Chapter-1

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1.1 Background

India espoused an inward looking industrialization strategy with emphasis on import substitution in the course of planning for the Indian economy, just after the independence. Export development was neglected by the early planners as it was believed that demand for India’s traditional exporting products is inelastic and, therefore, only after a strong industrial base larger export earnings would be possible. As a result, India could not integrate properly with the world trading system for more than four decades. Many trade theorists (Krugman 1986, Hussain 1988, and Bhagwathi and Srinivasan 1989) did not support this inward orientation and suggested a change in the development strategy by employing an outward oriented strategy. The view of these theorists also supported by the outcome of several committees such as Tandon Committee 1980, Abid Husain Committee 1984, and Narshimham Committee 1985 as these committees advocated the reform of trade policies by inculcating liberal measures in them. However, the disappointment in import substitution; the debt problems, which generated macro-economic instability; and the role of foreign creditors, such as the International Monetary Fund and the World Bank, have been some of the underlying causes of the economic reforms in India, which began in July 1991. The external sector reform such as foreign trade policy reform along with the liberalization in foreign investment has been the central feature of the economic reform process of India. A gradual process of liberalization in external trade regime has been implemented during the last eighteen years and India has integrated progressively in to the regional and the world economic system.

1.2 Why Foreign Trade?

The importance of foreign trade, as a significant growth factor has been recognised by many classical and neo-classical economists notably Adam Smith, J. S. Mill, Ricardo, Viner and Haberler, as in their view trade serves as an ‘engine
of economic growth’, ‘an activator of change’ and ‘a barometer of economic progress’. Jeffrey Sachs observes that “policies oriented towards international trade are among the most important factors that promote economic growth and convergence of developing countries”

Many empirical studies show a strong correlation between a country’s trade share and its economic growth performance (c.f. Edwards, 1992; Sachs & Warner, 1995; Frankel & Romer, 1999; Dollar & Kraay, 2004; Romalis, 2007). This relationship runs in both directions: the richer countries become the more, when they tend to trade; but more importantly, countries that engage in more trade grow richer more quickly. The East Asian experience of export-led growth over the past three decades provides powerful real-world evidence of the potential for trade to be an engine of growth and poverty reduction (Farole Thomas et al 2010).

Dr. Manmohan Singh, the propounder of Indian economic reforms of 1991, has asserted that ‘whatever the development strategy, the function of international trade as a supplier of “material means” indispensable for development’ (Manmohan Singh, 1964). The study of the pattern of foreign trade is, therefore, integral part of the study of a country’s economic development and moving the economy towards a new growth trajectory.

1.3 Why Trade Reform or Trade Liberalization?

Goods and services do not flow completely freely among countries, even among those with excellent relations. Countries put up barriers to trade for a number of reasons such as protecting home market from foreign competition. The rationale behind trade liberalization suggests that greater competition would induce the production units to improve productivity, which is instrumental for accelerating the overall economic growth. Since firms respond to the world market signals, the commodity structure of the country’s trade would undergo changes in accordance with the changing patterns of specialization. The conventional wisdom, based on the Heckscher-Ohlin-Samualson (H-O-S) model, is that trade liberalization would induce reallocation of productive resources from the import competing industries to those industries where the country has
comparative advantages (Veeramani, C., 2006). It is also highlighted in various studies that trade liberalization increases efficiency and economic growth as it provides:

- Better allocation of resources
- Opportunity for capital accumulation
- Stronger competition
- Investment friendly setting

Considering the importance of trade liberalization different economist advocated the emergence of an open trade regime in an economy. As quoted by Dani Rodrik “Recent economic history proves that countries with less barriers to international trade experience faster economic progress”. An OECD estimate indicates that scrapping all tariffs on merchandise trade and reducing trade costs by 1 per cent of the value of trade worldwide would add the equivalent of up to 2 per cent to the present annual gross domestic product (GDP) in some areas (OECD 2003). Thus, removal of unnecessary trade barriers can give a great boost to global economic welfare.

Martin (2001) also observes that precisely, an open trade regime has at least four major advantages over a closed economy approach to economic development. These advantages are:

- The comparative-static benefits from trade
- The ability of sectors with relatively high productivity to grow far beyond demand in the country itself
- Dynamic welfare gains arising from continuing rises in productivity
- Reductions in the incentives for unproductive activities and corruption associated with trade barriers.

1.4 What is Trade Reform?

World Development Report (1988) argued "Trade reform means policies that reduce protection (pg. 34).” Broadly speaking, trade reform comprises reduction or removal of restrictive measures that directly or indirectly affect trade
activities, monetary and fiscal policies, industrial policies, import tariff and export subsidy policies and quantitative controls of various kinds etc. To implement trade reform process different measures can be initiated such as conversion of quantitative restriction into tariff, reduction in average tariff rates and dispersion across sectors, direct measures for export promotion, measures for trade facilitation etc. Trade policy reforms include export policy which comprises measures for export promotion and liberalization and import policy which comprises of measures for import regulation and liberalization (Narayana and Nataraj 2002).

1.5 Process of Trade Reforms in a Planned Economy

Under a classical planned-economy trade regime, trade in each product is monopolized by a foreign trade corporation. Policy measures such as tariffs, quotas, licenses, and exchange rates play a relatively minor role, since most decisions about the level and composition of exports and imports are made through the planning system. Reform of such a system to a more market oriented trading system requires a number of steps, such as:

- Opening up the trade system to competing traders
- Developing indirect policy instruments such as tariffs and quotas and moving progressively to price-based measures
- Removing exchange rate distortions,
- The possible introduction of measures to reduce the impact of continuing distortions.

These trade reforms must take place in the context of fundamental reforms in the domestic economy (Martin, 2001). It is, further, evident from the above process that trade liberalization constitutes a significant aspect of overall trade reforms.

1.6 Foreign Trade Towards Liberalization

For hundred of years, foreign trade has served as a vehicle of extension of improved techniques of production to an ever increasing number of users. It has
served as medium for cross-fertilisation of different cultures and a connecting link between the activities of people all over the world. The economy of every country was synchronised with the economy of every other country to a greater or lesser degree through an interdependence that has evolved gradually as the countries have themselves developed over the year (M. C. Vaish, 1978) but the growth of trade has not been a smooth affair. It has changed gradually from the era of mercantilism to the current free trade practices.

Adam Smith, the founding father of modern economics, has been the first economist to advocate such a market base economic liberalization and free trade as the powerful instrument of growth market mechanism. Smith argued that economic specialisation could benefit nations just as much as firms could. Since the division of labour was restricted by the size of markets, he said that countries having access to larger markets would be able to divide labour more efficiently and therefore become more productive. Smith also stated that he considered all rationalisation of import and export controls “dupery” which hurt the trading nation at the expense of specific industries (Adam Smith, 1918). In 1817, David Ricardo, James Mill and Robert Torrnes showed that free trade might benefit the countries industrially weak as well as strong, in the famous theory of comparative advantage. This theory states that in support of free commerce, each country naturally devotes its capital and labour to such employments as are most beneficial to each. This pursuit of individual advantage is admirable connected with the universal good of the whole. Nevertheless, stimulating industry, by rewarding ingenuity, and by using most efficaciously the peculiar powers bestowed by nature, it distributes labour most effectively and most economically (David Ricardo, 1817).

However, by the year 1929, free trade was based on national advantage and not taken as a concept of global significance. It was only after the ‘Great Depression of 1929 that economic, social and political importance of free trade has grown because at that time, lack of free trade was considered by many as principle cause of the depression. Therefore, considering the need of collaborative effort to promote free trade among nations in the world, an agreement titled
‘Bretton Woods’ signed by 44 countries in 1944 which was intended to prevent trade barriers. A ‘General agreement on Tariffs and Trade (GATT)’ was also signed by 23 countries.

After that, a huge change came in the economic atmosphere of the world. This was facilitated by the economic reconstruction and industrialisation process of economies following the two world wars and multilateral initiatives by international organisations like GATT that enabled dismantling of trade barriers and non-tariff barriers among the industrialised countries imposed during the war period. Along with this, the economic stagnation in the countries of Latin America, most of which had followed the import substitution route, and in stark contrast, the rise of the East Asian “tiger” economies, which had adopted outward oriented strategies during the sixties and seventies, led some to seriously question the protectionist-growth nexus. In addition, technological revolution in communication and transport has given an impetus to foreign trade that has led to liberalization of policies towards free trade.

<table>
<thead>
<tr>
<th>Time</th>
<th>Trade Growth (Real)</th>
</tr>
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<tbody>
<tr>
<td>1850-1913</td>
<td>3.8</td>
</tr>
<tr>
<td>1950-2007</td>
<td>6.2</td>
</tr>
<tr>
<td>1950-1973</td>
<td>8.2</td>
</tr>
<tr>
<td>1974-2007</td>
<td>5.0</td>
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Source: World Trade Report 2008, WTO

Due to these liberalization moves, many changes have also noticed in world merchandise trade. As Table 1 above depicts that during the period of 1850-1913, which was a period of the first wave of globalization, the trade rose by 3.8 per cent per annum in real terms.

Then, taking the benefits of the first globalization wave trade expanded on average by 6.2 per cent in the entire 1950-2007 period. The trade growth was remained strong for the period of 1950-73 and trade increased by more than 8 per
cent per annum in real terms during this period. Trade growth slowed thereafter under the impact of two oil price shocks, a burst of inflation caused by monetary expansion and inadequate macroeconomic adjustment policies.

Specifically, last three decades of 20th century witnessed a revival in the world trade when economic reform process initiated in large number of developing countries. During the late seventies, many East Asian economies embarked on the path of export led growth to make possible development through trade. Trade integration between countries augmented during late eighties and nineties when reforms in developing countries intensified by following market oriented policies through the conditional assistance of IMF and World Bank, and eighth round of GATT, which went much beyond reduction in tariff and non-tariff barriers undertaken earlier. As pointed out by Razeen (2000) "Thirty-three developing countries (almost half of all developing countries with protectionist policies) swung from relatively closed to relatively open trading regimes between 1985 and 1995". By that, significant changes came in the world trade. The major structural changes were growth of world trade in volume, increase in Asia's share in world trade, shift of developing countries export basket towards high value added products and growth of trade between developing countries. Global trade relative to world GDP has grown from around 40 per cent in 1992 to over 50 per cent today. A turnaround has been taken by India also in July 1991 and Indian economy adopted a continuous process to make trade easier. As a result, the role of foreign trade is growing in India and remarkable changes are coming in its trade scenario.

1.7 India's Historical Movements towards Trade Liberalization

If the term globalisation means free trade and free movement of all factors of production including labour, then it can not be denied that India has been pioneer in the globalisation process in the history of the mankind. She also could use foreign trade quite successfully as the engine of growth and lead to her national and regional material prosperity especially in the first millennium (Sen, 2004). She had an active and mutually enriching trade relations with all the early
The most important feature of India's foreign trade was that India always had a surplus with the whole world including Europe, which was settled by the inflow of gold into India (Singh, 1985). But the benefits of India's high trade integration in the past gradually declined as (1) her share in global trade slowly declined for reasons which were economic, political and also geographic (many ports had to be deserted due to silting and/or shifting of rivers) (2) loss of competitiveness of her products due to better technology (ships of their competitors were improved both in terms of their built, size, speed and also armoury), and non-economic factors like inability to protect her trading infrastructure from trading invaders which resulted in plunder and destruction etc (Sen, 2004).

By the middle of the 2nd millennium, India, once rich, industrialised, outward looking and commercially vibrant economy became agricultural, inward looking, poor and underdeveloped according to modern terminology. Even in the 19th century it considered by many as a model of 'Asiatic mode of production' with self-sufficient villages or their clusters as the units of the economy, yet she had an experience of world globalisation process once more towards the end of the 19th and 20th centuries in the modern age. The 19th century globalisation started around 1870 in a global context and ended with the outbreak of the first world war in 1914 (Sen, 2004) when tighter controls were imposed on import to conserve foreign exchange and to finance deficits in balance of payments. For long, since then, India conflicted between liberalization and protectionism.

The 20th century globalisation, in a vigorous way, started only in 1991 when comprehensive and systematic liberalization-cum-structural adjustment reforms adopted to make trade easier. These reforms had two components. First, stabilisation part which aimed, in the short-run, at reducing the level of aggregate demand by: (a) reducing current account deficit (e.g. as a percentage of GDP) which is called the external stabilization programme, and (b) reducing the domestic rate of inflation which is called the internal stabilisation programme. Second, the structural adjustment part which aimed at increasing economic growth by: (a) shifting resources from import production activities to export
promotion activities, (b) increasing the degree of openness of the economy, (c) shifting resources from government sector to private sector activities, (d) changing the structure of incentives and institutions such that reliance on market is increased or the role of the state is reduced.

It is noticeable that one of the main reasons for the initiation of reforms was on account of the crisis in the external sector. For instance, the current account deficit that rose from an average of 1.3 per cent of GDP during 1980-85 to 2.2 per cent during 1985-90 increased to 3.2 per cent in 1990-91. The foreign exchange reserves in 1991 had reached an all time low of US $ 2236 million which was just enough to pay for three weeks of imports. It was at this critical economic situation that the Government initiated trade policy reforms with a view, among others, to improve balance of payments position. Thus trade policy reforms have been the core of the reforms.

Consequently, significant changes have taken place concerning the commodity composition and the direction of Indian merchandise as well as services during post liberalization period. It is the principle concern of this study to understand the changes in India’s foreign trade scenario and to examine the relaxed guidelines of foreign trade policies so that policy implications could be drawn regarding trade policy reforms for the future growth of India’s foreign trade in long-term perspective.

1.8 Review of Related Literature

The area of foreign trade being very wide, offers an unlimited scope for research. Many studies have been carried out and specific arguments have been presented in different directions about many aspects of foreign trade and economic reforms. In pre-reform scenario there was Manmohan Singh in fifties, Nayyar in the sixties, Bhagwati and Srinivasan in seventies, Wolfs (and various official committee reports) in the early eighties and Panchamukhi in mid eighties. The propounder of economic reforms in India, Dr. Manmohan Singh provided a detailed analysis of the sluggishness of India’s exports during the fifties and indicated the importance of external and internal factors in India’s foreign trade.
Deepak Nayyar presented a comprehensive study of India’s export performance and highlighted the emerging pattern of non-traditional exports in India’s export basket. Martin Wolf analysed India’s exports at the aggregate level and found out the effect of export policy on India’s export performance. V. R. Panchmuckhi emphasized the importance of trade policies as a determinant of trade patterns and attempted to provide quantitative measurement of trade policies of India. After initiation of reforms in 1991, a large number of studies have been carried out on this subject using different analytical tools like micro and macro economic modelling, statistical and econometric analysis; product wise case studies and interviews with exporters and importers. Along with it, as many countries liberalized their trade regimes during the decades of eighties and early nineties, so there are many studies in the different countries that review trade policy reforms and trade performance of individual countries and highlights different aspects related to foreign trade. Therefore, before proceeding to the details of the methodology that we have adopted, and the analysis work, we briefly survey some of the literature relevant to our study.

T. N. Srinivasan (May 1990) presents an extensive exploration of the development in foreign trade of India during the period of 1950 to 1989. With the focus on liberalization phases, the author explains the various changes in foreign trade policy of India as well as China during the period under study. Author also compares different trade regimes of both the countries and figures out some lessons from the experiences of India and China.

M. Ataman Aksoy (Oct. 1992) in a policy research working paper of World Bank studies the trade reform regime of India. In the study, author attempts to quantify the structure of the import-licensing regime and analyze the details and structure of tariff and excise taxes and their evolution. The author further explains the nature and magnitude of export incentives, which compensates for the import and tariff regimes. Study points out that despite attempts to liberalize India's import trade regime, the structure of import licensing is still restrictive and complex and for most products, the licensing systems probably offers no more
protection than tariffs do. Therefore, the study advocates that India’s import policy regime and tax system along with the export policy regime should liberalize to reap the maximum benefits of trade reforms.

**Jayanta Roy (1996)** in a study discusses India’s least outward-looking approach as compared to other countries of Asia prior to the economic reform of June 1991. The study assesses the liberal reform measures adopted in the area of foreign trade for the period 1991 to 1995 and find out that the result of the economic reform launched in 1991 has been encouraging. However, it suggests many tasks that have remained unfinished and are very necessary to achieve and sustain a rapid export growth.

**Hajra and Sinate (1997)** provide a detailed decade wise analysis of Indian trade performance since independence, relating it to domestic policies and external developments. Authors also discussed some issues in India’s foreign trade viz. trade-growth linkage, movements in India’s terms of trade and competitiveness of India’s export sector. Authors explain the growth of export in terms of exchange rate changes and foreign trade policies. They highlights that the poor performance was a result of the persistent overvaluation of exchange rate, inadequate coverage of export subsidies and other export incentives. Along with it, authors observes a marked lack of emphasis on the inter linkages of foreign trade sector with developments in the domestic economy and policy, particularly the high controls that the import substitution policy imposed.

**Rajesh Mehta (1997)** analyzes the impact of India’s trade policy reforms on external trade. The author uses the indices of trade liberalization like the Effective Rate of Protection (ERP) and the Nominal Rate of Protection (NRP) to quantify the extent of protection granted to the Indian industry. He also uses the index of structural change and the Sign test to verify the hypotheses that the distribution of India’s exports and imports by commodity composition during the year 1994-95 i.e. the post-reform period is not different from the year 1990-91 i.e. the pre-reform period. This study reveals that the liberalization process has led to...
significant decline in the protection of Indian industry through tariffs and non-tariff barriers but there has not been any significant change in composition of India’s import and export basket during the pre and post liberalization period. Author point out that liberalization process has enhanced the importance of international trade in our domestic economy and measures for the control of import have been dismantled.

Rajesh Chadha (1998), in a research paper reviews some aspects of India’s export performance since fifties focusing on the changing composition of various commodities/commodity groups with respect to India’s as well as the world’s exports. In order to analyze the differences in the growth experiences of India and other economies, author also attempts to explore India’s export basket in comparison with export baskets of China and other East Asian countries. Author further discovers the differences in developing countries, and developed countries exports and highlights the experiences of China and other East Asian countries from trade liberalization. Author suggests that India should learn from other’s experiences and the process of liberalizing its trade and industrial policies should be carried forward.

T. N. Shrinivasan (1998), in a study attempts to make a comparative analysis of the export performance of India. The study explains the overall trends of Indian exports since independence by using regression analysis method and some other explanatory techniques. The study find out that price competitiveness of exports is an important determinant of the volume of exports, and the relevant elasticity’s are more than adequate for a real depreciation to improve the current account even with a zero price elasticity of demand for imports. Author also compares the trends in market shares of India and her competitor in a few selected commodities in which India have potential to gain market share. The study indicates the importance of openness to international trade for rapid growth and describes some implications for the overall economic policy framework.
Veena Mishra (1998) in a study explores India’s export performance and the various policy regimes in force since independence. To present a comparative performance of India’s exports the study compares India’s rate of growth of exports (aggregate and sector wise) and its shares in total world exports since independence with those achieved by some other developing countries, e.g. China, Brazil, Indonesia, and South Korea. The study also illustrates the economic reforms of 1991 and their impact on the economy both at macro (economy) and the micro (firm) level. It also highlights the next logical steps in reforms like reforms of policies relating to small scale industries reservation and labour laws.

Arvind Panagariya (1999) illustrates the liberal measures adopted in the foreign trade policies of India on the basis of World Trade Organization’s trade policy review for India in 1998. This paper explains the trade performance of Indian economy, institutional structure of trade and various trade policy measures. These measures include measures directly affecting imports, measures directly affecting exports and measures to promote exports. After analyzing these measures thoroughly, study point out that despite of substantial reforms, India’s domestic and trade policies have remained highly distorted. Therefore, the study advocates that liberalization is essential in the areas like tariff policy and domestic policy, and more resources should be mobilize into infrastructure sector to reap the benefits from trade liberalization.

Tarlok Singh (2000) conducts an in-depth study on balance of trade, exchange rate policies, trade policy regimes, and more comprehensively the performance of external sector of India in retrospect. The study covers a period of nearly four and a half decades starting from 1950 to 1997 by dividing the whole period into three broad phases of (I) the pre liberalization phase (1950-65), (II) the first liberalization phase (1966-90) and (III) the second liberalization phase (1991 to 1996), to explain the trade policy regimes in India. The study presents a plan period profile of country’s balance of trade and analyses trends in trade flows by using a series of the real exports, imports, and output for the decennial periods.
The study finds out some substantial improvements in the external sector scenario after the trade policy reforms of the nineties, and advocates further emphasis on the supply side factors with recognition of quality of output and control of inflation. It also provides some major thrust areas for policy actions like improving and streamlining the export and import procedures by reducing the administrative controls and liberalizing foreign trade sector further.

Bhatia (2000) studies the association between improvement in aggregate economic measures and trade diversification that may follow attempts at trade liberalization. The study uses four proxy measures of trade liberalization such as Imports/GDP, Exports/GDP, Exports/Imports, and (Exports + Imports)/GDP. An assumption is also taken that economies experiencing trade liberalization will have an increasing share of imports and exports in GDP. The study concludes that trade liberalization does affect the performance outcome including trade diversification in individual countries; but the extent of the impact varies depending upon initial conditions, state of infrastructure, technological capability as well as external policy environment including changes in exchange rate, terms of trade and foreign resource inflow.

B. Bhattacharya (2000) examines empirically whether reforms of 1991 have resulted in a change of the India's merchandise export composition. Specifically, whether there has been a movement in favour of technology and knowledge intensive goods and away from primary resource intensive products. The analysis highlights that during the post 1991 period India's export of manufactures have shifted towards more value added product categories and this gain has primarily come at the cost of labour-intensive product categories. Resource intensive export products have not shown any definite trend over the period under study. Further, the study estimates the log liner trend lines from 1991-92 to 1997-98 to test whether India's experience is in line with global experiences of slower rate of growth in labour intensive products. The results state that the Indian experience is consistent with the global trend and country is making progress towards technology intensive exports from labour intensive exports. The study finds out
some reasons for growth of technology and knowledge intensive products such as exploitation of economics of scale, liberal technology import, inflow of direct investment and depreciation of Indian currency. Therefore, study concludes that the initial impact of the reforms on export composition has been satisfactory in India.

Banik (2001) identify the factors that were responsible for a significant turnaround in India’s export growth during the East Asian crisis era and examines some impediments for high export growth in a sustained manner. This analysis brings out that decline in Indian exports during 1996-97 was mainly due to a fall in the growth rate of export volumes and demand side factors such as price competitiveness, potential demand, and trade barriers in the form of tariff and non-tariff measures. The study describes that though, supply side bottlenecks like procedural delays, poor infrastructure, and domestic distortion are very important for maintaining a high export growth, but these bottlenecks cannot explain a sharp drop in export growth in 1996-97.

Nagesh Kumar (2001) in a study entitled “India’s trade in 2020: A mapping of relevant factors” provides a framework of different factors that are likely to shape the pattern and magnitude of India’s imports and exports over the coming two decades. The study explains main factors that affect demand for Indian exports of goods and services such as growth performance of world economy and key trading regions, WTO agreements, China’s accession to WTO, preferential trade arrangements in rest of the World, and regional free trade arrangements. It further discovers the factors that have significant impact on supply for India’s exports of goods and services like infrastructural bottlenecks, growth of domestic demand, inflow of export-oriented foreign direct investment, technological upgrading and movement along with the value chain, WTO regime, and exchange rate alignments. Moreover, it states the factors that affect the demand for imports of goods and services like India’s growth performance and trade liberalization, crude prices, and industrial restructuring and rationalization. This paper discovers that after liberalization particularly since 1991, the importance of international trade in
Indian economy has grown considerably. Moreover, it briefly summarizes emerging patterns of India's comparative advantages in exports of goods and services. At the end, Kumar suggests that targets should be set out for specific items of India's exports by 2020 and efforts should be made with strategic interventions in the realm of trade, investment, and technology policies to achieve them.

T. N. Srinivasan (June 2001) evaluates India’s transition from an inward oriented development strategy to greater participation in the world economy. This paper discusses the achievements in the reforms of trade policy such as the extent of trade liberalization measures and liberal reforms adopted in exchange rate policies. It also evaluates the impact of liberalization on the commodity composition and direction of India’s merchandise export and import. It further assesses India’s trade performance in comparison with that of three rapidly growing East Asian economies (China, South Korea and Taiwan), three Southeast Asian economies (Indonesia Thailand and Malaysia) and two of India’s Southeast Asian economies (Bangladesh and Pakistan) for the four pre-reform years (1987-90) and the corresponding levels for four post-reform years (1993-96). After a comprehensive evaluation, study indicates that although trade liberalization during the post-1991 period has improved India’s export performance, it is still lagging behind other rapidly growing Asian countries. Study highlights that East and Southeast Asian countries liberalized their trade and switched from import-substitution to export-orientation earlier than India. As a result, they exploit international trade successfully to step up and maintain a higher growth rate and developed resilience to cope successfully with international shocks. Study concludes that while tariff rates have decreased significantly over the past decades, India is still one of the most autarkic countries. Moreover, this paper outlines the future reforms that are most needed such as reform of labour and bankruptcy laws, real privatization, and fiscal consolidation and further assess chances of their undertaking.
Ramkishen S. Rajan and Rahul Sen (March 2002) attempts to assess the impact of India’s market-oriented economic reforms initiated in the nineties on its international trade linkages with the rest of the world. The study briefly summarizes recent trade reforms in India and documents the extent to which the country has integrated with the global trading system. It analyzes Indian merchandise export pattern during post-reform regime by using export index of revealed comparative advantage (XRCA). It highlights that there is a significant improvement in the country’s overall export performance since the reforms initiated, however India continues to lag far behind most of its East Asian neighbours. Moreover, the study explains the role of services trade and foreign direct investment in overall export growth of India.

Kaliappa Kalirajan (2003) provides a review of the impact of a decade of trade policies reforms on India’s international trade and the economy. This paper presents a simple model of economic reforms and discusses the specific policy reforms that were implemented from July 1991 to July 2001 to improve India’s international trade. This study also attempts to investigate an important empirical question i.e. how open has India’s trade been after a decade of economic reforms? At the end, it concludes that, though India’s trade has been open now as compared to that of pre-reform period, but in international comparison, India has to wide open her doors.

Parmjit Nanda and P.S. Rikhy (2003) in a paper evaluates the effect of the trade policy reforms of 1991 on India’s foreign trade sector from 1991-92 to 2000-01. Author reviews important aspects of trade liberalization policies and consider effect of policies on foreign trade performance at aggregate level as well as at disaggregated levels. After evaluating the whole scenario, authors provides the broad conclusions like Improved trade performance of India during post-reforms regime in terms of openness ratio, self-reliance ratios; improvement in income terms of trade; rapid increase in quantum index of exports as compared to unit value index of exports; rapid growth of agricultural products and of manufactured products. They also highlights the negative aspects of India’s trade performance
during the period under study such as small share of India's exports of world exports; higher increase in imports as compared to exports; increased balance of trade deficit; unsustainable export growth; higher imports/GDP ratio as compared to export/GDP ratio; possibility of dumping of import goods by trading partners; increased commodity concentration in exports, and decreased importance of developed countries in exports. They also summarizes the factors responsible for poor trade performance of India and suggests that second generation reforms should be integrated with long-term national export policy which can coordinate production, infrastructure and export marketing activities.

K. Haragopal (2003) attempts to analyze some important external variables such as exports, imports, trade deficits, current account deficits, gross fiscal deficits, external assistance, and foreign exchange reserves in relation to gross domestic product before and after the trade reforms in order to find out impact of these reforms on India's external trade. For the purpose of analysis, the data related to different variables is collected for the period 1980-81 to 1999-2000 and certain key indicators are used such as ratio analysis, marginal analysis, marginal effects, and growth rates. The study discovers a positive impact of trade reforms and a better performance of export sector in the post-reform period. However, the analysis bring out that even though export sector has performed better in the post-reform period, the performance of other variables such as trade deficit, current account deficit and gross fiscal deficits has not remain very encouraging, and to overcome this the export sector has to perform better.

S. Sindu and Ratinder Kaur (2004) conduct a study on emerging trends in foreign trade of India during pre and post-liberalization periods. The study is spans in a period of twenty years i.e. from 1980 to 2000 and evaluates the main factors of structural changes in commodity composition of Indian merchandise trade and the changes in the direction of Indian merchandise exports and imports. The study find that both merchandise exports and imports have grown after reforms of 1991 but the percentage change in merchandise exports is lower in comparison to the percentage change in merchandise imports resulted in growing
trade deficit. Therefore, the study advocates a need to review the foreign trade policy and provisions of some protective measures for the domestic sector.

**Achal Kumar Gaur and Alok Kumar Pandey (2004)** evaluate the overall export performance of the Indian economy for the period of 1985-86 to 2001-02 with an attempt to isolate the impacts of economic reforms and World Trade Organisation (WTO). The study employs a regression equation with slope dummy and intercept dummy for measuring the impact of economic reforms of 1991 on India’s exports. It analyzes both commodity wise and country wise exports performance of India in the studied period. The results of the study depict a decline in per annum growth rate of Indian exports and therefore it argues that a shift should be done in export strategies to augment the growth of Indian exports in future.

**N. Mukundan and M. Manaka (2005)** attempts to study growth of exports and imports in Indian foreign trade during pre and post-reforms period. The study explains the level of exports and direction of India’s foreign trade in selected countries. It indicates that there is positive relationship between import policy and value of imports and highlighted that India’s foreign trade has been gathering increasing momentum through the cascading effect of trade reforms and the rapid integration of the global economy.

**Kundal (2005)** explains impact of trade policy reforms on the performance of trade covering a period of twenty years starting from 1984 to 2004. Major findings of the study includes growing integration of Indian economy with world economy after reforms which results as high growth rate of both exports and imports. It also threw light on growing liberalization of the trade sector and resultant increase in the proportion of trade in gross domestic product; and due to higher import growth, a continual tendency for the economy’s resource utilization to exceed the amount of the resource generated within the economy. Therefore, the study advocates further reduction to tariff protection and liberalization of capital flows to enhance the efficiency of the economy.
Hosamane Manjappa D. and S. Bisaliah, (June 2006) in a study examines India’s exports behaviour during post-reform period with the help of a constant market share model (CMS). This study observes that there is an improvement in export competitiveness. It indicates that share in exports increased due to increase in volume of world trade (56.7 percent) and competitiveness in international market (53.5 percent). While India has lost (10.2 percent) market share due to dismantling of the then USSR, it is gained in Asia and European regions. Thus, CMS analysis suggests that the globalization has helped the Indian economy to increase competitiveness of its products in the world market and openness has led to growth of Indian trade.

Mitra (2006) deals with the study of India’s direction of trade post 1990. In the study estimates, a ratio titled as ‘ratio of contrary trend’ to capture the broad trend of trade flows in different regions/countries and to indicate the extent up to which the trend is contrary to the general flow of trade. This paper briefly discusses the broad features of India’s foreign trade direction during post-reforms regime like trade diversion from the developed market countries to the developing countries and the growing importance of China in India’s foreign trade in place of European Union. The study concludes that within a multilateral framework, trade blocks and regional economic cooperation agreements are best suited to the mutual interest of the partner countries; therefore, India’s trade and economic diplomacy should be made more integrated to ensure gains from such co-operative agreements.

Subhadip Roy (2006) attempts to find out whether there have been any significant changes in foreign trade of India after liberalization. The author tries to make a comparison between the exports and imports of the pre- and post-liberalization periods, using the time-series analysis. The study uses different regression models and found out corresponding growth rates. The study highlights that there is a significant difference in the growth rates of export and import in pre and post-reforms regime, but no significant difference in stability of growth rates.
Subrata Mukhopadhyay (2006) summarizes the changes came in pattern of India’s merchandise trade over the one and half decade of reform period. The study ranks top export destinations and import sources and observe about changing dynamics of Indian exports and imports. The study also highlights the growing importance of external sector in the Indian economy during the post-reforms era.

Chandrasekhar, C. and Ghosh, Jayati (June 2007) explains the nature of the export boom since reforms of 1991. After evaluating the recent pattern of export growth, the study discovers that the export growth indicates India’s competitiveness at the lower end of the global value chain but there is not yet any sign of significant shift in India’s competitive position in manufactured exports.

Kishor Bhanushali (March 2007) illustrates the recent changes in the pattern of foreign trade. The study provides information on various dimensions on India’s foreign trades like imports, exports, balance of payment, composition of trade by commodities and countries, and find out trend, pattern, and its impact on future trade flow. The study indicates that the volume of India’s trade has increased in recent years, but the trade deficit is increasing. The study suggests diversification in export basket and development of non-conventional energy sources to save foreign exchange and to reduce trade gap.

C. Veermani (June 2007) attempt to analyze the sources of India’s export growth during the pre-reforms period i.e. 1962 to 1990 and the post-reforms period i.e. 1993 to 2005. For analysis purpose, the study uses constant market share (CMS) analysis model and discovers that the actual export growth of India has been far below the potential offered by the growth of world trade in the most part of the pre-reforms period, mainly due to negative competitiveness effect and negative commodity composition effect. In contrast, the actual export growth of India, in case of both merchandise and services, has been above the potential throughout the post-reforms period, which indicates an improvement in the overall
competitiveness of India’s exports during this period. The study also highlights the improvements in non-price factors during the post-reform scenario as export were growing since 2002 despite the appreciation of real effective exchange rates. Therefore, the study suggests the government to adopt some other export promotion measures, rather than artificial depreciation of the currency, to improve the competitiveness of Indian exports.

**Rajat Acharyya (2007)** attempts to explore the rising pattern of global trade and India’s merchandise exports. In this paper, firstly, author provides a brief review of the growth in India’s exports over the last two decades i.e. eighties and nineties, and indicates the implications of such growth on Indian exports. Then author explore the nature and competitiveness of Indian merchandise exports during the period under study by using the Geographical Commodity Concentration Index (GCCI) and Geographical Concentration Index (GCI) and Coefficient of Complementarity (CC). By the analysis author indicates that there has been a steady growth in both merchandise exports and exports of goods and services during the period of economic liberalization and significant changes have also observed in the sectoral composition of these exports. However, author point out that Indian merchandise export trade performance have not fared well in terms of both diversification of export destination and basket, and the complementarity between India’s exports and import of each of the reported countries had fallen during the nineties.

**Banik, Nilanjan (2007)** in a research study explores the demand side factors that have been responsible for an increase in India’s export growth during post-reforms period and addresses the supply-side bottlenecks that may prevent growth in India’s exports in a sustained way. The study discovers that the increase in Indian exports during the years following 2000 is predominantly services driven and is attributed to an increase in factor productivity, growth in world trade, an increase in intra-industry trade and external sector reforms. Author suggests that although demand-side factors look favorable, there is a need to address supply-side bottlenecks.
Rajesh K Pillania (2008) in a paper reviews the trends of Indian merchandise export and import during pre and post-reforms regime. The study explores the composition and direction of Indian foreign trade since independence and provides an estimation of foreign trade by 2020. The study reveals a huge untapped potential of India's foreign trade in future.

Sandra Polaski et. al (Feb. 2008) in a report titled 'India's Trade Policy Choices' simulate the potential outcomes for India's economy of a Doha agreement and potential free trade agreement with the EU, United States, and China. Study find out that multilateral liberalization through the WTO's Doha round would produce larger gains for India than bilateral agreements with any of its major trading partners. Study further highlights that volatility in world agricultural prices would affect India more strongly after a reduction in tariffs toward trading partners. It suggests that both Doha and bilateral pacts require careful negotiation if India is to realize the modest gains on offer and avoid risking large negative affects on the country.

Vijay Kumar Sharma, Des Raj Gupta and Vivek Verma (2009) in a research paper attempts to analyze India's foreign trade before and after reforms of 1991. The authors observe that prior to mid-1991, the foreign trade in India suffered from a strict bureaucratic and disciplinary control. However, by the reforms measures focus shifted towards liberalization, openness, transparency and globalization with basic thrust on outward orientation focusing on export promotion activity, moving away from quantitative restrictions and improving competitiveness of the Indian Industry to meet global market requirements.

Przemyslaw Kowalski and Nora Dihel (May, 2009) in a paper examines economic implications of India's trade and trade policy reforms during the period from 1990 to 2007. It first describes India's economic growth and the composition and performance of its trade at the product and broad sector level. Next, it assesses recent reforms and the current trade policy stance and discusses the recommendations for further policy reforms. The paper also addresses the
impact of India’s openness on its total factor productivity. The analysis shows that India has gone a long way in reducing its tariffs on non-agricultural products as well as selected non-tariff barriers and that this has put a positive impact on the economy. Author, however, states that in the process of reforms India has developed a complex system of duty exemption schemes, special investment and establishment rules and special economic zones (SEZs) that provide incentives particularly to exporting firms. He argues that, while such a policy can have important demonstration effects, across-the-board reduction of trade and business barriers could have more beneficial economy-wide and export effects.

Added to this, a number of authors have commented on the impact of trade policies on the trade performance. The descriptive studies, such as, Debroy (1993) and Kathuria (1996) present a useful description of the various trade policy measures undertaken, over the years in India. Bhattacharyya, et al (1996) finds out the improvement in various parameters in the era of liberalization, like exports as percentage of tradable sector, net export specialization index, and intensity of intra-industry trade. Khan (1999) observes a remarkable improvement in trade ratios in the post-reforms period and better export instability index for the post-reforms period. Virmani (2003) finds out the liberalization of external sector has resulted in the openness of the economy and has helped in putting balance of payment on a sustainable path.

1.9 Rationale of the Present Study

After reviewing the relevant published literature, we felt that, there is a further scope for exposition of India’s foreign trade along with scrutiny of trade policy reforms. The exploration of these studies arises various policy issues and questions such as what is the course and characters of reform measures adopted in foreign trade policy of India. What changes came in India’s trade policy due to these reforms? What changes came in India’s trade policy posture due to commitment of WTO and various free trade agreements? What type of trade policy instruments used by the other countries that have a record of successful trade policy reforms and what lesson India can draw from their experience? How
far has this policy turnaround been successful in improving India’s foreign trade performance? What is the impact of trade reform measures on the volume, growth, composition, and direction of exports and imports? In particular, how well India has succeeded in diversifying into dynamic export products? What are the sources of India’s growth performance in the area of export and import? Thus, there is a need to carry out a comprehensive study to provide the plausible answer of these questions.

Added to this, India now completed more than eighteen years of reforms regime and this period is long enough to quantify, to the extent possible, the impact of the policy reforms on the composition and direction of external trade sector of the economy as well as, identifying areas where further reforms are required. In addition, considering our foreign trade prospects in the present globalize environment, it is also pertinent to examine its historical development in order to understand our strength and weaknesses, to understand the remarkable change in trade scenario and to examine the relaxed guidelines of our policies. Moreover, any analysis of India’s existing trade agreements as well as its position on important WTO issues has to bear in mind the trade and trade policy environment from which these strategies have evolved. Hence, an added analysis of foreign trade is necessity of the time so that suitable strategies can be made for the future growth of India’s foreign trade in long-term perspective.

1.10 Objectives of the Study

The following are the major objectives of the study:

1. To explore the course and character of reform measures adopted in foreign trade policy of India, especially since July 1991.

2. To trace out the significant aspects of trade policy reforms in some East and Southeast Asian countries and draw out some implications for trade policy reforms in India.

3. To examine India's changing trade policy posture during the post-reforms regime relating to multilateral trade negotiations under the auspices of
WTO, and bilateral free trade agreements (FTAs) in order to provide some direction for India's trade policy reforms.

4. To understand the dynamics and structure of India's service trade during pre and post-reforms regime in order to examine the performance of service trade.

5. To evaluate the trend, composition and destination of India's merchandise trade especially during post-reforms period in order to capture the impact of trade policy reforms on foreign trade.

6. To derive policy implications regarding trade policy reforms for the future growth of India's foreign trade in long-term perspective.

1.11 Research Methodology

The methodology of the study is descriptive cum analytical. It is descriptive in the sense that the author highlights the specific liberal measures adopted in the different phases of Indian foreign trade policy i.e. trade policy prior to reforms period i.e. 1950-51 to 1991-92 and after the initiation of reforms i.e. 1992-93 to 2008-09. The descriptive methodology is used to analyse alternative indices of trade liberalization for measuring trade policy reforms in India. This study is analytical also as it attempts to analyse the export-import trade performance of India over the years under study and examine the impact of trade reforms on the performance of foreign trade.

1.11.1 Sources of Data

For the purpose of evaluation, this study tapped secondary sources of data that has been drawn from various national and international sources.

- The international sources include World Trade Organization's publications (e.g. Trade Policy Reviews), the World Bank publications (e.g. World Economic Surveys, World Development Reports, and World Trade Indicators) and International Monetary Fund publications (e.g. International Financial Statistics).
• The national sources include the Government of India publications (e.g. Economic Survey), Reserve Bank of India’s publication (e.g. Annual Reports and Handbook of Statistics on Indian Economy), Directorate General of Commercial Intelligence and Statistics’ publication (e.g. Annual Reports), Centre for Monitoring Indian Economy’s publications under Economic Intelligence Services. Moreover, various specialized journals, related research work and internet search engines have been used.

1.11.2 Research Methods

The course of foreign trade policy reforms and collected data has been studied by dividing the whole period of study into two sub periods such as pre-reforms period and post-reforms period. The process of economic reforms including trade policy reforms were initiated in the country during the year 1991-92, therefore the period after that is taken as post-reforms period and the period since 1950-51 to 1991-92 is regarded as pre-reforms period. Throughout the study, the data has been presented in tabular form, in terms of absolute and percentage and with the help of graphs, charts etc.

Different statistical tools and techniques have been used for analyzing the data. Following three types of growth rate have been calculated:

(i) **Year to year growth rate** is measured by the formula as given in relation

Growth rate of variable (say y) in a period \( t = \frac{A}{B} \), Where

\[ A = \text{difference in the magnitude of the variable in period } t \text{ and } (t-1); \ B = \text{magnitude of the variable in period } (t-1). \]

(ii) **The linear growth rate** of the variable y can be determined from the specification i.e. \( y = a + bt \), where

\[ a = \text{constant term}; \ b = \text{coefficient of time or } \frac{dy}{dt}; \ t = \text{time variable} \]

In this case, the linear rate of growth of the variable y will be equal to

\[ (\frac{1}{y})(\frac{dy}{dt}) = (\frac{1}{y})b \]
The exponential trend in growth rate of the variable $y$ can be measured by using the relation, $y = (ab)^t$
or, $\log y_t = \log a + \log b_t + \log e_t$

To calculate the growth rate from this specification, we first have to estimate the relation in the above equation and then have to take antilog of the estimated value of $\log b$ and finally we have to subtract one from the resulting value. Ordinary least square (OLS) method has been used for the purpose of estimation the above two equations for these growth rates.

Instability indices and Concentration ratios have been calculated for the chapter wise and section wise commodity groups in India’s export basket. To understand the pattern of India’s foreign trade specialization, and to find whether or not the sector (in India) is globally competitive, the relative competitiveness of merchandise and service trade is reviewed with the help of the Revealed Comparative Advantage (RCA) of different merchandise and service trade sectors.

The RCA has been calculated based on following equation:

$$RCA = \frac{X_{iw}^k / X_{iw}^{\Sigma k}}{(X_w^k / X_w^{\Sigma k})},$$

where $X_{iw}^k$ is country $i$’s world exports of merchandise/services $k$; $X_{iw}^{\Sigma k}$ is country $i$’s total exports, $X_w^k$ is world exports of merchandise/services $k$; and $X_w^{\Sigma k}$ is world’s total exports. If the estimated RCA index of a sector is found to be greater than one, then it is considered as globally competitive (Balassa, 1965).

This index can be computed for commodities classified by product groups as well. However, a major limitation of this index is that at any point in time it takes into account only one side of the trade flows, i.e. exports or imports. Nonetheless, this index has been widely used to explain the export performance and similarity of trade patterns among the East Asian countries (for instance, see Chow, 1990 and Rana, 1990).

To explore the performance of India’s foreign trade the technique of slope dummy and intercept dummy has been employed (Gujarati, 2003). In order to
estimate growth of Indian exports and imports during the pre as well as post-reforms regime, we have fitted following regression model:

\[ \ln X = n_0 + n_1 t + n_2 D_1 + n_3 (D_1 \times t) + n_4 D_2 + n_5 (D_2 \times t) + u_i \ldots \]

Where, \( X \) is the export\import value, \( t \) is time trend, \( D_1 \) is the first dummy variable that try to capture the impact of trade reform measures on India’s exports, which takes value 0 for the period 1975-76 to 1990-91 and 1 for the period 1991-92 to 2009-10 and \( D_2 \) is the second dummy variable that attempts to capture the impact of WTO Arrangement of 1995 on India’s export which takes value 0 for the period 1991-92 to 1994-95 and 1 for the period 1995-96 to 2009-10 and \( u_i \) is the random disturbance term.

In the above regression equation, the growth in the period 1975-76 to 1990-91 will be measured by

\[ g_{yx\ 1975-90} = n_1 t \times 100 \ldots (1) \]

Also growth for the initial years of reform period is given by

\[ g_{yx\ 1991-95} = \left( n_1 t + n_3 (D_1 \times t) \right) \times 100 \ldots (2) \]

Similarly, growth for the period 1995-96 to 2009-10 is calculated from

\[ g_{yx\ 1995-2010} = \left( n_1 t + n_3 (D_1 \times t) + n_5 (D_2 \times t) \right) \times 100 \ldots (3) \]

The percentage export earnings as well as import outgoings from India to different countries have been calculated with a view to knowing the change in the direction of India’s trade basket. Added to this, the determinants of the remarkable export success and import growth of India during the post-reforms regime have also been explored empirically. Both domestic and external factors have been analyzed to clarify the issue. Statistical package E-Views 16 has been used for this purpose.

Various trade policy indicators such as tariff trade restrictiveness index or TTRI, percent share of tariff lines with domestic peaks, tariff restrictiveness quota usage in agricultural goods as a percentage, custom duties as a percentage of
goods imports, export license usage, export tax usage, the logistics performance index, rest of the world tariff measures, and market access tariff trade restrictiveness index or MA-TTRI has been used for illustrating the changes in India’s foreign trade policy during post-reforms scenario.

1.12 Limitations of the Study

Trade reforms are a part of external sector reforms in India. The external sector reforms are mainly of three types such as foreign trade reforms i.e. exports and imports in goods and services, foreign exchange reforms, reforms in the area of foreign investment. These three types of reforms in external sector are interrelated to each other. For instance, exchange rate reforms and reforms of foreign investment are complementary for trade sector reforms. Thus, it is quite difficult to take apart the impact of foreign trade reforms from the other external sector reforms. Further, external sector is only a part of overall national economy as the national economy may comprise several domestic sectors, such as industrial sector, financial sector, fiscal sector and public sector. These various sectors are both directly and indirectly related with the external sector and can not be easily separable from the external sector reforms in general and from foreign trade sector in particular (Narayana and Nataraj 2002). Thus, trade reforms and other external sector as well as domestic reforms are generally interrelated strongly. Therefore, the present study, though, focuses on foreign trade policy reforms yet attempt to capture the different aspects of external sector reforms.

Secondly, this study attempts to evaluate trends and patterns of total trade, its direction and its composition. However, an in-depth analysis of the trade basket of our important trading partners like USA, China, United Kingdom (UK), Japan and Germany has not been made. Added to this, individual commodities have not been separately analysed. The analysis has been done on commodity groups or on a section wise basis. Thirdly, the study is focused on trade reforms at the national level. Thus, no sub-national level reforms for promotion of foreign trade either directly or indirectly, are covered.
1.13 **Structure of the Study**

The present study is divided into seven chapters. A brief description of each chapter is as follows:

- **First chapter**, as illustrated above, provides an introduction of India’s trade liberalization movement and other related aspects. It also deals with the related periodical literature in order to provide justification for the present study and explains objectives, research methodology and limitation of the present study.

- **Chapter second** reviews the various phases of import policies and export policies of India during pre-reforms regime and evaluates the foreign trade performance of India in order to compare the changes came in India’s imports and exports profile with that of policy changes appeared in the pre-reforms regime.

- **Chapter third** highlights the major foreign trade policy developments that India has witnessed in the post-reform period. In particular, a detailed illustration of different Export and Import policy since 1991 is provided to identify the major reform measures.

- **Chapter four** presents an illustration about different lessons for India from East and Southeast Asian counties’ trade policy reforms experience. This chapter further discusses the trade policy commitments of India with World Trade Organization and India’s role in various negotiation procedures in an attempt to provide some direction to India regarding trade policy reforms. Added to this, it explores various regional and bilateral agreements of India that were initiated for liberalizing and opening trade with the rest of the world.

- **Chapter five** provides an examination of the overall trends of India’s export and import during post-reforms regime. This chapter also shows the analysis of trends and patterns of India’s service export and import.

- **Chapter six** explores the change in composition of merchandise trade for measuring the diversification in commodity trade and presents the
direction of merchandise trade to analyze the dynamism in trade direction. This chapter also evaluate empirically the performance of merchandise export and import of India.

➢ Chapter seven concludes the study by showing the observations and provides policy implications regarding trade policy reforms for the future growth of India’s foreign trade in long-term perspective.

1.14 References


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