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ECONOMY

As Global Trade Slows, India Needs to Start Firing on All Cylinders

BY NILANJAN BANIK ON 08/04/2016 • 4 COMMENTS

Exporters in eastern India are forced to transport edible items by road to Kakinada – a port in Andhra Pradesh which offers mid water loading facilities – to avoid contamination. Credit: Derell Licht, FLICKR/CC BY 2.0

An important paradigm shift is underway. Over the course of last century, global trade was growing faster than global GDP (read: income). However, post-2008, this trend is reversing. Presently, world trade is growing more slowly than world GDP. Recent estimates by OECD in 2015 indicate trade figures for the G-7 group of countries fell by 7.1 per cent while trade figures for major emerging economies including Brazil, China, India, Indonesia, Russia, and South Africa slumped by 9.5 per cent.

This trend is worrisome. The beneficial effect of trade in increasing productivity and income growth is well known. Economies such as South Korea, Taiwan, and much of the South East Asian nations catapulted to a higher growth trajectory through trade. In fact, as evidence from China suggests trade has been instrumental in lifting millions out of poverty.

Economists argue four important reasons as to why growth in global trade is slowing down. First, the financial crisis in the US, and more recently in Europe has slowed down world trade. These two regions account for more than half of world trade volumes, and a slowdown in these regions will naturally have an impact on global trade. Second, with an economic slowdown there will be a concomitant fall in investment across national boundaries, which means lower trade.

Third, a slower intra-industry trade, particularly, those associated with the international fragmentation of production. A fall in investment flow negatively affects trade in similar in commodities such as cars, computers, air conditioners, and refrigerators. Finally, in event of slower trade growth, individual countries turns protectionist. Protectionism is becoming evident in terms of an increase in applied tariffs (although, keeping them below the rates countries bound at WTO) and non-tariff barriers (NTBs), mainly in the form of anti-dumping measures, sanitary and phytosanitary sanctions, and even through the provisions granting subsidies to domestic producers.

In the event of this global scenario, India has a lot to worry about. Recent trade data for India (April-February 2015-16) suggests, in dollar terms, cumulative value of exports were at $238.4 billion as against $286.3 billion during corresponding period a year earlier, registering a negative growth of 16.7 per cent.

Pipe dream

Apparently, Prime Minister Narendra Modi's aim to almost double goods and services exports to $900 billion in the next four years, and grabbing a 5 per cent share of global trade by 2020 (up from 1.7 per cent global exports share at present) seems overly ambitious. India's largest export item, namely, refined petroleum products has fallen by 15 per cent, lowest in nine years. Interestingly, this fall is not only due to a fall in international crude price (as some experts would argue) but also because of declining export volumes. Growth of other important export items such as metal, electronics and machinery are also falling.

Interestingly, despite the Chinese economy slowing down, the export figures for China in 2014 was recorded at $2,342.3 billion in comparison to India's $317.5 billion. If one takes into consideration items such as iron and steel, chemicals, machines and telecommunication equipment, textiles and clothing, where China and India compete with each other in international market, the former's share in the world market is much higher.

Indian businesses are losing competitiveness due to high borrowing costs and because of country's long-standing weaknesses such as bad infrastructure, red tape and corruption.

In this regard there are important lessons to be learnt from China. The relative success of China lies in its ability to provide better physical infrastructure and easy availability of cheap credit. Within infrastructure funding, the contribution of India's private sector is only 36 per cent in comparison to China's 48 per cent. This is notwithstanding the fact that China's GDP is almost four times the size of India's GDP.

In many instances, Indian exporters of edible items like rice, tea etc., find it difficult to ship their product from the nearest port of exit. For example, exporters in eastern India are forced to transport edible items by road to Kakinada – a port in Andhra Pradesh which offers mid water loading facilities – to avoid contamination. The congested Kolkata port handles export of iron ore and other metals scraps, items which cause pollution (read dust particles) and thereby expose edible items to the risk of contamination.

The Chinese government offers other goodies as well. On top of cheaper credit, Chinese manufacturing units also avail cheaper power, water and land. Besides providing these indirect subsidies, the government also gave differential subsidy. For example, production of staple fibres, meant for domestic consumption, attract lesser subsidy as compared to when it is used as an input for making exportables, like, polyester yarn. The special economic zones (attracting zero tariffs) were built with the idea of making China the assembly hub of the world – where inputs were imported from neighbouring Asia, assembled in China and thereafter exported to the rest of the world. Coupled with these, a much larger scale of operation by lowering per unit cost of production, explains China's much higher share of world exports.

Lower transaction costs have also given Chinese exports a much-needed competitive edge. For example, it takes around 40 days to book a container for exports in India as compared to just one day in China. On the contrary, logistics costs in India are among the highest in the world at 13 percent of GDP. For instance, trucks in India have to pass through multiple checkpoints and stop at state borders to pay toll taxes and octroi, for inspections, etc. An estimate of the time taken at checkpoints shows that for a journey of 2,150 kilometres between Kolkata and Mumbai a truck had to stop at 26 checkpoints for as much as 32 hours. This torturous journey is likely to continue unless the government implements GST. With respect to 'Trading Across Borders', in 2013, India ranked 132 out of 189 countries, while Bangladesh, Nepal, Pakistan and Sri Lanka ranked 130, 177, 91, and 51, respectively.

Inadequate infrastructure is responsible for holding back GDP growth by roughly 2 per cent, or an annual hit of approximately $20 billion to economic progress. The government, on its part, has set a huge target of doubling investment in infrastructure from Rs. 20.5 trillion ($0.33 trillion) to Rs. 40.9 trillion ($0.65 trillion) during the twelfth five year plan period (2012-2017). To achieve this target, the government will require investment from the private sector.

Ease of doing business

Although reforms in India are taking place, they are far from complete. Companies face a maze of government orders, regulations, rules and procedures, which raise the cost of doing business in India. In its Doing Business Report-2015, the World Bank placed India in the 142nd position out of a sample of 189 countries, with a ranking that is worse than China, Sri Lanka, Bangladesh, and Pakistan when it comes to the convenience of doing business. The Doing Business Report-2016, saw India's performance improved, moving up by 12 places to 130th position, mainly because Central government specifically stepped in to improve the ease of doing business in Delhi and Mumbai (as opposed to the rest of India) – the two cities where World Bank observers undertake surveys to examine the ease of doing business.

Even in terms of productivity and efficiency, India needs to improve. According to the APO Productivity Database 2014, average Total Factor Productivity (TFP) growth in India rose from 2.0 per cent in 2000-05 to 4.7 per cent during 2005-10, but fell to 0.9 per cent in the following two years. However, for China average TFP growth was 3.9 per cent during 2000-05, rising to 4.2 per cent during 2005-10, and falling to 2.1 per cent over the next two years. During 2010-12, while TFP contributed 11 per cent to GDP growth in India, its share in China's GDP growth was 26 per cent. Average TFP growth over the last four decades in India has been 1.4 per cent as compared to 3.1 per cent in China.

Equally important is to undertake a more effective stance at regional trading forums. The South Asian Free Trade Area (SAFTA) has met with limited success. Negotiators from ASEAN regions accuse Indian policymakers of not willing to give them market access to items originating from ASEAN countries. Most of the tradable items are under negative lists (outside the purview of basic zero custom tariffs). India-Japan CEPA has resulted in limited gain for services involving movement of professionals such as nurse and yoga teachers, and trade in Indian generic pharmaceutical products. India policymakers need to indulge in more effective negotiation to sell our Mode 1 and Mode 4 services, areas where we have a comparative advantage.

Nilanjan Banik is an Economist and author of the book titled, The Indian Economy: A Macroeconomic Perspective

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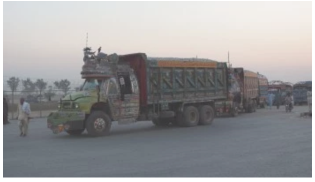

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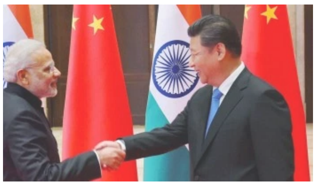

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satish • 2 months ago

India should focus on autarky. Instead, the Indian government bureaucrats, including at RBI are hell bent on making India dependent on foreigners and do not consider Indians good enough while enjoying all state benefits. The ONLY way for India to become the No. 1 economy in the world is to follow my eleven step guideline:

1. Elimination of all direct taxes, octroi, capital gains tax, state entry tax. GST rate should be less than 10%, ideally at 8%.
2. The RBI interest rate should be no more than 4% with commercial bank lending rates no more than 6%.
3. Indirect taxes should be no more than 12%.
4. Government, both central and states should charge for the services they provide

services they provide.
5. The absolute size of the government, both central and states should be decreased on year on year basis.
6. The government should get out of running businesses, airlines, etc. Navratna company holding by the government should be less than 25%. Executive decisions should be left to professionals. The IAS lobby should be removed from management.
7. Young, unemployed youth should be involved in either the defence sector, including air force, army, navy or in sports, focusing on getting Olympic medals rather than Cricket.
8. Education standard should be nationalized with certain minimum qualifications compulsory for any job. Proficiency in English should be mandatory.
9. Government should focus on industrialization with USA as the benchmark. It should aim to achieve supremacy over USA in every sector.
10. Education and especially higher education should be world class, with an aim for becoming the education center of the world.
11. And last but not the least, RESERVATION in jobs and promotion, and higher education should be permanently removed.

Of course, none of the above is likely in the next 50 years. The only option left for the intelligentsia is to abandon all hope and the country.

2 ^ | v • Reply • Share ›

criticalobserver • 2 months ago

China has a political system which may be described as "infrastructure construction friendly' whereas India has an unfriendly system. Much of it is due to the dysfunctional nature of Western style Multi-party democracy which is failing all over the world. Politicians spend their time arguing and debating with each other rather than doing things. That is the reason why the late Lee Kuan Yew of Singapore said that " Indians talk while the Chinese do" !

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Sayantan Hazra • 2 months ago

Great piece. However, it would to be nice to hear what progress has been made with respect of Ease of Doing Business, and why India's ranking has jumped 12th place. There must be something good happening.

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Srinivasan Gopalan • 2 months ago

No doubt, the author has made an excellent exposition on what constraints the country's export sector is plagued with and the various remedial measures he has outlined deserve a glance by the haughty officials cocooned in their Udyog Bhawan office. But the reality is that the world economic growth and the merchandise