



## **India's Merchandise Exports: Some Important Issues and Policy Suggestions**

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## **Executive Summary and Conclusion**

In this paper based on both desk research and meetings with stakeholders, an attempt has been made to examine the current trade scenario — both global and India and suggest policy measures both general and sector-specific to raise India's export share above a minimum threshold level. Highlights of the paper including the emerging trade situation, both global and Indian and some important policy measures, both general and sector specific are given below.

### **Current Trade Situation: Global and India**

The world economy has been receiving shocks at regular intervals since the 2008 crisis. While, there was recovery in global economy after the 2008 crisis, with developing countries leading the recovery and developed countries like US and Euro Area countries facing unemployment and recessionary trends, a reversal of roles seems to have taken place recently. The July 2014 update of the IMF's World Economic Outlook has lowered both the global growth projection and World trade volume projection for 2014 by 0.3 percentage points to 3.4 percent and to 4.0 per cent respectively.

In the last five years, India's export growth has seen ups and downs, being in negative territory twice in 2009-10 as an aftershock of the 2008 crisis and in 2012-13 as a result of the euro zone crisis and global slowdown. India's exports were US\$ 312.6 billion against a target of US\$ 325 billion during 2013-14, though they grew by a positive 4.1 per cent as compared to the negative growth of 1.8 per cent during the previous year. Export growth has picked up during 2014-15 (April-July) and was at 8.6 per cent over the same period of previous year. Import growth in 2014-15 (April-July) fell by 3.8 per cent over the same period of previous year.

The sharp fall in imports and moderate export growth in 2013-14 resulted in a sharp fall in India's trade deficit by 27.8 per cent. In absolute terms, trade deficit fell to US\$ 137.5 billion from US\$ 190.3 billion during 2012-13. However, there was not much change in the POL deficit which was hovering at around US\$100 billion in the last two years. With the fall in imports of both gold and capital goods, non-POL deficit fell sharply to US\$ 35 billion in 2013-14 from US\$ 87.2 billion in 2012-13. In 2014-15 (April- July) trade deficit fell by 24.4 per cent mainly due to the fall in gold and silver imports.

The international trade situation is still fragile with the Baltic Dry Index (BDI), a good proxy of the robustness of world trade, being in one of the lowest phases since the 2008 global financial crisis with sub 1000 indices. While the international trade situation is still fragile, there was some pick-up in India's exports in April-July 2014. The monthly export and import growth performance of some of the major trading countries also show some revival.

## Policy Issues

While India's export growth rates (both goods and services) have been impressive before the global financial crisis, and moderate to low thereafter, the share of India's exports (merchandise) in world exports is still just 1.7 per cent in 2013. If we compare the share of India and China in 1990 (after which economic reforms were introduced in India) and 2013 (the latest year for which data are available), India's merchandise exports share in world exports increased from 0.5 per cent to 1.7 per cent and China's share increased from 1.8 per cent to 11.8 per cent. India's aim should be to increase its share in world merchandise exports from 1.7 per cent in 2013 to a respectable ballpark figure of, say, at least 4 per cent in the next five years. For this the CAGR of exports in next 5 years should be around 30 percent, which is not an impossible task. Some policy issues in this regard both general and sector specific include the following.

**Product Diversification along with Market Diversification:** While there has been market diversification and compositional changes in India's export basket, not much of demand-based product diversification has taken place. In the top 100 imports of the world at four-digit HS level in 2013, India has only five items with a share of 5 per cent and above. Most of the items in the top 100 world imports include the three Es— electronic, electrical, and engineering items—and some textiles items. A demand-based export basket diversification approach with a perceptible shift to the three Es could lead to greater dividends for India.

**Export Infrastructure:** Export infrastructure, particularly ports-related infrastructure, which affects trade, needs immediate attention. Port infrastructure issues include poor road conditions and port connectivity, congestions, vessel berthing delays, poor cargo handling techniques and equipment, lack of access for containerized cargo, and frequent EDI server down or maintenance, resulting in multiple handlings, increased lead time, high transaction costs, and thus loss of market competitiveness. Export infrastructure should be built on a war footing. Some specific issues in different places include deepening of drafts at berths as nowadays worldwide the cargoes like steel are carried in handymax vsl i.e. 45000 - 52000 dwt vsl which normally needs a draft of 12 to 12.5 meters. For example, currently Mumbai port can accommodate vessels only in BPX berth where there is a draft of 10.5 meters (10 or 10.2 meters during monsoon) and two other berths in harbour wall which have a draft of 8 - 8.5 meters. All the other berths inside the dock can accommodate only smaller vessels. Hence, exporters will have to rely on smaller vessels and thereby pay higher freight compared to their international competitors like china. Other aspects of port infrastructure upgradation required all over India include the need for substantial improvements in road conditions to reduce jams and faster delivery; on line tracking of container position at all terminals of JNPT and other ports; updating gate cut-offs on on-going basis; improving movement of cargo from buffer yards; providing special purpose agri jetties for agricultural cargo in ports like Kandla and Mundra to reduce ship turnaround time and improve the supply chain efficiency; and installing mobile cranes with proper and sufficient capacity for loading cargo. Besides these there are issues like reduction of tariff for anchorage loading,

better connectivity from ports to ICDs, using minor ports, reduce inefficiency at Indian ports and addressing the issues of port congestion charges.

**Focus on useful Regional Trading Arrangements (RTAs):** Some FTAs/RTAs/CECAs of India have led to an inverted duty structure-like situation with import duty on some finished goods being nil or lower than the duty on raw materials imported from other countries. Besides, the domestic sector involving livelihood concerns has also been affected by some of them. Some such issues include imposing high duty on imports from India by Bangladesh on textile products, while imports from Bangladesh to India is at 'NIL' duty; the insistence of Nepal Banks on declaring the bank negotiating exchange rate in ARE-1 which is not possible as there is no field to mention this in the document and Indo-Nepal treaty does not provide for furnishing ARE-1 as mandatory; issue of exports to Nepal and Bhutan made under rupee payment for export incentives; and Japan imposing annual tariff rate quota on footwear imports from India. There are also issues with some other non FTA/RTA countries where Indian Exporters face discrimination. Some examples include the imposition of 10 per cent import duty by China on Indian cashewnuts exports while Vietnamese exports enjoy 'Nil' duty; need to negotiate with China to extend duty free access to exports of oilseeds, especially sesame seeds and groundnuts from India, since China provides zero duty access to competing countries; and the issue of allowing import of gelatin from India to China. These are issues with different countries which need to be taken up with them at bilateral and multilateral forums. Meanwhile, India's push towards regional and bilateral agreements should result in meaningful and result oriented FTAs /RTAs/ CECAs. So a reality check of existing RTAs/FTAs/CECAs is needed. India should also ready itself to face new threats like the Trans-Pacific Partnership (TPP) and Trans-Atlantic Trade and Investment Partnership between the EU and the US (TTIP). These will create the world's largest free trade areas. Both TPP and TTIP are likely to produce market access restrictions and discrimination for Indian exporters even where India has already signed FTAs with TPP members such as Japan. Further, they will hasten the momentum towards the multilateralisation of regionalism. A strategy must be devised by India to face this challenge. There is also need to have some useful FTAs, RTAs with countries like Chile which can help automobiles exports; with South Africa to help leather exports and with EU in the light of withdrawal of GSP benefits and to help sectors like textiles, coir, leather, etc.

**Issues of Inverted Duty Structure:** Inverted duty structure is making Indian manufactured goods uncompetitive against finished product imports in the domestic market. Under the inverted duty structure, finished goods are taxed at lower rates than raw materials or intermediate products which discourage domestic value addition. Manufactures like aluminum products, capital goods, cement, chemicals, electronics, paper, steel, textiles and tyres are subject to duty inversion. This inversion is not solely because of basic custom duty but in some cases a result of other additional duties. One of reasons for duty inversion is the regional/ bilateral Free Trade Agreements with countries like Japan, South Korea, ASEAN, etc. Some examples of duty inversion include aluminum ingots, billets, wire rods and rolled products having lower duty over raw materials like aluminum fluoride and coal tar pitch, cement being exempted from basic customs duty while its inputs are levied duty, electronics

items like desktops and notebooks having lower duty than key components, stainless steel products enjoying lower duty under India- Japan CEPA while raw materials have higher duty, brass products under FTA with some Asian countries having 'NIL' duty while raw materials like brass scraps have customs duty, tractors imported from Japan having concessional duty while inputs have higher duty, industrial boilers having higher duty than inputs, etc.

**Export Promotion Schemes:** There are multiple and overlapping export promotion schemes with many focus markets and focus products with items and markets getting added each year in the foreign trade policy. The multiplicity of schemes and concessions are also periodically extended. There is need to rationalize the export promotion schemes to a bare minimum which can also reduce transaction cost and trade litigations. There should not be many rates of concessions. Even for duty drawback scheme, there should be limited rates instead of having different rates even for similar items. This will make things simpler and limit discretionary decisions. Wherever tariffs are low or can be reduced, export incentives should be withdrawn as the transaction costs would be higher than the benefits owing to duty concessions.

**Export Credit and related Financial Issues:** Export credit as a proportion of net bank credit has declined from 9.8 per cent in March 2000 to 3.7 per cent in March 2013. While many countries such as Canada, Germany, Italy, Japan United States, China, etc., have become aggressive in their export credit financing, India has been losing its export potential, due to paucity of export credit. Therefore, there is a need to strengthen export credit facilities in India and also make it less costlier. Some issues in this context include the charges by 72 banks for issuing e-BRC; and RBI conditions for banks for handling merchant trade transactions or intermediary trade that in case advance against the export leg is received by the merchanting trader, the advance payment has to be held in a separate deposit / current account in foreign currency or Indian Rupee, thus denying the merchant exporter access to these funds and raising the cost of exporting for the merchant exporter.

**SEZ Issues:** SEZs were promised a tax-free regime, but minimum alternate tax (MAT) on SEZ units and developers and dividend distribution tax (DDT) were levied two years back. These have impacted the long term stability of the scheme and investor's confidence in SEZs and investments into SEZs have slowed down. While the new manufacturing zones (NMZ) are being planned, a lot of investment has already been made in SEZs waiting to be tapped to the full potential. SEZs are ready made Clusters with World Class infrastructure and governed by the SEZ act and rules. A clear signal needs to be given for Indian SEZs as fresh investments are slowing down in recent years and the greenfield SEZs have not really taken off full swing. Some other issues related to SEZs include the non-applicability of FTA concessions for SEZs' sales in DTAs; need to extend schemes under Chapter 3 like FTPE, FMS, special FMS and SHISS to units in SEZs; providing EDI connectivity and Operating only ICEGATE and the condition that SEZ manufacturing units must receive their payments from the EEFC account of DTA importers so as to meet their net foreign exchange (NFE) obligations. While there is no compulsion on the DTA importer to pay from their EEFC account while importing from abroad.



**Trade Facilitation (Documentation and Procedural Issues):** Greater trade facilitation by removing the delays and high costs on account of procedural and documentation factors, besides infrastructure bottlenecks is another major challenge. As per the World Bank and International Finance Corporation (IFC) publication 'Doing Business 2014', India ranks 134 in the ease of doing business with Singapore at first place and China at 96. In trading across borders India ranks 132. India needs 9 export and 20 import documents, time to export is 16 days in India, cost of exports per container is US\$ 1170 in India, US\$ 460 in Singapore, and US\$ 620 in China and cost of imports per container is US\$ 1250 in India, US\$ 440 in Singapore, and US\$ 615 in China. Some trade facilitation issues include coordination between Ministries to reduce inter-ministerial delays and ensuring at policy formulation stage itself that policies formulated by one Department are also honoured by others; high transaction costs of around 10-12 per cent faced by Indian exporters; container verification and delay in release of containers; validity of customs documents for LCL (less container load) shipments; need for round the clock customs and excise operations and efficient working of customs servers; provision for allowing amendments in online application; fixing time limit for issuing export obligation discharge certificate; delay in issuing cross border certificate; difficulty faced by exporters in implementation of risk management system (RMS); systems error in transmission of amendments in authorizations or scrips by DGFT to ICEGATE; making available shipping bills online; electronic crediting of benefits under FMS & FPS, issuing certificate for annual feed and acceptance of LUT for export incentive license issuance.

**Tax / Tariff Issues:** Some tax/tariff related issues include early implementation of goods and services tax (GST); stamp duty on imports at 0.1 per cent of c.i.f. value being collected on all imports into Mumbai and Nhava Sheva port while no other state levies such a duty; pending clarification from the Government with respect to the TDS on Foreign Agents Commission; service tax on the remittances of foreign currencies received by exporters from their overseas buyers; need for service tax exemption on services used in agro processing for export; double payment of cess on domestic area sales by 100 per cent EOU; making VAT, duty drawback, or any other refund available within 30 days of claim; service tax on foreign bank charges for handling export documents; exemption of service tax on ECGC premium instead of refund; and speedy settlement of tax related disputes as at the end, the government wins only in a few cases and a lot of time and money of exporters is wasted due to tax disputes.

**Long Term Vision in Multilateral Negotiations:** India has been successful in getting some of its concerns addressed in the WTO ministerial negotiations at Bali and has been able to successfully block the trade facilitation agreement in the recent WTO general council meeting at Geneva till India's concerns on food security are met. India had to negotiate on food security issues today, is because, India and other developing countries did not succeed earlier in negotiating what they wanted on subsidies at the time of Agreement on Agriculture (AOA). Similarly, we signed the ITA-1 which resulted in 'zero' duties for many electronic goods at a time, when the advanced countries and many newly industrialized countries had developed their semi-conductor sector, but India had not. All this was because in the early years of WTO negotiations, the Agenda was set by others and India and other developing



countries had to react to it. So long term objectives should be kept in mind during such negotiations and we should not fall into any traps. We also have to be cautious on the proposed ITA-2 negotiations.

**Intertwining of Domestic and External Sector Policy:** While a stable agri export policy is needed, any domestic shortage or excess affects exports. Similarly external shortages/excesses affect the domestic sector. So a smooth intertwining of domestic and external-sector policies particularly for agriculture related exports is needed.

**Greater Role for States in Export Effort:** Export sector should be accorded national priority sector and there should be greater involvement by the local and state governments while framing and implementing export policy. State wise exports show the domination of only two states with Gujarat at the top followed by Maharashtra. Tamil Nadu and Karnataka are a distant third and fourth. The central government also encourages states to export through the Assistance to States for Developing Export Infrastructure and Allied Activities (ASIDE) scheme which is based on export performance of states. States need to play a greater role in the export effort as they are also the beneficiaries of the resultant development.

**Role of Indian Missions in abroad in Export Promotion:** India's foreign missions should also play an active role to facilitate India's exports. At present the mission have commercial representatives who are supposed to help in export promotion. However, the focus of the mission is on attending to VIPs and facilitating the numerous government and international meetings rather than export promotion. There is a need to reorganise these missions and make them active trade facilitators.

**Effective use of Trade Fairs:** India organises many trade exhibitions in India and abroad. While there is a need to evaluate the outcome of these trade fairs and expos organised by ITPO, there is also a need to make them more focussed and result oriented. Some permanent exhibition centres of India in some important markets could also be set up.

**Reality Check of EPCs:** There are many export promotion councils (EPCs) and commodity boards (CBs) to help exports. While some of them were useful at the time of their setting up, now they have become less important and some new sectors have become important. The outcome of these EPCs and CBs needs to be evaluated and allocation of funds to EPCs should be based on a zero budgeting exercise. Merging some EPCs could also be thought of.

**Transportation related Issues:** Reforms related to transportation of goods for export and import can reduce a lot of costs for the exporters and importers. In this age of multimodal transport, the multimodal transportation of goods act 1993 needs a lot of revisions to ease the existing restrictions on transportation and documentation through different modes of transport, particularly restrictions in the Customs Act which do not allow seamless movement of goods; and restrictions on free movement of cargo between Inland Container Depots (ICDs), Container Freight Stations (CFSs) and Ports. The integration of transport related ministries is a step in the right direction. Some issues related to shipping companies include

higher exchange rate for freight payments and various additional charges collected by the shipping companies like washing charges, charges for issuing bill of lading, survey charges, damage charges, CFS charges and transport charges to CFS, security sub charges, container imbalance charges, Indian service recovery sub charges and international port sub charges. There is a need to see whether these charges are genuine or not and necessary measures should be taken to safeguard the interest of exporters/importers. There are also some issues related to loading export/import cargo. While the gang system in ports is an open secret, there are some regional versions of such systems also like the mathadi kamgar union in Maharashtra forcing themselves in the factories to employ them for loading and unloading export cargo despite being not trained for such work.

**Sector Specific Issues:** Besides the general issues, there are many sector-specific issues. They include the following.

Agriculture Related: They include the domestic market issues like absence of organised market in India and a need for uniform rules and norms in all states; limiting the value addition for the Agar Agar market to 5 per cent, instead of the present 15 per cent under advance authorization scheme to face Chinese competition in this market where export realization is less; levy of FDT (forest development tax) at 12 per cent for the products manufactured by rubber industry in Karnataka as it is considered as a Forest product, while such tax is not levied in neighbouring states like Kerala & Tamilnadu; reinstatement of VKGUY benefit for guar gum & sesame seeds with prices falling; and addressing the issue of inclusion of raw cashew nuts under FSSAI despite their being not readily edible.

Mining Sector: Mining is an important sector which needs special focus for quick growth of the economy as it can not only push up growth figures directly, but also indirectly due to its high linkage effects. While in the medium to long-term we have to devise policies to use our Iron ore domestically instead of exporting it and simultaneously importing Iron & Steel, in the short term there is a need to consider abolition of export duty on low grade Iron ore as it cannot be economically used in India and also addressing the additional freight costs on Iron ore to facilitate the exports of cheap grade iron ore. Greater focus on investment in mining industry is also required.

Engineering Sector: The issues in engineering sector include the 2.5 per cent import duty on metal scrap and 4 per cent on brass, making stainless steel manufacture less competitive than China which enjoys cost advantages in the form of lower power cost, lower interest cost, stable currency, abundant supply of coking coal (not found in India) and access to low cost Nickel pig iron; addressing the issue of definition of MSME in terms of Capital Investment as technological upgradation will entail investment in plant and machinery and also take a company out of MSME limits depriving it of interest subvention and other benefits.

Project Exports: Some suggestions related to project exports include the part payment issue and need for issuing multi-entry visa for personnel employed by Indian project exporters.

Textiles: In textile sector, major issues include customs duty reduction for synthetic garments machinery and synthetic garment fabrics; allowing overtime from 6 hours per week in alternative days to 12 hours per week; early signing of free trade agreement (FTA) with European Union to increase India's market share in the European Union, particularly in the light of Bangladesh, being a least developed country enjoying the duty free status and the total exports from Bangladesh reaching US\$ 22 billion against India's exports of US\$15 billion; and considering FTA with Canada.

Gems and Jewellery Sector: The major issues in this sector are the issue of the AD category-I banks not being permitted to approve suppliers' and buyers' credit including the usance period of letters of credit for import of rough, cut & polished diamonds beyond 90 days from the date of shipment; the issue of high premium charges for gold import from nominated agencies/banks with no policy to control the premium charges of banks/nominated agencies for gold import; allowing personal carriage of gems & jewellery export consignments from Jaipur using gateway ports other than Jaipur; requirement of separate room for appraisement of precious cargo at Netaji Subhash Chandra Bose International (NSCBI) Airport (cargo complex), Kolkata; and the requirement of placing technically qualified personnel as gold jewellery appraisers.

Electronics and IT Hardware Manufacturing: The major issues include the ITA-1 and the adverse effect of the inverted duty structure which have derailed the progress of the electronic manufacturing industry in India making India dependent on countries like China for import of finished IT products. The levy of the 4 per cent SAD on the components also affects the IT hardware manufacturing industry as CST is at 2 per cent making trading more viable than manufacturing. The important issue is of CENVAT credit. So either, the 4 per cent SAD could be removed on the components used in the manufacture of IT hardware products or at least brought down to 2 per cent which is the same as CST. This has been further aggravated by the invokement of rule 2(a) of general interpretation of rules whereby the components imported as (completely knocked down) CKDs by the manufacturers are classified as a finished products, which attracts higher rate of duty. The activity of electronic manufacturing has been arbitrarily declared as mere assembly thereby denying the local manufacturers the credit of being genuine manufacturers. This discourages the local manufacturers from carrying out the manufacturing activity. Many IT hardware manufacturing units have either discontinued their manufacturing activity or limited the same and ventured into trading. This issue therefore needs to be addressed.

Leather Industry: The main issue in this sector is tackling the removal of GSP by EU and the removal of GPT by Canada, while countries like Pakistan have been granted GSP + status by EU and countries like Bangladesh are enjoying zero import duty for most leather products and footwear in countries like European Union, Japan etc., on account of their Least Developed Country (LDC) Status. India needs to find ways to face this challenge including forming useful FTA with EU and Canada. FTA with major market like Australia and Russia could also help. Other issues include augmenting the raw material availability in the country by the measures like increasing the export duty on raw hides & skins and wet blue leathers

from the present 60 per cent to, say, 100 per cent and maintaining the export duty of 60 per cent on crust leather and 15 per cent on East India (EI) tanned leather; strict inspection of finished leather export consignments to prevent free outflow of raw materials and enhancing export of value added products; encouraging private bonded warehouses exclusively for importing and distributing hides, skins and leathers; restoring the facility of import of second hand machinery under EPCG (which was removed w.e.f. April 2013) as many factories are closing down in Europe due to fall in production base and the machinery; including places like Kanpur and Jalandhar as designated ports for importing raw hides & skins through establishment of animal quarantine and certification stations (AQCS); and focusing on exports of ladies and children's footwear as 75 per cent of the world footwear market is dominated by these segments, while these constitute only about 46 per cent of exports of India's footwear segment.

## **Conclusion**

The bunch of issues given in this paper are just illustrative and in no way exhaustive. If these and other such issues are addressed and the policy suggested in this paper examined and implemented quickly, the wheels of exports can move faster taking us near to the target of 4 per cent share in world exports in the next five years.

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## Chapter 1 Emerging Trade Situation: Global and India

### 1.1 Current Global Economic and Trade Situation

#### 1.1.1 World Economic Growth

The world economy has been receiving shocks at regular intervals since the 2008 crisis. While, there was recovery in global economy after the 2008 crisis, with developing countries leading the recovery and developed countries like US and Euro Area countries facing unemployment and recessionary trends, a reversal of roles seems to have taken place recently. Each update of the IMF's World Economic Outlook has lowered its earlier estimate in the last few years except the January 2014 update of the World Economic Outlook. While China's projections have been lowered both for 2014 and 2015, India's performance is relatively better with projections remaining unchanged both for 2014 and 2015.

The latest update, July 2014, has lowered the global growth projection for 2014 by 0.3 percent to 3.4 percent (Table 1.1), reflecting both the legacy of the weak first quarter, particularly in the United States, and a less optimistic outlook for several emerging markets. With somewhat stronger growth expected in some advanced economies next year, the global growth projection for 2015 remains at 4 percent. Global growth is expected to rebound from the second quarter of 2014, as some of the drivers underlying first quarter weakness, such as the inventory correction in the United States, should have only temporary effects, and others should be offset by policies, including in China. However, increased geopolitical risks could lead to higher oil prices and global growth could be weaker for longer, given the lack of robust momentum in advanced economies despite very low interest rates and the easing of other brakes to the recovery. In some major emerging market economies, the negative growth effects of supply-side constraints and the tightening of financial conditions over the past year could be more protracted.

**Table 1.1 GDP Growth and Trade**

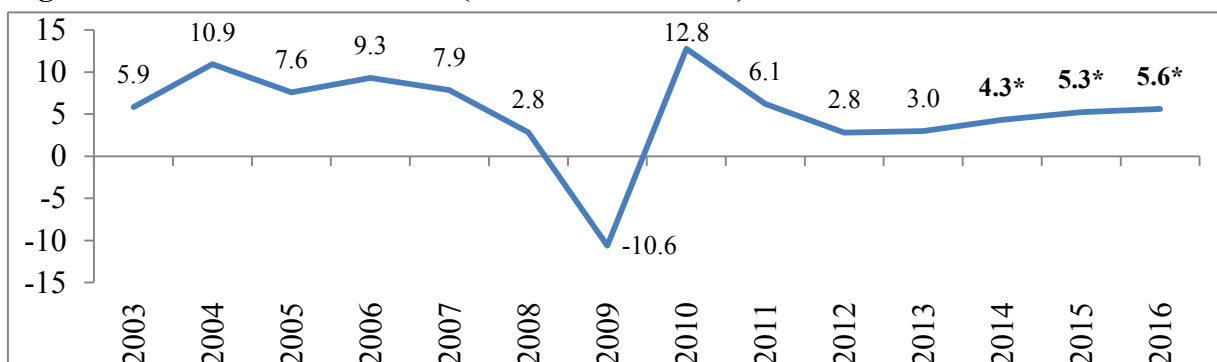
	Actuals		Projections		Diff. from April 2014 Projections	
	2012	2013	2014	2015	2014	2015
World Output	3.5	3.2	3.4	4.0	-0.3	0.0
Advanced Economies	1.4	1.3	1.8	2.4	-0.4	0.1
United States	2.8	1.9	1.7	3.0	-1.1	0.1
Euro Area	-0.7	-0.4	1.1	1.5	0.0	0.1
Emerging Mkt. and Developing Economies (EMDEs)	5.1	4.7	4.6	5.2	-0.2	-0.1
Emerging and Developing Asia	6.7	6.6	6.4	6.7	-0.2	-0.1
China	7.7	7.7	7.4	7.1	-0.2	-0.2
<b>India</b>	<b>4.7</b>	<b>5.0</b>	<b>5.4</b>	<b>6.4</b>	<b>0.0</b>	<b>0.0</b>
<b>World Trade Volume</b>	<b>2.8</b>	<b>3.1</b>	<b>4.0</b>	<b>5.3</b>	<b>-0.3</b>	<b>0.0</b>
Imports- Advanced Economies	1.1	1.4	3.5	4.6	0.0	0.1
EMDEs	5.7	5.7	4.7	6.4	-0.3	0.1
Exports *- Advanced Economies	2.1	2.3	4.2	4.8	0.2	0.1
EMDEs	4.2	4.4	5.0	6.2	-0.4	-0.1

Source: IMF, World Economic Outlook Update, July 2014. Note: \* -based of IMF WEO, April 2014

### 1.1.2 World Trade performance

World Trade volume projections have been lowered by 0.3 percentage points to 4.0 per cent for 2014 due to the lowering of projections for EMDEs. For 2015 and 2016 it is projected to be better at 5.3 per cent and 5.6 per cent respectively (Figure 1.1)

**Figure 1.1 World Trade Volume (Goods and Services) Growth**



Source: Based on IMF's WEO, April 2014 database. Note: \* indicates projected figures

### 1.1.3 Monthly Trade performance of some Trading Partner countries of India

**Exports:** Monthly export growth rates of some trading partner countries of India show a revival in USA, EU, China and Singapore in the last three months. However, export growths were negative or low in Hong Kong and Japan in the last three months (Table 1.2).

**Imports:** There has been low to moderate import growth in USA and EU in the last three months. However import growth was negative or low in China, Singapore, Japan and Hong Kong in the recent few months.

**Table 1.2 Monthly Exports & Imports Growth of selected Trade partners of India**

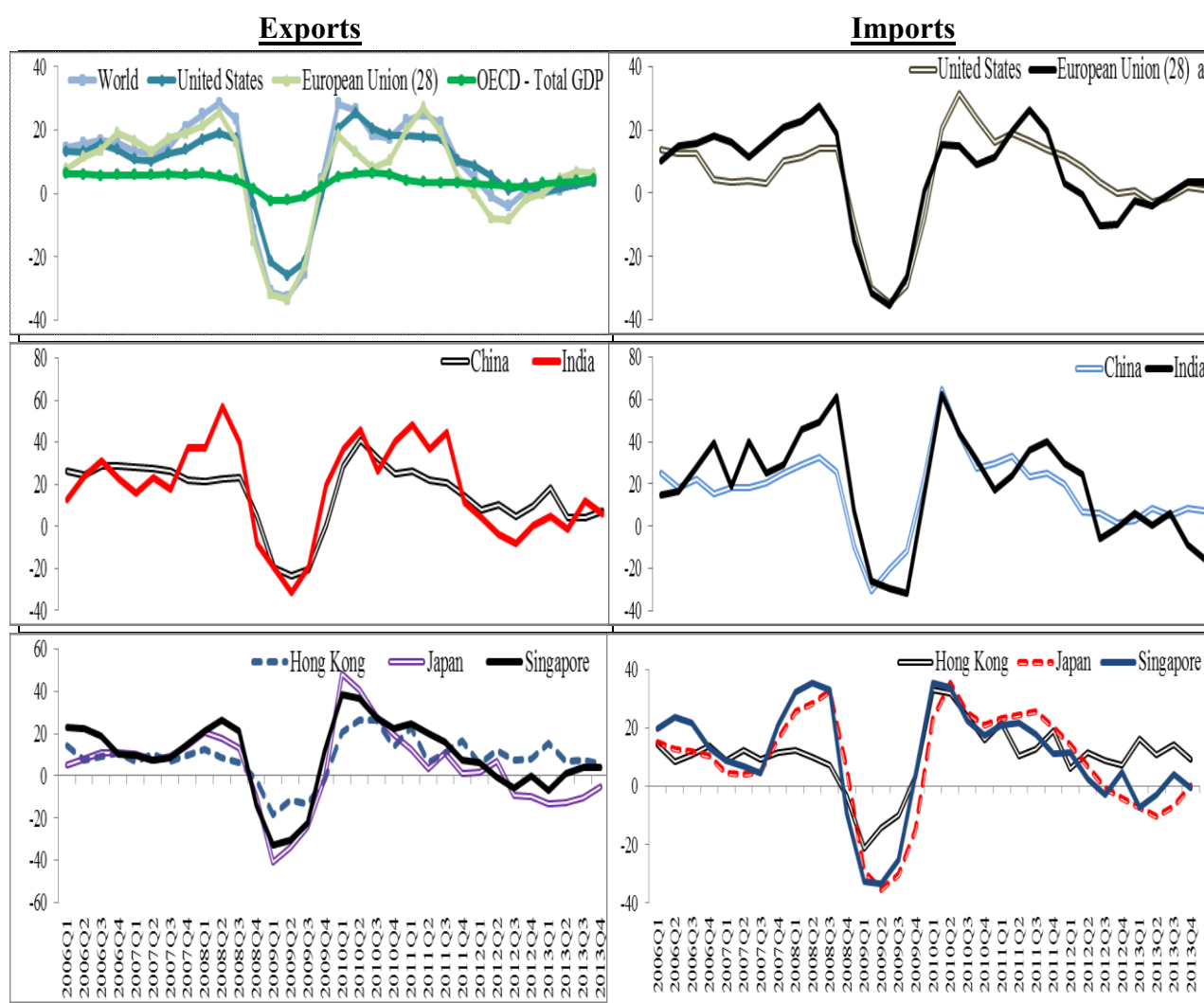
Months	USA		EU (28)		China		Hong Kong		Japan		Singapore	
	Export	Import	Export	Import	Export	Import	Export	Import	Export	Import	Export	Import
2013m1	4.5	1.0	6.9	4.4	25.0	29.6	23.4	26.2	-8.2	-7.5	4.5	1.0
2013m2	-0.1	-0.7	-1.1	-4.9	21.8	-15.0	-4.2	-9.3	-18.3	-5.9	-0.1	-0.7
2013m3	-2.5	-7.8	-4.6	-10.1	10.0	14.1	40.9	32.2	-12.1	-8.3	-2.5	-7.8
2013m4	1.6	0.7	7.4	1.1	14.6	16.6	18.0	12.2	-13.4	-8.8	1.6	0.7
2013m5	1.3	-0.8	2.6	-2.8	0.9	-0.5	10.4	9.1	-13.2	-13.3	1.3	-0.8
2013m6	1.7	-3.6	4.2	1.3	-3.1	-0.8	10.1	10.3	-12.5	-9.0	-1.8	-8.3
2013m7	4.9	2.4	9.9	7.3	5.1	10.9	18.0	15.6	-11.2	-5.2	4.6	5.5
2013m8	3.1	-0.9	2.9	-0.5	7.1	7.2	11.3	18.7	-7.9	-6.6	1.8	1.0
2013m9	0.2	3.4	7.5	3.5	-0.4	7.5	8.4	8.2	-12.3	-8.1	5.7	5.9
2013m10	6.4	3.2	6.4	2.7	5.6	7.5	20.5	15.2	-4.3	1.9	6.4	2.7
2013m11	4.7	-2.9	3.3	1.8	12.7	5.3	10.1	11.1	-4.2	-1.9	-1.0	-5.1
2013m12	0.9	3.1	10.2	6.7	4.1	8.3	2.1	1.6	-6.8	0.8	5.6	0.3
2014m1	3.6	-0.2	3.7	2.7	10.6	10.0	2.4	7.6	-6.1	7.3	0.6	-4.4
2014m2	0.2	-0.4	5.2	4.2	-18.1	10.0	-2.0	8.7	0.1	-0.6	8.6	4.2
2014m3	3.8	6.5	6.4	9.6	-6.6	-11.3	-11.7	-9.6	-5.6	9.6	6.1	13.4
2014m4	3.4	5.2	3.9	6.0	0.8	0.8	-8.2	-4.1	0.1	-1.5	4.1	4.3
2014m5	3.9	1.8	3.4	7.4	7.0	-1.5	-3.1	-6.9	-3.4	-4.2	-1.5	1.8
2014m6	2.7	6.7	3.6	5.2	7.2	5.6	2.7	-4.4	-6.5	3.4	4.7	1.6
2014m7	--	--	--	--	14.5	-1.5	--	--	--	--	0.5	-1.5

Source: Based on WTO database

### 1.1.4 Quarterly Export and Import Growth: India and major Trade Partners

The movements in quarterly world GDP growth (given by the proxy of OECD GDP growth) and the growth of exports and import of India and its major partner countries show a similar movement since 2006 Q1 indicating that export/import growths of different countries move in tandem with the world economic situation and world GDP (Figure 1.2).

**Figure 1.2 Export and Import Growths (Quarterly): World, US, EU, India, China, Hong Kong, Singapore, Japan and GDP growth of OECD**



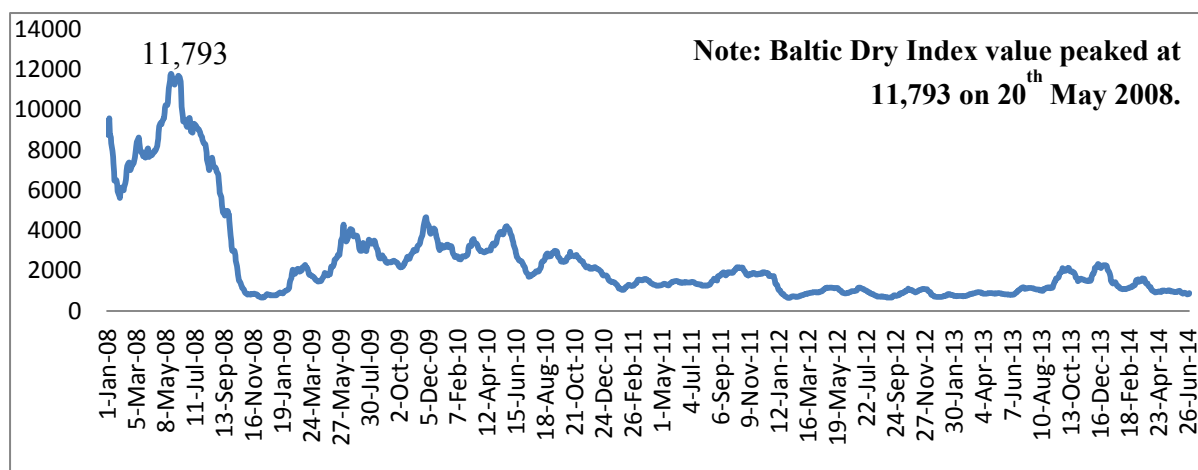
Source: Based on WTO and OECD database

### 1.1.5 The Baltic Dry Index (BDI)

The Baltic Dry Index (BDI) a good proxy for the robustness of world trade is in the red. After falling from the peak of 11793 on 29<sup>th</sup> May 2008 and reaching a low of 663 on December 8, 2008, it picked up in some months in 2009-10 and 2013. It is once again in one of the lowest phases since the 2008 global financial crisis with sub 1000 indices reaching 755 on 16<sup>th</sup> July 2014 (Figure 1.3). Thus the international trade situation is still fragile.



**Figure 1.3 The Baltic Dry Index (BDI) Close**



Source: Based on data extracted from [www.y-charts.com](http://www.y-charts.com)

## **1.2 Trends in India's Exports**

### **1.2.1 Export Growth**

India's exports have increased over the last two decades, from US \$17.9 billion in 1991-92 to US \$83.5 billion in 2004-05 and further to US \$312.6 billion in 2013-14. Similarly, the share of India's merchandise exports in the world exports has increased from 0.5 per cent in 1991 to 0.8 per cent in 2004 and 1.7 per cent in 2013. India's greater integration with the world economy was reflected by the trade openness indicator, the merchandise trade to GDP, which increased from 14.3 percent of GDP in 1991-92, to 28.2 in 2004-05 and further to 41.8 percent of GDP in 2013-14.

During the five-year period 2004-05 to 2008-09, India's merchandise exports grew at a compound annual growth rate (CAGR) of 23.8 per cent compared to the 14.0 per cent of the preceding five-year period. As a result of global financial crisis, export growth in 2009-10 was negative at (-) 3.6 percent and during the period 2009-10 to 2013-14, it grew by a CAGR of only 15.0 per cent. This low growth was a result of both external factors like low global demand and domestic factors like infrastructural bottlenecks and policy constraints.

In the last five years, India's export growth has seen ups and downs, being in negative territory twice in 2009-10 as an aftershock of the 2008 crisis and in 2012-13 as a result of the euro zone crisis and global slowdown. India's exports were US\$ 312.6 billion against a target of US\$ 325 billion during 2013-14, though they grew by a positive 4.1 per cent as compared to the negative growth of 1.8 per cent during the previous year. Monthly export growth rates have seen many ups and downs in 2013-14. After being in double digits continuously for four months from July to October 2013, they decelerated to single digit for three months from November 2013 to January 2014, remained in negative territory in the next two months, and ended with a positive but low growth of 4.1 per cent for the full year. In April 2014, export growth was slightly better at 5.3 per cent and with the 12.4 per cent growth in May 2014, double-digit growth is back after a gap of six months, though it is on a low base. Exports registered double digit growth for the second successive month in June 2014 at 10.2 per cent over June 2013. However, in July 2014 it was slightly lower at 7.3 per cent. Export growth during 2014-15 (April-July) was at 8.6 per cent over the same period of previous year.

### **1.2.2 Composition of Exports**

Noticeable compositional changes have taken place in India's export basket over the last 15-20 years with petroleum products coming to the top position among the top 6 export sectors with 20.1 per cent share in 2013-14 and textiles relegated to the sixth position with 9.7 per cent share. While engineering exports and agriculture and allied export gained in strength, gems and jewellery sector has lost some of its shine (Table 1.3). However, the top 6 sectors— petroleum products, engineering goods, chemicals and related products, gems and jewellery, textiles and agriculture and allied sector continue to dominate India's export basket, accounting for nearly 87 per cent of total exports of India in 2013-14, which is near to the 82 per cent in 2004-05. Electronic goods, an important item in world exports still has a small share of 2.5 per cent. This calls for further diversification of India's export basket.

**Table: 1.3 Share and growth of exports**

Commodity	Share			CAGR		
	2004-05	2008-09	2013-14	2004-05 to 2008-09	2009-10 to 2013-14	2004-05 to 2013-14
a) Plantation	0.8	0.6	0.5	13.7	10.9	10.5
b) Agri. & allied products	7.5	7.1	10.3	23.3	26.5	19.9
c) Marine products	1.7	1.2	1.6	1.6	24.4	14.9
d) Ores & minerals	6.1	4.9	1.8	11.7	-10.5	1.1
e) Leather and manufactures	2.9	1.9	1.8	10.3	14.0	10.0
f) Gems & jewellery	16.5	16.3	13.1	19.9	9.0	12.9
g) Sports goods	0.1	0.1	0.1	9.2	13.8	9.8
h) Chemicals & related products	15.8	13.7	14.0	16.3	15.7	14.3
i) Engineering goods	18.4	18.2	19.7	27.4	17.3	16.7
j) Electronic goods	2.3	3.1	2.5	39.5	8.1	16.9
k) Project goods	0.1	0.1	0.0	17.3	-21.2	-6.8
l) Textiles	15.5	10.7	9.7	10.6	12.2	10.0
m) Handicrafts	0.5	0.1	0.1	-5.3	5.3	-3.4
n) Carpets	0.8	0.4	0.3	5.4	8.9	5.6
o) Cotton raw incl waste	0.1	1.1	1.2	61.8	15.3	50.0
p) Petroleum products	8.4	15.8	20.1	40.9	22.1	27.6
<b>Total Exports</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>22.0</b>	<b>15.0</b>	<b>15.8</b>

### **1.2.3 Country-wise performance of different sectors**

Although, the top 6 commodities of exports accounted for more than 80 per cent in 2004-05 and 2013-14, there is a considerable change in the destination-wise composition of exports. Commodity wise analysis shows that the share of USA has increased substantially in the last five years in India's export of the three categories — primary products, manufactures and petroleum crude & products. In the case of India's exports to EU, the shares have fallen in petroleum crude & products, while the other two sectors have seen ups & down. In the case of India's exports to China, the share of primary products have fallen mainly due to fall in exports of ores and minerals, while there is marginal increase in share of manufactures. The share of China in India exports of petroleum crude & products is still very small. The share of rest of the world has increased mainly in India's exports of primary commodities.

**Table 1.4 Share of different markets in commodity specific exports**

		Share			CAGR 2007-08 to 2011-12	Growth rate	
		2007-08	2010-11	2013-14		2012-13	2013-14
<b>I Primary Products</b>	World	100	100	100	16.3	1.1	4.7
	USA	5.9	6.1	9.6	35.7	16.4	-20.2
	EU	12.8	11.5	11.9	11.9	4	10.1
	China	23.4	24.2	10.7	5.3	-41.9	-10.2
	Rest of the World	57.8	58.2	67.9	20.4	14.1	11.5
	<b>(a) Agri &amp; Allied Products</b>	100	100	100	23.4	9	5.1
	USA	7.2	7.3	9.9	43.1	15.5	-21.8
	EU	15.4	13.4	11.9	13.5	7.9	11.3
	China	4.4	10.6	6.6	31.3	-31.6	-13
	Rest of the World	73.1	68.7	71.6	21.6	16.1	11.6
	<b>(b) Ores and minerals</b>	100	100	100	-1.4	-33.6	1.4
	USA	3.1	2.7	6.7	-4.9	30.6	2.6
	EU	7.1	6.2	12.2	4.9	-16.3	2.4
	China	66.2	62.8	41	-5.5	-51.3	-6.6
	Rest of the World	23.6	28.3	40.1	10.6	-7.1	10.5
<b>II Manufactured goods</b>	World	100	100	100	18	-5.5	4.6
	USA	14.9	12.8	15.2	12.3	0.5	6.3
	EU	24.4	19.2	21.8	11.1	1.8	8.4
	China	2.3	3.8	4.4	29.5	4.7	18
	Rest of the World	58.3	64.3	58.6	21.8	-9.7	2
	<b>(a) Textiles incl. RMG</b>	100	100	100	10	-0.8	14.6
	USA	20.5	19	18.3	4.5	5.8	7
	EU	37.7	32.9	31.3	6.6	-3	13.5
	China	0.7	1.9	6.9	62.4	77.8	59.9
	Rest of the World	41	46.1	43.4	13.9	-6.7	13.6
	<b>(b) Gems &amp; Jewellery</b>	100	100	100	22.9	-3.2	-5.4
	USA	16.4	13	19	8	-0.4	15.4
	EU	11.6	7.8	9.5	16.6	-26.3	10.3
	China	2.7	0.2	0.3	35.9	-26.2	43.2
	Rest of the World	69.3	79	71.2	28.7	-0.3	-11.5
	<b>(c) Engineering Goods</b>	100	100	100	14.7	-2.7	8.8
	USA	12.6	10.3	10	12.1	-7.4	-2.7
	EU	25	19.4	20.8	8.5	9.2	6.3
	China	2.2	8	5.8	36.6	-11.8	20
	Rest of the World	60.1	62.3	63.4	16.1	-4.6	10.8
	<b>(d) Chemical &amp; Related Products</b>	100	100	100	15.1	5.3	5.9
	USA	13.8	15.5	16.9	20.6	11.5	6.7
	EU	22.6	20.5	22.8	11.7	19.8	5.8
	China	2	5.1	4.7	28.4	-0.5	-3
	Rest of the World	61.6	58.9	55.7	14.1	-0.8	6.5
	<b>(e) Leather &amp; leather mnfrs</b>	100	100	100	8.2	2	16.7
	USA	10.1	8.8	11.7	9.1	19.7	27.2
	EU	65.1	65.2	60.5	7.6	-2.5	15.4
	China	1.4	1.9	2.7	22.6	-0.3	23.4
	Rest of the World	23.5	24	25.1	8.3	7.2	14.8
	<b>(f) Handicrafts (incl. carpet)</b>	100	100	100	-5.9	5.7	10.9
	USA	32.4	32.1	36	-3.9	13.4	-1.3
	EU	41.1	34	40.1	-7.8	11.2	23.3
	China	0.5	0.5	0.9	20.4	-21	44.3
	Rest of the World	25.9	33.4	23.1	-6.4	-10.8	11.8
<b>III Petroleum, crude &amp; products</b>	World	100	100	100	18.4	8.8	4.2
	USA	0.6	2.2	6.1	16.3	45.8	121.2
	EU	15.2	20.5	13.8	18.7	31.5	-13.7
	China	0.4	1.9	1.6	62.3	-71.5	225
	Rest of the World	83.8	75.3	78.5	17.9	6	2.3
<b>Total Exports</b>	World	100	100	100	17	-1.8	4.1
	USA	11.4	10.1	12.5	13.8	4.1	8.3
	EU	21.2	18.3	16.5	11.1	-4.1	2.2
	China	5	6.2	4.8	13.6	-25.1	9.5
	Rest of the World	62.3	65.4	66.2	19.9	-0.2	3.4

Among manufactured goods, the share of textiles has fallen in the case of India's exports to US, EU and Rest of the world. However there is a noticeable increase in the share to China. In the case of Gems & Jewellery, the share of US has increased and in engineering goods, the share of both US and EU have fallen in the last five years. While the share of China has increased despite some ups & downs and the rest of the World, with a major share has registered marginal increase. The exports share of Chemicals & products increased both to US and EU, while the export share of leather & leather manufactures fell to its major market—the EU, though it increased marginally to USA. Thus, compositional shifts have taken place in India's exports to major markets.

### **1.2.4 Sectoral Performance of exports in 2013-14**

The recent sectoral performance of exports shows that while many sectors were in the negative growth zone in 2012-13, in 2013-14, except gems and jewellery and electronic goods all other major sectors have moved to positive growth territory (Table 1.5).

**Table 1.5 Exports: Sectoral Performance**

	2012-13	2013-14	2014-15 ( April)
Positive Growth	1. Project goods (75.4) { 0.1} 2. Agri & allied prdts (16.7) {10.7} 3. Carpets (16.6) {0.3} 4. Petroleum products (8.6) {20.3} 5. Chemicals & related products (5.4), {13.8} 6. Leather & mnfrs (1.6) {1.6} 7. Marine products (0.6) {1.2}	1. Marine products (44.8) {1.6} 2. Handicrafts (36.0) {0.1} 3. Leather & mnfrs (16.5) {1.8} 4. Textiles (15.2) {9.7} 5. Sports goods (14.4) {0.1} 6. Engineering goods (8.5) {19.7} 7. Chemicals & related products (5.4) {14.0} 8. Carpets (5.0) {0.3} 9. Petroleum products (3.0) {20.1} 10. Agri & allied prdts (0.8) {10.3}	1. Marine products (42.2){1.5} 2. Leather(30.4){1.8} 3. Engineering goods (21.2){22.3} 4. Ores and minerals (11.1){2.0} 5. Textiles (1.0) {10.9} 6. Chemicals and related products (7.7){10.8} 7. Electronic goods(3.6){2.1} 8. Petroleum products(0.7){20.1}
Negative Growth	1. Sports goods (-1.8), {0.1} 2. Engineering goods (-3.0), {18.9} 3. Textiles (-3.1) {8.8} 4. Gems & jewellery (-3.4) {14.4} 5. Plantation (-3.8) { 0.6} 6. Electronic goods (-9.9) { 2.8} 7. Cotton raw incl waste (-13.4) {1.3} 8. Handicrafts (-27.2) {0.1}) 9. Ores & minerals (-33.0) {1.9}	1. Ores & minerals (-0.5) {1.8} 2. Cotton raw incl waste (-3.3) {1.2} 3. Gems & jewellery (-5.2) {13.2} 2. Plantation (-8.2) {0.5} 3. Electronic goods (-8.9) {2.5} 4. Project goods (-72.8) {0.01}	1. Agriculture and allied products (-2.2){6.7} 2. Gems and Jewellery (-8.1){12.8}
Overall Exports Growth	(-1.8) {100 }	(4.1) {100}	(5.3){100}

*Source:* Based on M/o Commerce Database,

*Note:* Figures in first ( ) brackets indicates growth rate y-o-y, figures in second brackets { } indicates share to total exports

One interesting feature of the sectoral performance of exports is that many labour-intensive export sectors have performed relatively well in 2013-14. Textile exports grew by 14.6 per cent in 2013-14. The EU and USA accounted for nearly half of India's total textile exports and growth of our textile exports to these markets was 13.5 per cent and 7.0 per cent respectively in 2013-14. Another development is India's growing textile exports to China with China's share increasing from around 2 per cent in 2010-11 to 5 per cent in 2012-13 and further to 7 per cent in 2013-14. Export growth of another labour-intensive sector, leather and leather manufactures, was high at 16.7 per cent. Nearly 72 per cent of total leather exports was to the EU and USA in 2013-14 with growths of 15.4 per cent and 27.2 per cent respectively. Growth of exports of handicrafts including carpets was also in double digits at 10.9 per cent, though its share in total exports was only 0.4 per cent in 2013-14.

### 1.3 Trends in India's Imports

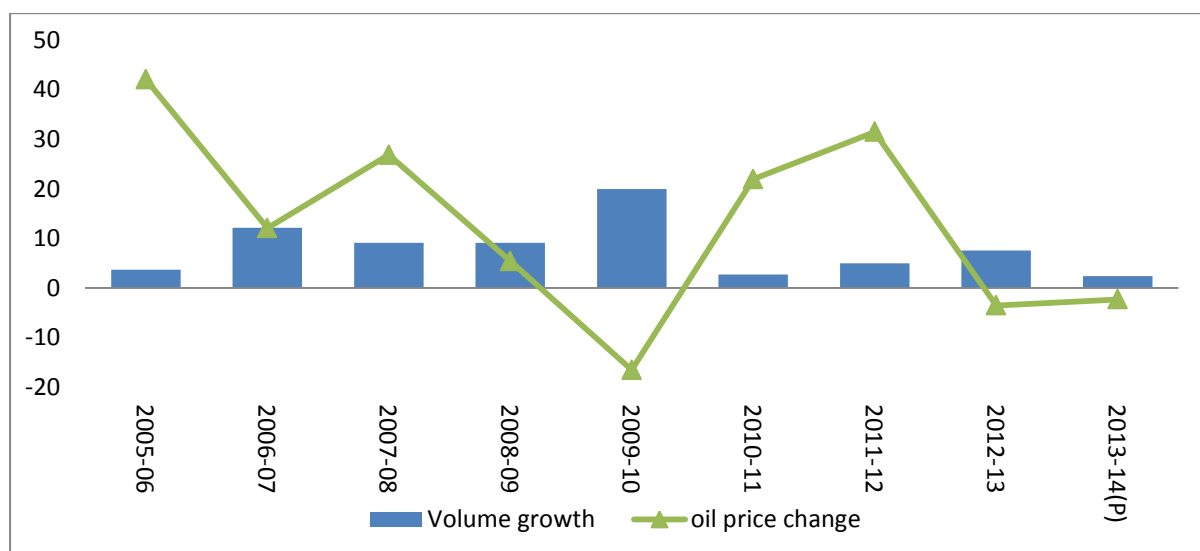
#### 1.3.1 Import Growths:

Import growth decelerated sharply from 32.3 per cent in 2011-12 to 0.3 per cent in 2012-13 and fell to a negative -8.3 per cent in 2013-14, owing to fall in non-oil imports by 12.8 per cent. In 2014-15 (April-July), import growth has been negative at (-) 3.8 per cent. After registering negative import growth continuously for 12 months, import growth was positive in June and July 2014 at 8.3 per cent and 4.3 per cent respectively.

#### 1.3.2 Composition and sectoral performance of imports:

Petroleum, crude and products, machinery, gold and silver and electronics goods are the major items of import of India. The share of POL imports increased from 26.8 per cent to 36.7 per cent in 2013-14 and this growing share is due to moderate quantity growth and rising, though fluctuating, international oil price over the last 10 years. During the period 2004-05 to 2013-14, the value of oil imports and net oil imports grew by 20.9 per cent and 18.1 per cent respectively with oil price and quantity growing by 11.6 per cent and 7.8 per cent respectively.

**Figure 1.4 Volume growth of crude oil imports and oil price change**



Another important item of import is gold, the value of which increased gradually from US\$ 11.1 billion in 2004-05 to US \$ 29.8 billion in 2009-10 and to US\$ 42.6 billion in 2010-11, jumped suddenly to US \$ 61.6 billion in 2011-12, but declined to US \$ 55.8 billion in 2012-13. High growth in the value of gold and silver imports is one of major reasons for India's higher trade deficit and current account deficit for 2011-12 and 2012-13. On the back of several measures taken by the government, value of gold and silver imports fell by 40.1 per cent to US\$ 33.4 billion in 2013-14.

Capital goods imports including machinery with shares of 13.0 per cent, 15.5 per cent and 11.9 per cent in 2004-05, 2008-09 and 2013-14 respectively grew by 39.3 per cent, (-) 3.9 per cent and (-) 14.7 per cent respectively. The negative growth of capital goods imports in 2013-14, as in 2012-13 is a cause for concern. Within capital goods, import growth of machinery except electrical and machine tools and transport equipment fell by more than 10 per cent in 2013-14. However, the quantum of capital goods imports has actually increased in 2012-13 (Table 1.6).

**Table 1.6 Share and growth of some select items of imports**

Commodity	Share			CAGR		
	2004-05	2008-09	2013-14	2004-05 to 2008-09	2009-10 to 2013-14	2004-05 to 2013-14
Fertilizers	1.2	4.5	1.4	77.6	-1.3	18.8
Edible Oil	2.2	1.1	2.1	8.3	13.6	15.9
Non-ferrous metals	1.2	2.0	1.2	46.4	16.1	17.2
Metalliferous ores & products	2.2	2.7	3.0	34.4	15.0	20.8
Iron & Steel	2.4	3.1	1.8	37.4	-1.0	12.8
Petroleum crude & products	26.8	30.8	36.7	33.1	17.3	20.9
Pearls, precious & semi-pre stones	8.4	5.5	5.3	15.6	10.2	10.9
Machinery	11.6	13.5	10.0	33.4	5.6	14.8
Coal, coke & briquettes	2.9	3.3	3.7	33.2	16.3	19.9
Organic & Inorganic chmls.	5.1	4.1	4.5	21.4	14.1	15.1
Artf.resins, etc.	1.3	1.3	2.0	28.6	16.2	22.6
Electronic goods	9.0	7.7	6.9	23.8	10.3	13.4
Gold & Silver	10.0	7.4	7.4	19.1	2.9	13.0
<b>Total Imports</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>28.5</b>	<b>11.8</b>	<b>16.8</b>

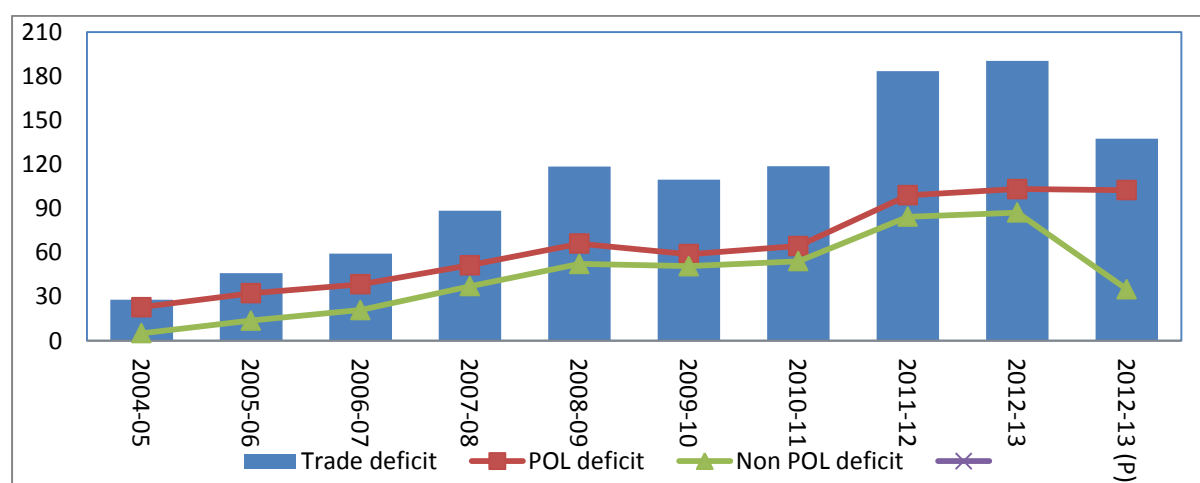
## 1.4 Trade Deficit

India's trade deficit has been increased steadily from US\$ 28.0 billion in 2004-05 to US\$ 118.4 billion in 2008-09 and it moderated to US\$ 109.6 billion in 2009-10. This moderation was due to decline in the value of oil imports by (-) 7.0 per cent, caused by fall in international oil price by (-) 16.5 per cent in 2009-10. In 2011-12, trade deficit increased to US\$183.4 billion from US\$ 118.6 billion in 2010-11, due to high growth of oil imports (46.2 per cent) and gold silver imports (44.7 per cent). Similar trend continued in 2012-13 with some moderation in the growth of gold and silver imports (-9.5 per cent).

The sharp fall in imports and moderate export growth in 2013-14 resulted in a sharp fall in India's trade deficit by 27.8 per cent. In absolute terms, trade deficit fell to US\$ 137.5 billion from US\$ 190.3 billion during 2012-13. However, there was not much change in the POL deficit which was hovering at around US\$100 billion in the last two years. With the fall in imports of both gold and capital goods, non-POL deficit fell sharply to US\$ 35 billion in 2013-14 from US\$ 87.2 billion in 2012-13 (Figure 1.5)

In 2014-15 (April-July), trade deficit fell by 24.4 per cent mainly due to the fall in gold and silver imports. After falling almost continuously for 11 months, trade deficit rose marginally by 4.3 per cent in June 2014, but again fell marginally in July 2014 by 2.1 per cent.

**Figure 1.5 Trade deficit (US\$ billion)**



### 1.4.1 Bilateral Trade Deficit

Concerns have increased on the bilateral trade deficit front with India's high and growing trade deficits with countries like China and Switzerland. During 2012-13, India's bilateral trade deficit with China and Switzerland are US \$ 38.7 billion and US \$ 31.1 billion respectively. In 2013-14, trade deficit with Switzerland has fallen sharply by 43.3 per cent while trade deficit with China fell marginally by 6.6 per cent.

**Table 1.7 : India's Bilateral Trade Balance**

	Countries	Value ( US \$ billion)			% Change(Y-o-Y) 2013-14(P)
		2011-12	2012-13	2013-14(P)	
<b>Top 5 Surplus</b>	U S A	11.4	11.0	16.9	53.8
	Singapore	8.5	6.1	5.7	-6.5
	Bangladesh	3.2	4.5	5.6	24.1
	Hong Kong	2.5	4.4	5.4	23.5
	Netherland	6.5	8.2	5.1	-38.3
<b>Top 5 Deficits</b>	China	-36.6	-38.7	-36.1	-6.6
	Saudi Arabia	-26.4	-24.2	-24.3	0.5
	Iraq	-18.2	-18.0	-17.6	-2.0
	Switzerland	-34.1	-31.0	-17.6	-43.3
	Kuwait	-15.2	-15.5	-16.1	3.6
<b>India's Total Trade Balance</b>		<b>-183.4</b>	<b>-190.3</b>	<b>-137.5</b>	<b>-27.8</b>

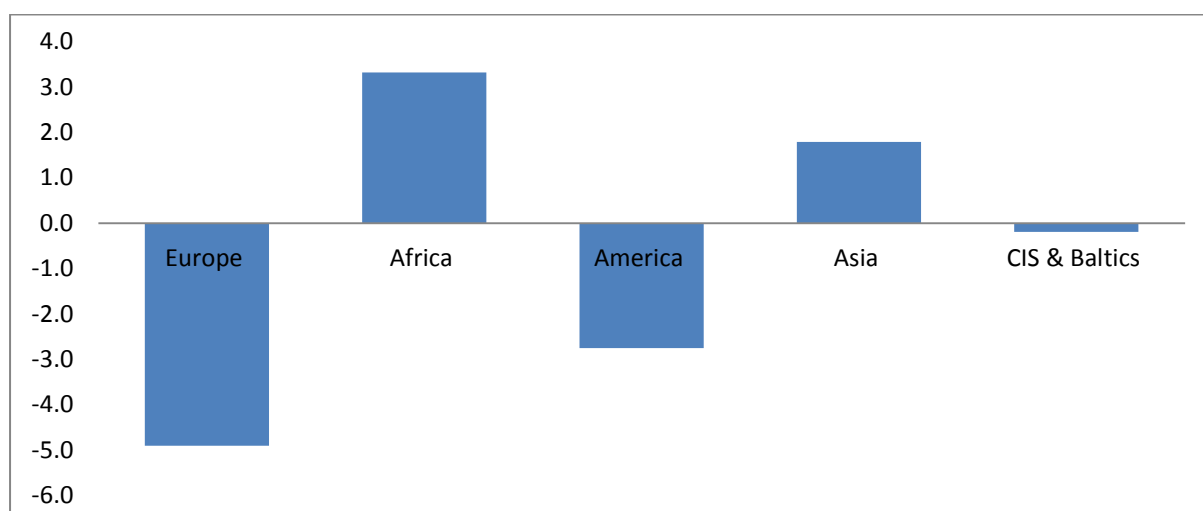
Source: Based on M/o Commerce database, P- Provisional



## 1.5 Direction of Trade

Unlike its export basket diversification, India witnessed greater diversification in its export destinations. Region-wise, there is a decline in India's exports share with respect to EU, America and CIS & Baltics. In the case of Africa and Asia, export share had increased during the period 2004-05 to 2013-14. The export share of EU and America in India's total exports which was 23.6 per cent and 20.1 per cent respectively in 2004-05 declined to 18.7 per cent and 17.4 per cent respectively in 2013-14. The share of CIS & Baltics in India's total exports which was only a little above 1 per cent witnessed a marginal decline during this period. There was substantial increase in the share of India's exports to African countries from 6.7 per cent in 2004-05 to 2013-14 (Figure 1.6). Similarly, the share of Asia has also increased from 47.9 per cent in 2004-05 to around 50 per cent in 2013-14. Within Asia, West Asia, North East Asia and ASEAN accounted for 39 per cent of total exports of India in 2013-14.

**Figure 1.6 Region-wise changes in the share of India's exports during 2004-05 to 2013-14**



In 2013-14, there was good growth of exports to North America (9.1 per cent) and Africa (7.2 per cent), low growth to Europe (4 per cent) and Asia (1.7 per cent), and negative growth to Latin America (-20 per cent) and the CIS and Baltics (-4.7 per cent). While export growth to the US was 8.3 per cent, it was just 2.2 per cent to the EU 27 as a result of the slowdown in the EU. Exports to the UAE fell to a negative -16 per cent. Exports to Asia still constitute around 50 per cent of India's exports. While India's exports to ASEAN (Association of South East Asian Nations) grew by a small 0.5 per cent, exports to South Asia grew robustly with high growths to all the four major SAARC (South Asian Association for Regional Cooperation) countries, Sri Lanka, Bangladesh, Nepal and Pakistan, besides Bhutan. There was also good export growth to China and Japan at 9.5 per cent and 11.7 per cent respectively. Region-wise, imports from all five regions declined, with the highest decline of-19.3 per cent in imports from Europe.

The share of the top 15 trading partners of India in India's trade at 58 per cent in 2013-14 was more or less the same as in earlier years. The top three trading partners of India are China, the

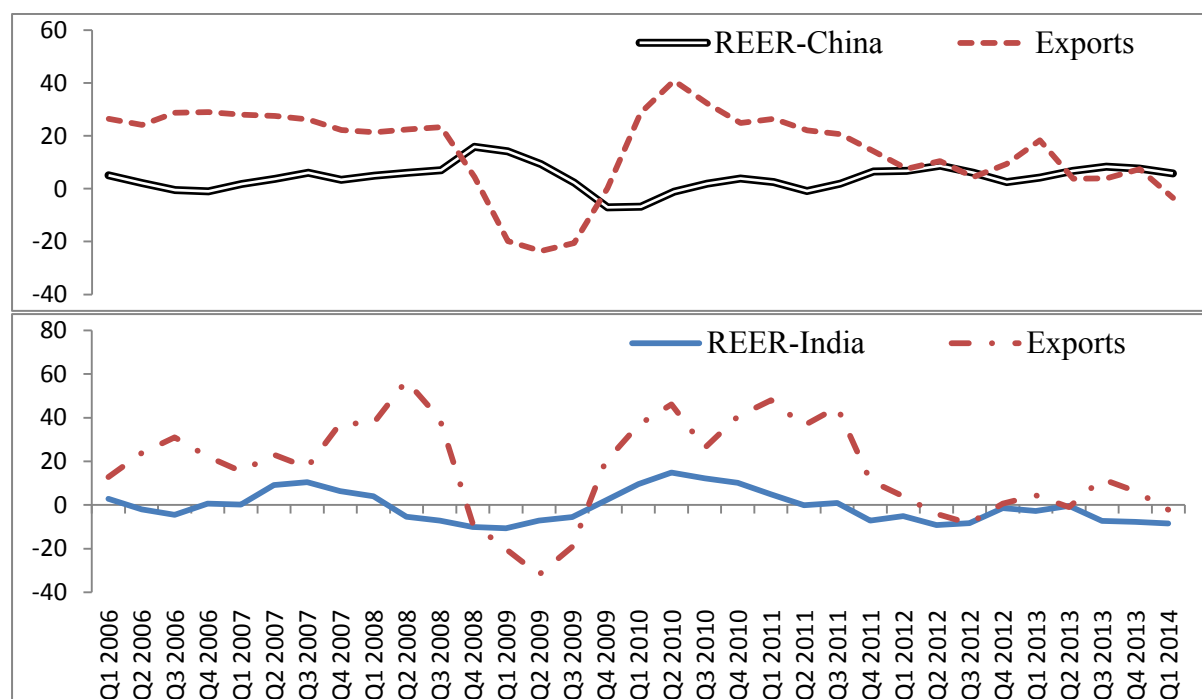
USA, and the UAE, with the top slot shifting between the three. Export import ratios reflecting bilateral trade balance show that among its top 15 trading partners, India had bilateral trade surplus with four countries, namely the USA, UAE, Singapore, and Hong Kong, in 2013-14 with high increase in the export-import ratio with the USA. India's bilateral trade deficit with Switzerland declined sharply from US\$ 31.1 billion in 2012-13 to US\$ 17.6 billion in 2013-14 owing to a fall in gold imports. India has high and rising bilateral trade deficit with China, which however fell by 6.6 per cent in 2013-14.

## 1.6 Enhancing India's export competitiveness

Whenever the issue of export competitiveness is discussed, exporters and even economists flag the issue of exchange rate of the currency and the Real Effective Exchange Rate (REER) of the rupee is considered as a measure of competitiveness of India's exports. However, the exchange rate affects India's exports in a limited way. For example, the REER (6 currency index) depreciated by 2.7 per cent, 3.4 per cent and 4.0 per cent in 2011-12, 2012-13 and 2013-14 respectively, and the 36 currency index depreciated by 2.1 per cent, 4.3 per cent and 2.2 per cent respectively while exports grew by 21.8 per cent in 2011-12, fell by 1.8 per cent in 2012-13 and grew by 4.1 per cent in 2013-14.

Even recently, since REER of India depreciated by 14.6 per cent during the period March 2011 to March 2014 while China's appreciated by 16.6 per cent during the same period, economists have started saying that the recent pick up in India's exports and the fall in Chinese exports is due to depreciation of the Indian rupee and appreciation of Yuan which is far from truth. In fact India's merchandise exports are basically dependent on World GDP/World Import growth and the effect of exchange rate is marginal. More important is the volatility in exchange rates (Figure1.7).

**Figure 1.7 Export Growth and Changes in REER Indices: China and India**



Source: Based on WTO for Exports and BIS (Bank of International Settlement) database for REER indices

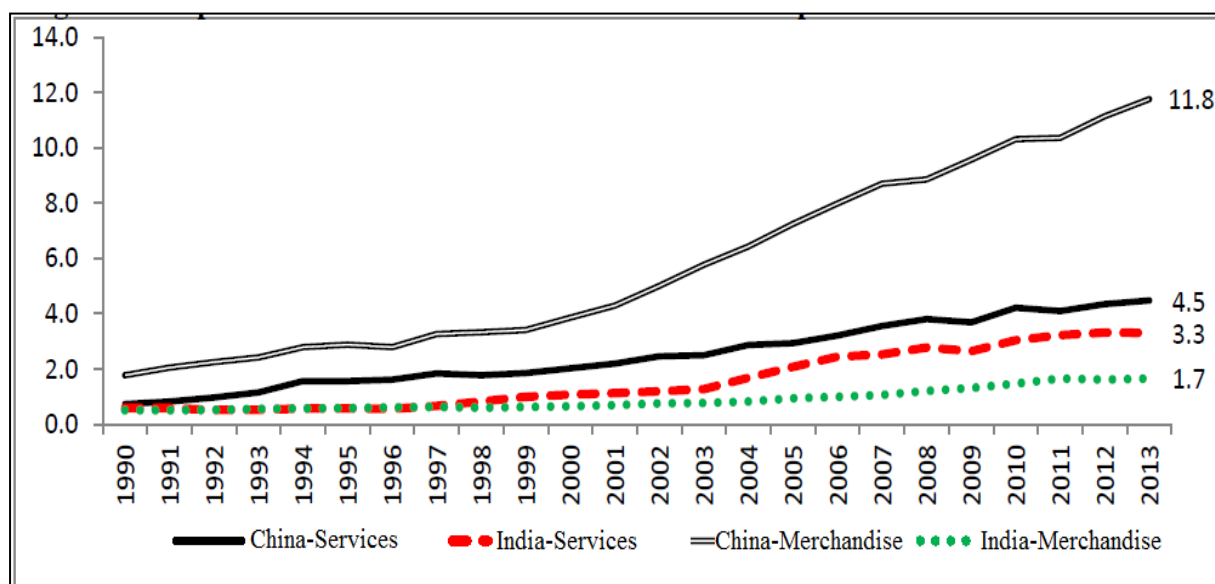
## **1.7 Export prospects**

The IMF's World Economic Outlook of April 2014 had projected world trade volume to grow from the 3.0 per cent in 2013 to 4.3 per cent in 2014 and 5.3 per cent in 2015 with a marked improvement in export and import growth of advanced countries. However the July 2014 update of WEO has scaled down the projections for 2014 to 4.0 per cent which is also in time with its fall in projections in world GDP growth. The lowering of the projections is mainly due to the lower export and import growth projections for EMDEs. The picture on the ground is also not so optimistic with the Baltic dry index (BDI), a good proxy of the robustness of world trade, being in the red. It is in one of the lowest phases since the 2008 global financial crisis with sub 1000 indices. While the international trade situation is still fragile, there was some pick-up in India's exports in April-July 2014, after five months of low/negative growth. The monthly export and import growth performance of some of the major trading countries also show some revival.

## Chapter 2 Policy Issues

While India's export growth rates (both goods and services) have been impressive before the global financial crisis, and moderate to low thereafter, the share of India's exports (merchandise) in world exports is still just 1.7 per cent in 2013. In the case of services, it is slightly better at 3.3 per cent. However, both these figures are much below our potential. The share of China is 11.8 per cent in merchandise exports and 4.5 per cent in services exports. If we compare the share of India and China in 1990 (after which economic reforms were introduced in India) and 2013 (the latest year for which data are available), India's merchandise exports share in world exports increased from 0.5 per cent to 1.7 per cent and China's share increased from 1.8 per cent to 11.8 per cent. While there is a yawning gap between India and China in goods exports, the gap is less wider in services exports. India's services export share increased from 0.6 per cent to 3.3 per cent, while China's share increased from 0.2 per cent to 4.5 per cent. These figures makes one wonder whether, India's exports have really taken off as claimed by many.

**Figure 2.1 Exports Share in World: China and India Comparison**



Source: Compiled from WTO data

Our aim should be to increase India's share in world merchandise exports from 1.7 per cent in 2013 to a respectable ballpark figure of, say, at least 4 per cent in the next five years. For this the CAGR of exports in next 5 years should be around 30 percent, which is not an impossible task. China has done it and from 2003-04 to 2007-08, India had continuously above 20 per cent annual export growth with 29 and 31 per cent growth in two years. Then, how to achieve this, is the question. Some policy issues in this regard are the following:

### 2.1 General Issues

#### 2.1.1 Product Diversification along with Market Diversification

While there has been market diversification and compositional changes in India's export basket, not much of demand-based product diversification has taken place. In the top 100

imports of the world at four-digit HS level in 2013, India has only five items with a share of 5 per cent and above. Even in this, except for diamonds (21.0 per cent) and articles of jewellery (11.2 per cent), with double-digit shares, the other three items have only around 6-7 per cent share. Most of the items in the top 100 world imports include the three Es— electronic, electrical, and engineering items—and some textiles items. Though the gain in shares of engineering goods in recent years is a positive sign, India lags behind many other competing countries. Special attention needs to be given to the electronics hardware sector which virtually collapsed with the signing of the Information Technology Agreement (ITA)-1 by India at a time when India's semiconductor sector was at a nascent stage of development, while that of newly industrialized countries (NICs) and developed countries had already taken off. Till now our focus was on exporting what we can (or supply based), now we have to shift to items for which there is world demand and we also have basic competence. A demand-based export basket diversification approach with a perceptible shift to the three Es could lead to greater dividends for India.

### **2.1.2 Export Infrastructure**

Export infrastructure, particularly ports-related infrastructure, which affects trade, needs immediate attention. Even the best of our ports do not have state-of-the-art technology as in Singapore, Rotterdam, and Shanghai. Port infrastructure issues include poor road conditions and port connectivity, congestions, vessel berthing delays, poor cargo handling techniques and equipment, lack of access for containerized cargo, and frequent EDI server down or maintenance, resulting in multiple handlings, increased lead time, high transaction costs, and thus loss of market competitiveness. Export infrastructure should be built on a war footing. Just as drastic changes have been brought about in India's airports and metro rail, sea ports should be the immediate priority. There are other issues like good roads to ports and export centres, cold storage facilities, requirements of offices and agencies related to exports in different places, etc. Some specific issues in different places are as follows:

- Deepening of drafts at berths: As fuel prices are rising and in general all cost relating to ship building are also rising, the trend worldwide is to build larger ships for getting the benefit of economy of scale. Hence nowadays worldwide the cargoes like steel are carried in handymax vsl i.e. 45000 - 52000 dwt vsl which normally needs a draft of 12 to 12.5 meters. In India, Mother Vessels seldom touch Indian ports because the turnaround time in Indian ports is rather high. Thus, exporters have to face higher freight charges as they have to use feeder vessels. Currently Mumbai port can accommodate vessels only in BPX berth where there is a draft of 10.5 meters (during monsoon this gets reduced to 10 or 10.2 meters) and two other berths in harbour wall which have a draft of 8 -8.5 meters. All the other berths inside the dock can accommodate only smaller vessels with a maximum beam of 85 feet for the vessel. Hence, exporters will have to rely on smaller vessels and thereby pay higher freight compared to their international competitors like china. Besides, whenever, the shippers try to book bigger vessels, these vessels face considerable berthing delays as they are restricted to only 3 berths which are extremely congested especially the BPX berth (deepest berth) where cargo is to be topped up. Even after waiting for this

deepest berth, the vessel has to load less than the full capacity as the draft is only 10.5 meters. So, deepening of draft at berths, entrance and main channel of Mumbai port needs to be carried out. With parcel size of vessels carrying export cargo increasing, the present draft is not sufficient to load such vessels, full load. To have better scales of economy, a minimum draft of 12 metres is needed. These suggestions made with regard to the Mumbai Port upgradation apply equally for ports in other parts of the country. In West Bengal, there is a need to speed up the “deep sea port” at Kulpi keeping in mind the cargo requirements of the country for the coming years.

- Other aspects of port infrastructure upgradation required all over India: These include the following:
  - Road conditions need substantial improvements to reduce jams and faster delivery;
  - On line tracking of container position required at all terminals of JNPT and other ports
  - Gate cut-offs should be updated on on-going basis;
  - Movement of cargo from buffer yards should be improved;
  - Agricultural cargo needs to be provided with special purpose agri jetties in ports like Kandla and Mundra to reduce ship turnaround time and improve the supply chain efficiency.
  - Deployment of shore mobile cranes: Any major engineering export port in the world has mobile cranes for loading cargo facility which is lacking in Mumbai as well as in other ports of the country. So there is a need for mobile cranes with proper and sufficient capacity for better efficiency.
- Reduction of tariff for anchorage loading: If a vessel has to load in anchorage because sufficient draft is not available at berth, the port charges stevedoring first at berth for loading cargo to barges and again charges for loading in anchorage. Thus, there is a double disadvantage for the exporters. If ports can provide proper facilities and has deep draft at berth then exporter does not have to load in anchorage. The Terminal Handling charges are also high. While the final solution lies in having ports with deeper drafts at berth, till then at least, streamlining the anchorage charges could be thought of.
- Using minor ports: A system of inland freight incentive scheme could be devised so that exporters and importers have an incentive to use minor ports or those ports whose services are not in great demand. This will ease the congestion in the major ports as well. The connectivity with inland transport networks also needs to be increased considering the increase in the volume of goods transported.
- Need for better connectivity from ports to ICDs: As there is growth in volume of traffic, better connectivity and frequency of trains from the various ICDs to the nearest ports as in the case of ICD Nagpur to JNPT is needed.
- Need to reduce inefficiency at Indian ports: Productivity in container handling of Indian ports is low compared to many other ports in the world (Table No. 10). Though

the turnaround time has fallen recently, compared to other countries it is still high. This along with few containers handled per hour, and high port charges lead to around 30 per cent higher working capital requirements in India. For some exports like engineering goods, freight rates contribute around 25-30 per cent of the total costs of exports and thus, port inefficiencies directly affect their export competitiveness.

**Table 2.1 Productivity in container handling at major ports: An international comparison**

Ports	Handling Productivity (moves per ship hour)	Throughput Per Day
<b>Chennai</b>		<b>310</b>
<b>JNPT</b>	<b>15</b>	<b>800</b>
Bangkok Laom Chabang	35	1300
Colombo	38	1400

*Source:* LBS Journal of Management & Research, 2007, Volume: 5, Issue: 1 and 2 quoting Fairplay report on Productivity in container handling at major ports: An international comparison

- Port congestion: Imports are held up due to port congestion at the JNPT Port at Mumbai. Congestion is charged at \$ 150 for 20 ft TEU and is being collected from importers on import consignments. Many vessels also by-passing the port, carrying containers to be delivered at their next voyage thereby delaying vital raw materials for the industry. Due to congestion export consignments are held up by the time the entry gates close, resulting in these export consignments being dumped in the buffer yard at a very high cost leading to delay in shipments and missing deadlines by the exporters.
- The Budget 2014-15 has announced some policies related to ports and shipping which help in improving export infrastructure and help Indian shipping. These include the following:
  - An institution to provide support to mainstreaming PPPs called 3P India will be set up with a corpus of ₹ 500 crores.
  - A policy for encouraging the growth of Indian controlled tonnage will be formulated to ensure increase in employment of the Indian seafarers.
  - Development of ports is also critical for boosting trade. Sixteen new port projects are proposed to be awarded this year with a focus on port connectivity.
  - ₹ 11635 crore will be allocated for the development of Outer Harbour Project in Tuticorin for phase I.
  - SEZs will be developed in Kandla and JNPT.
  - Comprehensive policy to be announced to promote Indian ship building industry.
  - Long term financing for infrastructure has been a major constraint in encouraging larger private sector participation in this sector. On the asset side, banks will be encouraged to extend long term loans to infrastructure sector with flexible structuring to absorb potential adverse contingencies, sometimes known as the 5/25 structure. On the liability side, banks will be permitted to raise long term funds for lending to infrastructure sector with minimum regulatory pre-emption such as CRR, SLR and Priority Sector Lending (PSL).



### **2.1.3 Focus on useful Regional Trading Arrangements (RTAs)**

Some FTAs/RTAs/CECAs of India have led to an inverted duty structure-like situation with import duty on some finished goods being nil or lower than the duty on raw materials imported from other countries. Besides, the domestic sector involving livelihood concerns has also been affected by some of them.

Some such examples are given below.

**Bangladesh:** India and Bangladesh are part of the Agreement on South Asian Free Trade Area (SAFTA) which also includes Pakistan, Nepal, Sri Lanka, Bhutan, and the Maldives; and also Asia Pacific Trade Agreement (APTA) including China, Lao PDR, Republic of Korea, and Sri Lanka. Some issues with Bangladesh are the following:

- Textiles: Bangladesh imposes high duty on imports sometimes as high as over 100 per cent (including basic customs duty, supplementary duty, VAT and advance trade VAT) from India on textile products, while India's imports from Bangladesh is at 'NIL' duty. This affect India's textile sector adversely. It is also reported that Chinese fabrics make backdoor entry from Bangladesh after conversion to garments as SAFTA rules of origin is ineffective.
- Printed materials: The import duty on printed materials (HS Codes 4819, 4820, 4821 & 49) from India has been raised to almost 90 per cent of the shipment value by Bangladesh. Indian exporters are accordingly losing out the entire business in the Bangladesh market.

**Nepal and Bhutan:** India has Indo-Nepal Treaty of Trade and India - Bhutan Agreement on Trade, Commerce and Transit with these two countries respectively. Some issues related to trade with Nepal and Bhutan are the following:

- Exports to Nepal: India gives major concessions to Nepal. But it faces many difficulties in its trade to Nepal. While there are issues like illegal imports to India with even container load of goods coming to India illegally (e.g. Arecanut), some major companies have also been facing issues related to Nepal Bank LC. This is due to different systems being adopted by various banks of Nepal due to the guidelines from The Nepal Rastrya Bank like the insistence of Nepal Banks to customize India Statutory documents like ARE-1 and HS code. Nepal Rastrya Bank vide circular no 383 (dt. 25/03/2007) and subsequent amendments in notification no 572 (dt.15/03/2012) and 573 (dt.22/04/2012) under clause 2.5.1 circular 383 NRB, for procedure related to trade in convertible foreign currency has made submission of ARE-1 compulsory. Under every LC mentioned, payment is to be made in convertible foreign currency. In commercial invoice, an equivalent value of ARE-1 named form issued by Indian Central Excise (introduced in circular 572 )or certified by manufacturer- exporter of India (introduced in circular 573) mentioning the LC number and date is to be compulsorily enclosed, without which payment will be done in Indian rupee only. This has resulted in major

anomalies and mismatches. In times of fluctuating prices the customer resorts to renegotiation of price to allow waiver. Nepal banks insist on declaring the bank negotiation exchange rate in ARE-1. However, this is not possible as ARE-1 is a statutory document by Central Excise and there is no field to mention this. Besides, Indo-Nepal treaty does not provide for furnishing of ARE-1 by Indian exporters as mandatory documents. Thus, the entire negotiating document becomes discrepant and Indian exporters are being asked to take waiver from customer and pay discrepancy fees, thus increasing transaction charges. Engineering Export Promotion Council (EEPC) India had taken up the matter with DGFT, MOF and in March, 2014, a meeting was held between Indian Embassy officials and Nepal Rashtriya Bank (NRB). At this meeting, NRB stated that ARE-1 was required by NRB to check excess dollar outflow by over-invoicing by Indian suppliers especially traders. The Indian side's contention is that since dollar trade is restricted to 160 items under India- Nepal treaty and all these are to be supplied by manufacturers/suppliers only, false declaration is not apprehended as traders are not involved. Even if it is required for submitting ARE-1, it can be done as post-verification without holding payment or making document discrepant based on it. This issue needs to be taken up formally with the Nepalese side.

- Exports to Nepal and Bhutan ( H S Codes 4819, 4820, 4821 & 49.): Presently, exports to Nepal and Bhutan made under rupee payment do not qualify for any export incentives. If this had been available, the price being offered to the customer in Nepal / Bhutan could have been made more competitive by passing on the benefits to the customer. Generally, the customers (including the Govt. agencies) in Nepal and Bhutan prefer to pay in Indian rupees to the Indian manufacturers for goods supplied to them. As against this, customers in Nepal and Bhutan can import goods from any other country at a more competitive price. Resultantly, it becomes cheaper for them to import goods from any other country rather than from India, and Indian exporters lose out in the competition. So, there is a need to consider giving incentives to exports to Nepal and Bhutan, even if the payments are received in Indian rupees. This would help exporters like printed material exporters and enable the printing industry to receive bulk printing orders from Nepal and Bhutan. However, there is a need to check if genuine exports take place and exporters do not resort to gaining benefits through hawala or other means.

**Japan:** India has a comprehensive economic partnership agreement (CEPA) with Japan. Some issues with Japan are the following:

- Annual tariff rate quota of Japan: Import of footwear into Japan is regulated by annual tariff rate quota which is calculated on the basis of 12,019,000 pairs and taking into consideration the imported quantity in the preceding fiscal year, international market situations and other relevant conditions. As a result the import duty is 17.3 per cent to 24 per cent for import duty within quota and 30 per cent for import duty or rate of Japanese yen 2400/4300/4800 per pair outside quota. Since

tariff concessions for most of the footwear are not included under Indo – Japan comprehensive economic partnership agreement, Indian footwear is subject to quota and higher import duties. Japan’s annual import of footwear is US\$ 5062 million whereas India’s exports to Japan is only US\$ 12.47 million, with a share of 0.24 per cent. So there is a need to negotiate on the removal of tariff quota and inclusion of all categories of footwear for duty concession under Indo – Japan CEPA.

There are also issues with some other non FTA/RTA countries where Indian Exporters face discrimination. Some examples are given below:

**China:** India and China do not have any FTA or PTA, but are part of the Asia Pacific Trade Agreement (APTA) (Bangladesh, China, India, Lao PDR, Republic of Korea, and Sri Lanka). Some issues are the following.

- Cashew nuts: Indian Cashew nut exports to China face 10 per cent import duty whereas, Vietnamese exports enjoy ‘Nil’ duty.
- Oilseeds: India is one of the most cost-efficient exporters of oilseeds in world markets. India has established its position as the largest exporter of Sesame seed, accounting for a share of 19.8 per cent global sesame seed exports. China is one of the key markets for Sesame seed. Over the past few years China’s imports accounted for about 30 – 35 per cent of the global trade. Though India is the largest exporter of Sesame seed, its share in China’s imports is very low (less than 1 per cent as per UN COMTRADE data). The competitive edge of Indian Sesame seed gets blunted due to the zero duty access provided by China to competing countries. Several African countries enjoy zero duty access for their products when imported into China. Similarly, duty free access is given to the competing countries for groundnut which also hampers the competitiveness of the Indian industry. There is a need to negotiate with China to extend duty free access to exports of oilseeds (specially sesame seeds and groundnuts) from India.
- Gelatin: Though China regularly exports gelatin to India it has banned import of gelatin (H S Code 0506 & 3503) from India. The export of gelatin (including its raw materials, crushed bones and ossein) is subject to quality control and inspection prior to export as per order S.O 725(E) and notification S.O 726 (E) dated 3rd April 2012 of Ministry of Commerce, GOI. The above regulations specifies the type of quality control, inspection and monitoring which shall be applied to gelatin including its raw materials, crushed bones and ocean, (from sourcing of raw materials to finished product) prior to export. In spite of compliance with the above regulations, China a big market for gelatin does not allow import of gelatin from India manufactured by the plants approved by the competent authority in terms of the provisions of the above order and notification. No other country has imposed ban on the import of gelatin from India.

**Turkey:** India does not have any trade agreement with Turkey. Some issues with Turkey include the following:

- **Footwear:** Turkey has quantitative quotas on footwear imports. For India, the annual quota is 801,789 pairs and import is permitted only against licence from Turkish Importation General Directorate. Turkey's annual import of footwear is US\$ 815 million whereas India's exports is only US\$ 2.50 million, resulting in a share of only 0.3 per cent. Thus, there is a need to negotiate with Turkey to relax the quotas.

The above is a sample list of issues with different countries which need to be taken up with them at bilateral and multilateral forums. Meanwhile, India's push towards regional and bilateral agreements should result in meaningful and result oriented FTAs /RTAs/ CECAs. So a reality check of existing RTAs//FTAs/CECAs is needed by evaluating the performance of the items for which duty concessions have been given along with the impact on domestic production. More involvement of stakeholders could also help in ironing out differences.

India should also ready itself to face new threats like the Trans-Pacific Partnership (TPP) between Australia, Brunei, Chile, Canada, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam and Trans-Atlantic Trade and Investment Partnership between the EU and the US (TTIP) to create the world's largest free trade area, protect investment, and remove unnecessary regulatory barriers. Both TPP and TTIP are likely to produce market access restrictions and discrimination for Indian exporters even where India has already signed FTAs with TPP members such as Japan. Further, they will hasten the momentum towards the multilateralisation of regionalism, which is increasingly seen as the only way out of the contradictions between the surge in preferential trade agreements and the WTO. A strategy must be devised by India to face this challenge. Meanwhile there is also need to have some new useful RTAs/FTAs/ CECAs, for some of which negotiations have already started like the following.

- **Chile:** Chile is a prominent market for Automobiles. While it has FTA with other countries, with 93 per cent of its imports from FTAs, it does not have FTAs with India, though there is an India – Chile PTA signed with effect from 2007. Indian automobile exporters face tough competition and also disadvantage due to absence of FTA with Chile. If India signs FTA with Chile, exports of automobiles to Chile could increase manifold.
- **South Africa:** India- SACU PTA (South Africa, Botswana, Lesotho, Swaziland and Namibia) is under negotiation. South Africa has high import duty of 30 per cent for footwear (Chapter 64) and leather goods (Chapter 42) compared to India's MFN import duty (Basic Customs Duty) of only 10 per cent. South Africa's annual import of footwear is US\$ 696 million and India has a share of only 6 per cent in this imports. India could negotiate with South Africa for greater market access in this item and some other items. A successful Indo-South Africa PTA could help.
- **EU:** The GSP benefits with respect to certain GSP sections in accordance with Regulation (EU) No.978/2012 of the European Parliament and of the council applying a scheme of generalized tariff preferences are being suspended. This will badly affect

many items including coir and coir products falling under Chapter 53 & 57. In the light of this regulation coming into force from 1<sup>st</sup> January 2014 and in view of the other likely benefits to sectors like textiles and leather, Indo- EU FTA should be successfully negotiated.

#### **2.1.4 Issues of Inverted Duty Structure**

Inverted duty structure is making Indian manufactured goods uncompetitive against finished product imports in the domestic market. Under the inverted duty structure, finished goods are taxed at lower rates than raw materials or intermediate products which discourage domestic value addition. Studies like that of FICCI have indicated that manufactures like aluminium products, capital goods, cement, chemicals, electronics, paper, steel, textiles and tyres are subject to duty inversion. This inversion is not solely because of basic custom duty but in some cases a result of other additional duties. The main reason identified for duty inversion in the survey is regional/ bilateral Free Trade Agreements with countries like Japan, South Korea, ASEAN, etc.

Some examples of inverted duty structure highlighted in FICCI study are the following:

- Aluminum & Articles : The basic customs duty of aluminum ingots (HS Code- 7601), Aluminum Billets (HS Code- 7604), Aluminum Wire rods (HS Code- 7605), Aluminum Rolled Products (HS Code- 7606) are at 5 per cent, while duty on raw materials like aluminum fluoride and coal tar pitch is higher at 7.5 per cent and 10 per cent respectively.
- Capital goods: In capital goods falling under chapter 84 like pressure vessels, parts of heat exchangers, parts of nuclear reactors, boilers and part of boilers, etc., basic customs duty is at 7.5 per cent, but certain tubes, forgings and welding consumables and other raw materials attract a duty of 10 per cent.
- Cement: Cement has been exempted from basic customs duty, while duty is levied on the inputs required for manufacture of Cement ranging between 2 per cent to 10 per cent.
- Chemicals: The basic customs duty in the case of finished product is lower than that of raw materials. For example, basic custom duty of final products like styrene, ethylene dichloride, and vinyl chloride monomer is 2.5 per cent whereas it is 5 per cent for the raw materials like ethylene and naphtha.
- Electronics: For products like desktops and notebooks, the total duty on final product is 4 percentage points less than the key components for the product which is mainly due to the special additional duty of 4 per cent on components like memory, chassis, battery etc. Also, in case of smart cards (HS Code- 85235290), the final product attracts a total duty of 6.18 per cent vis-à-vis the total duty on its components ranging from 12.36 per cent to 26.36 per cent.
- Paper: The final products namely Art paper and other paper attract 10 per cent basic custom duty, 4 per cent SAD and 6 per cent CVD whereas the raw material, namely, modified starch attracts 20 per cent customs duty, 4 per cent SAD and 12 per cent CVD and Bamboo attracts 30 per cent basic customs duty and 4 per cent SAD.
- Steel: Stainless steel products under the HS code 7219 & 7220 attract 3.30 per cent basic customs duty under India Japan Comprehensive Economic Partnership Agreement

(CEPA) whereas the raw materials for these products falling under the HS code 7202 attract a basic customs duty of 4.10 per cent. The CVD and SAD are same on finished goods and raw materials. In the case of India- Korea Comprehensive Economic Agreement also finished goods under HS code 7219 and 7220 attract basic customs duty at 3.75 per cent and its raw materials under HS code 7202 attract customs duty at 5 per cent.

- Textiles: The final product attracts lesser duty as compared to raw materials required by this sector as inputs. For example, basic customs duty of final products like Polyester staple fibre (PSF), partially oriented yarn of polyester (POY) is 5 per cent whereas it is 7.5 per cent for the raw materials like Spinnish oil and 10 per cent for Tio<sub>2</sub> (Titanium dioxide).

Some examples of inverted duty received from different stakeholders: These are as follows:

- Natural rubber: Natural rubber (i.e Raw materials required for production by the rubber manufacturing sector like synthetic rubbers, rubber chemicals, processing oils, tyres, etc) attracts import duty of 20 per cent. This may be needed to take care of the livelihood concerns of domestic cultivators. However, finished goods are being imported at lower import duties like rubber rice dehusking rolls at 2.5 per cent duty without CVD, Auto tyres at 7.5 per cent, and rubber hoses at 6 per cent to 7.5 per cent. Many of these products are being imported from China, where it is made from scraps and non-environmental friendly methods. These imports affect the Indian rubber product manufacturing sector and needs to be addressed.
- Brass scraps: Under FTA with some Asian countries, the finished and semi finished brass products are imported to India at 'Nil' rate of customs duty, whereas raw materials viz. copper scraps, brass scraps, zinc scraps are subject to customs duty at the rate of 5 per cent. There is also an import duty of 2.5 per cent on import of aluminium scraps and steel scraps into India introduced recently and 4 per cent SAD on import of brass scraps was also re-imposed. Though, this has no revenue impact, as SAD can be claimed as refund by traders and for manufacturers, it can be claimed as Input Cenvat Credit, the transaction cost is high which leads to huge blockage of working capital for manufacturers.
- Tractor imported from Japan: Tractors are imported from Japan at current concessional duty of 7.3 per cent. There is no countervailing duty. On the other hand, inputs of Indian manufacturers are subjected to excise duty @ 12 per cent + which is non cenvatable since tractors attract zero excise duty. As a result, Indian tractors become costlier by around 5 per cent over the Japanese tractor manufacturers. As per Indo-Japan CEPA, the present duty of 7.3 per cent will be gradually reduced to zero duty over a period of time which would affect domestic producers.
- Brass rods: Under the CEPA/PTA with Malaysia, brass rods are imported at 0 per cent duty from January 1, 2013, whereas import duties on the inputs required to make brass rods. viz., copper and zinc, are at 5 per cent even under the CEPA/PTA with Malaysia resulting in inverted duty structure. Domestic manufacturers of brass rods also pay a

CST of 2 per cent unlike importers of brass rods. While re-negotiating the treaty with Malaysia is not easy, the import duty on copper scrap (ITC HS Code 74040012) and zinc scrap (ITC HS 7902001) could be lowered to remove the problem of inverted duty. Quality certification norms should also be strictly adhered to so that the right product is imported into the country.

- PCB Drills and PCB Routers: The main input of manufacturers of PCB drills and PCB routers is solid tungsten carbide blanks/rods which attracts a total duty of 28.85 per cent whereas, the finished products i.e. PCB drills, PCB routers attract zero import duty.
- Industrial Boilers: For the inputs of the Boiler industry, the import duty is at 10 per cent whereas, for the final products, i.e. Boilers, the import duty is 7.5 per cent which affects the Boiler Industry adversely.

The above cases of inverted duty need to be examined and right balancing needs to be done.

Some inverted duties addressed in the Budget 2014-15: In the Budget 2014-15, the basic customs duty (BCD) were reduced on following items to boost domestic manufacture as well as address the issue of inverted duties.

- Fatty acids, crude palm stearin, RBD and other palm stearin, specified industrial grade crude oils from 7.5 percent to Nil for manufacture of soaps and oleo-chemicals;
- Crude glycerin from 12.5 percent to 7.5 percent and crude glycerin used in the manufacture of soaps from 12.5 percent to Nil;
- Steel grade limestone and steel grade dolomite from 5 percent to 2.5 percent;
- Battery waste and battery scrap from 10 percent to 5 percent;
- Coal tar pitch from 10 percent to 5 percent;
- Specified inputs for manufacture of spandex yarn from 5 percent to Nil.
- In order to encourage new investment and capacity addition in the chemicals and petrochemicals sector, the basic customs duty on reformat reduced from 10 percent to 2.5 percent; on ethane, propane, ethylene, propylene, butadiene and ortho-xylene from 5 percent to 2.5 percent; on methyl alcohol and denatured ethyl alcohol from 7.5 percent to 5 percent; and on crude naphthalene from 10 percent to 5 percent.

### **2.1.5 Export Promotion Schemes**

There are multiple and overlapping export promotion schemes with many focus markets and focus products with items and markets getting added each year in the foreign trade policy. One thing that is visible from the list of trade policy measures is the multiplicity of schemes and concessions that are also periodically extended. There is need to rationalize the export promotion schemes to a bare minimum which can also reduce transaction cost and trade litigations. Some specific issues are the following:



- Limit concessions: There should not be many rates of concessions. Even for duty drawback scheme, there should be limited rates instead of having different rates even for similar items. This will make things simpler and limit discretionary decisions. Wherever tariffs are low or can be reduced, export incentives should be withdrawn as the transaction costs would be higher than the benefits owing to duty concessions.
- Second hand capital goods to be allowed under EPCG: Earlier under Chapter 5 of Foreign Trade Policy as per Para 5.2(g) second hand capital goods without any restriction on age could be imported under EPCG Scheme. However, as per Notification No. 1 dated April 18, 2013, Para 5.1(e) second hand capital goods are not permitted for imports under EPCG Scheme. This affects the small scale industry which is not able to afford new machinery especially when bank rates are high. Import of second hand capital goods which are available at throw away prices in foreign countries was a boon to SSI units specially under zero per cent customs duty. There is a need to examine whether second hand machinery after due certification by designated agencies against each authorization could be allowed to be imported at zero per cent customs duty at least for specific sectors for SSIs. This could also encourage investment and promote employment and have a positive impact on Industry. For example, the machines used in the rubber product manufacturing sector are heavy machinery consisting of rolls and frames which may weigh 6 to 10 tonnes each. With change of motors and control panels the machine is as good as new. Not permitting its imports will affect its exports as the importer is under export obligation of six times the value of the duty saved within six years under zero duty EPCG scheme. This needs to be examined.
- Issues of export incentives for project exports: Engineering, procurement and construction (EPC) contractors undertake turnkey jobs and hence project exports include both goods and services. However, incentives are available only for physical exports and separating the services portion of project exports is generally not possible since the value of the contract is on lumpsum basis. Hence there is a need to devise schemes for project exports where incentives given should be based on both supply of goods and services.

#### **2.1.6 Export Credit and related Financial Issues**

RBI data suggests that export credit as a proportion of net bank credit has declined from 9.8 per cent in March 2000 to 3.7 per cent in March 2013. Cross country analysis reveals that while many countries such as Canada, Germany, Italy, Japan United States, China, etc., have become aggressive in their export credit financing, India has been losing its export potential, due to paucity of export credit. Therefore, there is a need to strengthen export credit facilities in India and also make it less costlier. Some issues are the following.

- Ensuring availability of export credit in foreign currency at lower cost to exporters: The disbursal of export credit in foreign currency at lower rate is unviable for the banks since the cost of foreign funds to the banks is much higher. As a result the

banks are charging as high as 2-4 per cent. The objective of providing funds at maximum of LIBOR plus 350 basis points is not achieved as the service charge component is very high. Suitable measures such as capping the service charges levied by banks need to be introduced to ensure that credit is available at lower cost to the exporters.

- Bank realization certificate: While the Government has streamlined Bank Realization Certificate by introducing e-BRC, only 17 banks are not charging for issuing certificate, but 72 banks are charging for issuing e-BRC. EBRCs should be put on line within 7 days of receipt of the payment, as an exporter cannot apply for the incentives / benefits under Focus Market and Product Linked Schemes without e-BRCs.
- New RBI circular on merchant trade transactions: RBI Circular A.P.(DIR Series) No.95 dated 17th Jan.2014 has laid down certain guidelines for banks for handling merchant trade transactions or intermediary trade. A condition is that in case advance against the export leg is received by the merchanting trader, the advance payment has to be held in a separate deposit / current account in foreign currency or Indian Rupee. This means denying the merchant exporter access to these funds, which raises the cost of exporting for the merchant exporter. In a situation where the delivery time of supplier is 3-4 months, this would block the cash flow of merchant exporter without any compensation. This issue needs to be examined.

### **2.1.7 SEZ Issues**

SEZs were promised a tax-free regime, but Minimum Alternate Tax (MAT) on SEZ units and developers and Dividend Distribution Tax (DDT) were levied two years back. These have impacted the long term stability of the scheme and investor's confidence in SEZs and investments into SEZs have slowed down. While the new manufacturing zones (NMZ) are being planned, a lot of investment has already been made in SEZs waiting to be tapped to the full potential. SEZs are ready made Clusters with World Class infrastructure and governed by the SEZ Act and Rules. A clear signal needs to be given for Indian SEZs as fresh investments are slowing down in recent years and the greenfield SEZs have not really taken off full swing. Some other issues related to SEZs are the following.

- Non applicability of FTA concessions for SEZs' sales in DTAs: There are areas where SEZs are worse off than domestic tariff area (DTA) units as in the case of non applicability of FTA concessions when SEZs sell in DTAs. For the FTA partner countries, India exempts or allows concessional rate of customs duties on the listed products. Though SEZs are treated as foreign territory for the purpose of law, supply of goods manufactured by SEZs to DTA, are not allowed such FTA benefits, whereby supplies to domestic markets from SEZs become costlier than the direct imports from the FTA partner countries to DTA. To enable SEZ units to compete with products sold by India's free trade agreement (FTA) partners, the concessional customs duties applied on the foreign products could also be applied on SEZ products also.

- Need to extend schemes under Chapter 3 to units in SEZ: The schemes under Chapter 3 like Focus Product Scheme (FPS), Focus Market Scheme (FMS), Special Focus Market Scheme, Status Holders Incentive Scrip Scheme etc., are not available presently to units in SEZs. However, these schemes are available to EOUs who do not avail direct tax benefits. Since the Chapter 3 schemes are promotional measures, these schemes could be extended to units in SEZ with the condition that they do not avail direct tax benefits as in the case of EOUs. If the intention of creating SEZs is to give special focus on exports in these SEZs, then the normal benefits available in DTA need not be denied to SEZs.
- EEFC account payments for sales into DTA: There is a condition that SEZ manufacturing units must receive their payments from the EEFC account of DTA importers so as to meet their net foreign exchange (NFE) obligations. The DTA importer can pay in free foreign exchange (FFE) to any overseas supplier and import the goods subject to tariffs. When there is no compulsion on the DTA importer to pay from their EEFC account while importing from abroad this stipulation for imports from SEZ units needs reconsideration.
- Providing EDI connectivity and Operating only ICEGATE: Instead of the SEZ Online system, ICEGATE must be used with EDI connectivity in the Zones. This will enable the exporters to get their export entitlements on time by filing their claims Online instead of manual filling. This will also help in capturing all the data on a real time basis.

The Budget 2014-15 underlined the commitment of the Government to revive the Special Economic Zones (SEZs) and make them effective instruments of industrial production, economic growth, export promotion and employment generation. For achieving this, the government would take effective steps to operationalize the SEZs, to revive the investors' interest to develop better infrastructure and to effectively and efficiently use the available unutilized land.

### **2.1.8 Trade Facilitation (Documentation and Procedural Issues)**

Greater trade facilitation by removing the delays and high costs on account of procedural and documentation factors, besides infrastructure bottlenecks is another major challenge. As per the World Bank and International Finance Corporation (IFC) publication 'Doing Business 2014', India ranks 134 in the ease of doing business with Singapore at first place and China at 96. In trading across borders India ranks 132, Singapore 1, and China 74. India needs 9 export documents compared to 3 in Singapore and 8 in China. Time to export is 16 days in India and 6 in Singapore. The number of import documents needed is 20 for India and 4 for Singapore. Cost of exports per container is US\$ 1170 in India, US\$ 460 in Singapore, and US\$ 620 in China and cost of imports per container is US\$ 1250 in India, US\$ 440 in Singapore, and US\$ 615 in China (Table 2.2).

**Table 2.2 Ease of Doing Business Index: Comparison**

Countries	Rank (Ease of Doing Business)	Rank (Trading Across Border)	Number of Exports Documents	Time to Exports (days)	Cost of Exports (US\$ per container)	Number of Import Documents	Time to Imports (days)	Cost of Imports (US\$ per container)
Singapore	1	1	3	6	460	3	4	440
Denmark	5	8	4	6	795	3	5	745
Malaysia	6	5	4	11	450	4	8	485
France	38	36	2	10	1335	2	11	1445
Sri Lanka	85	51	5	20	595	7	17	775
<b>China</b>	<b>96</b>	<b>74</b>	<b>8</b>	<b>21</b>	<b>620</b>	<b>5</b>	<b>24</b>	<b>615</b>
Vietnam	99	65	5	21	610	8	21	600
Pakistan	110	91	8	21	660	8	18	725
Bangladesh	130	130	6	25	1075	8	35	1470
<b>India</b>	<b>134</b>	<b>132</b>	<b>9</b>	<b>16</b>	<b>1170</b>	<b>11</b>	<b>20</b>	<b>1250</b>

*Source:* Based on "Doing Business 2014" of World Bank and International Finance Corporation (IFC)

Some issues, both general and specific are the following.

- Coordination between Ministries: One of the challenges faced by the trading community is the complexity of laws and the gap between policy pronouncements and their implementation by different agencies. For example, the DGFT by Public Notice No. 08(RE-2012)/2009-14 dated 6th July, 2012 directed banks to issue e-BRCs only. As result, the system of manual BRCs has been stopped by banks. However, land customs ports like Raxual are not releasing drawback payments unless manual BRCs are provided to them as they have not received any communication from the CBEC in this regard and the DGFT Public Notice is not binding on them. As a result, the exporters are being denied their drawback payment. There is a need to reduce inter-ministerial delays and ensure at policy formulation stage itself that policies that are formulated by one Department are also honoured by others. The present move towards integration of related ministries is a step in the right direction, though a lot more needs to be done. Policy announcement and issue of notification should happen simultaneously.
- High transaction cost: Indian exporters face high transaction costs compared to their counterparts which needs to be reduced at every level of the supply/value chain. Estimates by exporters indicate that the transaction costs of around 10-12 per cent compared to a little less than 1 per cent in some of the developed countries, 1-3 per cent in most of the developed countries, and 6-9 per cent in most of the developing countries. Businesses have to deal with more than 40 government departments, with many procedures and documents some of which are either superfluous or redundant. This issue needs to be addressed in right earnest as exporters estimates indicate that if

transaction costs are reduced by 5-6 per cent, it will increase export earnings to the tune of \$ 15-18 billion.

- Container verification and release: Even after introducing e-way for customs clearances, the customs department requires physical documents. Container verification is time consuming as customs officers check/verify every container. This could be avoided by automatic clearance without any customs verification for reputed companies which have been exporting for a long time without any complaints or faults or by random checking or checking only those containers for which some specific information has been received or there is some suspicion. There is also delay in the release of the containers. For example in India it takes 20-30 days to clear and release the container, while in the other countries, the containers are released within 8 hours. These issues need to be addressed.
- LCL (less container load) shipments: In some cases exporters of goods like engineering goods, have to make LCL shipments as there is no full container load exports till these exporters find a steamer which will carry LCL cargo to distant locations. The consignment remains at the dock for LCL cargo acceptance by the shipping line, and by then, the validity of customs documents may get over. Sometimes re-validation is permitted, depending upon the time the consignment remains at dock. However, in many cases, exporters are asked to call back the consignments which are referred as the "Back to town procedure". This process is not only time consuming, but also leads to extra expenses and unnecessary delay in executing order. Thus, a system needs to be developed which could ease shipment of LCL cargoes.
- Need for some essential government offices: In some places there is need for some government offices to speed up exports and reduce delays. For example in Trivandrum to clear documents of trade of forestry and herbal line products, there is no forestry board office and exporters have to get it cleared either from Cochin or Chennai. Manufacturer exporters also face problems due to the non-availability of agencies like National Small Industries Corporation (NSIC). For the imports of items like surgical and medical equipment, there is no office of Assistant Drug Controller in Kerala and import items have to be cleared from Chennai.
- Round the clock customs and excise operations: Operating major ports and trains round the clock and facilitating export clearances on all the seven days of the week in all major excise ranges could help in timely clearances and reduce cost.
- Efficient working of custom servers: Customs operations are hampered due to non-working of EDI system at ports because of server issues. Steps need to be taken to ensure that systems work round the clock without any interruption.
- Provision for allowing amendments in online application: DGFT encourages on-line applications for various reasons including reducing the interface. All applications, if

fresh, can be uploaded on-line but no amendments, whatsoever, can be made on-line. If an exporter wants to enhance his present EPCG authorization or advance authorisation, he has to make manual application which attracts higher fees. Enabling all types of amendments on-line, irrespective of the category of applications could help exporters in reducing costs and time.

- Issue of systems error: Transmission of amendments in authorizations or scrips by DGFT to ICEGATE often gets blocked as data error. Many a times, the data does not appear in ICEGATE due to which transactions, either export or import, are inordinately delayed, sometimes more than 6 months. There is also another issue related to systems error. As per DGFT policy an authorization is valid for import till the last date of month in which it expires. For example, if an authorization expires on 2<sup>nd</sup> of March, date of Bill of Lading can be 31<sup>st</sup> March to make it valid for import. Therefore the consignment may reach the port in April any day. However, after receiving the arrival information, when the importer approaches customs to log the authorization, the system will not allow it as the date of expiry as per the system is 2<sup>nd</sup> March and therefore this Bill of Lading becomes invalid. This needs to be examined and rectified.
- Delay in issuing cross border certificate: A lot of Shipping Bills are still pending with Kolkata Customs because of the internal procedural delays. Drawback claims are kept pending for want of Cross Border Certificate from Petrapole ICD resulting in delay in drawback claims.
- Time limit to be fixed for on line redemption: The time limit for issue of Export Obligation Discharge Certificate (EODC) needs to be fixed once the two key documents i.e. shipping bill from customs and EBRC from bank relating to advanced authorization and EPCG authorization are available.
- Making available shipping bills online: Shipping bill copies are needed for the purposes of (a) exporter copy – for submissions with jurisdictional customs range as proof of export, (b) exchange control copy – For submission to bank, and(c) export promotion copy – for claiming export incentives. Delay in getting these documents affects the business. Further, if any mistakes are made by the agent or there are systems issues, these documents will not be generated and has to be rectified by the technical team (ICEGATE). This is a very tedious and time consuming process. Process for rectification needs to be streamlined and these documents should be made available online for the exporter as well as the regulatory agencies/banks.
- Issue of export inspection for animal feed: The export inspection agency of India does not issue certificates to exporters of food for animal consumption mentioning that this food is fit for animal consumption as they issue the certificate only for food for human consumption. However, some countries like China provide such types of

certificates. As a result exporters are losing orders from Iran and other middle east countries. This could be easily addressed.

- Difficulty faced by exporters in implementation of risk management system (RMS): Implementation of risk management system (RMS) at Mundra and Pipavav Port has led to hardships for exporters as greater number of containers are opened for inspection. Of late, even self sealed containers are being opened with greater frequency than was the case in the past. Necessary steps to address this issue needs to be taken.
- Acceptance of LUT for export incentive license issuance: Export incentive licenses such as FPS (Focus Product Scheme), FMS, MLFPS were issued earlier on the basis of Revolving Letter of Undertaking (LUT) and proof of receipt of payment was to be submitted within a year's time. Now with the introduction of E-BRC initiative, the timeline for receipt of export incentive license has increased resulting in blockage of funds with DGFT office and exporters have to pay the import duties in cash. The average incentive realization period has increased by 90-120 days as most of the LC's are for 3 months period. It needs to be examined whether the LUT provisions could be restored and changes in software incorporated so as to have provision for making application for FPS & other licenses against letter of undertaking.
- Electronic crediting of benefits under focus market & focus product scheme: Under the duty drawback scheme, now the amount is directly credited to exporters account. However, for Focus Product Scheme (FPS) and Focus Market Scheme (FMS), the scrips are still being issued. This involves lot of paper work and adds to transaction cost. It needs to be examined whether the amount due to exporters could be directly credited to their account electronically instead of issuing duty credit paper scrips. This may also lead to doing away with the payment of VAT at the time of sale of scrips.
- Anomalies in advanced authorization scheme: Notification No. 31 (RE-2013)/2009-2014 dated 1<sup>st</sup> August, 2013, issued by DGFT regarding advance authorization/DFIA has inserted a new Para 4.1.15 after the Para 4.1.14 that wherever SION permits use of either generic inputs or alternative inputs, unless the names of the specific inputs used in the manufacture of the export product gets indicated/endorsed in the relevant shipping bill and these inputs, so endorsed, match the description in the relevant bill of entry the concerned authorization will not be redeemed. The changes brought in complicate the system. For example, the import items allowed against the exports of different types of tyres and other rubber products are mostly of generic nature. If the intention of this change is to protect growers of natural rubber in India, then specifications could be asked only for these items and not for chemicals, etc. The unintentionally mis-spelt grades of inputs could also give rise to lot of disputes. In the case of a sensitive input like "Synthetic Rubber", the declaration with regard to technical characteristics, quality and specification in shipping bill is followed as per Para 4.55.3 of DFIA Scheme. Besides, synthetic rubber like EPDM and some of the

rubber chemicals also attract antidumping duty. These need to be examined and addressed.

Budget 2014-15 has also taken some measures aimed at trade facilitation which include the following.

- As faster clearance of import and export cargo reduces transaction costs and improves business competitiveness, measures are being initiated to extend the existing 24x7 customs clearance facility to 13 more airports in respect of all export goods and to 14 more sea ports in respect of specified import and export goods.
- It is also proposed to implement an 'Indian Customs Single Window Project' to facilitate trade. Under this, importers and exporters would lodge their clearance documents at a single point only. Required permissions, if any, from other regulatory agencies would be obtained online without the trader having to approach these agencies. This would reduce interface with Governmental agencies, dwell time and the cost of doing business.

### **2.1.9 Tax / Tariff Issues**

Some tax/tariff related issues are the following:

- Early implementation of goods and services tax (GST): There is a need of early implementation of Goods and Services Tax (GST).
- Stamp duty on imports: An amount of 0.1 per cent is being collected towards stamp duty on c.i.f. value plus import duty on all imports into Mumbai and Nhava Sheva Port. No other state levies such a duty. The procedure for collecting this duty is also cumbersome. This levy is being collected at Nhava Sheva by State Bank of India or Bank of India Branch at Port Users Building. Thereafter, the CHA has to travel to Apollo container freight station (CFS) to collect the delivery which is 25 kms away. This could have been collected at the CFS itself. A service fee of ₹ 50/- to ₹ 500/- is also being imposed to collect this levy.
- TDS on foreign agents commission: A clarification from the Government sought with respect to the TDS on Foreign Agents Commission is pending. Since that clarification has not been given, respective assessment officers treat this in their own way resulting in increased litigation and transaction cost. A clarification on this issue could be issued.
- Service tax on foreign exchange transactions: Banks are debiting service tax on the remittances of foreign currencies received by exporters from their overseas buyers. In this connection a Clarification Circular No.163/14/2012-ST, dtd 10th July 2012 issued by the Central Board of Excise & Customs has clarified that *"there is no Service Tax per se on the amount of Foreign Currency remitted to India from overseas since the amount remittance comprises money and this activity does not comprise a*



*service.*” Moreover service has been defined in Clause (44) of Section 65 B of the Finance Act 1994, as amended which excludes transaction in money. This issue needs to be addressed.

- Service tax exemption on services used in agro processing for export: There are many services which are used by processors and exporters of agricultural products which could be included in the exemption list or negative list for service tax. The present system of first collecting the service tax and then giving refund to exporters results in additional costs and double work by the exporters as well as the Government and does not help in efficient tax administration. All services which are clearly identifiable as relating to exports could be included in the negative list. An indicative list of such services proposed for exemption given by exporters is at Box 1. The current system of a flat 0.2 per cent service tax refund for exports, irrespective of value of goods is also discriminatory to exporters whose value of goods is low. This needs to be examined and addressed. Budget 2014-15 has exempted services tax on loading, unloading, storage, warehousing and transportation of cotton, whether ginned or baled. Services provided by the Employees’ State Insurance Corporation for the period prior to 1st July 2012 is being exempted.

**Box 2.1 Indicative List of services which could be exempted from Service Tax**

- Transport of agricultural products from supplier to the premises of the exporter (local transport).
- Handpicking and Sorting, Shelling, Grading, Processing of agricultural products for exports on job work basis to an outside agency.
- Charges for hedging the export proceeds.
- Warehousing charges paid by exporter before the goods are sent to CFS.
- Pest control and fumigation services used in the unit of an exporter.
- Fumigation & Sterilization of cargo while packing in containers.
- Cleaning services used by exporter when goods are brought from Mandi.
- Pre-shipment testing & survey of cargo by laboratories.
- Certificate of Origin from Chamber of Commerce.
- Phytosanitary Certificate for export of agricultural goods.
- Remittance of commission to foreign agent.
- Membership of export promotion council.
- Taking a processing unit on lease basis.
- Service charge levied by banks for issuing bank Guarantee.

- Double payment of cess on domestic area sales by 100 per cent EOU: The goods manufactured by an EOU and cleared in the DTA are subject to excise duty. In terms of proviso to Section 3 (1) of the Central Excise Act, 1944 excise duty on any excisable goods which are manufactured by a 100 per cent EOU and cleared in the DTA shall be equal to the aggregate duties of Customs leviable on like goods if imported into India. However, Notification 2/95-C.E. dated January 4, 1995 (current Notification 23/2003-C.E. dated March 31, 2003) provided exemption in excess of 50 per cent of the aggregate duties of customs. While computing the total duty, education cess is levied on the CVD part of the duty and again cess is paid on

the total customs duty. The department has taken a view that the total amount of duty computed under notification 2/95 CE is only excise duty payable under section 3 of the excise act read with notification 2/95-C.E. and since education cess is levied under clause 83 of the Finance Act 2004, the EOUs have to pay education cess again on the total duty. The ruling by the High Court of Bombay states that once education cess is added to the customs duties to arrive at aggregate of customs duties, the question of charging education cess again does not arise. However, Department of customs and central excise in Kerala still demands EOUs to pay cess on total duty again. Cenvat credit is not allowed on such cess in some jurisdictions resulting in increased costs to the customers. This needs to be examined.

- VAT, duty drawback, excise refunds: VAT, duty drawback, or any other refund should be available within 30 days of claim. VAT refund claims have only been received for the year 2009-2010. The audit for the subsequent year has not yet been done, so the exporters have only got part refund, and a major chunk of refund for 2010/2011 and entire refunds for subsequent years has not yet been received. Even the duty drawback and excise rebate claims have been stopped since 1<sup>st</sup> January, 2014. As per exporters, over ₹ 10,000 crores worth duty drawback claims are pending across the country. In Chennai itself, the amount is over ₹ 1,041 crore. In Bangalore, the due amount is around ₹ 86.06 crore and in the whole of Karnataka, the amount is above ₹ 500 crores. These delays add to transaction costs and block the high interest bearing fund of exporters and need to be avoided.
- Investment allowance: In the budget 2013-14 an investment allowance of 15 per cent was given to investment of over ₹100 crores. This threshold needs to be lowered. The Budget 2014-15, has taken note of this lacunae and proposed to provide investment allowance at the rate of 15 percent to a manufacturing company that invests more than ₹ 25 crore in any year in new plant and machinery. This benefit will be available for three years i.e. for investments upto 31.03.2017. The Scheme announced in the 2013-14 Budget will also continue to operate in parallel till 31.03.2015.
- Service tax on foreign bank charges: As per the Trade Notice no 20/13-14-ST-I dated 20/02/2014, the foreign banks generally deduct some charges for handling export documents and the Service tax department collects service tax on such charges by using reverse charge mechanism and ask Indian banks to pay the service tax. The Indian Banks in turn have sent circulars, asking the branches to debit service tax to customers and make payment. When banks pay such service tax on the basis of reverse charge, they can avail CENVAT credit on such payments, which goes on to reduce their service tax liability. This being the case, debiting the service tax to the exporting customers seems inappropriate and needs to be addressed. Asking banks to deposit service tax on charges debited by foreign banks in handling export documents is also against the stated objective that, no taxes should be exported.

- Exemption of service tax on ECGC premium instead of refund: As per notification no.41/2007-Service Tax dated 6<sup>th</sup> October, 2007 section 65(105)(d), services provided to an exporter by an insurer, including a re-insurer carrying on general insurance business in relation to insurance of said goods is refundable provided document issued by the insurer, including re-insurer, for payment of insurance premium shall be specific to export goods and shall be in the name of the exporter. Payment of service tax for the premium paid to ECGC could be exempted either through banks or directly for insurance of export cargo to reduce paperwork / compliance cost.
- Pending tax related disputes: A lot of time and money of exporters is wasted due to tax disputes. The settlement of tax related disputes needs to be addressed urgently as at the end the government wins only in a few cases. There is a stipulation which gives a threshold monetary limit of ₹10 lakh and ₹ 25 lakh for cases to be taken up at High Courts and Supreme Courts respectively. In the Budget 2014-15, to expedite the process of disposal of appeals, amendments have been proposed in the customs and central excise acts with a view to freeing appellate authorities from hearing stay applications and to take up regular appeals for final disposal.

#### **2.1.10 Long Term Vision in Multilateral Negotiations**

India has been successful in getting some of its concerns addressed in the WTO ministerial negotiations at Bali and has been able to successfully block the trade facilitation agreement in the recent WTO general council meeting at Geneva till India's concerns on food security are met. But there is a need for introspection as to why India had to negotiate on food security issues today. This is because, India and other developing countries did not succeed earlier in negotiating what they wanted on subsidies at the time of Agreement on Agriculture (AOA). Similarly, we signed the ITA-1 which resulted in 'zero' duties for many electronic goods at a time, when the advanced countries and many newly industrialized countries had developed their semi-conductor sector, but India had not. All this was because in the early years of WTO negotiations, the Agenda was set by others and India and other developing countries had to react to it. Of course this has made us more alert and we also started putting forth our Agenda. However, we need to be cautious on the proposed ITA-2 negotiations. Thus, long term objectives should be kept in mind during such negotiations and we should not fall into any traps.

#### **2.1.11 Intertwining of Domestic and External Sector Policy**

While a stable agri export policy is needed, any domestic shortage or excess affects exports. Similarly external shortages/ excesses affect the domestic sector. So a smooth intertwining of domestic and external-sector policies particularly for agriculture related item is needed. Advanced economic and market intelligence to avoid major mismatches is also necessary.

#### **2.1.12 Greater Role for States in Export Effort**

Export sector should be accorded national priority sector and there should be greater involvement by the local and state governments while framing and implementing export

policy. State wise exports show the domination of only two states with Gujarat at the top followed by Maharashtra. Tamil Nadu and Karnataka are a distant third and fourth. In 2013-14, with a high export growth rate of nearly 20 per cent, Gujarat relegated Maharashtra to second place. Among the other states, Uttar Pradesh, West Bengal, and Odisha had double digit export growth. Kerala's export share fell by more than half owing to negative export growth of 55 per cent. This was mainly due to the fall in spices exports. The central government also encourages states to export through the Assistance to States for Developing Export Infrastructure and Allied Activities (ASIDE) scheme which is based on export performance of states. The outlay for the ASIDE scheme has two components: state component (80 per cent of the total outlay) and central component (20 per cent of the total outlay). For the financial year 2013-14, ₹ 745.1 crore (RE) has been allocated under the ASIDE scheme. States need to play a greater role in the export effort as they are also the beneficiaries of the resultant development. In countries like China, not only states, even districts play an active role and they even monitor district- wise exports as they have data on such exports.

The Budget 2014-15 has also emphasised the importance of states in export promotion. It has proposed to establish an Export promotion Mission to bring all stakeholders under one umbrella. As exports cannot be exponentially increased unless the states play a very active role in export promotion by providing good infrastructure and full facilitation.

#### **2.1.13 Role of Indian Missions abroad in Export Promotion**

Indian foreign missions should also play an active role to facilitate India's exports. At present the mission have commercial representatives who are supposed to help in export promotion. However, the focus of the mission is on attending to VIPs and facilitating the numerous government and international meetings rather than export promotion. There is a need to reorganise these missions and make them active trade facilitators.

#### **2.1.14 Effective use of Trade Fairs**

India organises many trade exhibitions in India and abroad. While there is a need to evaluate the outcome of these trade fairs and expos organised by ITPO, there is also a need to make them more focussed and result oriented. Some permanent exhibition centres of India in some important markets could also be set up.

#### **2.1.15 Reality Check of EPCs**

There are many export promotion councils (EPCs) and commodity boards (CBs) to help exports. While some of them were useful at the time of their setting up, now they have become less important and some new sectors have become important. Here also the outcome of these EPCs and CBs needs to be evaluated. Even allocation of funds to these EPCs should be based on a zero budgeting exercise. Merging some EPCs could also be thought of.

### **2.1.16 Transportation related Issues**

Reforms related to transportation of goods for export and import can reduce a lot of costs for the exporters and importers. In this age of multimodal transport, the multimodal transportation of goods act 1993 needs a lot of revisions to ease the existing restrictions on transportation and documentation through different modes of transport, particularly restrictions in the Customs Act which do not allow seamless movement of goods; and restrictions on free movement of cargo between Inland Container Depots (ICDs), Container Freight Stations (CFSs) and Ports. The integration of transport related ministries is a step in the right direction. In this context, there are some issues related to shipping companies. They are as follows:

- Higher exchange rate issue for freight payments: The shipping companies use high exchange rates to recover the freight in Indian rupees. So a clear directive or instructions needs to be given to use the exchange rate as declared by the Customs for exports. Since the Customs revise these rates every month, all shipments effective in that particular month should be charged as per the exchange rates declared by the Customs or by RBI.
- Various additional charges collected by the shipping companies: Apart from high freight rates many additional charges are collected on import / export consignments: Some are given below:
  - Washing charges: Most consignments are now palletized and stretch wrapped. Hence, this does not contaminate or dirty the container in anyway, but the shipping companies are charging between ₹1,500/- to ₹ 2,000/- as washing charges. No washing is done and it is just an additional charge for no reason at all.
  - Charges for issuing bill of lading: While issuing the bill of lading, the shipping companies are now charging an additional ₹750/- to ₹1,800/-.
  - Survey charges: An amount of ₹ 400/- to ₹ 600/- is recovered as survey charges even though in most cases no survey is required.
  - Damage charges: Many exporters have insured the cargo and the container for transit from the docks to their factory / warehouse. Even though no damage is being caused to the container, the shipping companies recover hefty sums on the pretext of damage to their container.
  - CFS charges and transport charges to CFS: The shipping companies recover a CFS charge of between ₹ 10,000/- to ₹ 15,000/- for taking the container from the ship to their designated CFS. They do not permit the use of importers choice of CFS where the charges are not more than ₹ 5,000/-. Also for transportation of the container from the port to the CFS, a distance of hardly 5 to 10 kms. they charge anywhere between ₹5,000/- to ₹10,000/- for taking the container to the CFS.
  - Other charges: These include security sub charges of ₹50/-, container imbalance charges between ₹8,600/- to ₹ 9,500/-, Indian service recovery sub charges between ₹11,460/- to ₹12,000/- and international port sub charges between ₹200/- to ₹300/-.

There is a need to see whether these charges are genuine or not and necessary measures should be taken to safeguard the interest of exporters/importers. There are also some issues related to loading export/import cargo. While the gang system in ports is an open secret, there are some regional versions of such system also. One example is as follows:

- Issue of mathadi kamgar employees: In Maharashtra, the mathadi kamgar union are forcing themselves in the factories to employ them for loading and unloading operations. These workmen are not trained for loading and unloading the products of the export markets and are basically designed to carry head loads in various wholesale markets and ports. They do not follow the instructions and just take their money without performing any functions. Maharashtra is the only state to have such an act. This act needs to be repealed immediately as their union is not prepared to take any responsibility for proper loading by the mathadi kamgar employees, which results in heavy loss to the exporters due to damages during loading.

## **2.2 Sector Specific Issues**

There are many sector-specific issues, besides the general issues. Some of the relevant issues highlighted by the exporters are given below:

### **2.2.1 Agriculture Related**

Domestic market issues: There is no organised market in India. The growers are scattered in large number of places. There is a need for an organised market from where exporters get as much quantity as they require to meet export demand which will reduce the efforts of exporters. There is also a need for uniform rules and norms in all states.

Agar Agar: The Agar Agar market in the world is highly competitive with China dominating the world market. Due to stiff competition from China and Chile, the world market place has become highly competitive and the export realization and consequent value addition will not be more than 5 per cent. To maintain and improve the present level of exports the value addition could be limited to, say, 5 per cent, instead of the present 15 per cent under advance authorization scheme.

Rubber products: The products manufactured by rubber industry in Karnataka are levied FDT (forest development tax) at 12 per cent as it is considered as a Forest product. However, this kind of tax is not levied in neighbouring states like Kerala & Tamilnadu putting Karnataka producers at a disadvantage.

Reinstatement of VKGUY benefit for guar gum & sesame seeds: Guar is an arid/semi-arid zone crop that is grown mainly in the less productive areas of Rajasthan, Haryana and Gujarat by marginal farmers. The 5 per cent vishesh krishi gram udyog yojana (VKGUY) incentive was given to this sector which was ploughed back into the industry by way of increased capacity and latest technology resulting in several thousand jobs and increased returns to the farmers. The VKGUY benefit was withdrawn for Gaur Gum as export prices had gone up abnormally from April 2012 onwards. However the abnormally high prices in the latter part of 2012 was an aberration owing to the involvement of non-industry speculators. In case of

Guar Gum Powder (treated & pulverized), the largest part of the conversion cost is cost of power & fuel in both drying and electricity. While for China, India's largest competitor, this cost is around ₹ 3/- per kg of Guar Gum, for India, it is to the tune of ₹ 6.5 to 7.0. Taking note of this and also the fact that prices have fallen since Sept 2013. VKGUY benefit could be given to Indian producers to give a level playing field vis-à-vis competitors.

#### Cashew:

- Currently, cashew export promotion council of India (CEPCI) has the authority to provide the Certificate of Origin to the countries of NAFTA & APTA. CEPCI could be given the authority to provide the Certificate of Origin to ASEAN countries and countries of other economic unions also which could help the exporters to these countries.
- Import duty on cashew kernels was revised on 02.12.2013. The same could be imposed on the import of roasted & salted cashew nuts also to check the huge amount of undervalued imports from different countries.
- Raw cashew nuts are not edible as such and considerable transformation by way of heating, burning, cooling, etc., is being undertaken while processing the raw cashew nut to extract the edible cashew kernel. However raw cashew nuts are under the purview of Food Safety and Standards Authority of India (FSSAI) stating that cashew is a food item. The various FSSAI regulations on raw cashew nuts delay the process of clearing imported consignments which also affects the quality of the raw cashew nuts. This also adds to the cost of the processed cashew kernels, thereby putting the Indian exporters at a disadvantage. This issue needs to be addressed.

Exports of value added products of red sanders wood: The DGFT notification allows export of value added products of Red Sanders Wood, such as chips, powder, extracts, etc, procured from legal sources. But exporters face difficulty while exporting them particularly at customs level as customs officers are wary of taking decisions in the case of such items. There is a need to ensure that once the Government allows an item for export, no obstacles are there for its export.

#### **2.2.2 Mining Sector**

Mining is an important sector which needs special focus for quick growth of the economy as it can not only push up growth figures directly, but also indirectly due to its high linkage effects. The supreme court orders and restrictions by state governments had limited mining activities and consequently exports. Mining sector growth in the last 5 years was at 1.8 per cent on an average and investment in mining as a percentage of GDP was only 0.5 per cent. A push to this sector can, not only help in growth of the economy but also exports of such ores not in immediate use in India. While a big investment push in mining is needed, some issues related to exports are the following:

- Low grade Iron ore fines cannot be economically used in India: India has abundant hematite fines and at present low grade coarse hematite ores do not have much use in India as magnetite is generally not part of the Indian supply chain. Thus, these low

grade hematite fines can be exported by India. China can use it as China produces abundant crude magnetite. So, there is a need to consider excluding such low grade fines from the export duty of 30 per cent ad valorem on iron ore.

- Railway freight costs issues: Railway freight costs has increased from 2007 to 2009 for Iron Ore with freight for approximately 600 kilometres at ₹ 700 becoming ₹ 900 for domestic transportation and ₹ 2900 for exporters. This needs to be addressed.

Thus, while in the medium to long-term we have to devise policies to use our Iron ore domestically instead of exporting it and simultaneously importing Iron & Steel, in the short term, there is a need to consider abolition of export duty on low grade Iron ore and also addressing the additional freight costs on Iron ore to facilitate the exports of cheap grade iron ore. Greater focus on investment in mining industry is also required.

The Budget 2014-15, announced the intention of Government to encourage investment in mining sector and promote sustainable mining practices to adequately meet the requirements of industry without sacrificing environmental concerns. It also stated that the current impasse in mining sector, including, iron ore mining, will be resolved expeditiously and changes, if necessary, in the Minerals Mines Development and Regulation (MMDR) Act, 1957 would be introduced to facilitate this.

### **2.2.3 Engineering Sector**

- Issue of 2.5 per cent import duty on metal scrap: The customs duty on stainless steel scrap (HS Tariff 72042190) and MS scrap (HS tariff 720449) was increased from nil to 2.5 per cent vide customs notification No. 25/2013-customs dated 8th May, 2013. On brass it is 4 per cent. Raw material accounts for 70 per cent - 75 per cent of the cost of production of stainless steel and Scrap in turn accounts for as much as 50 per cent of the raw material cost. Further, in India (as also in most other countries), stainless steel is produced through the electric arc furnace route, which automatically rules out the possibility of substituting scrap by iron ore or any other raw material. Since the requirement of both stainless steel scrap and MS scrap are mostly met through imports, the duty on stainless steel scrap and MS scrap has an adverse impact on the cost structure of domestic stainless steel producers affecting their competitiveness compared to China and Taiwan. The Chinese stainless steel manufacturers already enjoy cost advantages in the form of lower power cost, lower interest cost, stable currency, abundant supply of coking coal (not found in India) and access to low cost Nickel pig iron. This issue needs to be examined and addressed.
- Safeguard duty imposed on stainless steel imports from China: In January 2013, India imposed safeguard duty on stainless steel imports from China for a period of 200 days. Para 4.1.4 of the foreign trade policy stipulates that advance authorisations are exempted from payment of basic customs duty, additional customs duty, education cess, anti-dumping duty and safeguard duty. As such, Indian exporters imported stainless



steel which was allowed by the customs. In June 2013, the customs slapped show cause notice on the advance authorisation holders amounting to crores of rupees on the ground that the imports were from China, and the relevant customs notification stated Para 4.1.4 of the FTP becomes inoperative (safeguard duty imposed by customs notification 01/2013, dated 04.01.2013 under section 8C whereas in advance authorization issued under notification 96/2009 allowing exemption of safeguard duty under section 8B). Interestingly, if the imports were by an SEZ unit, no such safeguard duty is payable. Thus, DTA units are at disadvantage. Such contradiction in policy needs to be addressed. Anti dumping investigation has already been initiated by DGAD on March 11, 2014 for imports from Korea, Malaysia and China and there needs to be clarity in policy.

- Definition of MSME: The MSME segment contributes anything between 35 per cent-40 per cent of India's total engineering exports. Last year, the Government constituted an Inter-Ministerial Committee for Boosting Exports from MSME Sector. This Committee made some major recommendations, including increasing the capital investment limits in the definition of MSME; and enhancement of technical upgradation schemes with both capital subsidy and interest subvention. While, technological upgradation will entail investment in plant and machinery it may also take a company out of MSME limits and deprive it of interest subvention and other benefits which it receives unless the definition of MSME in terms of Capital Investment is also enhanced. This needs to be looked into. The Budget 2014-15 has stated that the definition of MSME will be reviewed to provide for a higher capital ceiling.

#### **2.2.4 Project Exports**

Projects Exports at ₹ 22,173.58 in 2013-14 grew by 124 per cent from the ₹ 10,110.38 crores in 2012-13. A large number of projects secured were in Indian rupees. Some suggestions related to project exports are the following:

- Long term buyers credit arrangements: These are needed from Indian agencies to make it attractive to engage in project exports.
- Part payment issue: For project exports, part payment is the norm. However, benefits under chapter 3 like FMS or FPS are given against a particular shipping bill and its eBRC, which shows only the part payment received. The exporter has to either wait till all the shipments for the project are over which may even taken 2-3 years resulting in blockage of funds or accept part payment and forfeit the balance amount. This needs to be examined and payment in two or three parts could possibly be allowed for project exports.
- Multi-entry visa: Non-Issuance of multi-entry visa of longer periods to project implementation and commissioning professionals affects project exports as unlike export of commodities project exports have a longer execution and realization period. Therefore there is a need for multi-entry visa for personnel employed by Indian project exporters.

### **2.2.5 Textiles**

- Customs duty reduction for synthetic garments machinery: Cotton exports from India are demanded only during summers in Europe and USA. To cater to all seasons in these markets, there is a need to focus also on synthetic textiles. Zero customs duty for machinery used for manufacture of synthetic garments could help in the production of synthetic garments both for exports and domestic market.
- Customs duty reduction for synthetic garment fabrics: The garment exporters are facing problems due to the non-availability of certain fabrics domestically in adequate quantum. As a result, exporters are not able to meet export orders for winter garments. Reduction of customs duty also for import of Synthetic / Blended / Specialty Fabric of Cotton could help.
- Overtime for labour: Existing labour laws allow only 6 hours per week as overtime in alternative days. This can be changed to 12 hours per week for the benefit of workers, since migrant labour in places like Tirupur want more over time working hours. Recently the cabinet has approved amendments to the Factories Act, 1948 relaxing restrictions on night duty for women in factories subject to certain conditions and increasing the limit of overtime to 100 hours from existing 50 hours per quarter.
- Free trade agreement with the European Union (EU): More than 50 per cent of India's knitwear exports is to European union and early signing of free trade agreement (FTA) with European union could help in increasing India's market share in the European union. This needs to be viewed in the light of Bangladesh, being a least developed country enjoying the duty free status and the total exports from Bangladesh reaching US\$ 22 billion against India's exports of US\$15 billion. Similarly FTA with Canada could also help this sector.

For the textiles sector, the Budget 2014-15 has proposed to set up a Trade Facilitation Centre and a Crafts Museum with an outlay of ₹50 crore to develop and promote handloom products and carry forward the rich tradition of handlooms of Varanasi, with an intention to support a Textile mega-cluster. It also proposed to set up six more Textile mega-clusters at Bareilly, Lucknow, Surat, Kuttch, Bhagalpur, Mysore and one in Tamil Nadu allocating a sum of ₹200 crore for this purpose. It also proposed to set up a Hastkala Academy for the preservation, revival, and documentation of the handloom/handicraft sector in PPP mode in Delhi with an outlay of ₹ 30 crore; starting a Pashmina Promotion Programme (P-3) along with a programme for the development of other crafts of Jammu & Kashmir with an outlay of ₹ 50 crore.

### **2.2.6 Gems and Jewellery Sector**

- Suppliers' credit: Indian diamond industry is totally dependent on import of rough diamonds from abroad as India virtually has no rough diamond production and the trading centres for rough diamonds are all situated abroad. Suppliers' Credit is availed

by Indian diamond & jewellery manufacturers against purchase of rough diamonds from secondary suppliers abroad and/or from mining and trading centres of Botswana, Antwerp, Israel etc. The manufacturing cycle of diamonds is more than 180 days right from purchase of rough till manufacture and sale of it in international market. As per the RBI Circular No. 59 dated May 06, 2011, the AD Category-I Banks are not permitted to approve Suppliers' and Buyers' Credit including the usance period of Letters of Credit for import of rough, cut & polished diamonds beyond 90 days from the date of shipment. This needs to be examined and addressed.

- Reducing documents for imports and exports of gems & jewellery: At present, for export of cut and polished diamonds, an exporter has to make 21 invoices, 2 GR forms, 3 Green delivery Challans and 4 Shipping Bills as per shipment. The total number of documents being filed is 30. Managing this documentation is a time consuming effort. Non submission of any of these documents can delay the process. Other major international diamond exporting centers do not have so many procedures. This needs to be addressed.
- High Premium charges for gold import from nominated agencies/banks: Since there is no policy to control the premium charges of banks/nominated agencies for gold import, the charges are high. This needs to be examined.
- EDI System implementation: Non-implementation of EDI systems (ICES) for exports at PCCCC, BDB, BKC affects exporters. This is because there is no refund of service tax, as the service tax department is unable to file the claim without EDI system generated invoice code. So, EDI System implementation is needed urgently.
- Personal carriage of gems & jewellery export consignments from Jaipur using gateway ports other than Jaipur: The personal carriage of Gems & Jewellery exports was allowed till the year 2006, but has been discontinued since then. With the discontinuation of this system, the exporters are now forced to carry the gems and jewellery consignments to the gateway port of Delhi or Mumbai in advance for its appraisal and clearance with the Customs there. This takes at least one day extra and also involves security risk to the exporters while carrying the shipment from one place to other. Earlier the exporters used to carry the customs appraised consignment by flight from Jaipur to the gateway port and take connecting international flights from the gateway port, which was time saving and not risky. The earlier system could be restored.
- Requirement of separate room for appraisal of precious cargo at Netaji Subhash Chandra Bose International (NSCBI) Airport (cargo complex), Kolkata. The jewellery exporters in Kolkata have their goods examined in a room along with all other commodities by a customs officer at the Kolkata airport. The existing premises/room, where such examination is undertaken is so small, that there is hardly any space to accommodate the customs officer with 2-3 representatives from the exporter. There is no proper waiting area where representatives of exporters can wait their turn for the examination which would result in theft/ pilferage and compromise in secrecy of

designs. After examination, the jewellery needs to be repacked, which is being done at the corridor outside the room. Then the exporter has to take the consignment to a diagonally opposite room for sealing. These issues need to be addressed.

- Requirement of placing technically qualified personnel as gold jewellery appraisers: Though the Gem Jewellery Export Promotion Council (GJEPC) trains Customs officials for gold appraisal, they are transferred/promoted quickly. The fresh appraisers, not being technically qualified, insist on bringing the valuer along with the export cargo resulting in higher cost for the exporters. This needs to be addressed.

In the Budget 2014-15, some measures for Gems and Jewellery exports were announced which include, among others, full exemption from basic customs duty for pre-forms of precious and semi-precious stones.

### **2.2.7 Electronics and IT Hardware Manufacturing:**

- ITA-1, adverse inverted duty structure and CENVAT credit: The Indian electronic assembly industry was expected to grow into a full blown manufacturing industry through its homegrown component industry. However, ITA-1 and the adverse effect of the inverted duty structure have derailed the progress of the electronic manufacturing industry in India and India has become dependent on countries like China for import of finished IT products. The levy of the 4 per cent SAD on the components also affects the IT hardware manufacturing industry as CST is at 2 per cent making trading more viable than manufacturing. The important issue is of CENVAT credit. So either, the 4 per cent SAD could be removed on the components used in the manufacture of IT hardware products or at least brought down to 2 per cent which is the same as CST. So, any excess credit on account of the existing inverted duty that remains un-utilized, could be refunded at the end of every quarter. Alternatively, the excess credit which is available with the manufacturer could be allowed to be utilized for payment of customs duty. This could be in line with the duty scrips which can be utilized for payment of the customs duty. Electronic manufacturers are also allowed to avail credit of service tax paid on availing the services in relation to the manufacturing of finished goods. Cenvat Credit on purchase of Capital Goods is also allowed which only contributes to accumulation of the unutilized Cenvat Credit. This has been further aggravated by the invokement of Rule 2(a) of General Interpretation of Rules whereby the components imported as (completely knocked down) CKDs by the manufacturers are classified as a finished products, which attracts higher rate of duty. The activity of electronic manufacturing has been arbitrarily declared as mere assembly thereby denying the local manufacturers the credit of being genuine manufacturers. This discourages the local manufacturers from carrying out the manufacturing activity. Many IT hardware manufacturing units like Gigabyte, Kobien, D-Link have either discontinued their manufacturing activity or limited the same and ventured into trading. This issue needs to be resolved.

To boost domestic production of electronics goods and reduce dependence on imports, Government has announced the following steps in the Budget 2014-15:

- Impose basic customs duty at 10 percent on specified telecommunication products that are outside the purview of the Information Technology Agreement;
- Exempt all inputs/components used in the manufacture of personal computers from 4 percent special additional duty (SAD);
- Impose education cess on imported electronic products to provide parity between domestically produced goods and imported goods;
- Exempt 4 percent SAD on PVC sheet and ribbon used for the manufacture of smart cards.
- Since the existing duty structure incentivizes imports rather than domestic manufacture of solar photovoltaic cells and modules. Exemptions from basic customs duty are given for the following:
  - specified inputs for use in the manufacture of EVA sheets and solar back sheets;
  - flat copper wire for the manufacture of PV ribbons.

#### **2.2.8 Leather Industry**

- Tackling removal of GSP by EU: European Union has removed the GSP benefits for finished leather exported from India for the period 1.1.2014 to 31.12.2016, which will increase the import duties by 2- 3.5 per cent, while countries like Pakistan have been granted GSP + status by EU, which poses a challenge to India. Countries like Bangladesh are also enjoying zero import duty for most leather products and footwear in countries like European Union, Japan etc., on account of their Least Developed Country (LDC) Status. The anti-dumping duty of 16.5 per cent levied for China and 10 per cent levied for Vietnam by EU for import of leather shoes under HS Code 6403 has been removed after March 2011 resulting in the increase in the competitive advantage enjoyed by these countries. Also, exports of leather footwear under 6403 from China & Vietnam to EU have increased in 2012 as compared to 2011 while exports from India have fallen. India needs to find ways to face this challenge including forming useful FTA with EU.
- Removal of GPT by Canada: Canada will also be removing the General Preferential Tariff (GPT) tariff for 72 countries including India with effect from 1.1.2015 resulting in import duties for leather goods and footwear increasing in the range of 1 per cent - 20 per cent for these items. Footwear including Non-leather footwear is the major product of import by Canada accounting for about 40 per cent of its total imports. India's competitors, Pakistan and Bangladesh will continue to enjoy the GPT status offered by Canada even after 1<sup>st</sup> January 2015. India needs to be ready for this situation and useful FTAs with Canada needs to be pursued.

- Raw material availability- constraints on supply side: The Government of India has fixed an export target of US\$ 14 billion for the leather sector to be achieved by the end of XII Plan i.e. by 2016-17 for which about 6.2 billion sq.ft of leather is required, as against the present production of 2.00 billion sq.ft. Even assuming that the industry is not able to reach the export target of US\$ 14 billion, but aims to double its exports from the current level of US\$ 5 billion per annum to US\$ 10 billion in 2016-17, the requirement of leather will be to the tune of 5 billion sq.ft, that is an additional 3 billion sq.ft. In order to augment the raw material availability in the country, the following measures could be considered.
  - Increasing the export duty on raw hides & skins and wet blue leathers from the present 60 per cent to, say, 100 per cent and maintaining the export duty of 60 per cent on crust leather and 15 per cent on East India (EI) tanned leather;
  - Strict inspection of finished leather export consignments to prevent free outflow of raw materials and enhancing export of value added products.
  - Encouraging Private Bonded Warehouses exclusively for importing and distributing hides, skins and leathers.
  - Including places like Kanpur and Jalandhar as designated ports for importing raw hides & skins through establishment of Animal Quarantine and Certification Stations (AQCS)
  - Restoring the facility of import of Second Hand Machinery under EPCG (which was removed w.e.f. April 2013) as many factories are closing down in Europe due to fall in production base and the machinery in these factories are in very good condition. India needs these machinery as about ninety eight per cent of the tanning machinery and ninety five per cent of the footwear and products machinery are imported as such machinery are not manufactured domestically.
  - Early finalization of negotiations for Trade Agreements with EU, Russia, Canada, Australia etc., where there is good market potential for Indian leather sector.
- Product diversification: There is a need to focus on exports of ladies and children's footwear as 75 per cent of the world footwear market is dominated by these segments, while these constitute only about 46 per cent of exports of India's footwear segment.

### **2.2.9 Rubber products**

- Safeguard duty for carbon black: Carbon black, an important input for manufacturing rubber products has been put under safeguard duty under section 8(b) when imported from China. Due to this reason when an exporter imports the same under advance authorization he is required to pay the said duty. Earlier safeguard duty was imposed under Section 8(c) which would exempt the advance authorization holder for payment of such safeguard duty. This needs to be examined and addressed.

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