CHAPTER - 1

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1.1 INTERNATIONAL TRADE-AN ENGINE OF ECONOMIC GROWTH:

In modern age, international trade is assumed an engine of economic growth and development. It facilitates vast international market with unlimited opportunities, technological advancements, competitive and efficient allocation of resources into units of economic size. It translates the agrarian and traditional economy into the modern industrialized economy. It expands entrepreneurship and tertiary sector also. Hence, it is a great stimulus for growth and development. In the earlier stage United Kingdom, USA, Germany, Japan and France had achieved higher growth rates and become advanced and developed countries of the World through international trade. Newly developed countries South Korea, Taiwan, Singapore, Hong Kong, known as "Asian Tigers" have also accelerated their growth rates through international trade.

International trade has great importance for Indian economy also. In the year 2000-2001 the contribution of trade was 22.58 percent of the GDP. Thus, more than one-fifth share of GDP is obtained from the trade sector only. Foreign trade is a vital variable of strategic importance in the economic equation of India. It constitutes the life-line of the Indian economy. Trade indeed activated the use of the unexploited natural resources and expanded the frontiers of the domestic market and energized the otherwise stagnant economy. While import have played a vital role in hastening the process of industrialization by supplying from abroad, the most crucial raw materials, capital goods, technical know-how and other inputs, which are indispensable for development. Export expansion has helped in minimizing the dependence on foreign aid, which since long is believed to be a 'sin qua non' for accelerating the pace of economic transformation. Thus foreign trade
plays a crucial role in the economic development of India. The total turnover (i.e. the value of imports plus the value of exports) has gone up from Rs. 3,169 crore in the year 1970-71 to Rs. 3,67,508 crore in the year 1999-2000. It reveals 114.97th fold increase during the period. It also indicates the significance of foreign trade in Indian economy. Inspite of this tremendous growth, India's share in world trade was 0.6 percent in 2001 which was less than that of small countries like Taiwan and Singapore. It is a very crucial issue, hence it should be increased. Observing the performances of the East Asian Countries India has also opened its economy by introducing "Economic Reforms in the year 1991 and Indian Economy is linked with Global economy. India has completed the First Phase of Economy Reform in Ninety decade. Now, India has determined to introduce Second Phase of Economic Reforms" in the new Millenium. Hence, international trade has become crucial issue in Indian Economy.

1.2 CONTRIBUTION OF FOREIGN TRADE TO ECONOMIC DEVELOPMENT:

Foreign trade contributes to economic development in a number of ways. First, the primary function of foreign trade is to explore means of procuring import of capital goods, without which no process of development can start. Secondly, it provides for flow of technology, which allows for increases in total factor productivity, and some short-run multiplier effects for countries with unemployed labour.¹ Thirdly, it generates pressure for dynamic change through:

(i) Competitive pressure from imports;
(ii) Pressure of competing for exports markets; and
(iii) A better allocation of resources.

Fourthly, exports allow fuller utilization of capacity, increased exploitation of economies of scale, separation of production pattern from domestic demand, and increasing familiarity with absorption of new technologies.² Fifthly, foreign trade increases most worker's welfare.³ It does so at least in three ways:

(i) larger exports translate into higher wages;
(ii) because workers are also consumers, trade brings them immediate gains through cheaper imports.
(iii) it enables most workers to become more productive as the goods they produce increase in value;
(iv) trade increase technology transfers from industrial to developing countries and the transferred technology in biased in favour of skilled labour;⁴ and

Finally, increased openness to trade has been strongly associated with the reduction of poverty in most developing countries, as the historian. Arnold Toynbee said 'Civilization' has been spread through mimesis: Simple coping. Hence, foreign trade is important to every country for it is a well established fact that trade and commerce are not just the sum of exports and import, they constitute a growth factor that benefits both the exporting and importing countries.

In order to understand the nature and problems of foreign trade, we have defined some terms used in the study:

(i) TRADE: Trade implies the sale and purchase of goods and services. Trade can be local, regional and international. But generally trade is considered as Internal trade and International trade.

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(ii) INTERNATIONAL TRADE: International trade is the trade between two or more than two countries. When exchange of goods and services take place between two individuals living in different countries, such trade is called ‘International trade’. To be more precise, international trade is goods and services may take place between two countries. Hence, the trade between two countries is called the International trade.

(iii) INTERNAL TRADE: When exchange of goods and services take place between two individuals or firms or institutions within the same country, it is called ‘domestic’ or ‘Internal’ Trade.

(iv) TERMS OF TRADE: The terms of trade is one of the measurements of the gains from international trade to a particular country. In international economics, the phrase terms of trade refers to the ratios index of export prices to import prices. In other words, it is the rate at which a country’s exports are exchanged for imports.

(v) VALUE OF TRADE: It means the money value of all goods exported and imported by a country.

(vi) VOLUME OF TRADE: It means the physical quantity of the goods exported and imported.

(vii) COMPOSITION OF TRADE: It denotes different items that a country imports and exports. The composition of imports indicates the need of the country while the composition of exports indicates the goods that a country is capable of offering for sale.

(viii) DIRECTION OF TRADE: By direction of trade, we mean the countries with which our country has trading relations.

S.S.M. Desai “Scope of international Economics” 1990, pp. 15
D.M. Mithani, “The nature of International trade”, 1993, pp.1-7
(ix) STRUCTURE OF TRADE: In structure of foreign trade we include the size of foreign trade, Export and import of commodities and their shares in total trade, balance of trade, balance of payment and direction of trade.

(x) BALANCE OF TRADE: It means the difference in the value of exports and imports of goods. If exports are more than imports, the balance of trade in called favourable. On the other hand if imports are more than exports, the balance of trade is called unfavourable.

1.3 STRUCTURE OF FOREIGN TRADE OF INDIA: The structure of foreign trade of India is divided in to two major parts, i.e. (a) Import structure; and (b) Export structure.

(a) Import Structure: All commodities imported are grouped into groups which are as follows:

I Food and Live Animals chiefly for food;
II Crude materials, Inedible except fuel.
III Mineral Fuels, Lubricants and Related Materials,
IV Animals and Vegetable oils, Fats and Waxes,
V Chemicals and Related Products,
VI Manufactured goods chiefly classified by materials,
VII Machinery and Transport Equipments; and
VIII Miscellaneous Manufactured Goods.

First four groups are included under Agriculture or Traditional imports while rest of the groups are included under manufacturing sectors.

(b) Export Structure: All commodities exports are grouped into mine groups which are as follows:

I Food and Live Animals chiefly for food,
II Beverages and Tobacco,
III Crude Materials, Inedible except fuels,
Food & Live Animals; Beverages & Tobacco; Crude Materials; Mineral Fuels, Animal and vegetable oils are included under Agricultural or Traditional exports while chemicals and Related products; Manufactured Goods, Machinery and Transport Equipment, and Miscellaneous Manufactured goods are included under the manufacturing sectors.

1.4 ORIGIN OF OECD (ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT): Organization for Economic Development and Co-operation was established on 30th Sep. 1961. The OECD replaced the organization for European Administration of Marshall Plan aid and the Co-operative long been completed, though many of its activities had continued or had been adjusted to meet the needs of economic expansion. By the 1960s the once seemingly permanent dollar gap had disappeared, many quantitative restrictions on trade within Europe had been eliminated, and currency convertibility had been largely achieved. This increased economic interdependence suggested the need for an organization in which North American States would participate on an equal footing. Thus the OEEC, of which Canada and the United States had been only associate members, was transformed into the OECD. The new grouping was also viewed as a means of overseaing foreign aid contributions to less developed states. It later expanded to include virtually all the economically advanced free-marked states. Japan became a full member in 1964, followed by Finland in 1969, Australia in 1971, and New Zealand in 1973. The membership remained static
until Mexico's accession in 1994. Subsequently, the Czech Republic (1995),
Hungary (1996), Poland (1996), and South Korea (1996) joined. The member
countries of OECD as follows: Australia, Austria, Belgium, Canada, Czech
Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland,
Ireland, Italy, Japan, Republic of Korea, Luxembourg, Mexico, Netherlands,
New Zealand, Norway, Poland, Portugal, Spain, Sweden, Switzerland,
Turkey, United Kingdom, USA. The aim of the OECD is to Co-ordinate the
Welfare Policies of the member countries for promoting welfare activities in
their respective economies.

1.5 JUSTIFICATION OF THE STUDY: We have selected this topic for
research because more than 50 percent trade is recorded with OECD counties.
Changes in trade between countries. Changes in the trade between OECD
countries and India will not only affect our growth and development but also
our national economy. Therefore, we selected the topic to find out the impact
of liberalization policies of the Govt. on Indo-OECD trade. The study period
has been divided into three parts:

(i) Pre-Earlier Period 1970-71 to 1979-80


(iii) Post Earlier Reform period during 1991-92 to 1999-00.

1.6 OBJECTIVES OF THE STUDY: The basic objectives of study are as
follows:

I. To find out growth and trend of import, export and balance of trade of
India with OECD countries at constant prices during 1970-71 to 1999-
2000 period.

II. To analyse the share of OECD countries in imports and exports of
India during the study period.
III. To find out the impact of Post - liberalization policy on Import and Export of India on total trade and share of OECD countries in trade during the study period.

IV. To find out the India's trade with major trading countries of OECD like USA, U K, Germany, Japan and France during the period.

V. To find out the direction of trade to different regions during the period.

VI. To find out the drawbacks of the foreign trade of India with OECD countries and suggest measures to improve the balance of trade position of India with OECD countries.

1.7 RESEARCH METHODOLOGY : The present study is entirely based on secondary data collected from the following various sources:


(ii) Director General of Commercial Intelligence Statistics, Calcutta,

(iii) Central Statistical Organization, New Delhi.

The period under investigation of this study refers during the period 1970-71 to 1999-2000, which in divided into three sub periods, the Earlier Period 1970-71 to 1979-80, the Pre-Economic Reforms period, 1980-81 to 1989-90 and the Post Economic Reforms period 1991-92 – 1999-00. Time Series data on exports and imports in terms of value and GDP at market prices are drawn from the issues of Economic Survey and Handbook of Statistics on Indian Economy, 2000 RBI. Wholesale Price Index (WPI) has been taken from the Handbook of statistics on Indian Economy, 2000 RBI and CSO, assuming 1993-94 as the base year. The price index adjustment has been made for the year 1970-71 to 1992-93. For this we have used the following formula –

\[
\text{Base Shifting} = \frac{\text{Current year's Old Index No.}}{\text{New base year's Old Index No.}} \times 100
\]
To find out the amount of export and import at constant prices, the amount of export and import have been deflated taking 1993-94 price index as base year and the following formula has been used:

\[
\text{Amount of Exports/Imports at constant Prices} = \frac{\text{Current price of Exports/Imports of the year}}{\text{WPI of the year taking 1993-94 as base}} \times 100
\]

Compound Growth Rate: To find out the trend lines, we have used the following exponential growth model:

\[Y = a + bt,\]

Where,

"Y" refers to the value of exports imports in year.
'a' in the constant 'b' in the coefficient (here it in growth rate) and
'b' refers to time.

Arithmetic mean and Coefficient of Variation have been used to find out the variation in export and import during the study period and in various sub periods. Hence, following formula of arithmetic mean and coefficient of variation are used:

Arithmetic Mean:

\[\bar{x} = \frac{\Sigma x}{N}\]

Where,

\[\bar{x} = \text{Arithmetic Mean}\]
\[\Sigma x = \text{Summation of the amount}\]
\[N = \text{Number of observation / year}\]

Coefficient of Variation (C.V.)
\[ \text{C.V.} = \frac{\text{SD}}{\bar{x}} \times 100 \]

Where,
- \text{C.V.} = \text{Coefficient of variation}
- \text{SD} = \text{Standard Deviation}
- \bar{x} = \text{Arithmetic Mean}

The Percentage and Annual Growth rate:
The percentage and the annual growth rate of export, import and trade balance of OECD have been worked out. The formula used to find out percentage in-

\[
\text{Percentage of OECD export/import and balance of trade} = \frac{\text{OECD trade amount}}{\text{Total Trade}} \times 100
\]

The formula used to find out the annual growth rate is

\[ \text{AGR} = \frac{\text{Currant Amount} - \text{Preceding Amount}}{\text{Preceding - Amount}} \times 100 \]

Terms of Trade: The Net Barter Terms of Trade has been calculated by taking 1970-71 as the base year. Net barter terms of trade implies unit value index of export expressed as a percentage of unit value index of imports, the formula has been used to calculate the Net barter terms of trade -

\[ \text{NBTT} = \frac{\text{Pix}}{\text{Pim}} \times 100 \]

Where,
- \text{NBTT} = \text{Net Barter Terms of Trade}
- \text{Pix} = \text{Unit value index of exports}
- \text{Pim} = \text{Unit value index of imports}

Hypothesis: To be test the hypothesis we have used Student's 't' test.
The formula has been used to calculate the ‘t’ test:

\[ t = \frac{\bar{X}_1 - \bar{X}_2}{\sqrt{1/n_1 + 1/n_2}} = \frac{\bar{X}_1 - \bar{X}_2}{S} \sqrt{n_1 + n_2} \]

Where,

\[ \bar{X}_1, \bar{X}_2 = \text{Arithmetic mean of sample} \]
\[ n_1, n_2 = \text{Number of observations} \]
\[ S = \text{Difference of two samples of standard deviation} \]

The formula used to find out

\[ S = \sqrt{\frac{\sum d_1^2 + \sum d_2^2}{n_1 + n_2}} \]

To find out the result we have test degree of freedom = \( n_1 + n_2 - 2 \)

1.8 LIMITATION OF THE STUDY: The present study makes an analysis of Indo-OECD trade. However, we have certain limitations found during the study period:

(i) The year 1991 is excluded from the study because it was an abnormal year in which the country was facing the severe crisis of Balance of Payment.

(ii) The period 1970-71 to 1979-80 is not considered for the whole study period because, the trade amount of OECD countries are found in dollar terms during the period 1970-71 to 1979-80 but 1980-81 to 1999-00 are found in Rupee terms.

(iii) Commodity-wise export and import of OECD countries are not available. So, we have not analysis the commodity wise export, import to India from OECD countries.

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