CHAPTER 1
INTRODUCTION
Introduction:

India is a country of vast resources, but it remains very poor. Why is this? History shows that embracing the global economy is integral to economic development. Scan the list of the world’s most successful developing countries over the past 25 years—China, Chile, Egypt, Mexico, the Philippines, Poland and South Korea. Encouraging trade and foreign investment has been a central element of the successful reform programs in each of these transition countries. On the other extreme, countries that have resisted globalization have generally lagged there more open neighbours—for example, Burma, the Ukraine, Venezuela, Zimbabwe… and India. (Kennedy Robert E, 2002)

The mammoth spurt in the international trading activity and the ensuing benefits needs to be comprehended. At the beginning of the new century, the value of global trade in goods and services stood at nearly U.S. dollar 8 trillion (thousand billion), about 25 percent of the world Gross Domestic Product (GDP). This is a dramatic increase over the past 30 years; in 1970, total trade of goods and services were just U.S. dollars 1.5 trillion in current dollars, and made up about 13 percent of GDP. Today, at just over U.S. dollars 6 trillion, trade in goods accounts for the lion’s share of global flows, forward trading commercial services, which represents another U.S. dollar 1.5 trillion. Although global trade flows are dominated by exchanges within and between Europe, North America, and East Asia—which currently make up 65 percent of world trade—trade flows involving developing countries have expanded significantly. Developing countries have also increasingly become producers and traders of manufacturers. The share of manufacturers in total exports of developing countries reached 70 percent in 1990s and is projected to rise to 80 percent in 2005. Moreover, around 40 percent of all developing country exports are destined for other developing countries—South-South trade is increasingly important. ……. The experience of many countries in recent years shows a strong positive relationship between openness to trade and income growth, raising the living standards for poor as well as rich people. …….. (Stern Nicholas, 2002)

Thus its high time that a serious look is given to a sincere and continued integration with the global economy as the wondrous benefits can no more be ignored by India for petty reasons. Its prudence and nothing more to talk of sincere integration as….. Among major developing countries, India ranks very low on most measures of globalization. Three common measures are the trade-to-GDP, the FDI-to-GDP ratio, and per capita FDI. The following table reports these measures for a sample of large developing countries that have undertaken programs of economic liberalization.
Table 1.1

Measures of Globalization (2001)

<table>
<thead>
<tr>
<th></th>
<th>Trade/GDP</th>
<th>Inbound FDI/GDP</th>
<th>FDI/Person($)</th>
<th>Per Capita GDP($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>India</td>
<td>24%</td>
<td>0.5%</td>
<td>2.24%</td>
<td>449</td>
</tr>
<tr>
<td>Egypt</td>
<td>41%</td>
<td>1.2%</td>
<td>17.00</td>
<td>1,216</td>
</tr>
<tr>
<td>China</td>
<td>41%</td>
<td>4.0%</td>
<td>30.87%</td>
<td>915</td>
</tr>
<tr>
<td>Mexico</td>
<td>63%</td>
<td>2.5%</td>
<td>121.42</td>
<td>7,068</td>
</tr>
<tr>
<td>Poland</td>
<td>61%</td>
<td>4.9 %</td>
<td>188.10</td>
<td>4,553</td>
</tr>
<tr>
<td>Non India average</td>
<td>51.5%</td>
<td>3.2%</td>
<td>89.35</td>
<td>3,438</td>
</tr>
</tbody>
</table>


Notice that every country is significantly more exposed to international trade and capital flows than is India, and each is much wealthier. Of the group, China and Egypt have the least trade exposure. But both are still about 70 percent higher than India. Similarly, other large countries receive significantly more inbound FDI than does India. Measured as a percentage of GDP, the countries average more than six times India’s FDI inflows. Measured on a per person basis, the multiple is nearly 40. Imagine how Indian living standards would increase if annual FDI inflows rose from only U.S.$2.24 to U.S.$ 90 per person. Many factors beyond trade influence a country’s standard of living, including history, natural endowments and proximity to developed country markets. But experience and numerous academic studies indicate that openness to international trade and investment flows are critical ingredients for development. Raising political and procedural objections cannot erase if India is a country of Boston resources the unpleasant fact that, among large developing countries, India ranks near the bottom on measures of global openness .... and on income per person. Reluctance to embrace the global economy is not the whole story, but it is an important element of the story. It needs to be in the minds of the policy makers that ....Engagement in international trade and investment is integral to development because it increases the productivity of local resources, which invariably leads to higher wages and living standards. Free trade encourages a country to focus on those things to it does relatively well, and the stumbling things and it does relatively poorly (economists refer to this as comparative advantage). Most developing countries have lots of workers, but are deficient in capital, infrastructure and the capacity to produce sophisticated products. Developing countries are thus better off when they import capital and sophisticated products (e.g. airplanes, telecommunication equipment) and pay for them with exports of labor-intensive goods and services. Trade thus causes a shift from activities in which a country is comparatively less efficient to those in which it is comparatively more efficient. Trade has a
second important benefit. It increases the range and quality of options available to local consumers and forces local producers to improve their offerings in order to compete. This pressure is inconvenient for local producers but it makes consumers much better off. Countries that have lowered their tariff barriers and increase the intensity of competition in the local market often see rapid improvements in productivity, as local producers rush to upgrade their products and processes.

(Further), nearly all academic studies indicate that recipient countries realize many and varied benefits from FDI. (Kennedy, Robert E, 2002).

India has witnessed the gains so far from the international trade alignment. The need is to emphasize the continuance of the reform drive with all solemn intentions translated into deeds. Although the process started with an economic compulsion in the decade of 1990s but as of now ample positive results have started flowing in. The benefits of international trade, thus, can now be reckoned. It can essentially be realized that … A driving contributor to India’s growth over the last decade has been its increased participation in global markets, both as a buyer and as a seller. Trade liberalization during the 1990s resulted in productivity gains associate with increased competition, innovation, and acquisition of new knowledge and technologies, all of which have contributed to raising living standards in the country. The gains from trade are apparent in India’s economic performance in the recent period of greater openness…. The average growth rate in the ten-year period since India initiated an intensification of the process of the reforms from 1991 has been around six percent, making India one of the fastest growing developing countries in the 1990s. Furthermore, several studies document a significant decline in poverty in this reform period of at least one percentage point per year in terms of the fraction of the population living below a dollar a day. (Stern Nicholas, 2002)

The Outpacing Dragon and the Sleeping Giant:

Attention now needs to be turned to the reasons that were behind the marvelous growth of China and why India though being a dormant tiger could never catch it. This has important bearing on the analysis of the growth factors that India needs to imbibe.

While India’s export growth since 1970s has been rapid compared to the earlier two decades, it is still far too slow in comparison to that of China. A drop could be seen in the ratio of India’s exports to China for the period 1958-1993. At one time, from 1968-1972, the Indian exports were at least as large as the Chinese exports. By the end of the 1970s, despite a
very high export growth India, Chinese exports were double the level of India’s. Since then, the Chinese exports have far outpaced India’s export growth. The fast growth of exports displayed by the Asian NIEs throughout the period 1970-1990 made India to lose its share in world exports from 1 percent in 1970 to 0.5 percent in 1990. The gap between the growth performance in India and China was created with India’s a exports of 18 million U.S. dollars in 1990 has compared to China’s 62 billion U.S. dollars. The reason was that India did not learn from the concept of strategically managed trade which was successfully followed by several exporting East Asian (including China and South Korea) and Southeast Asian countries. These countries followed export oriented industries in a more open economy policy regime generally lowering tariffs and non-tariff barriers over time and encouraging inflows of foreign direct investment (FDI) into export oriented industries and into special exports zones and technological Parks based on the advantage of their cheaper labor into the areas of the international competitiveness advantage. India did not think of the orienting its policies in those directions until 1991. (Bhide Shashankha and Chadha Rajesh, 1997)

A Look Back Since 1947:

Tracing the years that have gone by, since 1947 India has been displaying more or less this pattern on its external front. At the time of gaining independence in 1947, India inherited a colonial pattern of foreign trade tied to the former “mother country” namely the United Kingdom. The Indian exports in 1947 were 2.5 percent of the world exports. Nearly 50 percent of the India’s exports where then absorbed by the western developed countries notably UK and USA. Although being a founding member of the general agreement on tariffs and trade (GATT) yet India implemented protectionist measures to reduce foreign competition between 1947 and 1951. It was the self-sufficiency that was emphasized by the government of India over the foreign trade. The import controls and the tariff policy between 1952-1960 where such which stimulated the production of import-substitution goods by local manufacturers. Coupled with this the government of the independent India imposed strict controls on exports. The policy framework chosen by the Indian planners since 1956 was a development strategy of import substitution led by a planned industrialization of the economy. The Indian planners in the 1950s and 1960s believed in the then prevailing theories and empirics of “export pessimism”. Thus, very little scope was seen for increasing India’s exports in the short- and medium-term. An inward looking development strategy based on import substitution at any cost was then seen and adopted as the only meaningful development strategy. The race to industrialize the economy in the
shortest possible time based on the self-reliant development of heavy necessitated huge import bills that outpaced the exports. The *forex crisis* erupted in 1957 and the second gripped the economy in 1966-67. The 1957 crisis brought out the need to promote the exports of non-traditional manufactured goods. Hence for the first time export promotional measures were announced in 1957.

It needs to be noted that during 1960s India's share of world trade shrunk drastically as the country got isolated from the international market. The government-owned industries faced little competition or pressure to maintain efficiency and as a result the Indian exports competed on the basis of price rather than quality. Thus, during the 1960s the building up of high tariff walls and quantitative restrictions combined with strict exchange controls and overvalued rupee made India a *'high cost economy'*. The balance of payments crisis of 1966-67 saw the devaluation of the rupee by nearly 38 percent. The decision to devalue the rupee was ill-timed as it was preceded by an acute drought in 1965 and an industrial recession that created a supply side bottleneck. Hence, the Indian economy could register a relatively slower growth of exports during the post-devaluation period (1966-70).

During 1970s the rising oil prices and the subsequent balance of payment difficulties prompted to India to promote its exports. Still the country's exports could not gain much strength as the government's policy was of reserving the manufacture of most labor-intensive, low-tech products for the small scale sector to promote employment. The tiny producers could not compete with titanic international players. Anyhow, the exports grew at an average annual compound growth rate of 15.6% (US dollar terms) during 1970-1980 which was much higher than the 4.3% rate of growth in the previous decade.

In the start of the 1980s India's share in the world trade fell down to 0.4 percent. The exports were financing 60 percent of the imports. It was in 1984 that the then Rajiv Gandhi Government went in to have a relook at the export promotion measures to boost the export growth of the country. The Committee on Trade Policies chaired by Dr. Abid Hussain submitted its report in the year 1984. This committee had clearly the recommended additional liberalization of imports of capital goods and technology as an effective tool for modernization and technological upgradation of Indian export industries for improving their international competitiveness in fiercely competitive global markets. The government accepted this major recommendation of the Abid Hussain Committee Report. The emphasis in all announcements of export and import policies and changes there in during the
remaining decade of the 80s distinctly shifted to import liberalization for export promotion. It was during 1985-1988 that the first ever long-term (with three years validity) export-import policy was announced by the government to meet the persistent demands of Indian exporting and importing communities for the formulation and implementation of a stable long-term export-import policy. This was expected to help the export units to plan better for their future export marketing operations. Thus, during 1985-1989 the beginnings of trade liberalization were visible. The widening of the investment opportunities for the private sector, reduction in tax rates and import deficits being financed through commercial borrowings were some of the characteristics of a somewhat liberalized trade regime. But still it needs to be confessed that the profligate fiscal policy during 1980s contributed to a fiscal deficit amounting to 10% of GDP and a current account deficit of 3% of GDP in 1987-88. The trade regime in this period was among the most restrictive in the non-socialist world. The throes of forex crisis in which India found itself in 1991 was, thus, a result of the financial mismanagement of the 1980s. (S. Go Delfin and Mitra Pradeep, 1998)

The period since 1991:

India faced the greatest balance of payments crisis in its history in 1990-91. Foreign exchange reserves in June, 1991 had dwindled to a dangerously low level which could barely cover two weeks of imports. With large outflows taking place on capitol and found, as the economic survey, 1997 had pointed out, India was close to defaulting on external payments obligations in 1990-91. India turned this crisis into an opportunity. It responded by taking a near U-Turn its policies based on a relatively closed economy. it a launched a more open economic and market driven and private sector led economic reforms in June, 1991 under the new government led by Mr. P.V. Narasimha Rao as the prime minister and Dr. Manmohan Singh as the finance minister. The reforms have been on-going and have covered both areas of macroeconomic policy reforms and structural economic reforms. The structural economic reforms have dominantly covered both areas of sectors like trade and industry and have used instruments like tariffs and exchange rate for effecting changes.

The anti-export policy biases of the million measures taken by the government policies of the last 40 years were fully recognized in the post-1991 period. Thus, sustaining the growth of India’s exports at an adequately high level was incorporated as an integral element of the new economic policy. Such a growth of exports was considered by the government as being vital for the ultimate success of India’s post-1991 economic reforms.
CHAPTER 1:
INTRODUCTION

Many major measures taken by the government to impart a new meaning and urgency to the national export promotion policies the post-1991 period. These included the exchange rate management, reduction of tariff and non-tariff barriers, the regular major export incentives (e.g. duty exemptions scheme, EPCG etc.), monitoring review and reformulation of overall and sector-specific export promotion policies by the ministry of commerce, temporary reversal of the easy money and credit policies by the RBI and the WTO-related export issues and India’s strategic response to them.

Indian exports after 1991 registered an annual growth rate (in dollar terms) of 10.7 percent in 1992; 10.2 percent in 1993; 16.3 percent in 1994 and 22.4 percent in 1995. The deceleration in the growth of exports (in dollar terms) had started since 1996. In 1996 the registered a growth rate of 7.4 percent in dollar terms. As a result of the growth in exports during 1993 to 1996 the exports accounted for 8% share of the GDP by the end of 1996 (up from 5% in 1990). Exports also financed as much as 95.4 percent of the imports in 1993-1994 (compared to 75.4 percent in the crisis year of 1990-91). The new also marginally improved its share in global exports to 0.6 percent in 1995-96. On the whole, despite good progress made during the 1993-96 period on the export front by previous Indian standards, Indian exports were not yet sufficiently competitive. On the external front, three main factors need to be mentioned which happened to be the principal reasons for the poor export performance of India since 1996. First, the western developed countries continued to practice and to intensify newer forms of neo-protectionist policies. Secondly, there has been a clear the deceleration in the growth of world’s exports in 1996 (and just 3.5 percent in dollar terms compared to 19.7 percent growth in 1995). Almost all major Asian six will exporting countries had experienced big falls in the growth rate of their exports (in dollar terms) in 1996 going by the data provided in the IMF’s international financial statistics. For example, China’s annual growth rate of exports fell sharply from 22.9 percent in 1995 to just 1.6 percent in 1996; Malaysia’s from 26 percent to 0.3 percent in the corresponding period. Thirdly the major setback to India’s exports since August, 1997 has come in the form of major currency depreciations against the U.S. dollars in east Asia and southeast Asia since June, 1997. This has led to a noticeable rise in the real effective exchange rate of the rupee and distinct erosion of international competitiveness of India’s exports since mid-1996.

On the internal front the supply side bottlenecks were there. The initial push to its higher growth of exports was due to the devaluation of the rupee in 1991. This has not been followed by any noticeable increase in the international competitiveness of Indian exports through significant improvements in their productivity and quality. There has also not been
the generation of adequate export surpluses in the commodities in which India possesses (actual and potential) competitive advantage. They have also been infrastructural bottlenecks in the form of power shortages, congestion and occasional strikes at ports and airports, shortages of railway wagons. In an effort to contain inflation, tighter monetary policy was practiced between 1991-92 and 1996-97 leading to costlier export credit. (Wadhva, Charan D. 1998)

The recapitulations made above lend an appropriate context to analyze the performance of the country on the external front and propose suggestive measures for the period 1996 onwards. It is for this reason that the trade performance of India is being studied for the period 1997-2002. It was the period when the second five year EXIM policy was floated and made co-terminus with Ninth Five Year Plan. It may be recalled that the first such policy was for the period 1992-1997. The analysis of the period 1997-2002 assumes importance as the country witnessed a downfall on its export front after 1996. What have been the underlying reasons that have led the thrust given by the Indian Government to the external trade sector to pale into insignificance. What more needs to be done to attain the target on external front are the pertinent questions that require a meticulous probe. It is with this aim that the trends in Indian foreign trade, composition and direction, are analyzed for the period 1997-2002. It is also essential to analyze the promotional aspects, the insurance and financing of the Indian foreign trade for 1997-2002. The altered role being played by the state trading and the public sector enterprises in the country's foreign trade also assumes importance in the study. The need is also to comprehend a still larger environment that includes the bilateral, multilateral trading arrangements and the regional economic trade blocs and groupings that impact India's foreign trade. At the grass root level it is pertinent to study the contemporary economic problems being faced by the exporters, importers and the Indian industry and agriculture. The analysis of these varied issues would provide sufficient inputs to paint a picture of the Indian foreign trade as it would appear beyond 2,001. Suggestive recommendations then need to be incorporated that spell the words of wisdom and help in charting the future course of the ship.
References:

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4. Bhide Shashankha. And Chadha Rajesh India’s Exports: Direction and Composition; Foreign Trade Review; volume XXXI No.4 January-March 1997; Quarterly Journal Of Indian Institute Of Foreign Trade