UNIT V

FOREIGN TRADE IN INDIA

FOREIGN TRADE

Foreign trade or International trade is the exchange of capital, goods, and services across international borders or territories. In most countries, such trade represents a significant share of gross domestic product (GDP). It is a trade between two nations or two countries. International trade is also a branch of economics, which, together with international finance, forms the larger branch called international economics.

INTER- REGIONAL OR DOMESTIC OR INTERNAL TRADE:

Inter -Regional trade refers to trade between regions within the country. It is otherwise known as Domestic or Internal trade.

NEED FOR FOREIGN TRADE:

- Attaining a high profit.
- Expansion of production over & above the domestic requirements.
- Meeting tough competition in the home country.
- Inadequate scope in home market.
- Political in stability.
- Ample scope of advanced technology & managerial competence.
- Liberalization & Globalization.

FEATURES OF FOREIGN TRADE:

- Immobility of resources.
- Heterogeneous markets.
- Trade among different nations.
- Trade between different political unities.
- Different types of currency.
- Geographical & Climatic differences.
- Problems of BOP.
- Different Transport Cost.
- Different Economic Environment.

MERITS OF FOREIGN TRADE:

(i) Optimal use of natural resources.

International trade helps each country to make optimum use of its natural resources. Each country can concentrate on production of those goods for which its resources are best suited. Wastage of resources is avoided.

(ii) Availability of all types of goods.

It enables a country to obtain goods which it cannot produce or which it is not producing due to higher costs, by importing from other countries at lower costs.

(iii) Specialisation.

Foreign trade leads to specialisation and encourages production of different goods in different countries. Goods can be produced at a comparatively low cost due to advantages of division of labour.

(iv) Advantages of large-scale production.

Due to international trade, goods are produced not only for home consumption but for export to other countries also. Nations of the world can dispose of goods which they have in surplus in the international markets. This leads to production at large scale and the advantages of large scale production can be obtained by all the countries of the world.

(v) Stability in prices.

International trade irons out wild fluctuations in prices. It equalizes the prices of goods throughout the world (ignoring cost of transportation, etc.)

(vi) Exchange of technical know-how and establishment of new industries.

Underdeveloped countries can establish and develop new industries with the machinery, equipment and technical know-how imported from developed countries. This helps in the development of these countries and the economy of the world at large.

(vii) Increase in efficiency.

Due to international competition, the producers in a country attempt to produce better quality goods and at the minimum possible cost. This increases the efficiency and benefits to the consumers all over the world.

(viii) Development of the means of transport and communication.

International trade requires the best means of transport and communication. For the advantages of international trade, development in the means of transport and communication is also made possible.

(ix) International co-operation and understanding.

The people of different countries come in contact with each other. Commercial intercourse amongst nations of the world encourages exchange of ideas and culture. It creates co-operation, understanding, and cordial relations amongst various nations.

(x) Ability to face natural calamities.

Natural calamities such as drought, floods, famine, earthquake etc., affect the production of a country adversely. Deficiency in the supply of goods at the time of such natural calamities can be met by imports from other countries.

(xi) Other advantages.

International trade helps in many other ways such as benefits to consumers, international peace and better standard of living.

<u>DEMERITS OF INTERNATIONAL TRADE:</u>

(i) Impediment in the Development of Home Industries.

International trade has an adverse effect on the development of home industries. It poses a threat to the survival of infant industries at home. Due to foreign competition and unrestricted imports, the upcoming industries in the country may collapse.

(ii) Economic Dependence.

The underdeveloped countries have to depend upon the developed ones for their economic development. Such reliance often leads to economic exploitation. For instance, most of the underdeveloped countries in Africa and Asia have been exploited by European countries.

(iii) Political Dependence.

International trade often encourages subjugation and slavery. It impairs economic independence which endangers political dependence. For example, the Britishers came to India as traders and ultimately ruled over India for a very long time.

(iv) Mis - utilisation of Natural Resources.

Excessive exports may exhaust the natural resources of a country in a shorter span of time than it would have been otherwise. This will cause economic downfall of the country in the long run.

(v) Import of Harmful Goods.

Import of spurious drugs, luxury articles, etc. adversely affects the economy and well-being of the people.

(vi) Storage of Goods.

Sometimes the essential commodities required in a country and in short supply are also exported to earn foreign exchange. This results in shortage of these goods at home and causes inflation. For example, India has been exporting sugar to earn foreign trade exchange; hence the exalting prices of sugar in the country.

(vii) Danger to International Peace.

International trade gives an opportunity to foreign agents to settle down in the country which ultimately endangers its internal peace.

(viii) World Wars.

International trade breeds rivalries amongst nations due to competition in the foreign markets. This may eventually lead to wars and disturb world peace.

(ix) Hardships in times of War.

International trade promotes lopsided development of a country as only those goods which have comparative cost advantage are produced in a country. During wars or when good relations do not prevail between nations, many hardships may follow.

SIMILARITIES BETWEEN INTERREGIONAL TRADE & FOREIGH TRADE:

- Consumer Satisfaction
- Building up of Goodwill
- Need for Market Research
- Product Planning & Development

DIFFERENCES BETWEEN INTER REGIONAL AND FOREIGN TRADE:

- Sovereign Political Entities
  a) Distance
  b) Inadequate Transport & Communications
  c) Diverse Languages, Customs & Traditions
  d) Risks & Uncertainties
  e) Customs Formalities
  f) Shipping & Insurance
  g) Foreign Trade Quotation
  h) Too Many Middlemen

- Different Legal Systems
- Different Monetary System
- Lower Mobility of Factors of Production
- Differences in Market Characteristics

GAINS FROM FOREIGN TRADE:

- International Specialization
- Increased Production & Higher Standard of Living
- Availability of Scarce Materials
- Equalization of Prices between Countries
- Evaluation of Modern Industrial Society
- Lead to Higher level of Employment
- Enables people to earn Income
- Provides for transfer of Capital & Technical know – how
- Exposure to Technological Development
- Makes the Countries Dependent on each other

ROLE OF FOREIGN TRADE IN ECONOMIC DEVELOPMENT:

There are two ways to express the Role of Foreign Trade in Economic Development.

- Direct Benefits
- Indirect Benefits

DIRECT BENEFITS:

- To break the vicious circle of poverty & promote economic development
- Extension of Market
- Increased Investment level
- Surplus Production
- Proper Utilization of Resources
- Internal & External Economies

INDIRECT BENEFITS:

- Import of Capital goods against Export of Staple Commodities
- Important Educative Effects
- Development of Industrial Technology
- Basics for Importation of Foreign Capital
- Checking of Inefficient Monopolies

EXPORT PROMOTION

It is a policy and practice by which the exports of the country can be increased to the maximum possible extent to bridge the balance payments deficits as quickly as possible.

NEED FOR EXPORT PROMOTION

a. Increasing the traditional items exports to already existing customers.
b. Increasing number of customers for traditional exports i.e., diversification of exports and
c. Increasing the base of our exports by introducing non-traditional units.

The GOI appointed Export Promotion Committee in Feb1957. The committee recommended large number of measures to increase export. But the recommendations were not accepted by the government.

In the year 1962, the government appointed "Import and Export Policy Committee" popularly known as "Mudaliar Committee". This committee stressed the importance of export promotion through import license, besides giving adequate tax relief and freight concessions. The committee suggested that all handicaps and disincentives to export trade should be removed, as providing aids and incentives would be of no avail without removing the handicaps. It aims at export promotion and import substitution to bridge the ever – widening trade gaps.

EXIM BANK OR EXPORT AND IMPORT BANK

The GOI set up the EXIM Bank of India in January 1982. This is a statutory cooperation wholly owned by the Union Government.

OJBECTIVES

a. To ensure an integrated and coordinated approach to solving the problems of exporters.
b. Proving special attention to capital goods exports and export of technical services.
c. To tap domestic and overseas markets for resources for undertaking development and financial activities in the area of exports.

FUNCTIONS OF EXIM BANK

a. Financing the exports from and imports into India, as well as third countries.
b. Financing of joint ventures of foreign countries.
c. Financing of export and import of machinery and equipment on lease basis.
d. Providing loans to Indian parties to enable them to contribute on the share capital of joint ventures in foreign countries.
e. Undertaking promotional activities in the field of exports.
f. The promotional activities of the EXIN bank cover planning and development of exports and imports.
g. It introduced a number of schemes for the promotion of exports of engineering and capital goods.
h. It also undertaken many technical and consultancy services.
i. It gives financial assistance on flexible terms to the Indian exporters.
j. It also operates scheme for financial assistance to foreign buyers for purchasing Indian Engineering goods.

EXPORT INCENTIVE AND ASSISTANCE

In order to boost exports, the government has devised many incentives and assistance. These are modified from time to time to meet the changing conditions in the international trading.

CLASSIFICATION OF INCENTIVES

The incentives are classified as follows

a. Fiscal incentives. – concession in income tax, custom duty.
b. Financial incentives. – cash assistance is given for specified export promotional efforts.
c. Special incentives. –IPRS International Price Reimbursement Scheme.

ORGANISATIO FOR EXPORT PROMOTION

The government has set up several specialized organizations for the purpose of export promotion. They are

a. The Central Advisory Board on Trade.
b. The Trade Development Authority.
c. The Federation of Indian Export Organisation.
d. Export Promotional Council.
e. Commodity Boards.
f. STC-State Trading Cooperation – 1956.

IMPORT SUBSTITUTION

IT means a shift in the source of supply, from imports to domestic production. Or, imports are done away with these commodities which could be produced at home. It tries to conserve the foreign exchange by reducing the imports, the ultimate object being the building up of the foreign exchange reserves.

It is possible in some areas by adopting the following methods.

a. Imported raw materials, components and spare parts have been substituted with indigenously manufactured material.
b. Consumption of imported raw materials and components of production have been reduced.
c. Change- over of production of chemical and chemical products from intermediate inputs to basic raw materials.
d. Substitution of imported raw materials by suitable alternatives with consequential changes in the specification of the end products.
e. Acceleration of the phased manufacturing programmes to achieve greater indigenous content in the shortest possible time.

BALANCE OF PAYMENTS (BOP)

It is a systematic record of all its economic transactions with the outside world on a given year. It is a statistical record on the character and dimensions of the country's economic relationship with the rest of the world.

DEFINITION OF BOP

According to Bo Sodersten, "The BOP is merely a way of listing receipts and payments in international transactions for a country"

According to B.J. Cohen, "It shows the country's trading position, changes in its net position as foreign lender or borrower, and changes in its official reserve holdings".

COMPONENTS OF BOP

1. Current account
2. Capital account
3. Official settlement account

BOP ALWAYS IN EQUILIBRIUM

BOP always balance means the algebraic sum of net credit and debt balance of current account, capital account and official settlements account must equal to zero.

$B = R_j - P_j$
Where B = BOP,
R_j = receipts from foreigners,
P_j = payments made to foreigners.

a. When $B = R_j - P_j = 0$ BOP is in equilibrium.
b. When $Rj - P_j$ greater than 0. Receipt exceeds the payments is surplus BOP.
c. When $Rj - P_j$ less than 0. Payments exceeds receipts is deficit BOP.

MEASURING DEFICIT OR SURPLUS IN BOP

There are three ways of measuring deficit or surplus BOP.

a. Basic Balance
b. Net Liquidity Balance
c. Official Settlement Balance

ROLE OF WTO

The original GATT (General Agreement on Tariffs and Trade) is now a part of the WTO agreement which came into force from January1, 1995. The WTO is the successor to the GATT. It is properly established permanent world trade organisation. It has a legal status and enjoy privileges and immunities on the same footing as the IMF and the World Bank.

STRUCTURE OF WTO

a. It is headed by the ministerial conference composed of representatives of all members which meet at least once every two years. It is the supreme authority of WTO.
b. General Council composed of representatives of all the members to oversee the operation of the WTO agreement and ministerial decisions on regular basis. Head office in Geneva to meet on an average of once a month.
c. The secretariat of the WTO headed by the Director General. He is appointed for a four years term.

OBJECTIVES OF WTO

a. Its relations in the field of trade and economic endeavour.
b. To allow for the optimal use of the world's resources.
c. To make positive efforts designed to ensure that developing countries.
d. Substantial reduction of tariffs and other barriers to trade.
e. To develop an integrated, more viable and durable multinational trading system.

f. To ensure linkages between trade policies, environmental policies and sustainable development.

FUNCTIONS OF WTO

a. It facilitates the implementation, administration and operation of the objectives of the Agreement and of the Multinational Trade Agreement.
b. It provides the framework for the implementations, administration and operation of the Plurilateral Trade Agreements relating to trade in civil aircraft.
c. It provides the forum for negotiations among its members concerning their multilateral trade relation in the matters relating to the agreements.
d. It administers the Undertaking on Rules and Procedures governing the Settlement of Disputes of the Agreement.
e. It co- operates with IMF and World Bank.

WTO AGREEMENT

a. Multilateral Agreement on Trade in Goods: GATT Rules 1994.
b. General Agreement on Trade Services – Agriculture, Textile and Clothing.
c. TRIPS Trade Related Aspects of Intellectual Property Rights.
d. TRIMs Trade Related aspects of Investment Measures.
e. SCM Subsides and Countervailing Measures.
f. GATS General Agreements of Trade in Services.
g. PTA Plurilateral Trade Agreement.
h. DSS Dispute Settlement System.
i. TPRM Trade Policy Review Mechanism.

CRITICISMS

a. Agriculture.
b. Textile and Clothing.
c. TRIMs.
d. GATT Rules.
e. Dispute Settlements.

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