Trade policy

Recent trade policy measures

6.108 Recent trade policy measures include reduction in peak rate of basic customs duties from 12.5 per cent to 10 per cent, reduction in the customs duty on polyester fibres and yarns, cut and polished diamonds and rough synthetic stones, etc., raw materials such as DMT, PTA and MEG, textiles machinery, etc., announced in the Union Budget 2007-08 and subsequently. The Mid-term Review of Annual Policy for the Year 2007-08 of RBI has also permitted all exporters to earn interest on their Exchange Earners Foreign Currency (EEFC) accounts as a temporary measure. The range of hedging tools available to the market participants has been further expanded keeping in view the changes in the foreign exchange market. To make exports an effective instrument of economic growth by giving thrust to employment generation particularly in semi-urban and rural areas, in the Annual Supplement to Foreign Trade Policy (FTP) 2004-09 in 2007, initiatives have been announced which include broadening the scope of Vishesh Krishi and Gram Udyog Yojana (VKGUY) by inclusion of forest-based products like artistic wooden furniture, etc., and a number of new agricultural products. The Foreign Trade Policy measures also include the inclusion of new markets and products under the Focus Market Scheme (FMS) and the Focus Product Scheme (FPS), respectively, exemption/refund of service tax on services related to exports whether in India or rendered abroad, duty free import of tools, machinery and equipment for handicrafts and gems and jewellery sector, and enhancement in the limit of duty free import of samples to Rs. 75,000 per annum.

6.109 A new scheme was launched for duty free import of capital goods related to infrastructure meant for agro processing to promote agricultural exports and provide employment. On the technology front, to harness the potential of skilled manpower, high-tech products scheme was initiated allowing duty free credit as an incentive against such exports. EPCG Scheme has been rationalized and the tiny and cottage sector has been provided extended export obligation facility. Provision has also been made for waiver of export obligation because of *force majeure* or other unforeseen circumstances/reasons leading to the inability of exporters to fulfill export obligations. Issue of EPCG for import of spares, tools, spares and refractory was also allowed for existing imported plant and machinery (whether earlier imported under EPCG Scheme or not).

6.110 To promote exports from 100 per cent export-oriented units, incentives in the form of VKGUY, FMS and FPS have been extended to such units not availing of IT benefits. DEPB Scheme's validity was extended up to March 31, 2008. The scheme has been modified to allow reimbursement of the cost of duty on fuel and special additional duty by way of notifying brand rate of DEPB for such products. On the trade facilitation front, a number of measures have been taken to further reduce transaction cost. These include dispensing with the requirement of double verification at customs for EPCG and advance authorization schemes, downsizing of the application forms required for availing of various schemes, and removing uncertainty regarding taxation for EOU units.

6.111 All the above policies announced in the budget, the subsequent policy announcement by the RBI and the Foreign Trade Policy, 2004-09 in April 2007 helped India's merchandise exports to grow at more than 20 per cent during the first nine months of this fiscal, despite appreciation of the rupee.

State-wise exports

6.112 State-wise exports are reflected in data on state of origin of export goods which at present is the only available comparable data for State-wise exports. Maharashtra followed by Gujarat, Tamil Nadu and Karnataka were the major merchandise exporters with a share of 68.2 per cent in total exports in 2006-07. In 2006-07, export growth was high in the case of Gujarat, Andhra Pradesh, Tamil Nadu and Orissa (Table 6.31).

6.113 To encourage exports among States, allocation under the Assistance to States for Development of Export Infrastructure and Allied Activities (ASIDE) scheme has been increased from Rs. 400 crore in 2005-06 to Rs. 440 crore in 2006-07. Under ASIDE, projects aimed at balancing of critical infrastructure for exports are approved viz. creation of new Special Economic Zones and augmenting facilities in existing ones, equity participation in infrastructure projects, development

Table 6.31 Exports by state of origin of export goods during 2005-06 and 2006-07

State	(US$ million) 2006-07	Share (%) 2006-07	Growth rate (%) 2006-07
Maharashtra	36143	28.6	13.0
Gujarat	24209	19.2	66.1
Tamil Nadu	13097	10.4	29.4
Karnataka	12676	10.0	13.8
Andhra Pradesh	5479	4.3	35.9
Delhi	4880	3.9	-7.2
West Bengal	4011	3.2	12.6
Haryana	3792	3.0	16.1
Uttar Pradesh	3632	2.9	7.2
Rajasthan	3356	2.7	20.3
Kerala	2293	1.8	16.1
Punjab	2148	1.7	-8.9
Madhya Pradesh	1993	1.6	-25.0
Orissa	1971	1.6	35.5
Grand Total	**126360**	**100.0**	**22.6**

Source: DGCI&S.

Note: The above data has been generated by "state of origin of export goods" as reported in the DTRs by the customs.

of complementary infrastructure such as roads connecting production centres to ports, setting up Inland Container Depots (ICDs) and Container Freight Stations, stabilizing power supply, etc. States have shown keen interest in funding projects under ASIDE scheme and the funding pattern of the projects shows a healthy mix of ASIDE funds, State Government funds and private sector participation, in a ratio of 4:4:2 indicating successful leverage of funds. States like Maharashtra, Tamil Nadu, Orissa, Karnataka and Gujarat have sanctioned quite a large number of projects under the ASIDE scheme. While 13 States have used ASIDE funding to an extent of more than 80 per cent of the project cost and have not leveraged any private sector funds or State Government funds, States have also leveraged funds from other sources.

Special Economic Zones

6.114 Another major policy issue in the trade sector which created a lot of heat was that of SEZs. The SEZ Act, 2005, supported by SEZ Rules, came into effect on February 10, 2006. The main objectives of the SEZ Act are generation of additional economic activity, promotion of exports of goods and services, promotion of investment from domestic and foreign sources, creation of employment opportunities and development of infrastructure facilities. Various incentives and facilities are offered to both – units in SEZs for attracting investments into SEZs (including foreign investment) as well as for SEZ developers. These incentives and facilities are expected to trigger a large flow of foreign and domestic investment in SEZs, particularly in infrastructure and productive capacity, leading to generation of additional economic activity and creation of employment opportunities. The SEZ Rules provide for different minimum land requirements for different classes of SEZs. Every SEZ is divided into a processing area where alone the SEZ units are set up and a non-processing area where the supporting infrastructure is to be created. The SEZ Rules also provide for simplified procedures for development, operation and maintenance of the SEZ and setting up units in SEZs, single window clearance both relating to Central as well as State Governments for setting up of an SEZ and units in a SEZ and simplified compliance procedures/documentation with emphasis on self-certification.

6.115 Consequent upon the SEZ Rules coming into effect from February 10, 2006, 439 formal approvals where granted, of which 195 Special Economic Zones have been notified and are in various stages of operation. These approvals are spread over 22 States and Union Territories and over 23 sectors. The benefits derived from SEZs is evident from the investment, employment, exports and infrastructural developments additionally generated (Box 6.7).

Customs duty exemptions

6.116 The Indian customs tariff regime was strewn with concessional duty notifications in the pre-1991 period, sometimes more than 500 in a year with the result that the schedule rate was practically inoperative. The exemption rate by notification ruled the tariff. The reduction of the peak tariff rate has made many exemptions redundant and simplified tariffs to an extent. However, exemptions including those given under special circumstances such as sudden increase in prices to provide relief to consumers, are still an important part of the customs tariff. As on January 1, 2008, there were 527 cases of duty exemptions industry/category-wise, the highest

Box 6.7 Special Economic Zones: Some facts

Exports from Special Economic Zones have been showing steady increase. As compared to exports of Rs. 22,840 crore made by SEZs in 2005-06, exports to the tune of Rs. 34,615 crore have been effected in the year 2006-07, registering a growth of 52 per cent. Projected exports for 2007-08 from Special Economic Zones is Rs. 67,088 crore.

In the SEZs which have been setup/notified prior to the coming into force of the SEZ Act, 2005, at present there are 1,277 units in operation, providing direct, employment to over 2 lakh persons (about 40 per cent of whom are women). Out of this, 36,463 persons are in the private/State Government SEZs, most of which had come up after February 2006. The newly notified SEZs, which have come up after February 10, 2006, have provided direct employment to 61,015 persons.

Private investments in the 19 SEZs which were set up prior to coming into force of the SEZ Act, 2005, is of the order of about Rs. 7,104 crore. Investment of the order of Rs. 67,347 crore has already been made in the newly notified SEZs which came up after February 10, 2006.

Apprehensions have been expressed on misuse of the scheme and relocation of existing industries into SEZs. However, experience has shown that these apprehensions are ill founded and fresh investments and employment have been flowing into the Special Economic Zones. For example, Nokia electronics hardware SEZ in Sriperumbudur is already providing employment to 6,637 persons, majority of whom are women. Hyderabad Gems SEZ has already employed 2,000 persons after providing training to them, out of which 1,200 are girls. They have projected direct employment of about 30,000 persons. Apache SEZ, being set up in Andhra Pradesh, is expected to employ 20,000 persons to manufacture 10,00,000 pairs of shoes every month. Current employment in Apache SEZ is 4,500 persons. Brandix Apparels, a Sri Lankan FDI project, is expected to provide employment to 60,000 workers over a period of three years. Even in the services sector, 12.5 million sq metres space is expected to be created in the IT/ITES SEZs which is estimated to translate into 12.5 lakh jobs. The benefits derived from multiplier effect of the investments and additional economic activity in the SEZs along with the employment generated is estimated to far outweigh the revenue losses on account of tax exemptions given to the SEZs. These SEZs are freshly developed industrial clusters and are not relocated from elsewhere.

Concerns have also been expressed regarding acquisition of agricultural land for setting up SEZs. The State Governments have been advised by the Centre that in case of land acquisition for Special Economic Zones, first priority should be for acquisition of waste and barren land and if necessary single-crop agricultural land could be acquired for the SEZs. If perforce a portion of double-cropped agricultural land has to be acquired to meet the minimum area requirements, especially for multi-product Special Economic Zones, the same should not exceed 10 per cent of the total land required for the SEZ. Various issues related to setting up of SEZs in the country, including issues raised by various political parties, have been addressed by the Empowered Group of Ministries (EGOM). Pursuant to the decision taken by the EGOM, all State Governments have been informed that the Board of Approval will not approve any SEZs where the State Governments have carried out or propose to carry out compulsory acquisition of land for such SEZs after April 5, 2007.

exemption (17.6 of the total) was for machinery. Exemptions under project imports where the duty ranges from Nil to 5 per cent as against the normal 7.5 per cent are important under the machinery head. The IT Agreement (ITA) signed at WTO under the "zero for zero" negotiations is another major category under exemptions. Under ITA, there are 82 entries in the exemption notifications covering some 217 lines for zero duty import. Agriculture is the third major sector under exemptions and this category along with edible oils has the highest exemption rates.

6.117 Formally, inter-budget tariff rate changes are also made through so-called "exemption notifications." Thus, for instance, a sharp rise in wheat prices may induce a reduction in import duty to zero. This change in duty is to be

Box 6.8 Types of customs duty exemptions

	Numbers
■ **Industry groups exemptions**	
● Exemptions without documentation or end-use/user conditions	348
● Exemption with documentation or end-use/user condition	174
● Exemptions based on tariff rate quotas	5
Total industry group exemptions	**527**
■ **Thematic exemptions**	
● Inputs for exports (raw material, components, consumables, machinery)	84
● Country preferences	26
● Government imports (defence)	2
● Disaster relief	2
● Personal imports and baggage	14
Total thematic exemptions	**128**
Total exemptions	**655**

Source: Based on BIGs Easy Reference Customs Tariff 2007-08 and a study.

distinguished from a duty exemption that applies only if the wheat is imported by a designated agency or only for supply to a designated user. There are many types of customs exemptions serving different purposes (Box 6.8). Exemptions result in distortions and discriminations in the economic structure resulting in tax arbitrage, rent seeking and a rise in transaction and administrative costs. There is a need for a systematic policy to weed out exemptions on both basic and additional duty. The ideal system is to adopt a low tax regime supplemented with very few exemptions in special cases. Each exemption notification could have a sunset clause which would trigger automatic review of the exemptions.

Contingency trade policy and non-tariff measures

6.118 Contingency trade policy and non-tariff measures (NTMs) continue to act as significant barriers to exports from developing countries, but with somewhat reduced intensity. Such barriers are considerably stiffer for products with lower value addition and lower technological content (for example, agriculture, textiles, and leather products), which are of major interest to developing countries like India. With its diversified manufacturing and export base, India has been one of the major users as well as one of the major targets of anti-dumping measures in the world (Table 6.32). During January-June 2007, WTO members reported

Table 6.32 Investigations initiated by top 10 users of anti-dumping measures, 1995-2007

Country	1995	2000	2001	2002	2003	2004	2005	2006	2006 Jan-June	2007 Jan-June	1995-June 2007
India	6	41	78	81	46	21	28	34	20	13	474
United States	14	47	75	35	37	26	12	7	0	2	375
European Community	33	32	28	20	7	30	25	35	17	0	363
Argentina	27	43	26	14	1	12	12	15	5	3	220
South Africa	16	21	6	4	8	6	23	3	2	3	203
Australia	5	15	23	16	8	9	7	10	9	0	189
Canada	11	21	25	5	15	11	1	7	4	0	141
Brazil	5	11	17	8	4	8	6	12	3	4	138
China PR	0	6	14	30	22	27	24	11	3	4	138
Turkey	0	7	15	18	11	25	12	8	0	0	109
All countries	**157**	**290**	**364**	**312**	**232**	**213**	**200**	**200**	**87**	**49**	**3097**

Source: WTO.

initiating a total of 49 new investigations. India reported the highest anti-dumping initiations with 13 new initiations (taking each country as one case), though it was lower than corresponding previous period, followed by Brazil (4) and China (4).

6.119 Countries use many mechanisms to restrict imports. Till the beginning of 1970s, tariffs were the principal mode of protectionism. But with successive rounds of GATT negotiations, there was a large drop in the average tariff levels of manufactured goods in the developed country markets. When tariffs paled into insignificance, NTMs were resorted to by a number of these countries. Despite the provisions under the various agreements and ministerial decisions for eliminating or disciplining NTBs, they continue to be largely non-transparent, ad hoc and complex. While direct NTBs (such as quantitative restrictions, tariff quota, voluntary export restraints, orderly marketing arrangement, export subsidy, export credit subsidy, government procurement and import licensing, etc.) are explicitly designed and implemented for purposes of restrictive trade, indirect NTBs (such as health and safety regulations, technical standards, environment controls, customs valuation procedures, rules of origin, labour laws, anti-dumping duties, countervailing duties, regional subsidization and subsidization of public enterprise, etc.) are notionally implemented to meet some other policy target but affect the trade flows in the process. While some NTBs are genuine, others are intended to restrict imports, insulating domestic producers from the effect of world prices. Of late, the nature of NTBs are changing with declining importance of traditional NTBs and growing importance of knowledge-based NTBs embodied in SPS (sanitary & phyto-sanitary) and TBT (technical barriers to trade) measures.

6.120 A significant proportion of exports of developing countries like India is affected by single or multiple NTMs imposed by developed countries on account of health safety, environmental and other concerns. Indian exports, in general, faced NTBs relating to (i) packaging and labeling regulations, (ii) standards, (iii) uniformity requirements, (iv) labour standards, (v) documentation and related procedures, and (vi) company and product registration. Compliance cost with the regulatory requirements is severe for smaller firms than bigger firms. India has been actively negotiating at multilateral and bilateral levels for removal of NTMs. However, India also has to improve its own standards related to SPS and TBT which can lessen the impact of these NTBs. Greater FDI and useful FTAs with major trading partners can also lessen the impact of NTBs. There is also a need to build up and update regularly the empirical database on NTBs which can provide inputs for arriving at suitable policies for negotiations at multilateral and bilateral levels and also help in the preparation of export strategies and policies.