CHAPTER THREE

POLICY FRAMEWORK

SINCE

INDEPENDENCE

This chapter presents foreign trade policy of India in two phases - pre 1991and post 1991. To accelerate growth process India followed the policy of import substitution and export promotion in pre 1991 phase but post economic reforms period (1991) India adopted the policy of market oriented and product diversification to accelerate trade (exports & import). This chapter also examines the technology policy, foreign direct investment policy and industrial policy of India. India started pursuing the path of planned economic development scheme post independence. Since then more than six decades have passed and there have been substantial changes in India's commercial policies. A brief discussion of these policies is as follows;

3.1 Foreign Trade Policy:

3.1.1 Introduction of Trade Policy

The analysis of foreign trade policies or trade policy as it is related to trade liberalization has received a significant attention in the recent literature on international trade. Foreign trade policy alternatively known as Export-Import (EXIM) policy refers to policies adopted by a country with reference to export and imports. In general, trade policy can be Protective trade policy or free trade policy. Protection is a policy of restriction of international trade, with the aim of preventing unemployment or capital losses in industries threatened by imports, promoting particular types of industrial development, affecting the internal distribution of income, or improving a country's terms of trade by exploiting its international monopoly power. A protective trade policy pursued by a country seeks to maintain a system of trade restrictions with the objective of protecting the domestic economy from the competition of foreign products. Protective trade policy constituted an important plank in the commercial policies of underdeveloped countries during the 50s, 60s, and 70s and to some extent in the 80s. Many of the underdeveloped countries continue to have protective trade policies even today. And a free trade policy is one which does not impose any restriction on the exchange of goods and services between different countries. According to Bhagwati, free trade policy is "absence of tariffs, quotas, exchange restrictions, taxes and subsidies on production, factor use and consumption[90].

On the other hand, foreign trade policy may be characterized as inward or outward looking. An inward looking foreign trade policy stresses the need for a country to evolve its own style of development and to be the master of its own fate, with restrictions on the movement of goods, services and people in and out of the country. An inward looking foreign trade policy encourages the development of indigenous technologies appropriate to a country's resource endowment. An outward looking foreign trade policy encourages not only trade but also the free movement of capital, labours, enterprises and students a welcome to the multinational enterprises, and an open system of communications like as 'economic union'. Foreign trade policy is an important economic instrument which can be used by a country, with suitable modifications from year to year, to achieve its long- term goals.

3.2 India's Trade Policy:

3.2.1 Pre-Independence

After independence India adopted trade policy of the colonial era for decades[91]. Later India's trade policy was driven by perceived foreign exchange scarcities and the desire to ensure that scarce foreign exchange is used only for significance purpose of economic development. Industrialization and self-availability in important goods were the important objectives of India's trade policy.

3.2.2 Pre-Reform Trade Policy (1991)

The trade policy of India in the immediate post-independence period was liberal and was to meet the demand released by Second World War. However, this import policy soon resulted in a heavy deficit in balance of trade and government had to impose restrictions on imports from hard currency area. The trade policies were modified from time to time while India moved ahead (from 1st five year plan onwards).

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90. Bhagwati, J. (1986), International trade, P.10
91. Mathur, Vibha, (2006) 'Foreign Trade of India 1947-2007': Trends, Policies and Prospects, New Delhi: New Century Pub.

India introduced the first five-year plan in the 1951-56, in this plan period there was disequilibrium in the balance of payment of Rs.5877 million due to increase in import bill over export earnings. During this period, there was no clear foreign trade policy and import restrictions of any kind were not in use. In the second five-year plan (1956-61) heavy industries were established to achieve which target. The rapid rise in imports put pressure on India's balance of payments (Rs.18360 million).The Government of India imposed quantitative restrictions on selective goods and government allowed imports to particular industries through import licenses. Import substitution was stimulated while exports were not considered a line of activity to be stimulated. In the third five-year plan (1961–66) government continued quantitative restrictions on imports and actions were taken to boost exports by creating a favorable atmosphere for export industries, diversification of their markets and the development of export support services. In this period, import increased further accentuating balance of payment problem (Rs.24146 million deficits). During 1966-75 India's economy faced many challenges. The government addressed these problems by taking policy steps like devaluation of rupee, bank nationalization & enacting, monopoly & restriction on trade and practice (MRTP), foreign exchange regulation act (FERA) etc. Rupee was devalued (vis-à-vis US $) in June 1966, to systematize and rationalize the export incentive system. During this period, export subsidies were decreasing, export duties imposed, and import duties were reducing. The net devaluation after allowing for these changes was, on an average, less than the gross devaluation of 57.5 percent and varied among commodities[92, 93, & 94]. According to Bhagwati and Srinivasan the total net devaluation on the trade account was 21.6 percent for exports and 42.3 percent for imports. Consequently, the net effect was a further stimulation of import substitution over export production.

During this period 1975-85, India's Import allocation rules were made simpler. Protective quotas, however, remained intact and domestic industry continued to be

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92. Singh, M., (1964), India's Export Trends and the Prospects for Self sustained Growth, Oxford: Clarendon Press.
93. Bhagwati, J.; Srinivasan, T.N., (1975), Foreign Trade Regimes and Economic Development: India, New York: Columbia University Press
94. Veeramani, C., (2007), Sources of India's Exports Growth in Pre and Post Reform Periods, Economic and Political Weekly, July 23-30, P. 2419 – 2427.

completely shielded from competition, like as closed economy. In April 1985, the government announced new Export-Import policy for a period of three years. The objectives of policies (liberalization reached to privatization and globalization) were to bring some stability to the policy and thereby reduce the uncertainty about year to year changes that exports and imports faced. Although the stringency of the import regime did not dilute substantially, the two three-year policies (1985-88 and 1988-91), did represent some major simplifications. Due to unforeseen political changes, the second policy was terminated one year earlier and the third policy, covering the period, April 1, 1990 to March 31, 1993, was announced by government of India, on March 30, 1990.

3.2.3 New Economic Policy (1991)

India continued to face balance of payment crisis in mid 80s and early 90s. The government responded to the crisis by introducing economic reforms in the country. Reforms were introduced in all major sectors like Industrial sector, financial sector, External sector and Fiscal sector. The Economic reform comprised wide ranging changes in trade policies, a part from industrial policies. These policy changes aimed at strengthening export incentives, eliminating a substantial volume of import licensing and optimal import compression. Essential imports of sensitive item (such as POL and fertilizers) were fully protected, but other imports of raw materials and components were linked to export performance through enlargement and restructuring of replenishment licensing system. Main features of trade policies (trade reforms) are as follows:

(a) Reforms in import licensing system or Quantitative restriction.

(b) Reforms in Tariff Structure.

(c) Decimalizations of Public Sector Trading Agencies. And

(d) Devaluation and Convertibility of Rupee on Current Account.

On the other hand, India has also used the trade policy to make export more competitive as well as profitable. For this purpose trade policy provides for special schemes like Export Promotion Capital goods Scheme **(EPCG)**, Market Access Scheme **(MAI)**, Exports Oriented Units **(EOU)**, Export Processing Zones **(EPZs)** was replaced by Special Economic Zones **(SEZs),** Focus Market Scheme **(FMS),** Focus Product Scheme **(FPS)**, Agriculture Export Zones **(AEZs))** etc and Foreign Exchange Regulation Act **(FERA)** was replaced by Foreign Exchange management Act **(FEMA)** [95].

India now (1991) follows a five-year trade policy, though some fine–tuning of policies is made annually, depending on the evolving trading conditions and industry's felt need, in regard to regulation and liberalization of import and promotion & liberalization of exports. The trade policies were modified from time to time while India's new foreign trade policy continues since 1992.

3.3 Briefly explain of India's foreign trade policies

Foreign trade policy was known as EXIM policy. The policy period usually covers five years. The Government of India announced first five year export-import policy (EXIM policy) on 31st March 1992-97. After first five year export-import policy government announced 1997-2002, 2002-2007, 2004-2009, and 2009-2014.

The new five-year Export-Import Policy (1992-97) was introduced with effect from April 1992 and was in sync (synchronization) with the Eight Five Year Plan (1992-1997). For the first time, the policy was given an export bias. Earlier this policy was known as Import-Export policy, the new policy was titled Export-Import policy (EXIM Policy). 1992-97 policy, after the liberalization of the Indian economy, aimed at removing the regulatory and protectionist policy and moving towards a global economy. This gave a further push to liberalization by freely allowing imports of all items except a negative list, decancelising a large number of raw materials and further liberalizing imports of capital goods against exports obligation. Second EXIM Policy (1997-2002) came into force with effect from 1st April, 1997 and was in sync (synchronization) with ninth plan period. The policy carried further the process of trade liberalization. The new EXIM policy has cut down the list of quantitative restrictions on imports simplified procedures, reduced multiplicity of schemes, provided special incentives for agro and allied sectors and encouraged domestic sourcing in inputs. Next Export-Import Policy was announced for the period 2002-2007, and was in sync (synchronization) with the Tenth Five Year Plan. 2002-2007 policy aimed at simplification of process and procedures of

95. Malik, J.K., (2005), India's Exports- Policy defeating Exchange Rate Arithmetic, Economic and Political Weekly, Dec 24-31, 2005, P. 5486 – 5496.

exports and imports with special emphasis on exports. Doubling of international trade was the objective of foreign trade policy of 2004-2009.Foreign trade policy of 2009-14 had two main objectives, (1) To double our percentage share of global merchandize trade within 5 years, (2) Use trade expansion as an effective instrument of economic growth and employment generation. Focus Market scheme (FMS), Focus Product Scheme (FPS), Market Linked Focus Product Scheme (MLFPS), Agri Infrastructure Incentive Scrips and Vishesh Krishi and Gram Udyog Yojana (VKGUY) have been added under FTP 2009-14[96].

3.4 The Impact of Foreign Trade Policies (EXIM Policies) on Indian Economy

3.4.1 Globalization of Indian Economy

The EXIM Policies proposed with an aim to prepare a framework for globalizations of Indian economy. This is evident from the very first objective of the policy, which states, "To accelerate the economy from low level of economic activities to- high level of economic activities by making it a globally oriented vibrant economy and to derive maximum benefits from expanding global market opportunities"[97]. To insulate Indian exports from the decline in demand from developed countries, in this Policy (Focus Market Scheme) focus is on diversification of Indian exports to other markets, especially Latin America, Africa, parts of Asia and Oceania. To achieve globalization and diversification of Indian exports, following initiatives have been taken under this Policy. (a) Many countries have been included within the ambit of Focus Market Scheme. (b) The incentives provided under Focus Market Scheme have been increased from 2.5% to 3%. (c) There has been a significant increase in the outlay under 'Market Linked Focus Product Scheme' by inclusion of more markets and products. This ensures support for exports to all countries in Africa and Latin America. In the last ten years our exports witnessed robust growth to reach a level of US$ 466 billion in 2013-14 from US$ 63 billion in 2003-04. The share of India's exports in World's exports 0.52 percent in 1990-91 to 2.0 percent in 2013-14.

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96. Government of India, publications 'Export-Import policies 1992-97, 1997-2002, 2004-2009, 2009-2014' Handbook of procedures.
97. Ibid.

3.4.2 Impact on the Indian Industry

In the EXIM policies a series of reforms measures have been introduced in order to give boost to India's industrial growth and generate employment opportunities in nonagricultural sector[98]. Nearly 14 million jobs were created directly or indirectly as a result of augmented exports in 2003 to 2008. These include the reduction of duty from 15% to 10% under EPCG scheme that enables Indian firms to import capital goods and is an important step in improving the quality and productivity of the Indian industry. Liberalization of EPCG scheme would help Indian industries to promote. Quality up gradation and would also enable sick units to revive. License, certificate, permissions and customs clearances for both imports and exports on self declaration basis, priority finance for medium and long term capital requirement and 100% retention of foreign exchange in Exchange Earner's Foreign Currency (EEFC) account would definitely benefit Indian industries and would encourage Indian producers to enter the export field. The export oriented unit (EOU) and export promotion zone (EPZ) schemes were liberalized. 100 per cent foreign equity participation in EOU/ EPZ units was allowed Ministry of Commerce.

3.4.3 Impact on Agriculture

Agriculture being the backbone of Indian economy, many encouraging steps has been taken in the EXIM Policies in order to give a boost to Indian agricultural sector, especially for promotion of exports from agricultural sector [99]. "To reduce transaction and handing cost a single window system to facilitate export of perishable agricultural produce has been introduced. The system has involved creation of multi – functional nodal agencies to be accredited by APEDA". These steps includes provision of additional SIL of 1 % for export of agro products, allowing EOU's and other units in EPZs in agriculture sectors to 50% of their output in the domestic tariff area (DTA) on payment of duty. Removal of quantitative and packaging restrictions on certain agricultural products and on export of all cultivated varieties of seed would give a major boost to the export of these items. Identification of 20 Agricultural Export Zones would help in development of

98. Dr. Mane Vinod, (2013), "Impact of Various EXIM Policies on Indian Economy" Asian Journal of Multidisciplinary Studies Volume1, Issue.1, August 2013, P. 2
99. Ibid. P.5

specific geographical areas for export of specific products. Other measures such as transport subsidy, 3% special DEPB rate, would definitely give a fillip to exports from agricultural sector.

3.4.4 Impact on Foreign Investment

In order to encourage foreign investment in India, the EXIM Policies has permitted 100% foreign equity participation in the case of 100% EOUs, and units set up in EPZs. As part of the economic liberalization in 1991, the government of India implemented industrial policy to decide the flow of FDI in many sectors. Hence, the government has opened the door of FDI under government route as well as automatic route. As results, the flow of FDI has been increasing since 1991 in many sectors. The total FDI inflows in India during 1991–2012 amounted to US$ 187682 million.

3.4.5 Removal of quantitative restrictions (QRs)

One of the important aspects of India's EXIM policies has been the gradual removal of quantitative restrictions **(**QRs). Under the WTO agreement, every member country is required to remove QRs, except in case of poor BOP situation. In May 1997, India had 2714 imports items on which QRs existed which were phased out by 1 April 2001. Thus the removal of QRs merely affects a specific list of consumer goods. As a result of the EXIM policies, exports have vigorously responded to the removal of protective measures. Domestic industry has been encouraged by expanded availability of imported inputs and capital goods and to meet the challenge of competing in the international market[100].

3.4.6 Impact on foreign exchange reserves

During the period 1991-1992 India was facing the problem of acute shortage of foreign exchange. This led to the opening up of our economy and the EXIM policy of 1992-97 enabled India to come out of the problem. The present level of foreign exchange reserve is sufficient to cover about 10 month imports payments[101].

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100. Jhigan.M.L,(2012), 'International economics' vrinda pub., P. 526
101. www.sib.co.in

3.4.7 Impact on Self-Reliance

The EXIM policies successfully fulfill one of the India's long terms objective of self-reliance[102]. The EXIM policies have achieved this by encouraging domestic sourcing of raw materials, in order to build up a strong domestic production base. New incentives added in the EXIM Policies have also added benefits to the exporters.

3.5 Technology Policy

The role of technology in economic development is many folds; it helps achieve competitive advantage over others to produce commodities at the lowest cost, maintaining the given quality. Secondly, it helps generate employment by developing new areas of production and distribution. Thirdly, it also develops infrastructure and increases access to global resources by all sections of people. A part from large –scale use of capital, highly sophisticated technology has played a crucial role in the recent development of Western Europe, America and Japan. Developing nations like India which embarked on a programme of reconstructing its economy after independence had the choice between emphasizing on indigenous technology–development and importing technology from the developed countries. Foreign technology can come in several forms. It can come as direct foreign investment in a subsidiary of foreign company. It can come in the form of collaboration with a domestic firm. It can come in the form of purchase of technology know–how, finally domestic personnel can be trained abroad to absorb foreign technology. Since, technology is continuously passing through the process of evolution, will be permitted to a limited extent even in areas where the country possesses know–how.

3.5.1 Objectives of Technology Policy

The corner stone of technology policy is said to be the technology self-reliance. This does not mean self-sufficing. Rather, it seems to imply that while import to latest technology will be permitted there will be compulsion to absorb and adopt technology so that the need for imported materials, equipment and technical services does not extend beyond a

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102. Op.cit, P.6

limited period. Appropriateness of the imported technology has been stressed on the premise that foreign technology unless suitably adapted are not appropriate for our factor endowments abundance of labor and scarcity of capital. In the initial years of development the concern of policy planners was largely with the cost of imported technology and what is called unpacking. A Technology package consists of product or process know–how, equipment, materials and technical personnel.

In India substantial amount of effort has been expended in bolstering the domestic research and development activity in academic institutions and government research laboratories, while considerable success has been achieved in some areas like agricultural research, performance in industrial technology development has not been up to the mark. As far as possible, Indian technical and consultancy services should be utilized in implementing the project. As part of the new Industrial policy 1991, announced by the government, there are some policy changes with regard to foreign investment and import of technology.

3.6 Foreign Direct Investment Policy

In case of India, starting with the absence of foreign investment industrialization model of the early years, on the other hand, foreign investment had played a very limited role in India's economy prior to 1991. The Government of India has embarked on a number of initiatives towards making FDI in India attractive. As part of the economic liberalization in 1991, the Government of India implemented industrial policy to decide the flow of FDI in many sectors. As a result the flow of FDI has been increasing since 1991 in many sectors. The new policy welcomes foreign investment with its advantages for technology transfer, marketing expertise, introduction of modern managerial techniques in the country and export promotion. These changes have made the technology policy more flexible and outward looking. Now FERA has been replaced by a FEMA.

3.7 Industrial Policy

Industrialization & industrial revolution are indicators and engine of economic development. The Industrial policy in India has come a long way from exclusive government and state control in 1948. The industrial policy of a country is probably the most important official source of information to understand the nature of the relationship between government and industry. The industrial policies in the past were based on the Nehruvian model of economy, which was socialistic in its approach, thus laying more emphasis on the development of the public sector.

India launched its market-oriented industrial reforms in 1991 and is now well on its path of integrating its economy with the global economy. The new policy has placed India on the road to market and free economy. The government of India has launched new economic policy to improve the socio- economic conditions of the people as well as attract multinational companies to invest in India. Therefore, in 1991, the Government of India removed License, Permit and Quotas (LPQs) regime and implemented Liberalization, Privatization and Globalization (LPG) to attract private and foreign investors.

3.8 Target of Economic Reform

The main target of economic reform is to bring about rapid and sustained improvement is the quality of life of the people of India. Central to this goal is the rapid growth in incomes and productive employment. Such growth requires investment in farms, in road, in irrigation, in industry, in power and above all, in people, and this investment must be productive. Successful and sustained development depends on continuing increases in the productivity of our capital, our land, and our labour. Investment in people and capital is necessary, but not enough for rapid productivity growth. We must also foster an environmemt which encourages full utilization of our material and human resources and ensures that they are deployed in the most productive manner.

The target of our economic reforms is to improve the living standards of all of our people, not just the rich and privileged. Reforms will be difficult and will take several years but the alternative of continuing widespread poverty, unemployment, illiteracy, disease, malnutrition, rising inflation and stagnant production. If exists on this earth as only economic reform.

3.9 India's Experiment in Privatization

The term Disinvestment is the opposite of the term Investment. Disinvestment is called as Partial Privatization or a part of privatization. Disinvestment is the sale of equity holdings and reducing capital stock held by the Government in Public Sector undertaking Enterprise (PSU). In simple words, Disinvestment is the process of reducing the capital stock. The first attempt in the direction of disinvestment was made by the Government of India in the financial year 1991-92. The Government of India sold equity shares of Public Sector Undertaking (PSU) mainly to public sector mutual funds. The main objective of this policy has to improve the fiscal deficit, social sector development (education and health) & managerial efficient development of PSU.

Disinvestment policy is continue year to year since 1991 and modified time to time. Strategic sale policy was introduced in 1999, it continued till 2004. Strategic sale policy has been replaced by Initial Public Offer (IPO) policy. As results, the disinvestment income has been increasing since 1991. The total disinvestment income receipts in India during 1991–2013 amounted to Rs 219207 crore[103].

3.10 Trends of Foreign Trade of India

The trends of India's trade also show that India has found new trading partners after 1991. Before independence UK was the main partner of India accounting for 34 percent of India's exports and 30 percent of India's imports. The diversification of certain industries along with specialization in certain goods has helped India to secure new markets for her products. Besides UK, the other countries of importance are USA, Japan, Russia, West Germany, and member of the OPEC. India has also made substantial inroads into the markets of East and South East Asia [Look East policy (LEP)]. Now present time India has tried to diversify its trade. According to the Department of Commerce, the fifteen largest trading partners of India represent 60% of total trade by India. The largest Indian partners with their total trade (only trade in goods) in financial year 2012–2013 are as follows: UAE, China, United States, Saudi Arabia, Switzerland,

103. Prof. S.N. Lal & S.K. lal (2015), "Indian economy survey and analysis" Shivam publishers, Allahabad, P. 7.31-32.

Singapore, Germany, Hong Kong, Indonesia, Iraq, Japan, Belgium, Kuwait, Iran, and South Korea etc.

3.11 Present foreign economic strategy of India

India launched its “Look East Policy” in 1991 and India has signed Free Trade Agreement **(FTAs** with many countries like Sri Lanka, Nepal, Bhutan, Thailand, New Zealand)**,** Regional Trade Agreements **(RTAs** with ASEAN, SAARC, SAFTA IBSA, BRICS, BASIC etc.**)** and Comprehensive Economic Cooperation / partnership Agreement **(CECA or CEPA)** with many countries like Singapore, South Korea, Malaysia, Japan and Canada with a view to protect foreign trade. India has already concluded bilateral investment protection agreements in the form of Double Taxation Avoidance Agreement **(DTAA)** with 83 countries.

Conclusion

After independence India followed policy of import substitution to make rapid growth in industrilisation. Foreign trade policy suitable for pursuing this strategy was put in place. Obviously, this was restrictive trade policy. Gradually changes were brought about in trade policies and complete overhaul was made in 1991. Indian economy leading to a process of integration of an economy links the rest of the world. Policy of import substitution was replaced by export led growth. India now follows a five-year trade policy, though some fine–tuning of policies is made annually, depending on the evolving trading conditions and industry felt need, in regard to regulation & liberalization of import and promotion & liberalization of exports. Policy modification was carried out as per new priorities and goals.