E-Content for M. A. IV Sem.

Paper IV

Dr. Hilal Ahmad

Department of Economics

S.J.N.M. (P.G.) College

India's Trade Policy Since 1947-1991

Historically, **India's trade policy** has passed through many stages, studded with a number of transitory variations. In a sense, it consisted of a series of short-term measures for dealing with an ever-changing economic situation. Broadly speaking India pursued a path of planned regulation till mid-1980s, a partial liberalisation from mid-1980s and explicit liberalisation 1990 onwards. The process of liberalisation is still on and far from finished.

It is noteworthy that India did not have a clear cut Ex-Im trade policy before Independence, except that the Government had adopted a form of discriminatory protection policy since 1923 in the form of protective import duties for selected products. After Independence, our foreign trade policy became an integral part of our general economic policy and planned development.

It was meant to sub serve the objectives of our planned growth. Factually, however, we made several mistakes, such as, over-dependence upon official regulation and import substitution. In contrast, insufficient attention was paid to building up our export competitiveness and diversification into new export items and new export markets.

Our trade policy, prior to the one adopted in July 1991, may be examined with reference to the following time spans.

Trade Policy 1947 to 1952:-

Theoretically speaking, during this period, we could liberalise our imports to some extent by drawing upon our accumulated sterling reserves (that is, foreign exchange reserves in the form of British currency on account of trade surplus during World War II). However, the British authorities were not in a position to allow a free use of these balances. The reason was that, having suffered during the War, British economy was not able to supply us with our import needs against our accumulated sterling balances.

We could meet our import needs only from the US and for that we had to sell pounds, buy dollars and pay the US exporters. But on account of destruction caused by the War, Britain was itself in need of aid from the USA. Consequently, we were compelled to adopt an overall restrictive import policy supplemented by measures for boosting exports to the US. One of the steps for boosting exports to the dollar area was devaluation of the rupee in September 1949.

However, the export promotion measures had a limited impact. This was because our economy was facing a widespread scarcity of both essential and exportable goods. In addition, the Indian authorities failed to relax restrictions on exports including those in the form of export quotas, export duties and export controls. Thus, relying solely upon devaluation of the rupee for remedying trade deficit could not be expected to succeed.

Trade Policy 1952 to 1957:-

This period was marked by limited, liberalisation of our foreign trade. There was a perceptible improvement in our food supply, and exports were encouraged by removal or relaxation of some export restrictions. But our exports could not increase significantly due to a widespread scarcity of supplies. Moreover, our exports were mainly primary sector items. As yet, we were not in a position export industrial products and at competitive rates.

On the other hand, liberalisation of imports led to a tremendous increase in our imports. Deficit trade balance depleted our foreign exchange reserves which led to unfavourable balance of payment (BoP). In the absence of adequate capital inflows, we were forced to reverse our trade policy.

Trade Policy 1956-57 to 1965-66:

This period was marked by a persistent shortage of foreign exchange and deficit trade balance. But our trade policy laid greater emphasis on import restrictions than on increasing export earnings. A reformulated rigorous trade regime made an extensive and simultaneous use of not only overall import controls, but also of controls meant for specified individual items. The trade regime was also backed by an elaborate system of "exchange control" (that is, a set of restrictions on making payments in foreign exchange). Faced with a persistent shortage of foreign exchange, the authorities also initiated steps for numerous trade agreements with Soviet Russia and other Eastern European countries for barter trade and trade based on rupee payments. At the same time, it was realised that a long-term solution of the problem of deficit balance of trade lay in increasing and diversifying our exports.

However, we failed to relax the bureaucratic grip upon our exports. An effective solution to this problem would have been that of removing official controls and regulations and providing export subsidies. This, however, hardly, took place. Rather, exporters had to surrender their earnings of foreign exchange to the authorities. And, this amounted to a major disincentive for them, particularly because they could easily sell their products within the sheltered domestic market at high profit margins.

Also, the policy of depending upon traditional trade partners with insufficient exploration and development of new markets continued to be a hallmark of our foreign trade policy. For meeting our payment obligations, we tried to increase our external borrowings (which eventually made us heavily indebted to foreign countries).

Another strategy adopted for solving our deficit trade balance was that of import substitution. This policy suffered from some fundamental drawbacks. In several cases, it involved use of imported technology which added not only to our current import needs but also increased our future maintenance imports. Dogged by bureaucratic intervention and monitoring, delays and cost over-runs became an integral part of our import substitution projects.

Trade Policy 1965-66 to 1975-76:-

The salient feature of our foreign trade policy of this period was the devaluation of the rupee on 6thJune, 1966. Mudaliar Committee (1962) had made some recommendations for reformulation of our trade policy. However, its recommendations were meant to be implemented without dismantling the bureaucratic regulatory framework and planning. They included, among others, increased allocation (obviously by the authorities) of raw materials to export-oriented industries, income tax relief on export earnings, export promotion through import entitlement, setting up of an Export Promotion Advisory Council, and a Ministry of International Trade.

That way, even this Committee stuck to the prevalent atmosphere of those times, and recommended, not the strengthening of market forces, but that of the administrative controls and government intervention. Such an approach suffers from some inherent drawbacks and is prone to failure.

During the period under consideration, the structure of our economy was such that it was not possible to reverse our deficit trade balance simply by devaluing rupee. Since we failed to take appropriate follow up steps, our balance of trade worsened from a deficit of Rs.599 crore in 1965-66 to Rs. 921 crore in 1966-67.

However, the situation started improving from the following year, and by 1970-71 our trade deficit had declined to Rs. 99 crore, and in 1972-73 we had, for the first time, a trade surplus of Rs. 104 crore. But this situation proved to be unsustainable in the wake of a major hike in petroleum prices. Our trade deficit, with a transitory surplus of Rs.68 crore in 1976-77, continued to rise till 1990-91.

Trade Policy 1975- 76 to 1990-91:-

1975-76 marked an adoption of liberal import policy by the government which, backed by certain measures, was expected to effectively tackle the problem of persistent trade deficit. During 1977-79, import of essential goods was also liberalised as a means for checking inflationary price rise.

However, this was the period when we were also faced with restricted export markets on the one hand and increasing import prices on the other. The result was that our trade deficit increased from Rs.1085 crore in 1978-79, to Rs. 2725 crore in 1979-80 and further to Rs. 5838 crore in 1980-81.

It is noteworthy that in 1981 we had to go in for an IMF loan. IMF, as matter of policy, insisted on several pre-conditions. It insisted that we should try to remedy deficit trade balance by measures of export promotion and also use import liberalisation as a means for export promotion. This approach was also endorsed by the P.Tandon Committee (1982).

However, this policy could not help us in reducing trade deficit. Our imports rose faster than our exports. Trade deficit shot up from Rs. 2725 crore in 1979-80 to Rs. 5838 crore in 1980-81 and with some variations, rose to Rs. 8763 crore in 1985-86, and further to Rs. 10645 crore in 1990-91.

Though Abid Hussain Committee (1985) advocated an approach of balancing import liberalisation with export promotion, the government continued with its emphasis on import liberalisation by claiming that it was necessary to do so for export promotion. It may be noted here that the measures adopted by the government in the latter half of 1980s did result in a rapid increase in our volume of trade, but the increase was an imbalanced one.

Our exports increased by nearly two and half times between 1985-86 and 1989-90, but increase in imports was faster still. In 1990-91, our exports and imports had reached Rs. 32553 crore and Rs. 43198 crore respectively as against Rs. 6711 crore and Rs. 12549 crore in 1980-81.

A concomitant result of this new policy was our growing need to borrow from abroad. This added to our external indebtedness and cost of debt servicing. The Import-Export Policy announced on April 30, 1990, for a period of three years revealed a shift in government thinking. It accepted that that our balance of payments position could be improved not so much through import restrictions as through export promotion.

Consequently, it quickened the pace of import liberalisation coupled with added incentives for export promotion. Amongst other measures, it expanded the list of imports under Open General License (OGL) and introduced a scheme of automatic licensing up to 10 per cent of the value of the previous year's import license. It also modified various other provisions and regulatory measures. However, in totality, the trade continued to be over-regulated.

By this time, it was amply realised by observers and analysts that our trade policy was not fully compatible with our social and economic objectives and it did not fit in with the realities of international markets. While there was an all-round recognition of the need for a more fundamental change in our policy, the liquidity crisis of 1991 necessitated an immediate shift in it.

Suggested Readings:-

1. Economic Survey of India
2. Indian Economy by Dutt and Sundaram
3. Indian Economy by Misra and Puri