian Nations (ASEAN) and the (-) 5.8 per cent growth for North America which are among our major trading partners and the high negative growth of 22 per cent for the Commonwealth of Independent States (CIS) contributed to this fall in quantum of exports. Similarly a dissection of the import unit value indices, region-wise, shows that the negative growth for the first time in the decade was due to the negative growth of unit values in imports from all the regions, with the South African Development Community being the exception.

7.22 The deceleration of imports in rupee terms in 2009-10 was mainly due to the high negative growth of unit value indices even while volume growth was moderately high. This, in turn, was due to the high negative unit value growth in chemicals and related products despite the moderate quantum growth;

negative unit value growth of machinery and transport equipment coupled with the low quantum growth; negative unit value growth in miscellaneous manufactured articles and mineral fuels and non-fuel crude materials, despite their positive quantum growths.

7.23 The net terms of trade, which measures the unit value index of exports as a proportion of unit value index of imports, improved by 12.3 per cent. This was despite the very marginal positive growth in unit value index of exports as the growth of unit value index of imports was negative for the first time in this decade at 10 per cent. Income terms of trade, reflecting the capacity to import, grew at 11 per cent like in the two previous years. But unlike the earlier two years this was due to the high favourable growth in net barter terms of trade while export volume growth was negative for the first time in this decade.

7.24 India's share in world merchandise exports has started rising since 2007 albeit by a very slow 0.1 percentage point so as to reach 1.3 per cent in 2009 and 1.4 per cent in 2010 (January-June). This was mainly due to the relatively slow rise or greater fall in world export growth than India's (Table 7.4). The increase in China's share of world exports between 2000 and 2009 at 5.8 percentage points is 50 per cent of the total increase in the share of

Table 7.4 : Export growth and share in world exports : India and other select countries

	Value (US\$ billion)	Growth rate %				Share in world exports (%)				change in shares
		CAGR	Annual			2000	2008	2009	2010 (Jan- June)	
			2000- 07	2008	2009					
China	1202	25.4	17.3	-15.9	35.1	3.9	8.9	9.7	10.0	5.8
Korea	362	11.6	13.6	-14.3	34.3	2.7	2.6	2.9	3.1	0.2
Hong Kong	319	7.9	5.3	-12.2	24.8	3.2	2.3	2.6	2.6	-0.6
Russia	303	18.9	33.1	-35.7	51.4	1.7	3.0	2.5	2.7	0.8
Singapore	270	11.7	13.0	-20.2	37.4	2.2	2.1	2.2	2.3	0.0
Mexico	230	7.3	7.3	-21.3	35.4	2.6	1.8	1.9	2.0	-0.8
Taiwan	204	7.6	3.5	-20.1	49.3	2.3	1.6	1.6	1.9	-0.7
India	165	19.8	29.7	-15.2	35.3	0.7	1.2	1.3	1.4	0.7
Malaysia	157	8.7	19.1	-24.9	36.9	1.5	1.3	1.3	1.4	-0.3
Brazil	153	16.5	23.2	-22.7	27.5	0.9	1.2	1.2	1.3	0.4
Thailand	152	12.1	12.9	-12.0	36.8	1.1	1.1	1.2	1.3	0.1
Indonesia	119	8.8	18.3	-14.4	38.1	1.0	0.9	1.0	1.0	-0.1
South Africa	63	12.8	21.3	-26.0	31.2	0.5	0.5	0.5	0.5	0.0
EDEs	4572	16.9	25.3	-24.4	26.7	25.4	37.9	37.0	37.4	11.6
World	12,358	11.7	15.9	-22.7	24.0	100.0	100.0	100.0	100.0	-

Source : Computed from IMF, International Financial Statistics, November 2010.

Note: EDEs stand for emerging and developing economies.

emerging and developing countries over this period, while India's rise in share of 0.7 percentage points forms only 6 per cent of the total increase. However, China's export growth rate which was above 25 per cent in this decade till 2007, moderated to 17.3 per cent in 2008 and became a negative (-) 15.9 per cent in 2009 due to global recession. It improved to 35.1 per cent in the first half of 2010, following the general trend, as a result of recovery and low base effect. India's export growth was also negative at (-) 15.2 per cent in 2009 but recovered to 35.3 per cent in 2010 (January-June). While Russia's export growth in the first half of 2010 at 51.4 per cent is very high, standing at (-) 35.7 per cent in 2009, its fall had been equally great with Russia's share in world exports falling from 3.0 to 2.5 per cent.

7.25 International trade activity in Asia, which rebounded appreciably in the first two quarters of 2010, has tapered in the third quarter. This is partially due to the base effect and partially a reflection of the global trend in trade in Q3 of 2010. Both exports and imports have exhibited almost similar growth patterns with a deceleration in Q3 for most emerging Asian countries, except Hong Kong and Philippines, where growth in exports have improved marginally compared to the earlier quarter or earlier two quarters.

7.26 India's merchandise imports, also affected by global recession, fell to US\$288.4 billion with a

Table 7.5 : Quarterly Trade Growth of Major Asian Economies in 2010

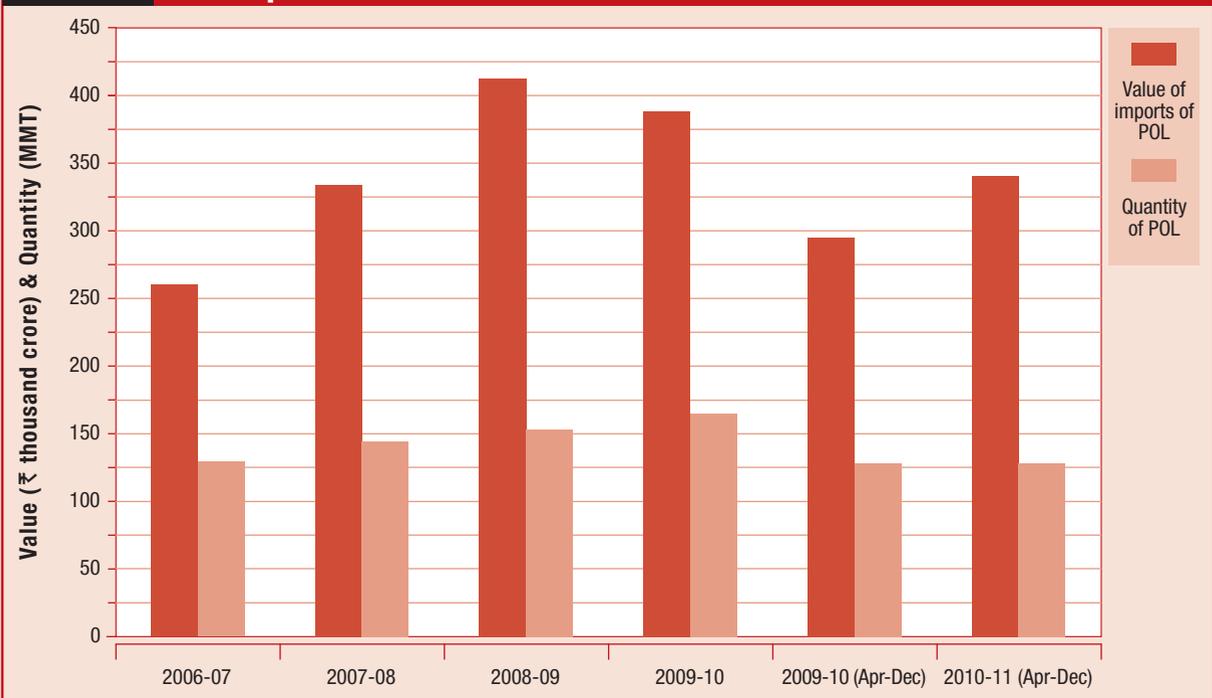
Country		Y-o-Y Growth (%)		
		Q1	Q2	Q3
China	Exports	28.7	40.9	32.3
	Imports	64.8	43.6	27.1
	Total Trade	44.1	42.2	29.8
Hong Kong	Exports	25.8	23.9	27.4
	Imports	34.2	29.4	23.8
	Total Trade	30.1	26.7	25.5
India	Exports	36.4	30.1	19.6
	Imports	61.6	32.3	31.0
	Total Trade	50.8	31.5	26.5
Indonesia	Exports	44.7	32.5	24.2
	Imports	49.9	44.7	29.6
	Total Trade	47.0	37.8	26.6
South Korea	Exports	35.8	33.1	23.7
	Imports	37.4	43.0	24.5
	Total Trade	36.6	37.5	24.1
Malaysia	Exports	40.8	33.2	23.1
	Imports	45.4	42.7	29.9
	Total Trade	42.7	37.4	26.1
Philippines	Exports	42.9	33.3	39.9
	Imports	33.3	25.4	21.3
	Total Trade	37.5	28.9	29.9
Singapore	Exports	38.3	36.6	27.5
	Imports	35.3	33.8	22.6
	Total Trade	36.9	35.3	25.2
Thailand	Exports	31.6	41.5	21.9
	Imports	58.1	46.0	30.5
	Total Trade	43.4	43.6	25.9

Source: Computed from WTO data.

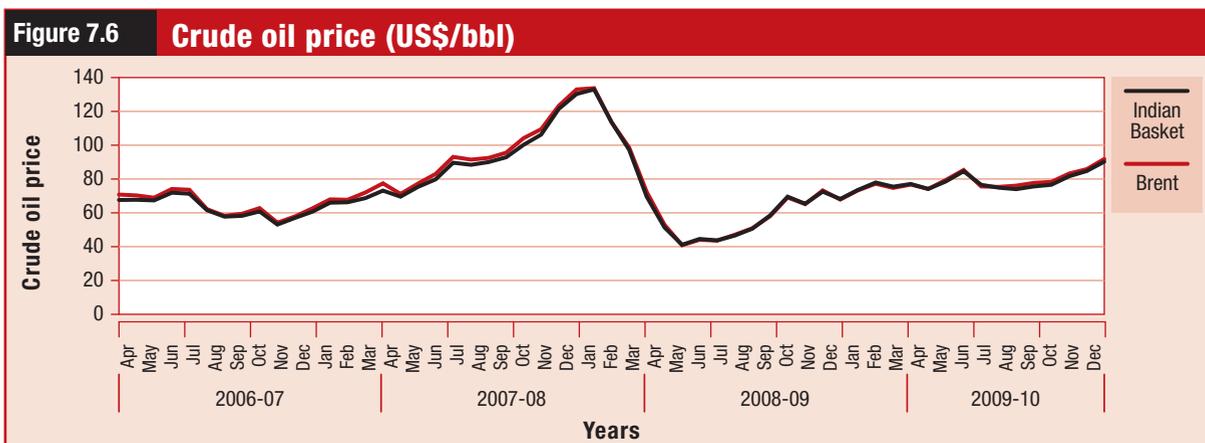
Note: Y-o-Y—year on year.

negative growth of -5.0 per cent in 2009-10. This was due to the fall in growth of petroleum, oil, and

Figure 7.5 POL Imports



Source : Ministry of Petroleum and Natural Gas (MOPNG).



Source : Based on MOPNG data.

lubricant (POL) imports by 7.0 per cent and non-POL imports by 4.2 per cent. POL import growth was low mainly due to decline in import price of the Indian crude oil import basket by 16.5 per cent despite the increase in quantity by 7.7 per cent (Figure 7.5).

7.27 International oil prices recorded an unprecedented rise during 2008 and remained considerably volatile during the entire ensuing period. The price of the Indian basket of crude oil which moved in tune with international oil prices was also volatile, averaging at US \$83.57 per barrel during 2008-09 after reaching an unprecedented US \$ 142 per barrel on 3 July 2008 before declining sharply following global recession. The monthly movements in oil prices from 2006-07 to 2010-11 (April-December) clearly reflect this volatility (Figure 7.6). Current oil prices are around US \$ 95-100 per barrel with Brent crude price even crossing the US\$100 mark in February 2011 and Indian crude oil basket reaching US\$ 98.4 per barrel on 11 February 2011.

7.28 Non-POL non-bullion imports declined by 8.6 per cent in 2009-10 reflecting relatively low demand for imports for industrial activity, partly due to low industrial growth and fall in exports resulting in lower demand for imports of inputs needed for exports. Imports also started picking up in the second half of 2009-10, though with a month's lag ending the nine-month continuous negative growth in December 2009. The rebound in imports was much sharper with import growth as high as 73.5 and 78.3 per cent in February and March 2010. This was partly due to base effect and partly due to the pickup in exports and industrial activity. During 2010-11 (April-December) import growth was at 19 per cent accompanied by an increase in both POL and non-POL imports at 17.7 per cent and 19.6 per cent respectively. Gold and silver imports registered a growth of 8.7 per cent. Non-POL non-bullion imports increased by 21.2 per cent due to recovery in industrial activity and exports.

7.29 Trade deficit (on customs basis) increased by 2.4 per cent to US\$ 82 billion in 2010-11 (April-

Table 7.6 : Growth in POL trade and non-POL imports (US\$ terms)

	Total imports	POL imports	POL exports	Net POL imports	Non-POL imports	Gold & silver imports	Non-POL, non-gold & silver imports
2001-02	1.7	-10.5	13.3	-13.8	7.2	-1.2	8.5
2002-03	19.4	26.0	21.6	26.8	17.0	-6.4	20.3
2003-04	27.3	16.6	38.5	12.9	31.5	59.9	28.5
2004-05	42.7	45.1	95.9	34.4	41.8	62.6	39.0
2005-06	33.8	47.3	66.5	41.4	28.8	1.5	33.1
2006-07	24.5	29.8	60.1	18.9	22.3	29.5	21.4
2007-08	35.5	39.8	52.5	33.7	33.6	21.0	35.2
2008-09	20.7	17.4	-3.0	28.7	22.2	26.4	21.7
2009-10	-5.0	-7.0	2.3	-10.9	-4.2	32.8	-8.6
2010-11(Apr.-Sept.)	26.0	29.7	66.0	15.1	24.5	12.1	26.3

Source : Computed from DGCI&S data.

December) from US\$ 80.1 billion in the corresponding period of the previous year. Trade deficit reached a peak of US \$ 118.4 billion in 2008-09 and moderated to US \$ 109.6 billion in 2009-10. The relatively higher import growth compared to export growth in the first half of 2010-11, raised the alarm of a possible unmanageable current account deficit. With import growth slowing down from October 2010 and exports picking up in November 2010, the fear that the high current account deficit may be due to high merchandise trade deficit is disappearing. Net POL import growth, which has been positive since 2002-03, became negative at -10.9 per cent in 2009-10 after a gap of seven years. However, during 2010-11 (April-September), it turned positive again with a growth of 15.1 per cent (Table 7.6).

TRADE COMPOSITION

Export composition

7.30 The export basket has seen major compositional changes in this decade with a 10 percentage point fall in shares of manufactures, a 12.6 percentage point gain in shares of petroleum crude and products, and a 3.3 percentage point fall in shares of primary products. This trend continued during the last two years, i.e. from 2008-09 to the first half of 2010-11, with the share of the major category, i.e manufactures, stagnating at 68.9 per cent and even falling in 2009-10; share of primary products falling to 12.7 per cent in the first half of 2010-11 after increasing in 2009-10; and share of petroleum crude and products increasing continuously both in 2009-10 and the first half of 2010-11 to reach 16.9 per cent. Within manufactures, there has been no major compositional change in the last two years. However, compared to 2000-01 the share of engineering goods has increased substantially while that of textiles including readymade garments (RMG) has fallen heavily from 23.6 per cent in 2000-01 to 9.5 per cent in the first half of 2010-11. The chemicals and related products category has made some gains in share, while leather and leather manufactures and handicrafts have lost shares.

7.31 A comparison of the commodity-wise growth of major exports of India to the major destinations in the first half of 2010-11 over 2008-09 shows a fall in the shares of manufactures exports to the USA and EU, while there is a rise in the case of 'Others'. In the case of petroleum, crude, and products, there is a gain in export shares to all the three destinations with a major gain to EU market, with high growth of

exports to EU and US markets in 2009-10 and the first half of 2010-11. In the case of primary products, the only major change was the fall in share of 'Others' (see Table 7.7).

7.32 While India's manufactures exports to the EU suffered a high negative growth in 2009-10, the recovery in the first half of 2010-11 was moderate compared to the robust recovery of manufactures exports to the other two destinations. Among manufactures, the performance of different product groups was varied. In the case of textiles exports to the US and EU, there was a fall in shares with a greater fall in the case of the latter. Negative export growth to the EU continued even in the first half of 2010-11, while there was moderate export growth to the US after three successive years of negative growth. In gems and jewellery also, in the first half of 2010-11, the share of exports to both the US and the EU fell with a higher fall in case of the former. In the case of exports of engineering goods to the US and EU there was a fall in shares with a relatively higher fall in the case of the latter in 2009-10 and a rise in shares in the first half of 2010-11. There was a rise in share of exports to 'Others' with a high growth of 50 per cent in the first half of 2010-11 (see Box 7.2). In the case of chemicals and related products, the share of exports to the US increased by nearly 3 percentage points, while it was stagnant in the case of the EU and fell slightly in the case of 'Others' in the first half of 2010-11 compared to 2008-09. The slowdown in India's exports to the EU where the recovery from global recession is weak is a cause for concern.

Import composition

7.33 The composition of imports also underwent changes in this decade. The share of food and allied products imports which fell to 2.1 per cent in 2008-09 from 3.3 per cent in 2000-01, increased to 3.7 per cent in 2009-10 and fell to 3.2 per cent in the first half of 2010-11 with slight fall in import shares of edible oils and pulses (Table 7.8). The share of fuel imports, however, remained at around 33 per cent. The most notable change is the sudden rise in share of capital goods imports from 10.5 per cent in 2000-01 to 15.0 per cent in 2009-10 and again a fall to 13.1 per cent in the first half of 2010-11 due to the see-saw movement in shares of imports of transport equipment. The share of gold and silver and electronic goods in the import basket decreased in the first half of 2010-11 compared to 2008-09 and 2009-10. The share of pearls, precious, and semi-precious stones saw a see-saw movement with negative

Box 7.2 : Indian Engineering Sector : Need for More Focus

The engineering industry is the largest segment of the Indian industrial sector. It accounts for 3 per cent of India's GDP with a 30.5 per cent weight in the index of industrial production (IIP); 29.9 per cent share of total investment; and 62.8 per cent share in foreign collaborations. Engineering exports are one of the largest foreign exchange earners for the country and account for over 20 per cent of India's total exports with around 35 per cent of the engineering exports contributed by the micro, small, and medium enterprises (MSME) sector.

India's export of engineering goods grew at 25.2 per cent (CAGR) during 2000-01 to 2007-08. In 2008-09, the growth moderated to 18.7 per cent and in 2009-10 it declined by 19.6 per cent because of global recession, with its share in total exports falling to 18.2 per cent. In the first half of 2010-11, there was a robust growth of 46.0 per cent partially due to base effect and partially due to global recovery following stimulus measures.

The performance of principal categories of engineering items export shows that in 2009-10, all the major categories of engineering goods had negative growth. In the first half of 2010-11, all the major categories like machinery, iron and steel, and other engineering goods registered high growth with the major sub-categories like transport equipment, primary and semi-finished iron and steel, non-ferrous metals and manufactures of metals registering whopping growths of 61.8 per cent, 65.0 per cent, 61.5 per cent, and 40.3 per cent respectively. Only one major sub-category, i.e. machinery and instruments registered moderate growth of 10.5 per cent (see Table 1)

Table 1 : Export Performance of Different Engineering Goods

Engineering Categories	Share in India's Total Exports(%)		Growth Rate (%)			
	2008-09	2009-10	2009-10 (Apr.- Sept.)	2010-11 (Apr. Sept.)		
1) Machinery	12.2	11.0	12.5	13.3	-13.3	37.7
a) Machine Tools	0.2	0.2	0.2	0.1	-26.4	-1.2
b) Machinery & Instruments	5.9	5.3	5.7	4.8	-13.3	10.5
c) Transport Equipment	6.1	5.5	6.7	8.3	-12.9	61.8
2) Iron & Steel	3.2	2.0	1.9	2.3	-39.2	63.9
a) Iron & Steel Bar Rods, etc	0.6	0.4	0.4	0.4	-34.2	59.1
b) Primary & Semi-finished Iron & Steel	2.6	1.6	1.5	1.9	-40.4	65.0
3) Other Engineering Items	6.4	5.2	5.1	6.2	-21.7	59.8
a) Ferro Alloys	0.8	0.5	0.4	1.0	-43.1	229.4
b) Aluminium other than Products	0.3	0.3	0.3	0.3	11.3	63.5
c) Non-ferrous Metals	1.1	1.2	1.0	1.3	5.4	61.5
d) Manufacture of metals	4.1	3.1	3.3	3.6	-27.2	40.3
e) Residual Engineering Items	0.1	0.1	0.1	0.1	-5.9	37.6
Total Engineering Exports	21.8	18.2	19.5	21.8	-19.6	46.0

Source: DGCIS

The major markets for Indian engineering exports are the USA, Singapore, UAE, UK, China, Germany, and Italy. Notably, while there was a fall in growth of India's engineering exports to most of the markets in 2009-10, its engineering exports to China grew by over 62 per cent.

With a 0.8 per cent share of world engineering exports in 2008, India ranks 30th – below all comparable countries – in the global engineering exports market. This low position is primarily attributable to three factors: 1) Low exports-to-GDP ratio: exports-to-GDP ratio of 15 per cent for India vis-à-vis 27 per cent for comparable countries 2) Low engineering-to-total exports ratio: engineering exports to total exports ratio of 24 per cent for India vis-à-vis 30 per cent for comparable countries 3) Low technology-intensity of engineering exports: share of high and medium technology products in engineering exports is 62 per cent for India vis-à-vis 71 per cent for comparable countries. Given India's current low share of world engineering exports and the significant scope for improvement in competitiveness, there is potential for achieving higher growth in this major sector of world trade.

Table 7.7 : Composition of exports by major markets

	Percentage share				CAGR 2000-01 to 2007-08	Growth rate ^a				
	2000-01	2008-09	2009-10	2009-10 (Apr.- Sept.)		2008-09	2009-10	2009-10 (Apr.- Sept.)	2010-11 (Apr.- Sept.)	
I Primary Products										
World	16.0	13.9	14.9	13.4	12.7	19.7	1.7	3.8	-27.8	23.2
USA	9.4	7.2	6.8	7.0	7.7	7.9	2.9	-13.5	-27.4	42.6
EU	13.1	8.4	8.6	9.0	8.5	12.7	1.7	-5.7	-23.5	15.8
Others	19.8	16.7	18.0	15.7	14.5	22.8	1.6	6.6	-28.5	23.0
(a) Agri & Allied Products										
World	14.0	9.6	10.0	9.3	8.5	14.6	9.7	1.1	-28.4	18.7
USA	9.0	6.0	5.8	5.9	6.6	4.4	13.1	-12.1	-25.9	45.1
EU	11.9	6.9	7.1	7.4	7.1	10.6	6.6	-6.4	-23.5	17.1
Others	16.8	11.0	11.6	10.4	9.1	17.1	10.0	3.8	-29.5	16.6
(b) Ores and Minerals (excl. coal, incl. mica)										
World	2.0	4.3	4.9	4.1	4.2	38.9	-12.5	9.9	-26.5	33.5
USA	0.4	1.2	1.0	1.1	1.1	37.9	-29.6	-21.1	-34.5	29.8
EU	1.3	1.4	1.5	1.6	1.4	26.0	-16.7	-2.5	-23.3	9.5
Others	3.0	5.7	6.5	5.3	5.4	40.7	-11.4	11.9	-26.5	35.7
II Manufactured Goods										
World	78.8	68.9	67.2	71.1	68.9	16.7	23.1	-5.9	-21.4	26.1
USA	90.6	90.2	89.1	88.5	88.7	11.3	7.1	-8.7	-24.9	30.4
EU	86.8	79.3	73.2	77.3	73.5	15.8	20.6	-15.4	-29.5	15.7
Others	70.9	62.0	62.0	66.5	64.5	19.3	28.9	-1.3	-17.3	28.7
(a) Textiles incl. RMG										
World	23.6	10.2	10.5	11.3	9.5	8.1	4.4	-1.2	-8.4	9.7
USA	27.2	18.4	18.4	19.1	16.9	7.1	-4.8	-7.6	-14.1	15.1
EU	29.2	18.2	18.5	19.9	15.7	11.4	7.9	-6.7	-10.5	-4.1
Others	19.8	6.4	6.9	7.5	6.7	6.3	6.2	6.9	-3.9	18.1
(b) Gems & Jewellery										
World	16.6	15.1	16.2	17.0	14.9	15.0	42.1	3.7	-20.9	14.2
USA	29.3	21.7	24.2	24.2	20.3	8.9	-7.7	2.8	-23.3	8.9
EU	11.5	8.3	6.7	6.9	6.4	11.3	24.8	-26.2	-48.5	12.8
Others	13.9	16.1	17.8	18.7	16.3	19.8	66.2	8.8	-15.5	15.4
(c) Engineering Goods										
World	15.7	21.8	18.2	19.5	21.8	25.2	18.7	-19.6	-32.1	46.0
USA	13.4	23.9	17.1	16.4	22.2	19.5	16.1	-33.9	-48.7	75.8
EU	14.0	25.4	20.8	22.2	22.1	27.1	25.7	-25.1	-41.0	21.1
Others	17.2	20.0	17.6	19.2	21.7	26.0	16.6	-13.1	-24.7	50.2
(d) Chemical & Related Products										
World	10.4	12.3	12.8	12.7	12.1	24.3	7.2	0.9	-18.1	23.8
USA	5.7	14.8	17.2	15.8	17.6	26.8	12.8	7.4	-9.9	45.5
EU	9.7	13.0	12.5	12.4	13.0	24.4	7.4	-11.8	-26.4	27.5
Others	12.5	11.6	12.2	12.3	11.0	23.7	6.0	4.0	-16.9	18.2
(e) Leather & leather mnfrs										
World	4.4	1.9	1.9	2.0	1.7	8.7	1.5	-5.5	-20.2	14.1
USA	3.7	1.7	1.5	1.6	1.4	-1.5	16.1	-17.8	-24.4	14.5
EU	11.4	5.9	6.3	6.7	6.0	9.5	1.0	-2.1	-16.9	8.2
Others	1.6	0.7	0.6	0.7	0.7	12.6	-2.1	-9.4	-26.8	31.1
(f) Handicrafts including Handmade Carpets										
World	2.8	0.6	0.5	0.5	0.5	2.3	-25.8	-10.6	-30.4	22.6
USA	6.0	1.6	1.5	1.5	1.4	-1.7	-30.6	-14.7	-32.2	21.6
EU	4.4	1.1	1.1	1.1	0.9	1.9	-18.0	-7.5	-29.4	3.2
Others	0.8	0.2	0.2	0.2	0.2	10.6	-30.2	-10.6	-29.4	56.4
III Petroleum, Crude & Products (incl. coal)										
World	4.3	14.9	15.8	13.3	16.9	46.8	-3.0	2.3	-42.5	66.0
USA	0.0	0.8	2.3	2.2	2.7	214.9	-76.2	180.3	21.5	61.4
EU	0.0	10.6	16.9	12.6	17.4	683.2	5.7	45.4	-10.9	67.9
Others	7.9	18.6	18.1	15.8	19.5	43.7	-5.0	-3.9	-47.8	64.5
Total Exports										
World	100.0	100.0	100.0	100.0	100.0	20.4	13.6	-3.5	-25.7	30.1
USA	100.0	100.0	100.0	100.0	100.0	12.1	2.0	-7.6	-23.5	30.1
EU	100.0	100.0	100.0	100.0	100.0	18.3	13.9	-8.4	-26.8	21.7
Others	100.0	100.0	100.0	100.0	100.0	23.5	15.7	-1.3	-25.7	32.6

Source : Computed from DGCI&S data

Note : Totals of I, II, and III may not add up to total exports due to some unclassified items.

^a Growth rate in US dollar terms

Table 7.8 : Commodity composition of imports

Commodity Group	Percentage share				CAGR 2000-01 to 2007-08	Growth rate (per cent) ^a			
	2000-01	2009-10	2009-10 (Apr.- Sept.)	2010-11 (Apr.- Sept.)		2008-09	2009-10	2009-10 (Apr.- Sept.)	2010-11 (Apr.- Sept.)
I Food and Allied Products, of which	3.3	3.7	3.5	3.2	19.3	9.1	69.0	59.8	13.7
1 Cereals	0.0	0.0	0.0	0.0	73.8	-93.3	123.1	-2.7	237.5
2 Pulses	0.2	0.7	0.6	0.5	42.6	-2.4	58.8	47.1	4.2
3 Edible Oils	2.6	1.9	1.9	1.8	9.7	34.4	62.3	69.7	17.6
II Fuel, of which	33.5	33.2	32.5	33.2	26.0	17.7	-5.5	-39.7	28.9
4 POL	31.3	30.2	29.2	30.1	25.8	17.4	-7.0	-40.8	29.7
III Fertilizers	1.3	2.3	2.6	2.4	33.3	156.8	-48.3	-55.4	14.4
IV Capital Goods, of which	10.5	15.0	15.9	13.1	37.2	-3.9	-8.2	-20.0	4.2
5. Machinery except electrical & machine tools	5.9	7.4	8.0	7.3	33.1	7.7	-10.2	-24.3	15.7
6 Electrical machinery	1.0	1.1	1.2	1.0	28.7	27.7	-15.1	-28.9	7.4
7 Transport equipment	1.4	4.1	4.2	2.1	61.1	-34.3	-11.6	-18.1	-36.1
V. Others, of which	46.3	42.6	42.5	43.2	22.6	23.8	1.3	-27.8	28.0
8 Chemicals	5.9	5.2	5.6	5.7	22.1	23.0	0.0	-22.9	26.7
9 Pearls, Precious, Semi-precious Stones	9.6	5.6	4.3	7.7	7.2	107.7	-2.4	-47.8	128.9
10 Gold & Silver	9.3	10.3	9.1	8.1	20.8	26.4	32.8	-23.9	12.1
11 Electronic Goods	7.0	7.3	8.3	6.3	28.1	15.3	-10.0	-17.7	-5.3
Total Imports	100.0	100.0	100.0	100.0	25.6	20.7	-5.0	-30.7	26.0

Source : Calculated from DGCI&S data

Note : * Growth rate in US dollar terms.

Totals of I, II, III, IV, and V may not add up to total imports due to some unclassified items.

growth in 2009-10 and very high growth (129 per cent) in the first half of 2010-11.

Export diversification

7.34 In 2009, India had a global export share of 1 per cent or more in 48 out of a total of 99 commodities at the two-digit Harmonised System (HS) level, but

a significant share of 5 per cent or more in 12 items (Table 7.9). Among these, three items, pearls, precious stones, metals, coins, etc.; manmade filaments; and ores, slag, and ash had an increase in global share by 0.5 per cent point or more in 2009 over 2008. Six items, which include silk; carpets and other textile floor coverings; lac, gum, resins, and other textile floor coverings; lac, gum, resins,

Table 7.9 : India's Share in World Exports: Commodity-wise (share of more than 5 per cent)

Sl. No.	Product Code	Product Label						Change in Share
			2005	2006	2007	2008	2009	2009/2008
1	71	Pearls, Precious Stones, Metals, Coins, etc.	8.2	6.5	6.6	5.7	10.1	4.4
2	50	Silk	12.5	11.4	10.5	10.2	9.7	-0.5
3	57	Carpets and Other Textile Floor Coverings	9.0	9.6	8.7	8.4	8.4	0.0
4	13	Lac, Gums, Resins, Vegetable Saps and Extracts nes	11.4	10.6	9.5	9.7	7.9	-1.8
5	52	Cotton	5.5	6.8	8.5	8.6	7.7	-0.9
6	53	Vegetable Textile Fibres nes, Paper Yarn, Woven Fabric	4.8	4.2	4.6	6.1	6.3	0.2
7	63	Other made Textile Articles, Sets, Worn Clothing, etc.	7.0	6.4	5.7	5.4	5.5	0.1
8	54	Manmade Filaments	2.5	2.6	2.9	3.7	5.1	1.4
9	67	Bird Skin, Feathers, Artificial Flowers, Human Hair	3.4	4.4	5.0	5.0	5.1	0.1
10	14	Vegetable Plaiting Materials, Vegetable Products nes	5.1	4.5	4.8	5.4	5.1	-0.4
11	09	Coffee, Tea, Mate, and Spices	4.7	5.0	5.2	5.3	5.1	-0.3
12	26	Ores, Slag, and Ash	6.8	4.8	4.8	4.5	5.0	0.5

Source : Calculated from National Centre for Trade Information (NCTI) data based on UN-ITC Trade Map Data 2009.

vegetable saps and extracts; cotton; vegetable plaiting materials, vegetable products; and coffee, tea, mate, and spices, lost global shares in 2009 over 2008. Noticeable is the near doubling in share of pearls, precious stones, metals, coins, etc., with growth in trading activity, and the fall of nearly 2 percentage points in lac, gums, resins, vegetable saps, and extracts, due to crop failures coupled with competition from substitute products and competing countries. Of the remaining 38 items, 11 lost their shares in 2009 over 2008.

DIRECTION OF TRADE

7.35 The directional pattern of India's trade after changing in the first half of this decade with the share of the top 15 trading partners increasing by 5.5 percentage points to 60.3 per cent in 2007-08 compared to 2000-01, has not changed much after that with the top 15 countries continuing to hold the share of around 60 per cent even in 2009-10 and 2010-11 (April-September) (Table 7.10). In the first half of 2010-11, their share was 59.8 per cent. An interesting development in the direction of India's trade is that the USA which was in first position in 2007-08 has been relegated to third position in 2008-09, with the UAE becoming India's largest trading partner, followed by China. This position continued

in 2009-10 and the first half of 2010-11. This is mainly due to India's exports and imports of gems and jewellery items followed by POL to the UAE. In both 2009-10 and 2010-11 (April-September), India's exports to the UAE were higher than imports, while India's exports to China are lower than imports. The high and rising trade with the UAE may also be due to circular trading to some extent.

7.36 Export-import ratios in Table 7.10 show that among its top 15 trading partners, India had bilateral trade surplus with five countries, namely the UAE, USA, Singapore, the UK, and Hong Kong in 2009-10 and the first half of 2010-11. India's trade deficit with the USA and Singapore in 2007-08, turned into trade surplus thereafter. The export-import ratio fell in 2008-09 in the case of Hong Kong, though it recovered in 2009-10. India's export-import ratio in the case of China is not only low but has been stagnating at around 0.3 though it increased to 0.4 in 2009-10, to again fall to 0.3 in the first half of 2010-11.

7.37 The UAE has displaced the USA as the topmost destination of India's exports in 2008-09 and 2009-10 with an export share of 13.2 per cent and 13.4 per cent respectively. In 2009-10, India's exports to the top two destinations, i.e. the UAE followed by the USA, registered growth of (-)2.1, and (-)7.6, per cent respectively.

Table 7.10 : India's trade and export-import ratio with major trading partners

	Share in total trade					Export/Import ratio ^a				
	2007-08	2008-09	2009-10	2009-10 (Apr-Sept)	2010-11 (Apr-Sept)	2007-08	2008-09	2009-10	2009-10 (Apr-Sept)	2010-11 (Apr-Sept)
1 UAE	7.0	9.9	9.3	8.8	9.9	1.2	1.0	1.2	1.5	1.2
2 China	9.2	8.6	9.1	9.1	9.3	0.4	0.3	0.4	0.3	0.3
3 USA	10.1	8.1	7.8	8.6	7.6	1.0	1.1	1.2	1.0	1.4
4 Saudi Arabia	5.6	5.1	4.5	4.4	4.5	0.2	0.3	0.2	0.3	0.2
5 Germany	3.6	3.8	3.4	3.6	3.0	0.5	0.5	0.5	0.5	0.5
6 Switzerland	2.5	2.6	3.3	2.7	3.2	0.1	0.1	0.0	0.0	0.0
7 Singapore	3.7	3.3	3.0	3.2	3.0	0.9	1.1	1.2	1.2	1.3
8 Australia	2.2	2.6	3.0	2.9	2.4	0.1	0.1	0.1	0.1	0.1
9 Iran	3.1	3.0	2.9	3.2	2.2	0.2	0.2	0.2	0.2	0.2
10 Hong Kong	2.2	2.7	2.7	2.6	3.0	2.3	1.0	1.7	2.3	1.4
11 Korea RP	2.1	2.6	2.6	2.4	2.4	0.5	0.5	0.4	0.4	0.3
12 Indonesia	1.7	1.9	2.5	2.7	2.5	0.4	0.4	0.4	0.4	0.5
13 UK	2.8	2.6	2.3	2.4	2.1	1.4	1.1	1.4	1.4	1.5
14 Japan	2.5	2.2	2.2	2.2	2.4	0.6	0.4	0.5	0.5	0.7
15 Belgium	2.1	2.1	2.1	2.0	2.4	1.0	0.8	0.6	0.6	0.6
Total (1 to 15)	60.3	61.0	60.5	60.9	59.8	0.6	0.6	0.6	0.6	0.6
Total Trade	100.0	100.0	100.0	100.0	100.0	0.6	0.6	0.6	0.6	0.7

Source: Computed from DGCI&S data.

Note: ^aA coefficient of export and import ratio between 0 and 1 implies that India's imports are greater than exports and if the coefficient is greater than one, India exports more than what it imports.

7.38 Region-wise, over half of India's exports (53.5 per cent) in the first half of 2010-11 were to Asia (including ASEAN), up from around 40 per cent in 2001-02. During 2010-11 (April-September), exports to Asia (including ASEAN) increased by 29.2 per cent and to Europe by 23.3 per cent. India's merchandise exports to South Asian countries increased by 29.2 per cent.

7.39 In 2010-11 (April-September), Asia and ASEAN continued to be the major source of India's imports accounting for 61.5 per cent of the total. Country-wise, China remained the largest source with a 12 per cent share in India's total imports followed by the UAE (7.5 per cent), Saudi Arabia (6 per cent), and USA (5.9 per cent). India's import growth from 13 of its top 15 trading partners was positive, the USA and Iran being the exceptions.

SERVICES TRADE

7.40 In recent years, the focus of services trade has shifted away from just facilitating trade in goods as the sector has emerged as an independent entity in itself with services trade in the four supply modes opening up new opportunities. The integration of telecommunication and computer technology has made virtually all services tradable across borders. Virtually all commercial services are now tradable across borders. The trend towards globalization, reinforced by liberalization policies and the removal of regulatory obstacles, has fuelled steady growth of international investment and trade in services.

World Trade in Services

7.41 The US\$ 3.35 trillion world export of commercial services was dominated by the developed countries in 2009, with the exception of India and China which were also among the top 12 exporters. As in the case of merchandise trade, India has improved its rank in commercial services trade. As per the latest 'International Trade Statistics 2010'

brought out by the WTO in 2009, world export and import growth in services fell to (-)12 per cent in 2009. The decline was more or less similar in most of the major regions like North America, Europe, and Asia. Import growth in commercial services fell in the US, EU, and Japan and was at (-)9 per cent, (-)13 per cent, and (-)10 per cent, respectively. While India's import growth and export growth of commercial services were at (-)9 per cent and (-)15 per cent respectively, those of China were at 0 per cent and (-)12 per cent respectively. While India ranks 21st in world merchandise exports in 2009 compared to China which is in first position, in commercial services exports it ranks 12th compared to China at fifth rank.

7.42 The three broad categories of commercial services, namely transport, travel, and other commercial services witnessed a decline in export growth in 2009 (Table 7.11). Among top exporters/importers of services (with EU-27 taken as a single unit) India ranked among the first five countries in the export of other commercial services, computer and information services, communication services, and personal, cultural and recreational services in 2009/2008 (Table 7.12).

7.43 As per the WTO's International Trade Statistics 2010, in 2009, all commercial services sectors were affected by the global crisis but not to the same extent. Transport services growth fell mirroring the fall in world trade. Financial services were severely hit due to the turmoil in the financial markets resulting in world exports of financial services declining by 15 per cent in 2009 though they began slowly to recover in the last few months of the year. Europe's financial sector was the most affected by the economic crisis. The EU's exports of financial services plummeted by 19 per cent, to US\$ 133 billion in 2009. In the United States, the second largest world exporter of financial services, as well as in Hong Kong, the decline was by 7 per cent. At the start of 2010, there was an upward trend

Table 7.11 : World exports of commercial services trade by major category, 2008

	Value (US\$ billion) 2009	Annual percentage change			
		2000-09	2007	2008	2009
Commercial services	3350	9	20	13	-12
Transport	700	8	20	17	-23
Travel	870	7	15	10	-9
Other commercial services	1780	12	23	12	-9

Source : WTO

Table 7.12 : India's sector-wise Rank and Share in World Exports / Imports of Services

		Rank	Share		Per cent Change
		2009	2000	2009	2009
Transportation Services	Export	13	0.6	1.5	-5
	Import	13	2.1	4.2	-17
Travel Services	Export	14	0.7	1.2	-10
Other Commercial Services	Import				
	Export	4		3.7	-17
Communication Services*	Import	8		2.4	0
	Export	4		0.6	43
Construction Services*	Import	11		1.5	-11
	Export**	12		1	-5
Insurance Services*	Import**	13		1.5	178
	Export	7			
Financial Services*	Import	7		5.4	17
	Export	7			
Computer and Information Services*	Import	5		2.1	-1
	Export**	2		1.8	163
Other Business Services*	Import**	4		1.3	19
	Export**	6		0.6	-42
Personal, Cultural and Recreational Services*	Import**	6		1.4	40
	Export**	5		7.7	-6
	Import	12		9.4	

Source: Compiled from WTO, International Trade Statistics 2010.

Note : * data relate to 2008; ** WTO Secretariat estimates.

in exports of financial services. Estimates for the first quarter of 2010 indicate recovery across all countries. Construction, the most dynamic sector in 2008, also saw its growth fall sharply. Computer and information services as well as royalties and licence fees were more resilient. World exports of computer and information services decreased by 6 per cent in 2009, after record growth of 23 per cent in 2008. While exports of computer and information services fell by 9 per cent in Europe and by 14 per cent in the CIS, in North America, they stagnated and in Asia, fell by 2 per cent. In 2009, world travel exports fell by 9 per cent, reflecting the worldwide drop in international tourism with tourist arrivals down by 4 per cent. The decline was most pronounced in Europe (-13 per cent), North America (-11 per cent), and the CIS (-22 per cent). Asian economies were less affected with a 3 per cent decline. World tourism is recovering rapidly with forecasts from the World Tourism Organization indicating that the number of international tourists will increase by 3-4 per cent in 2010.

7.44 In commercial services imports, India moved from 13th position in 2005 and 2008, to 12th position in 2009, with a 2.5 per cent share. The United States, the European Union, China, and Japan are the major importers of services in the world.

India's Services Trade

7.45 India and China are the two important developing countries which are making rapid strides in the services trade sector. However, the pattern of growth of the different services in India differs from that of other countries. While other commercial services is the major category for most of the top service exporters, in the Indian case its share is proportionately higher than in that of others at 77.4 per cent in 2008 compared to 56.5 per cent for the USA, 54.8 per cent for the EU, 45.9 per cent for China, and 60.6 per cent for Japan. Thus this category containing many dynamic services is important for India. The share of travel at 11.5 per cent is relatively lower than in most other countries. The shares of the US and China are more than double that of India. Even in transportation, India's share is less than half that of many leading exporters of services, partly reflecting India's lower volume of merchandise trade and partly the relatively lower participation of India's shipping sector in India's export trade. Thus the composition of services exports highlights the need to pay special attention to developing shipping and travel services in India. The composition of India's imports compared to other service trading countries also shows the relatively higher importance of other commercial services particularly in 2009-10.

India's Services Exports

7.46 India, is moving towards a services-dominated GDP growth with a 10 per cent CAGR for services which is higher than the 6.7 per cent for non-services during 2004-05 to 2009-10. It is also moving towards a services-dominated export growth with a CAGR of 16.7 per cent for services during 2004-05 to 2009-10 (the CAGR was 28.7 per cent during 2000-01 to 2006-07) which is slightly higher than the 16.4 per cent for merchandise exports during the corresponding period. Services exports reached US\$ 106 billion in 2008-09 with a moderate growth of 17.3 per cent over the previous year. As a result of global recession, they declined to US \$ 95.8 billion in 2009-10 with a negative growth of (-)9.6 per cent. The miscellaneous item of services exports with a nearly three-fourths share of total services exports, slightly improved its share in the first half of 2010-11 with a growth of 28.2 per cent. The share of software services declined to 45.7 per cent in the first half of 2010-11 from 50.8 per cent in the corresponding period of 2009-10. This was a result of moderate growth of 14.7 per cent in the first half of 2010-11 and the revival of non-software services exports. Non-software services exports which had registered a high negative growth of (-)41.2 per cent in 2008-09 increased their share to 29.5 per cent with the high growth of 56.9 per cent.

The revival of this sector which had a CAGR of 33.9 per cent during 2000-01 to 2007-08 is a good sign, though it is partially due to the base effect. The increasing share of business services in non-software services exports is noteworthy. Both business services and financial services exports registered very high growth of 111.4 per cent and 64.9 per cent. More than the base effect, this was due to the revival of these exports, following global recovery (Table 7.13). The fall in share of travel services from 21.5 per cent in 2000-01 to 11.4 per cent in the first half of 2010-11 is a cause of concern. This reflects the fact that we have not yet tapped the vast tourism potential of India.

India's Services Imports

7.47 Imports of commercial services have become important in recent years reaching US\$ 52 billion in 2008-09 and US \$ 60 billion in 2009-10. But it had low growth of 1.1 per cent in 2008-09 and moderate growth of 15.3 per cent in 2009-10 (Table 7.14). Business services are the most important category of services imports, followed by transportation and travel. Import growth of business services declined by (-)7.5 per cent in 2008-09 picked up by 17.8 per cent in 2009-10. It grew robustly at 62.9 per cent in the first half of 2010-11. Import growth of transportation and travel which fell in 2009-10 turned positive in the

Table 7.13 : India's Exports of Services

Sl. No.	Commodity Groups	Percentage share				CAGR 2000-01 to 2007-08	Growth rate*			
		2000-01		April-September			2008-09		April-September	
		2009-10	2010-11	2009-10	2010-11		2009-10	2010-11	2009-10	2010-11
1	Travel	21.5	12.4	11.5	11.4	18.3	-4.0	8.9	-5.2	26.2
2	Transportation	12.6	11.7	11.6	11.5	25.5	12.9	-1.2	-10.3	26.6
3	Insurance	1.7	1.7	1.8	1.5	29.4	-13.2	12.7	6.2	10.4
4	GNIE	4.0	0.5	0.5	0.4	-9.2	17.6	13.2	-5.2	9.5
5	Miscellaneous	60.3	73.8	74.7	75.2	31.6	22.3	-13.8	-16.4	28.2
	a) Software Services	39.0	51.9	50.8	45.7	30.2	14.9	7.4	-8.2	14.7
	b) Non-software Services	21.3	21.9	24.0	29.5	33.9	33.5	-41.2	-36.6	56.9
	of which:									
	i) Business Services	2.1	11.9	11.6	19.3	75.0	10.9	-38.9	-46.4	111.4
	ii) Financial Services	2.1	3.9	4.2	5.5	37.5	37.7	-15.6	-19.2	64.9
	iii) Communication Services	7.0	1.3	1.7	1.3	11.3	-4.6	-46.5	-42.0	2.3
Total Services Exports		100.0	100.0	100.0	100.0	27.8	17.3	-9.6	-16.8	27.4

Source : Calculations based on RBI data.

Note : * Growth rate in US dollar terms.

GNIE= Government not included elsewhere.

Table 7.14 : India's Imports of Services

Sl. No.	Commodity Groups	Percentage share				CAGR 2000-01 to 2007-08	Growth rate*			
		2000-01		April-September			2008-09		April-September	
		2009-10	2010-11	2009-10	2010-11	2009-10	2010-11	2009-10	2010-11	
1	Travel	19.2	15.6	17.8	14.0	18.6	1.8	-0.9	-9.9	15.6
2	Transportation	24.4	19.9	20.3	18.4	18.3	11.3	-6.9	-29.4	33.2
3	Insurance	1.5	2.1	2.7	1.9	24.7	8.3	13.8	22.9	6.3
4	GNIE	2.2	0.9	0.9	1.0	2.4	111.2	-33.7	13.2	49.4
5	Miscellaneous	52.6	61.5	58.3	64.7	21.1	-4.8	32.5	9.2	63.1
	a) Software Services	4.1	2.4	3.4	3.2	28.2	-23.6	-42.7	-53.4	39.9
	b) Non Software Services	48.6	59.1	55.0	61.5	20.4	-2.4	40.1	18.9	64.5
	of which:									
	i) Business Services	7.0	30.1	32.1	35.5	48.9	-7.5	17.8	10.9	62.9
	ii) Financial Services	13.5	7.7	8.0	9.1	6.8	-5.6	56.9	24.2	68.0
	iii) Communication Services	0.9	2.3	2.4	1.4	31.4	26.5	24.6	13.0	-14.2
Total Services Imports		100.0	100.0	100.0	100.0	19.8	1.1	15.3	-4.7	46.9

Source : Calculations based on RBI data.

Note : *Growth rate in US dollar terms. GNIE= Government not included elsewhere.

first half of 2010-11. Financial services imports grew by 68 per cent.

Balance of Trade in Services

7.48 There is growing concern about a high merchandise trade deficit coupled with inflation derailing the growth momentum. However the less known fact is that the falling services trade surplus is adding to the woes on the current account deficit front, instead of acting as a cushion as was the case earlier. Services trade surplus which increased steadily in this decade to reach US\$53.9 billion in 2008-09, fell drastically in the global crisis year of 2009-10 to US\$ 35.7 billion. This was caused by the collapse in exports of non-software services, particularly business services, the slow growth of software services, and the rise in import of non-software services, particularly business and financial services. The low service trade surplus situation continued in the first half of 2010-11. This was due to the sudden rise in imports of non-software services, particularly business and financial services which overshadowed the rise in exports of business and financial services. If this situation continues in the second half of this year and coming years, then we have to reconcile to the fact that the hitherto extra cushion provided by the services sector for trade balance will not be available. The impact on growth of the rising import of business and financial services also needs to be evaluated (see Table 7.15).

Table 7.15 : India's Exports, Imports and Balance of Trade in Services

(US \$ billion)			
	Exports	Imports	Balance
2000-01	16.3	14.6	1.7
2001-02	17.1	13.8	3.3
2002-03	20.8	17.1	3.6
2003-04	26.9	16.7	10.1
2004-05	43.2	27.8	15.4
2005-06	57.7	34.5	23.2
2006-07	73.8	44.3	29.5
2007-08	90.3	51.5	38.9
2008-09	106.0	52.0	53.9
2009-10	95.8	60.0	35.7
2009-10 (April-September)	43.8	24.7	19.1
2010-11 (April-September)	55.7	36.2	19.5

Source : Computed from RBI data.

Policies and Barriers to Trade in Services

7.49 In the light of the global recession, some measures were taken to help the services sector. These include extension of sunset clauses for Software Technology Parks of India (STPIs) and

export-oriented units (EOUs) up to 2010-11 and doubling of duty free entitlement to hotels under the 'served from India' scheme. A coordinated and synchronized effort is needed towards the services sector as at present services activities are dispersed and fall within the purview of different departments of the Government (also see Box 7.6). There are also many barriers to trade in services. These include the State-level licensing and the 'Buy American' provisions in the case of business services and IT services in the US; the requirement of the Office of the Comptroller of Currency (OCC) in the US and some State banking supervisors to maintain 'asset pledges' in addition to the paid up capital they maintain in their home country in the case of financial services; the fragmentation of the US insurance market into 56 different jurisdictions and direct discrimination on a number of fronts; restrictions in the case of transport and related services and the recent protectionist policies in the US and other economies that deny market access to other countries. There is need to negotiate at bilateral and multilateral levels for the removal of the market access barriers to trade in services.

TRADE POLICY

Recent Trade Policy measures

7.50 Trade policy measures taken by the Government and the RBI in 2009-10 and 2010-11 focused on reviving exports and export-related employment. The Government followed a mix of policy measures including fiscal incentives, institutional changes, procedural rationalization, and enhanced market access across the world and diversification of export markets. Improvement in infrastructure related to exports; bringing down transactions costs, and providing full refund of all indirect taxes and levies, were the three major areas of focus (see Box 7.3).

7.51 Some of the trade policy measures to check inflation in the country are the following:

- Import duties reduced to zero for rice, wheat, pulses, edible oils (crude), butter and ghee and to 7.5 per cent for refined and hydrogenated oils and vegetable oils;
- Import of raw sugar allowed at zero duty under open general licence (O G L).
- Import of white/refined sugar allowed. The facility has been extended up to 31 December 2010 without any quantitative cap.

- Levy obligation in respect of all imported raw sugar and white/refined sugar removed.
- Export of non-basmati rice, edible oils (except coconut oil and forest based oil), and pulses (except Kabuli chana) banned.
- Minimum export price (MEP) used to regulate exports of onion (at \$1200 per tonne for December 2010) and basmati rice (\$900 PMT).
- Export of onion (all varieties) including Bangalore rose onions and Krishnapuram onions fresh or chilled, frozen, provisionally prepared, or dried but excluding onion cut, sliced, or broken in powder form not permitted with effect from 22 December 2010 and until further orders.
- Full exemption from basic custom duty provided to onions and shallots with effect from 21 December 2010. Consequently, these items also exempt from special additional duty of 4 per cent, education cess, and secondary and higher education cess. The exemption is open ended and does not carry a validity clause prescribing a terminal date.

Policy for Promoting State-wise Exports

7.52 State-wise exports as reflected in the data on state of origin of exports of goods show clear domination of Maharashtra and Gujarat. Tamil Nadu, Karnataka, and Andhra Pradesh fall in the second rung of exporting States. In 2009-10, the growth of exports from all the States was negative, except Haryana, Kerala, Goa, and Rajasthan. High negative export growth was registered by Delhi, followed by Uttar Pradesh, West Bengal, and Karnataka. In the first half of 2010-11 export growth to all destinations was positive except for Kerala (Table 7.16) To encourage exports outlay under the Assistance to States for Developing Export Infrastructure and Allied Activities (ASIDE) scheme for the Eleventh Five year plan was increased to ₹ 3793 crore.

Market Access Initiative (MAI) and Market Development Assistance (MDA) Schemes

7.53 The MAI scheme was launched in 2003 to act as a catalyst for India's exports on a sustained basis. The scheme is formulated on a focus product-focus country approach to evolve specific strategy for specific market and specific product. To further enable better coordination, synergising, and facilitating of India's export promotion activities by the Indian Missions abroad, a 'Challenge Fund' has

Box 7.3 : Trade Policy Measures

Market and Product Diversification and Expansion of Markets:

- 27 new markets added under the Focus Market Scheme (FMS) with incentive of duty credit scrip at 3 per cent of exports.
- Market Linked Focus Product Scheme (MLFPS) with incentive of duty credit scrip at 2 per cent, has been significantly broadened by inclusion of a large number of products linked to their markets.
- All of Africa, Latin America, and a large part of Oceania covered under the FMS and MLFPS (13 countries added under the MLFPS at the time of release of the FTP 2009-14 in August 2009 and two countries added in January 2010).
- The incentive available under the FMS has been raised from 2.5 per cent to 3 per cent; and for the Focus Product scheme (FPS) and MLFPS from 1.25 per cent to 2 per cent; and Special Focus Products at 5 per cent.
- Additional benefit of 2 per cent bonus, over and above the existing benefits of 5 per cent / 2 per cent under the FPS allowed for about 135 existing products, which have suffered due to recession in exports. Major sectors include all handicrafts items, silk carpets, toys and sports goods (all of which were earlier eligible for 5 per cent benefits); leather products and leather footwear, handloom products, and some of engineering items including bicycle parts and grinding media balls (all of which were earlier eligible for 2 per cent benefit).
- 256 new products added under the FPS (at eight-digit level), which became entitled for benefits at 2 per cent of FOB value of exports to all markets. Major sectors / product groups are engineering, electronics, rubber and rubber products, other oil meals, finished leather, packaged coconut water, and coconut shell worked items.
- Instant tea and CSNL cardinol included for benefits under the Vishesh Krishi Gram Upaj Yojana (VKGUY) at 5 per cent of FOB (free on board) value of exports.
- Nearly 300 products (at eight-digit level) from the readymade garment sector incentivized under the MLFPS for a further six months from October 2010 to March 2011 for exports to 27 EU countries.

Support for Technological Upgradation

- The zero-duty Export Promotion Capital Goods (EPCG) Scheme and Status Holder Incentive Scrip (SHIS) scheme introduced in 2009 for limited sectors and valid only for two years initially, extended by one more year till 31 March 2012 and the benefit of the scheme expanded to additional sectors.
- Three additional Towns of Export Excellence (TEEs) announced, taking the list to 24.

Availability of Concessional Export Credit:

- Interest subvention of 2 per cent extended up to March 2011 for certain labour-intensive sectors of exports.
- Interest rates on export credit in foreign currency reduced to LIBOR + 200 bps in February 2010 from the earlier LIBOR+350bps.

EOUs/STPIs

- Sections 10A and 10B (sunset clauses for STPI and EOUs schemes respectively) extended for the financial year 2010-11. Anomaly in Section 10AA relating to taxation benefit of 'unit vis-à-vis assessee' removed;

Services

- FTP also provided fillip to the services sector (hotels) by doubling duty-free entitlement under the Served From India Scheme (SFIS) from 5 per cent to 10 per cent of foreign exchange earnings.

Others

- Duty Entitlement Passbook (DEPB) Scheme extended beyond 31 December 2010 till 30 June 2011.
- Time period of export realization for non-status holder exporters increased to 12 months, on par with the status holders. This facility has been extended up to 31 March 2011.
- Advance Authorization for Annual Requirement now exempted from payment of Anti-dumping and Safeguard duty.
- Value limit on duty-free import of commercial samples enhanced from Rs 1 lakh to Rs 3 lakh per annum.
- DEPB and Freely Transferable Incentive Schemes provisionally allowed without awaiting receipt of bank realization certificate (BRC).
- Export obligation period under Advance Authorization Scheme enhanced from 24 months to 36 months without payment of composition fee.
- Facilitation of Trade through various Electronic Data Interchange (EDI) initiatives, namely online filing and processing of various authorizations to reduce transaction cost and time.

Table 7.16 : State-wise Exports of Top 15 States

(US\$ million)

Sl. No.	State			(April-September)		Share(%)	Growth rate* (%)	
		2008-09	2009-10	2009-10	2010-11		2009-10	2010-11 (Apr-Sept.)
1	Maharashtra	44,661	43,351	20,275	23,405	24.3	-2.9	15.4
2	Gujarat	40,268	38,771	16,341	24,593	21.7	-3.7	50.5
3	Tamil Nadu	18,538	16,083	7899	8404	9.0	-13.2	6.4
4	Karnataka	12,295	9092	4206	5011	5.1	-26.0	19.1
5	Andhra Pradesh	9896	8558	4594	6620	4.8	-13.5	44.1
6	Kerala	4752	5842	2783	2647	3.3	22.9	-4.9
7	Haryana	4791	5678	2653	3575	3.2	18.5	34.8
8	Uttar Pradesh	7570	5523	2762	3848	3.1	-27.0	39.3
9	Delhi	8466	5187	2575	2933	2.9	-38.7	13.9
10	West Bengal	5582	4197	1826	2821	2.3	-24.8	54.5
11	Rajasthan	3313	3338	1434	1853	1.9	0.8	29.2
12	Orissa	3351	3230	1233	2736	1.8	-3.6	121.9
13	Punjab	3015	2732	1260	1904	1.5	-9.4	51.1
14	Goa	1781	2481	557	1074	1.4	39.3	92.7
15	Madhya Pradesh	2945	2357	916	1147	1.3	-20.0	25.2
Total exports		1,85,295	1,78,751	80,950	1,05,352	100.0	-3.5	30.1

Source : DGCI&S.

* Growth rate in US \$ terms

recently been set up. Individual Missions would 'bid' for support from the Fund by submitting innovative export promotion project proposals. Priority would be given to focused, specific projects with quantifiable/tangible results. During 2010-11 (up to 31 December 2010), a total of 205 projects/export promotion events and eight market studies/export promotion surveys were approved for assistance under this scheme.

7.54 To stimulate and diversify the country's export trade, the Marketing Development Assistance (MDA) Scheme is under operation. During the year 2010-11 up to 31 December 2010, a total of 411 projects/export promotion events have been approved for assistance.

Special Economic Zones (SEZs)

7.55 India recognized early the effectiveness of the export processing zone (EPZ) model in promoting exports, with Asia's first EPZ set up in Kandla in 1965. With a view to overcome the multiplicity of controls and clearances; absence of world-class infrastructure; and an unstable fiscal regime to attract larger foreign investments in India, the Special Economic Zones (SEZs) Policy was announced in

April 2000. SEZs in India functioned from 1 November 2000 to 9 February 2006 under the provisions of the Foreign Trade Policy and fiscal incentives were made effective through the provisions of relevant statutes. The SEZ Act 2005, supported by SEZ Rules, came into effect on 10 February 2006, providing for drastic simplification of procedures and for single window clearance on matters relating to Central as well as State Governments. The SEZ Rules provide for different minimum land requirements for different classes of SEZs.

7.56 In addition to seven Central Government SEZs and 12 State/private-sector SEZs set up prior to the enactment of the SEZ Act 2005, formal approval has been accorded to 580 proposals out of which 374 SEZs have been notified. The performance of SEZs has been reasonably good despite some criticism (see Box 7.4)

Tariff Reforms

7.57 The global recession forced a review of the tariff reform process. The pause button was pressed on peak duties in the last two years with the highest rate on manufactures continuing at 10 per cent. The only movement in tariffs was in the area of free trade

Box 7.4 : Performance of SEZs in India

SEZs are becoming increasingly important in India's exports. The performance of SEZs is mainly examined in three areas, exports, employment, and investment.

Exports: A total of 130 SEZs are already exporting. Out of this 75 are information technology (IT)/ IT enabled services (ITES), 16 multi-product and 39 other sector specific SEZs. The total number of units in these SEZs is 3139. The physical exports from the SEZs have increased by 121 per cent to ₹ 2,20,711 crore in 2009-10 with a CAGR of 58.6 per cent during 2003-04 to 2009-10 compared to the CAGR of 19.3 per cent for total merchandise exports of the country for the same period. When the whole world including India was reeling under the effects of the global recession, growth in exports from SEZs was 121 per cent in 2009-10 compared to a paltry 0.6 per cent growth in total exports from India. Exports during the first three quarters of the current year have been to the tune of ₹ 2,23,132 crore. The share of SEZs in India's total exports has increased consistently from 4.7 per cent in 2003-04 to 26.1 per cent in 2009-10 and 29.7 per cent in the first three quarters of 2010-11 (see Table 1).

Table 1 : SEZs Exports and India's Total Exports: A Comparison Year

	Exports from SEZs		Exports from India		Share of SEZs Exports in Total Exports
	Value (₹ crore)	Growth (%)	Value (₹ crore)	Growth (%)	
2003-04	13,854	39.0	2,93,367		4.7
2004-05	18,314	32.2	3,75,340	27.9	4.9
2005-06	22,840	24.7	4,56,418	21.6	5.0
2006-07	34,615	51.6	5,71,779	25.3	6.1
2007-08	66,638	92.5	6,55,863	14.7	10.2
2008-09	99,689	49.6	8,40,755	28.2	11.9
2009-10	2,20,711	121.4	8,45,534	0.6	26.1
2010-11 (Apr.-Dec.)	2,23,132	-	7,51,633	23.4	29.7

One of the criticisms SEZs face is that exports are mainly from the old SEZs which were formerly free trade zones (FTZs) and not from greenfield SEZs. It is interesting to know that not only have many greenfield SEZs started exporting but also the exports of new SEZs, i.e. SEZs notified under the SEZ Act 2005, have grown rapidly over the years resulting in the highest share of 53.4 per cent for this category in 2009-10 compared to Central Government SEZs and State Government / private SEZs established prior to the SEZ Act 2005 (see Table 2).

Table 2 : Exports from New and Old SEZs

	2005-06	2006-07	2007-08	2008-09	2009-10
Central Govt SEZs					
Value (in ₹ crore)	19,657	25,358	39,275	46,985	58,037
Growth (%)	-	29	54.9	19.6	23.5
Share (%)	86.1	73.3	58.9	47.1	26.3
State Govt/Pvt SEZs Established prior to SEZ Act, 2005					
Value (in ₹ crore)	3183	9134	22,167	31,640	44,729
Growth (%)	-	187	142.7	42.7	41.4
Share (%)	13.9	26.4	33.3	31.7	20.3
SEZs notified under SEZ Act, 2005					
Value (in ₹ crore)	-	122	5195	21,064	1,17,946
Growth (%)	-	-	4158.2	305.5	459.9
Share (%)	-	0.4	7.8	21.1	53.4

Employment: Out of the total employment of 6,44,073 persons in SEZs, an incremental employment of 5,09,369 persons was generated after February 2006 when the SEZ Act came into force. At least double this number obtains indirect employment outside the SEZs as a result of the operations of SEZ units. This is in addition to the employment created by the developer for infrastructure activities.

(Contd.....)

Box 7.4 : Performance of SEZs in India (Contd....)

Investment: The total investment in SEZs till 31 December 2010 is approximately ₹ 1,95,348 crore including ₹ 1,91,313 crore in the newly notified zones. In SEZs 100 per cent FDI is allowed through automatic route. The Government's role has been more as a facilitator by fast tracking the approvals rather than providing any direct monetary support. SEZs being set up under the SEZ Act 2005 are primarily private investment driven.

Issues: Some important issues relating to SEZs are the following:

Direct Tax Code (DTC) Impact: The issue is related to deadlines for profit-linked deductions: As per the DTC, SEZ developers will be allowed profit-linked deductions for all SEZs notified on or before 31 March 2012. Units in SEZs that will commence commercial operations by 31 March 2014 too will be allowed profit-linked exemptions. Developers and units notified after these dates will only have investment-linked exemptions and not profit-linked exemptions. There is concern about these dates among developers and units particularly in the big SEZs with long gestation time.

Goods and Services Tax (GST): As per the GST model being considered, GST will be levied on imports with necessary constitutional amendments. Though full and complete set off would be available on the GST paid on import of goods and services, after the introduction of the GST, tax exemptions, remissions, etc. related to industrial incentives should be converted, if at all needed, into cash refund schemes after collection of tax, so that the GST scheme on the basis of a continuous chain of set-offs is not disturbed. Regarding special Industrial Area Schemes, such exemptions, remissions would continue up to legitimate expiry time both for the Centre and the States. However, any new exemption, remission, or continuation of an earlier one would not be allowed. In such cases, the Central and State Government could provide reimbursement after collecting the GST.

Issue of Power generation and distribution: Another area of concerns is the generation and distribution of power by the SEZ developers/units. While one opinion is that it should be left to the entrepreneur to decide whether he would like to provide power as an infrastructure, as defined in the SEZ Act, or set up a unit to sell power as a good, another view is that power cannot be an infrastructure and can be only a good to be generated and distributed by the unit. It may be worth considering appropriate policy to encourage power generation and distribution.

Coordination issues: The Directors, STPI, have been declared Development Commissioners (DCs) for the IT SEZs under their respective jurisdiction. An STPI is under administrative control of the Department of Information Technology. Other multi-product and sector-specific SEZs are under the charge of DCs appointed by the Department of Commerce. However a number of issues, for example processing of notification of IT SEZs, coordination with state governments etc, relating to IT SEZs are also looked after by the DCs appointed by the Department of Commerce. This leads to a situation of dual control adversely impacting effective coordination and needs to be resolved.

Disinvestment: The new SEZs have come up mainly in the private sector with no funding from the Government. Now the time has possibly come to see whether some of the established SEZs which are state owned could also be privatized. Disinvestment in these SEZs could not only add to the kitty of the Government and release more money for social-sector development but could also make these SEZs more efficient.

agreements (FTAs) like the one with ASEAN. The tariff policy in 2009-10 focused on tackling inflation by lowering import duties of specific items. While the current concerns on current account deficit may lead to the pause button remaining pressed, a step forward in tariff reforms could be taken even in these trying times (see Box 7.5)

7.58 The other tariff reforms could include measures like reducing end-use exemptions as the revenue foregone on account of export promotion concessions in 2009-10 was ₹ 43,622 crore, rectifying the inverted duty structure, removing Quantitative Restrictions (QRs) from petroleum products as the Administrative Price Mechanism (APM) has been dismantled, and introducing sunset clauses for export promotion schemes having tariff concessions.

Contingency Trade Policy and Non-tariff Measures

7.59 Anti-dumping investigations initiated by all countries started falling after reaching a peak in 2001, numbering 165 in 2007. However, in 2008, they again rose to 213. While they fell marginally to 209 in 2009, there seems to be a downward movement in 2010, with only 69 investigations initiated in the first half of the year (Table 7.17). India's anti-dumping initiations fell from 55 in 2008 to 31 in 2009. In the first half of 2010, there were 17 anti-dumping initiations by India. During 2010-11 (up to 31 December 2010), the Directorate General of Antidumping and Allied Duties has initiated 13 fresh anti-dumping investigations. The products involved are certain hot rolled flat stainless steel products, azodicarbonamide, sewing machine needles,

Box 7.5 : Lowering Peak Duties with Least Revenue Loss

Peak duties for manufactures could be reduced from 10 per cent by tinkering intelligently with the tariffs without any fall in collection rates given the fact that total collection rates (an indicator of overall incidence of tariffs including countervailing and special additional duties) have fallen to a low of 5.9 per cent in 2009-10 (see Table 1). The falling collection rate is a function of both rising import volumes as well as leakages due to exemptions on account of end use and the countervailing excise duty applicable on import goods.

Table 1: Tariff collection Rates for selected import groups*

SI No.	Commodity Group	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10
1	Food Products	19.3	22	32.2	23.2	19.3	4.2	2.5
2	POL	11.2	9.9	5.9	5.4	5.7	2.7	1.9
3	Chemicals	24.1	21.6	20.1	22.1	21.6	16.4	13.9
4	Man-made Fibre	45.9	38.7	33.6	28.3	30.1	17	22
5	Paper and Newsprint	7.2	7.4	9.2	9.5	10.3	8.4	7.7
6	Natural Fibre	13	10.6	12.5	12.1	12.6	5.6	4.3
7	Metals	32	25.8	25	24.1	24.3	16.8	17.4
8	Capital Goods	19	15.8	12.5	14.3	15.7	12.5	11.3
9	Others	7.6	5.5	5.2	5.7	6.1	4	3.8
10	Non POL	14.4	12.1	11.5	12.3	12.8	8.7	7.6
	Total	13.5	11.5	9.8	10.2	10.4	6.9	5.9

Source: Department of Revenue, Ministry of Finance.

* Collection rate is defined as the ratio of revenue collection (basic customs duty+ countervailing duty) to value of imports unadjusted for exemptions, expressed in percentage.

SI No.1 includes cereals, pulses, tea, milk and cream, fruits, vegetables, animal fats, and sugar.

SI No.3 includes chemical elements, compounds, pharmaceuticals, dyeing and coloring materials, plastic, and rubber.

SI No.5 includes pulp and waste paper newsprint paperboards and manufactures and printed books.

SI No.6 includes raw wool and silk.

SI No.7 includes iron and steel and non ferrous metals.

SI No.8 includes non-electronic machinery and project imports, electrical machinery.

In 2009-10, there are 340 tariff lines under capital goods and 4135 lines under intermediates consisting mainly of goods going into manufacture of finished products with tariffs of 10 per cent and above. The two groups in the high duty category account for as much as 39 per cent in the total number tariff lines. The share of the two categories in the duty slab of 10 per cent and above in notional duty (that is the revenue which should have come to the exchequer from the import volumes and duty rates but for the end use exemption or special category like export promotion) is 2.5 per cent (in the case of capital goods) and 33.5 per cent (in the case of intermediate goods) of the total notional revenue estimated at ₹ 2,02,705 crore. If both capital and intermediate goods are brought under the 7.5 per cent duty slab and if collection rates are assumed to be the same, then there is a revenue loss of around ₹ 11,747 crore. However, in the case of intermediate and capital goods the collection rates are higher in the 7.5 per cent duty slab compared to the 10 per cent and above slab. If these collection rates were factored into the calculations, there could be an actual gain in revenue due to better compliance and fall in undervaluation associated with improved collection rate in the low duty 7.5 per cent slab as compared to the 10 per cent plus slab. One of the reasons for this is that countervailing duty exemptions, for example in textiles, are high in the 10 per cent slab compared to the 7.5 per cent slab.

Moving capital and intermediate goods to the 7.5 per cent slab would result in the number of tariff lines with duty of 7.5 per cent accounting for 79.6 per cent (or nearly 80 per cent) of the total. They will cover 97.45 per cent of imports. Even if some intermediate goods and all capital goods are moved to the 7.5 per cent and below category, then a major part of manufactures will have peak duty of 7.5 per cent or less. This will give a big push to industrial growth and exports, besides giving leverage power in WTO negotiations as well as FTAs.

Table 1 also shows that the collection rates for capital goods are still relatively high at 11.3 per cent in 2009-10 after all the exemptions including concessions under the Export Promotion Capital Goods (EPCG) scheme. This also needs attention.

Table 7.17 : Investigations initiated by top ten users of anti-dumping measures 1995-2010

Country	1995	2000	2001	2004	2005	2006	2007	2008	2009	2010*	1995-2010*
India	6	41	79	21	28	35	47	55	31	17	613
United States	14	47	77	26	12	8	28	16	20	2	442
European Community	33	32	28	30	25	35	9	19	15	8	414
Argentina	27	43	28	12	12	11	8	19	28	7	277
South Africa	16	21	6	6	23	3	5	3	3	0	212
Australia	5	15	23	9	7	10	2	6	9	4	212
Brazil	5	11	17	8	6	12	13	23	9	5	184
Canada	11	21	25	11	1	7	1	3	6	1	152
China PR	0	11	14	27	24	10	4	14	17	4	182
Turkey	0	7	15	25	12	8	6	23	6	1	145
All Countries	157	298	371	220	202	203	165	213	209	69	3752

Source: WTO *Upto June 2010.

caustic soda, paranitroaniline, stainless steel cold rolled flat products of 200 series having width below 600 mm, stainless steel cold rolled flat products of 400 series having width below 600 mm, soda ash, opal glassware, melamine, morpholine, geogrids and aniline-III. The countries involved in these investigations are the European Union, Korea, South Africa, Taiwan, the USA, China PR, Thailand, Norway, UAE, Kenya, Iran, Pakistan, Turkey, Ukraine, Indonesia, Japan, Malaysia.

7.60 Over the last two decades the world has witnessed rapid expansion of global trade and reduction in tariff rates both through the multilateral arrangement under the WTO as well as various types of trade cooperation agreements including FTAs. However, at the same time developed countries are increasingly resorting to the use of non-tariff measures (NTMs) to protect their domestic industries.

7.61 The WTO-UNCTAD (United Nations Conference on Trade and Development)-OECD Reports on G-20 trade and investment measures (the fourth one being the latest) states that the number of new measures imposed by G-20 countries is still increasing, but more slowly than in the past and with a welcome decline in the initiation of new

trade remedy actions (anti-dumping duties, countervailing measures, and safeguards). The new restrictive measures introduced during different periods following the global recession show a fall, covering only 0.3 per cent of total G-20 imports and 0.2 per cent of world imports in May 2010-October 2010 (see Table 7.18).

7.62 However, there is an accumulation of the trade restrictive measures with limited progress in unwinding them. Since October 2008, on aggregate, new G-20 trade restrictions have grown to cover 1.8 per cent of G-20 imports and 1.4 per cent of total world imports. Only around 15 per cent of the trade restrictive measures introduced since the outbreak of the crisis have so far been removed, which indicates that the bulk of them still remain in force.

7.63 In terms of number of trade measures, the most affected sectors include electrical machinery and equipment; chemical products; mineral fuel; machinery and mechanical appliances; iron and steel; cereals; plastic products; and dairy products. The sectors most heavily affected in terms of coverage of restrictive trade measures were electrical apparatus for line telephony, bio diesel, and automatic data processing machines. The large majority of G-20 actions since mid-May 2010 have been trade

Table 7.18 : Share of New Trade Restrictive Measures

	Oct. 2008–Oct. 2009	Nov.2009–May 2010	May 2010–Oct. 2010
In total world imports	0.8	0.4	0.2
In total G20 imports	1.0	0.5	0.3

WTO NEGOTIATIONS AND INDIA

Trade Negotiations

remedies, in particular the initiation of new anti-dumping investigations, followed by increases in tariffs and other import-related taxes. Among non-verified measures, the most frequent actions were related to export taxes or restrictions, non-tariff measures (import bans, licences, or other border controls), and government measures aimed at favouring domestic industries or products. The most frequently reported export measures concern restrictions on some agricultural products (export bans and quotas affecting grains) and some minerals (export quota reductions and reported informal bans on rare earth minerals)

7.64 Some G-20 members have raised tariffs and introduced new non-tariff measures to protect domestic production in certain sectors, notably steel and motor vehicles. G-20 members have continued to use trade defence mechanisms in these as well as other sectors like non-automatic import licenses. The US and EU have re-introduced agricultural export subsidies for the dairy sector, measures that are generally acknowledged to be among the most highly trade-distorting. Some of the fiscal and financial packages that have been introduced to tackle the crisis contain elements such as state aids, other subsidies, and 'buy/lend/invest/hire local' conditions that favour domestic goods and services at the expense of imports. Stricter application of Sanitary and Phytosanitary measures (SPS) and TBT (technical barriers to trade) regulations and slower procedures and additional procedural requirements are the other measures imposed by countries. Thus, in the area of trade, there has been policy slippage since the crisis began and this has continued after the G-20 London Summit in April 2009.

7.65 India has adopted a multi-pronged strategy to deal with the issues relating to non-tariff measures (NTMs). On the export side, an online database has been set up, on the SPS and TBT notification (which may result in NTMs) notified to the WTO by members. This is to provide information to exporters about the regulatory regime of other countries. Besides, steps are being taken to upgrade the infrastructure and surveillance system at the major ports and airports to ensure due compliance with our standards and regulations. Moreover, wherever India's export interest is affected, issues are raised by the Government in suitable redressal forums available under the WTO such as in the SPS and TBT Committee. These issues are also taken up in bilateral forums.

7.66 The Doha Round of trade negotiations at the WTO has been under way since 2001. Discussions were slow to resume after they paused in December 2008 and there has not been much progress since. A stock taking exercise at the level of senior officials took place in the WTO in March 2010, where members agreed to take the discussions ahead based on the work already done while maintaining the focus on the development dimension of the Round. The positive signals given by world leaders at the G-20 Leaders' Summit held in Seoul in November 2010, have imparted a sense of urgency amongst members regarding the Geneva process that is supposed to resume in January 2011. The Director General, WTO, has suggested a cocktail approach of discussions combining the Chair-led processes within the negotiating groups and bilateral contacts, both in specific areas and at horizontal level. India is willing to work with the coalition groups in the WTO towards an early conclusion of the Doha Round. Its stand, however, is unequivocal: the protection of poor, subsistence farmers of developing countries and vulnerable industries is a priority.

7.67 In the area of agriculture, discussions are still taking place on the basis of the revised draft agriculture modalities text of 6 December 2008. As per this draft, developed countries would have to reduce their bound tariffs in equal annual installments over five years with an overall minimum average cut of 54 per cent. Developing countries would have to reduce their bound tariffs with a maximum overall average cut of 36 per cent, over a larger implementation period of ten years. Both developed and developing country members would have the flexibility to designate an appropriate number of tariff lines as sensitive products, on which they would undertake lower tariff cuts. Developing countries would have a special products (SP) entitlement of 12 per cent of agricultural tariff lines. An average tariff cut of 11 per cent is proposed on SPs, including 5 per cent of total tariff lines at zero cuts. There are also reductions/disciplines proposed for various categories of domestic and export subsidies.

7.68 In the case of Non-Agricultural Market Access (NAMA) negotiations, the tariff reductions are proposed through a non-linear Swiss formula with a three-tiered coefficient of 20, 22 and 25 for formula reductions linked to specific flexibilities for protecting sensitive NAMA tariff lines of developing countries

and a coefficient of 8 for tariff reduction of developed countries. With regard to the Sectoral proposal of some countries, by which the tariffs in certain identified sectors are proposed to be brought to zero or near zero levels, India's negotiating position has been that participation in sectoral initiatives must be non-mandatory and on a good faith basis without pre-judging the outcome. Another important aspect of NAMA negotiations pertain to Non-Tariff Barriers (NTBs). With regard to this, India is one of the initial proponents of the Horizontal Mechanism (HM) proposal. It aims to bring in a ministerial decision on "Procedures for the facilitation of NTBs". This proposal has received the support of more than 100 WTO Member countries. Though the Doha mandate refer to NTBs in the context of 'products of export interest to developing countries', there have been some moves to utilize this increasing market access of remanufactured goods by some countries, led by United States of America. India's negotiating position on this is that since there is no agreed definition on remanufactured goods, a work programme is required in the first place for defining and distinguishing remanufactured goods in contrast to other second hand goods which might have grave implications on the environment and livelihood aspects of the developing countries. The work programme has now got support from around 17 countries.

7.69 In services, India has been a demandeur. It has also offered substantial sectoral and modal coverage in its initial offer (January 2004) and the first revised offer (August 2005) of the ongoing services negotiation. At the Signaling Conference (July 2008) which was held on the sidelines of the Mini-Ministerial meeting, some further improvements were also conveyed. However, India's offers / signals are conditional on receiving satisfaction in respect of its Modes 1 / 2 and Mode 4 requests.

7.70 The services negotiations at the WTO have been rejuvenated after the G-20 Meeting. Substantive interest has been evinced by all members to intensify the negotiations to make use of the limited window of opportunity (2011) to conclude the negotiations. As a part of the plurilateral process (where more than two countries are involved), 22 plurilateral groups have been formed at the WTO in service sectors/modes. India is the coordinator of the plurilateral requests in Mode 1 (cross-border supply) and Mode 4 (Movement of Natural Persons) - the core areas of its interest in the services negotiations. India is also co-sponsor of plurilateral requests in computer and related services (CRS) and architectural, engineering and integrated engineering services.

7.71 India has shown considerable movement from Uruguay Round commitments to revised offers; however its primary requests in Modes 1 and 4 have not been addressed by key developed countries. Some of the major developed country members have shown little or no movement in their Mode 4 offers which is a major cause of concern to India. The US and other developed countries such as Australia are trying to introduce a new approach to services negotiations by way of the clustering initiative. India has opposed this cluster approach on procedural as well as substantive grounds. The lack of progress in services under the Doha Round is not due to problems with the approach of negotiations but because of lack of political will, inadequate response from developed countries in sectors and areas of export interest to developing countries, and little movement in agriculture and NAMA.

7.72 One of the areas of crucial interest to India is development of disciplines in domestic regulations (DR) involving qualifications and licensing requirements and procedures without which Mode 4 access gets severely impeded. Negotiations on this subject are proceeding on the basis of the Chairman's text of March 2009. In order to take the negotiations forward, a fresh round of offers would need to be tabled at the WTO by member countries. A timeline for the submission of the second revised offers in services would be decided after a breakthrough is achieved in agriculture and NAMA. An ambitious outcome in services has to be an essential part of any breakthrough package. India has repeatedly stated that any future work in services must be anchored in Annex C of the Hong Kong Ministerial Declaration. Members need to spell out clearly how they intend to meet the modal objectives outlined in Annex C. In particular, developed countries need to provide clear signals of market openings in sectors and modes of interest to developing countries, particularly in Modes 1 and 4.

Rules Negotiations

7.73 Negotiations are taking place in the Negotiating Group on Rules (NGR) aimed at clarifying and improving disciplines under the Anti Dumping Agreement and the Agreement on Subsidies and Countervailing Measures (ASCM), while preserving the basic concepts, principles, and effectiveness of these agreements and their instruments and objectives. Members are also discussing new disciplines for fisheries subsidies.

7.74 The discussions on Chair's draft text of 18 December 2008 continued during 2010. Consensus eludes on the bigger issues in anti-dumping such as zeroing, sunset reviews, lesser duty rule, public interest, causation, and anti-circumvention. In Subsidies Agreement, considerable divergence remains in the proposals on specificity, subsidies in the case of inputs provided at regulated prices, and benchmarks for export finance. India has been seeking strengthened anti-dumping rules so as to prohibit the use of zeroing in dumping margin calculation, strengthening of the rules for conduct of sunset reviews, and mandatory application of lesser duty. In the Subsidies Agreement, India is opposed to the enlargement of the scope of prohibited subsidies in the ASCM and /or limiting of the existing flexibilities for the developing countries. In the negotiations on the new disciplines on fisheries subsidies, India is seeking effective special and differential (S&D) treatment for the developing countries, particularly in the light of employment and livelihood concerns for small, artisanal fishing communities and for retaining sufficient 'policy space' so as to enable it to develop its infrastructure.

Trade Facilitation

7.75 Another important area of the Doha round is the negotiations on trade facilitation. Simplification of trade procedures by reducing trading costs is in the interest of all WTO members. A Draft Consolidated Negotiating Text on Trade Facilitation was worked out by the WTO members on 14 December 2009. The draft text has since been revised six times in 2010 through discussions in the meetings of the Negotiating Group on Trade Facilitation. India has been actively participating in these meetings and has also tabled a few proposals on 'Customs Cooperation', 'Rapid Alerts System of Customs Union', and 'Appeal Mechanism'. Developed countries do not want to change their trade procedures but expect others to do so. Developing countries have, by and large, adopted an extra defensive approach to negotiations. Least developed countries, in general, do not want to undertake any binding commitment. Capacity constraints and lack of resources are two major factors that prevent developing countries (and least developed countries) from taking on binding commitments in trade facilitation. The current scenario indicates that developed countries and other donors may not invest in building physical infrastructure in these countries, although the July 2004 Framework Agreement clearly links

commitments to support and assistance for infrastructure development. It is important that this linkage is respected by the entire WTO membership, particularly the developed countries and that adequate assistance is provided for implementation of commitments so that a high standards agreement on trade facilitation can be reached.

BILATERAL AND REGIONAL COOPERATION

7.76 In the past, India had adopted a very cautious and guarded approach to regionalism. However, recognizing that Regional and Preferential Trading Agreements (RTAs) would continue to feature prominently in world trade and given the slow nature of multilateral negotiations, India began moving in most cases towards Comprehensive Economic Cooperation Agreements (CECAs). Some of the recent developments related to major FTAs/RTAs/CECAs are the following:

- **India-EU Trade and Investment Agreement Negotiations:** Negotiations for a Broad-based Bilateral Trade and Investment Agreement (BTIA) between India and the EU started in June 2007. So far eleven rounds have been held. The last round was held in India in January 2011.
- **India-Japan Economic Partnership Agreement (EPA) Comprehensive Economic Cooperation Partnership Agreement (CEPA) Negotiations:** The negotiations for a CEPA started in January 2007 and an 'in principle' Agreement was signed during the 14th Round on 9 September 2010 in Tokyo.
- **India-Malaysia Comprehensive Economic Cooperation Agreement (CECA):** India-Malaysia CECA negotiations were launched in February 2008. The negotiations have been concluded in September 2010. The CECA including trade in goods, services, investment, and other areas of economic cooperation, would be signed as a Single Undertaking. Taking into account the India-ASEAN Trade in Goods Agreement that was implemented in January 2010 between India and Malaysia, both sides have offered 'ASEAN plus' market access in goods. On 27 October 2010, the Prime Ministers of India and Malaysia have announced conclusion of the negotiations with the Agreement scheduled to be signed by early 2011 and implemented by 1 July 2011.

- **India-Korea CEPA: An** India—Korea CEPA was signed on 6 August 2009 and implemented with effect from 1 January 2010 covering trade in goods, investment, services and bilateral cooperation in areas of common interest. Under the CEPA, tariffs will be reduced or eliminated on 93 per cent of Korea's tariff lines and 85 per cent of India's tariff lines. It will facilitate trade in services through additional commitments made by both countries to ease movement of independent professional and contractual service suppliers.
- **India-ASEAN Trade In Goods Agreement:** On 13 August 2009, India and ASEAN comprising Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam signed the Trade in Goods Agreement under the broader framework of a Comprehensive Economic Cooperation Agreement (CECA) between India and ASEAN. The Trade in Goods Agreement provides for elimination of basic customs duty on 80 per cent of the tariff lines accounting for 75 per cent of the trade in a gradual manner starting from 1 January 2010. India has excluded 489 HS 6 digit lines from the list of tariff concessions and 590 HS 6 digit lines from the list of tariff eliminations to address sensitivities in agriculture, textiles, auto, chemicals, crude and refined palm oil, coffee, tea, pepper, etc.
- **Asia Pacific Trade Agreement (APTA):** APTA includes Bangladesh, the Republic of Korea, Sri Lanka, China, Lao PDR and India. The fourth round of negotiations was launched in Goa in October 2007 in the Second Session of the Ministerial Conference. To move forward the fourth round of negotiations, the third meeting of the Ministerial Council and the 35th Session of the Standing Committee were held on 15 December 2009 and 13 – 14 December 2010 respectively in Seoul, South Korea.

CHALLENGES AND OUTLOOK

Outlook

7.77 The outlook for India's trade sector has brightened with a good growth of 29.5 per cent in 2010-11 (April-December), a robust growth of 36.4 per cent in December 2010 and similar signs for January 2011. However, this bright picture needs to be moderated on account of the recent developments

in world trade, though transient in nature at present. While world merchandise trade picked up in the first half of 2010, there was a slowdown in the third quarter of 2010 due to the base effect and drying up of fiscal stimulus. The growth of exports and imports has also moderated in India's major trading partners in the last few months of 2010. In particular, the import growth of the EU has been decelerating even before it could fully pick up, falling to as low as 7.8 per cent and 6.1 per cent in July and September 2010 respectively and picking up in October and November 2010 to 9.3 per cent and 12.6 per cent respectively. This situation in the EU may continue for some time with fresh bouts of financial turbulence flaring up in the periphery of the Euro area in the fourth quarter of 2010. Deceleration was also registered in other markets like Hong Kong, USA, Japan, and Singapore.

7.78 On the import side there is new trouble brewing up in the Middle East resulting in oil prices (Brent) which were hovering at around US\$ 95 per barrel crossing the US \$ 100 mark in February 2011 and gold prices steadying at around US\$1341 per troy ounce (as on 28 January 2011) after reaching a peak of US\$1423 on 7 December 2010. Although the concerns on the trade deficit front have subsided with pickup in exports in the last five months and slowdown in imports in the last three months of 2010-11 (April-December), the situation needs to be watched. However, the deceleration in net surplus of services trade is a cause for worry on the current account deficit front.

Challenges

7.79 After withstanding the crisis successfully, the short-term challenges on the trade front for India are related to speeding up and maintaining the tempo of export growth and ensuring that the slightly dimmed prospects on the trade growth front do not come in the way of the reforms agenda. The gradual withdrawal of stimulus measures by India and other countries is not likely to adversely affect India's rising exports. However, there is need to be vigilant about any fallout of the financial turbulence in the periphery of the Euro zone and the new disturbances in the Middle East. Equally important is the need to guard against new protectionist measures. Though many of these are on the decline, those already in place need early winding up. India may have to raise its pitch in bilateral and international forums on early withdrawal of these trade distorting measures and also insist on sunset clauses for the remaining measures. The continuation of inflation concerns on

Box 7.6 : Trade Policy Reforms : Some Challenges for the Medium and Long Term

Some important challenges for India's trade sector in the medium and long term are the following:

Challenge of becoming a major player in world trade: The challenge for India is to achieve a share in world trade commensurate with its size. Despite making great strides in its export growth with 20 per cent plus growth continuously from 2002-03 to 2007-08, India has not made much progress in terms of the share in world trade. While India's exports were higher than those of China till 1954, they started lagging thereafter. In 1990, shares in world exports of China and India were 1.8 per cent and 0.5 per cent respectively and in 2009, their respective shares stood at 9.7 per cent and 1.3 per cent. If India can attain at least half of China's share in world exports, the impact on its employment and manufacturing activity will be enormous. While trade policy measures, shift in focus to some markets and some products, trade facilitation, tariff reforms, etc. have helped in some measure, if India has to achieve a substantial share in world exports, a big push will be needed.

Challenge of real diversification of India's exports: While India has diversified its export basket as well as export markets over the years, substantial diversification in tune with world demand has not taken place. This can be seen by matching India's exports with the top 100 imports of the world at the six-digit HS level. The exercise based on PCTAS data 2010 (data for 2008) shows that India's presence in these top items of world demand is negligible except for a few items such as diamonds and jewellery, oil cakes, t-shirts, mens/boys trousers, flat rolled iron products, and maize (corn). There are many electronic, electrical, and engineering items (the three Es) in the top 100 imports of the world where India's presence is negligible.

Challenge of increasing export competitiveness: India's export competitiveness is being challenged not only from China and the South East Asian countries but also from the newly emerging Asian countries, less developed countries like Bangladesh, and small countries like Vietnam in items like textiles. At macro level, the two major determinants of export competitiveness are the exchange rate and inflation reflected in the real effective exchange rate (REER). As per the RBI, there has been a distinct divergence between the movements of six-currency and 36-currency REER indices so far during 2010-11. While the six-currency REER remained above base level by 16 to 20 per cent, signifying higher inflation differentials with these economies, the 36-currency REER largely remained below or around base level, implying that inflation in India has been comparable to or below the levels prevailing in its trading partners in the developing world. The magnitude of nominal exchange rate appreciation/depreciation of the currencies of these countries also differed, as reflected in the 30-currency REER derived after the exclusion of the 6-currency index from the 36-currency index. If the positive inflation differentials persist and the tendency among some countries to use undervalued exchange rates to boost their export further amplifies, then the competitiveness of Indian exports may come under pressure. At the micro level there are issues like the high transaction cost in exports. The recent Department of Commerce report of the 'Task Force on Transaction Cost in Exports' also highlights this issue. Quoting the World Bank 'Doing Business' Report it states that it takes 17 days to export a container from India and costs US\$945 per container, compared to US\$450 and US\$ 500 in Malaysia and China respectively. Denmark, Brazil, Mexico and China take 5 days, 12 days, 14 days and 21 days respectively to export a container from their countries. The report estimates the magnitude of transaction cost at approximately US\$ 13 billion. It has identified 44 issues for action, of which 21 issues have been implemented and 11 issues are under the process of implementation. Implementation of the 21 issues and another 2 issues is likely to mitigate the transaction cost by ₹ 2100 crore (i.e. around US\$467 million). Further efforts to reduce transaction cost could increase India's export competitiveness.

Challenges related to tariff reforms: India has been progressively lowering peak customs duty. The fall in peak duty has not led to the feared collapse in revenue collections. The duty cuts have neither wiped out the domestic manufacturing sector nor resulted in large-scale unemployment as forecasted by many. The data show that progressive peak duty cuts have been accompanied by rise in customs duty collections. However, further bold tariff reforms with minimum revenue loss are needed to reach levels comparable to those in ASEAN both for peak rate as well as total duty (also see Box 7.5). One area of tariff reforms is related to customs duty exemptions and export promotion schemes. As a percentage of aggregate tax collection, revenue foregone remains high with more than half of all notional revenues flowing into the foregone account. What is worse, an increasing trend is visible over the last three years. In financial year 2009-10, only 41.7 per cent of notional duty was collected compared to 44.6 per cent and 51.1 per cent in 2008-09 and 2007-08 respectively. Substantial revenue is foregone on account of the different export promotion schemes. In 2010-11, revenue foregone will continue to be significant at more than ₹ 50,000 crore due to enlargement of the scope of schemes under the Foreign Trade Policy 2009-14 (FPS/FMS/VKGUY) and improvement in export promotion rates in the Duty Entitlement Passbook (DEPB) Scheme coupled with pickup in exports. The revenue loss from end-use exemptions will also go up with rising imports. There is also the question of accountability in the case of different schemes, which involve substantial exemptions. While some exemptions are needed particularly at this juncture to promote exports, there is scope for reducing the duty foregone by rationalization and convergence of these schemes. One such example is related to the Export Promotion Capital Goods (EPCG) scheme. With import duties of general capital goods being reduced consistently, the differential with total EPCG has come down from 35.4 per cent to 21.5 per cent during the last five years. Another reduction in import duties for all capital goods preferably to the 3 per cent duty level stipulated for the general EPCG and simultaneous withdrawal of the EPCG scheme could help in avoiding revenue leakages and serve as a major step

(Contd.....)

Box 7.6 : Trade Policy Reforms: Some Challenges for the Medium and Long Term (Contd...)

in rationalizing export promotion schemes. It will also serve as an upfront push to the import of capital goods for modernization of the manufacturing and services sector in general and export manufacturing in particular.

Challenges related to FTAs/Comprehensive Economic Cooperation Agreements (CECAs) in the absence of successful WTO negotiations. The proliferation of FTAs in the world is characterized as the 'spaghetti bowl' in which trade criss-crosses in a complex fashion between countries based on tariff differentials and complicated rules of origin. In recent years, India too is a part of many regional and bilateral groupings. While there are benefits from these FTAs for Indian exports, in some cases the benefits to the partner countries are much more, with net gains of incremental exports from India being small or negative. FTAs also lead to a new type of inverted duty structure with duties for final products being lower from FTA partners compared to duties for the previous-stage raw materials imported from non-FTA countries. This acts as a disincentive to local manufacturing which is not competitive against FTA imports because of the inverted duty structure phenomenon. For example, the normal customs duty on Indian TV sets is 10 per cent, but in the case of imports from Thailand and Singapore there is zero duty subject to the rules of origin requirement. There are similar issues even in agricultural items. For example, arecanuts or betel nuts have a basic customs duty of 100 per cent. But this duty is nil or at concessional low rate at different levels for imports from Sri Lanka under the Indo-Sri Lanka FTA and the South Asian Free Trade Area (SAFTA) agreement and from FTA partners like Myanmar, Bhutan, and Nepal. This could affect some regions which depend mainly on cultivation of arecanuts for livelihood. Following the ban of some States on arecanut products, demand crashed. Allowing imports at concessional duties under FTAs for items that are banned by some States needs reconsideration. The policy challenge related to FTAs/CECAs should take note of specific concerns of the domestic sector and ensure FTAs do not mushroom. Instead they should lead to higher trade particularly higher net exports from India.

Challenges related to services trade: Services trade is uncharted territory with plenty of opportunities and challenges. A more conducive environment for trade in services can be created by liberalizing FDI in services as FDI inflows and trade in services have a close relationship given the nature of intra-firm trade of multinational parent firms with affiliates; rationalizing taxes in services like shipping and telecom; going forward with totalization agreements; streamlining domestic regulations like licensing requirements and procedures, technical standards, and regulatory transparency which can help in the growth and export of services; and continuing with the focus on services in multilateral and bilateral negotiations. These, along with systematic marketing of services, collection and dissemination of market information by setting up a portal for services, streamlining the services data system, and a more focused, coordinated, and synchronized policy by the different agencies involved, could help the services sector make further strides. (Also see Chapter 10)

the domestic front would also mean that trade policy measures could be put to further test in the coming fiscal year to tackle inflation. This could further erode the exports of the already battered agricultural export sector. This has necessitated the formation of a systematic inflation-tackling mechanism with early warning systems, rather than resorting to ad hoc policy measures.

7.80 The challenges in the medium to long term have to be seen in the light of the many paradoxes in the Indian trade sector (Also see Box 7.6). While India is becoming an active player in world trade

negotiations and shaper of world trade policy, it is still a small player in world trade. While it is trying to gain markets and increase competitiveness in new areas, it is losing markets and competitiveness in some of the traditional areas. While it has made some forays into exports of some dynamic commodities having high shares and high growth, it has not been able to make a real dent in the trade of these big ticket items which are top of the list of world demand. Thus the potential for India in trade is great, but the challenges are also aplenty.