At a standstill

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US move to withdraw privileges provides an opportunity for India to introspect on the general state of its exports.

The recent decision of the US to give notice of its intention to rescind India's export privileges under the Generalised System of Preferences (GSP) has refocused attention on the state of Indian exports. Under the GSP programme, the US provides duty-free access to 4,800 different goods from 129 designated countries. The immediate loss for India is preferential access at zero or minimal tariffs to the US market for around 1,900 products, which is over half of all Indian products.

The ministry of commerce has reacted to the news by asserting that the losses from the GSP withdrawal are going to be minimal. This assertion is based on the fact that the actual tariff advantage that India was getting from the programme was a meagre USD 190 million, which is just 0.4 per cent of the USD 50 billion over all Indian exports to the US.

The government's argument, unfortunately, misses the point that India is competing for market share in the US with a host of other low-income countries, including Mexico. In industries where margins are small, a very small increase in the market price can cause a large fall in the quantity exported. A potential fall in quantity exported will, of course, imply a much larger cost of losing GSP access. If exporters absorb the tariff increase, then their profit margins will fall, potentially inducing some of them to exit this market completely. The tariff benefit that India currently enjoys is low simply because average tariffs in the US are low. It cannot be used as an indicator of the potential cost to India of losing its GSP privilege.

The GSP development, though, provides a good opportunity for India to introspect on the general state of Indian exports. The raw fact of the matter is that India's share of world exports has been stuck at around 2 per cent for some time now. Essentially, our exports have been growing at the same rate as the rest of the world. For a country that has consistently been one of the fastest growing economies in the world, India's exports should be growing much faster. This is what one saw with China and the other East Asian economies over the last 30 years, and with Japan earlier. Clearly, something isn't working in India.

Despite the overwhelming attention that Indian service sector exports receive, around 63 per cent of total Indian exports are still of goods. It is true that the Indian service sector's share of world services exports rose sharply from 0.5 per cent in 1990 to 3.7 per cent in 2017. But this performance is hardly earth-shattering. The much less discussed Chinese service sector's share of world service sector exports more than tripled from 0.9 per cent in 1992 to 3.8 per cent in 2017.

The big disparity between China and India is goods exports. India's share of world goods exports rose from 0.5 per cent in 1990 to 1.7 per cent in 2017 while China's rose from 1.8 per cent to 12.8 per cent during the same period. Indeed, this has been one of the key vehicles for the rapid Chinese growth take-off. Rapid growth of the large-scale, low-tech, labour intensive merchandise goods export sector created a simultaneous increase in demand for relatively unskilled Chinese labour as well as an increase in demand for the rapid infrastructure rollout that China invested in. The labour demand soaked up the labour being released from agriculture while the infrastructure demand implied that the infrastructure investment was cost-effective.

The Indian export portrait, however, looks very different from the Chinese export landscape. Merchandise exports in India are concentrated in eight industries which collectively account for 85 per cent of India's merchandise exports. Amongst these top-8 industries are textiles, chemicals, machinery, vehicles and parts etc. Factories in these industries are mostly small, employing 100 or fewer workers. The productivity levels in these manufacturing establishments are also low. Though exporters tend to be larger and more productive than non-exporters, these are low by international standards.

The problem with the Indian export sector appears to be two-fold. The first is the general malaise afflicting the manufacturing sector. Existing labour and land laws make growing in scale a difficult proposition for firms. In addition, the infrastructure support that is needed to sustain production and distribution at scale is often missing. These include transport connectivity and reliable power supply. Firms find it optimal to stay small and operate with old technologies. Fixing this requires concerted action on multiple fronts. Addressing just a subset of these constraints is unlikely to work.

The second important issue is the trade regime. India has to send out unequivocal signals that it is a reliable trade partner that wants to become part of the global supply chain. To achieve this, India has to avoid falling back on discredited policies such as raising import tariffs under various guises like furthering the Make In India initiative or addressing current account imbalances. The withdrawal of GPS by the US is partly a response to these kinds of protectionist moves that have begun to again rear their heads over the last few years. Bad ideas, like bad smells, tend to hang around long enough to drive away customers. They need to be strenuously kept away from the policy levers.

Lastly, the EU is a bigger entity than even the US. Negotiations on a free trade agreement with the EU have been ongoing since 2007. The textile industry in Bangladesh has benefited at India's expense over the last decade due to the absence of such a trade agreement. It is high time we conclude an agreement with the EU.

Generalised System of Prefernces (GSP)

Why in the discussion?

- Most recently, US President Donald Trump has decided that he will remove the name of India out of the list of those countries, who are taking advantage of the generalised system of preferncal(GSP) program.
- This benefit is taken on those products, which are exported to the US.
- According to the US, these steps been have taken due to not a proper business coordiration by India.
- Apart from India, the name of Turkey has also been excluded from this list by US. Earlier, last year, Trump had ened the duty-free concession on 50 products imported from India.
- The United States began reviewing the conditions set for GSP in April 2018.

What is it?

- Thousands of products from the countries listed in the GSP list were brought in the US by allowing tax free exemption to promote economic development.
- The United States launched GSP on January 1,1976 to boost the economic growth in developing countries.
- So far, nearly 129 countries have got the benefit under the GSP for about 4,800 goods.
- The generalized preference system is an extended preferable system for developing countries (preference recipients or beneficiary countries) by developed countries (preference provider or donor country).

Benefit

- Under this system, developing countries get duty free access or entry with minimum fee or duty-free access in the market of developed countries with certain conditions.
- Through this, developed countries promote economic growth in developing countries and in less developed countries.
- Priority duty free arrangement is ensured for nearly 30-40 percent products of the nominated beneficiary developing counties. India is also a beneficiary developing country.
- Australia, Belarus, Canada, European Union, Iceland, Japan, Kazakhstan, New Zealand, Norway, Russian Federation, Switzerland, Turkey and the United States give GSP.

Effect on India

- The listed beneficiary countries in the US GSP program.
- Under this program, India gets exemption on the exports of 5.6 billion dollars (40 thousand crores). India will not get these benefits after being out of the program.
- In the year 2017, the US goods and services trade deficit with India was $ 27.3 billion ($ 2,730 million).
- India is the 11th largest trade surplus country for the US.

Expected Questions (Prelims Exams)

1. Consider the following statements :-

1. Generalized System of Preferences was started in June, 1976 by USA to boost the economic growth in developing countries.
2. At present India is the 11th biggest trade surplus country of America.

Which of the above statements is/are correct?

(a) Only 1 (b) Only 2

(c) Both 1 and 2 (d) Neither 1 nor 2

Expected Questions (Mains Exams)

Q. How the intention of rescinding the export privileges of India under the Generalized System of Preferences by the US will affect India ? Discuss.

(250 Words)

Note: Answer of Prelims Expected Question given on 15 Mar. is 1(c)