Research Paper

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Trade Liberalisation and its Impact on the Economy

Economics

KEYWORDS : Trade liberalisation, net factor income from abroad, trade composition, direction of trade

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ABSTRACT

Trade liberalisation has changed both the direction and composition of the country. It has worsened the situation of net factor income from abroad. However, this policy is unable to worsen the agricultural base of net factor income from abroad in the case of India.

Introduction

India's trade policy is decided by the Director General of Foreign Trade (DGFT) that belongs to ministry of Commerce and Industry. It is empowered under section-5 of 1992 Act of foreign trade to announce the trade policy. The trade policy which is being followed these days by India was announced in 2009 for 2009-2014. India followed various trade policies since 1991, the year of economic crisis. The present paper will make an effort to find an impact of this trade policy on the Indian economy since 1991.

Literature Review

International trade helps in upgrading technology, capital accumulation, changing industrial structure and institutional advancement. Trade affects positively to the national income **(Frankel and Romer, 1999).** Import of capital increases productivity in manufacturing sector **(Lee, 1995).** There is positive relationship between the GNP growth and import **(Kavoussi, 1984).** Active participation in import increases both the competition and terms of trade in the international market. Outward developing economies achieved much more growth in national income than inward developing countries **(Baassa, 1986).** Average growth rate of the economy becomes more in liberalized period than that of pre-liberalised one (**Sachs and Warner, 1995)**.

None of the literature has been done to know the impact of liberalization on the net factor of income. The present study makes an effort to do so in this field.

Objective

The present study aims to know the impact of trade liberalisation on the net factor income from abroad.

Methodology

The present paper follows the trade liberalisation data of India for the period of 1991 to 2012 to know its impact on direction, composition and on net factor income from abroad.

Analysis

India faced economic crisis in 1991. India had a trade deficit of $9.4 billion. The foreign exchange reserve in 1991 was able not to meet even more than four weeks of imports. Fiscal deficit was rising. Oil price was soaring high due to gulf war. Soviet block was broken out. India was suffering from political crisis. Credit rating of India was downgraded repeatedly. Non-resident Indian investment was fighting out. Investors were losing confidence in India.

India announced a new trade policy in 1991 and took various steps. It liberalised its economy. Foreign investors were given due confidence to invest in India. Industrial licensing Raj was abolished. Information technology was promoted. Monopoly and Restrictive trade was abolished. Producers were given freedom to diversify their production. New technologies were imported. Investment limit in SSI (Small Scale industry) was increased to attract investment. Restriction in importing capital goods was abolished. Indian currency was made convertible in current account. Industrial, trade and financial sectors were reformed. Deregulation of industrial sector was done to improve efficiency and competition. Number of industries reserved under government sector was reduced from 18 to 03 (Rail, Atomic and Defence). India switched over to flexible exchange rate. Quantitative restriction on import of manufactured consumer good was abolished. Interest rates on both the saving and fixed deposits have been deregulated. Consequently FDI (Foreign Direct Investment) increased in India.

Steps taken under 2009-2014 trade policy can be enumerated below. Under section-3 of trade policy Act, India provided incentives to exporters of various products. This trade policy started imposing **zero duty** on exporting capital goods to enhance technological capacity of India under **Export Promotion Capital Good Scheme.** India started **Focus Market Scheme at** international level to diversify markets itself. **Special funds** have been earmarked for SSI. Some towns have been identified to achieve export excellence. Under Town of Export Excellence Scheme Jaipur, Ludhiane, Muradabad and Kanpur have been selected. Under Focus Product System incentive of 3.00 per cent in the form of subsidy is given to producers. Paper less work has been started in trade sector to make it transparent. Ayat Niryat Form has been introduced to make simple process. Indian Trade Code (ITC) has been developed to code 153 products.

Impacts of various trade policies followed by India since 1991 may be enumerated as well as below.

(1) Impact on Direction of India's of Foreign Trade

India's export direction has been switching over from OECD countries to OPEC and developing countries. India's export share to OECD countries decreased from 56.40 per cent in 1991 to 33.81 per cent in 2012. This share to developing countries increased from 17.00 per cent in 1991 to 44.00 per cent in 2012 as shown as in table-1.

Similarly, India's import switched from OECD countries to OPEC and developing countries. The share of import from OECD countries declined from 54.00 per cent in 1991 to 29.67 per cent in 2012. This figure form developing countries increased from 18.40 per cent in 1991 to 32.25 per cent in 2012.

Table-1: Export direction of India

Countries to which India exports	1991	2012
OECD	56.40	33.81
OPEC	5.60	19.02
Eastern Europe	17.90	1.06
Developing Countries	17.10	44.00
Others	3.00	2.1
Total	100	100

Source: Economic Survey, Govt. of India

Table-2: Import direction of India

Countries from where India Imports	1991	2012
OECD	54.00	29.67
OPEC	16.30	35.44

Eastern Europe	7.80	1.75
Developing Countries	18.40	32.25
Others	3.50	0.89
Total	100	100

Source: Economic Survey, Govt. of India

(2) Impact on Composition of India's Foreign Trade
Export composition as shown as in table-3, infers that share of crude and a petroleum product has increased from 2.90 per cent in 1991 to 18.25 per cent in 2012. Export share of both the agricultural and industrial products has declined in 2012 in the comparison of 1991.

Import composition, as shown as in table-4, delves that share of petroleum products has increased while those of the commodities has decline in the 2012 in the comparison of 1991.

Trade policy has affected the India's trade composition in both the export and import.

India is exporting crude petroleum products and importing petroleum products. In this field, import substitution has not taken shape.

Table-3: Export Composition of India

Exported Commodity	1991	2012
Agriculture and allied products	19.50	12.29
Ores and minerals	4.40	2.67
Manufactured goods	73.0	61.32
Crude and petroleum products	2.90	18.25
Other unclassified items	0.2	5.47
Total	100	100

Source: RBI

Table-4: Import Composition of India

Imported Commodity	1991	2012
Petroleum Products	24.90	31.67
Capital goods	24.10	20.32
Pearls and precious stones	8.70	6.24
Iron and steel	5.00	2.46
Fertilisers	4.10	2.37
Edible oils	0.80	1.97
Others	32.40	20.97
Total	100	100

Source: RBI

(3) Impact on Net Factor Income of India from abroad
India's trade libaralisation has worsened the situation of net factor income from abroad. Net factor income from abroad was - $ 168.49 billion in 1991 which further declined to - $ 518.28 billion in 2012. Net factor income of both the industrial and services sector in India is negative while that of agricultural sector is positive. It clearly shows that liberalisation is still unable to break the position of agriculture, which is the backbone of India.

Table-5: Net Factor Income of India from abroad (Rs. Billion)

year	Net Factor Income from abroad (NFIA)			
	Agriculture (a)	Industry (b)	Services (c)	NFIA (a+b+c)
1990-91	48.06	-66.18	-224.62	-168.49
1991-92	63.59	-7.46	-188.1	-176.3
1992-93	61.64	-49.84	-294.74	-178.12
1993-94	102.59	14.03	-147.33	-162.05
1994-95	72.85	-87.57	-244.25	-164.3
1995-96	145.07	-65.12	-259.19	-176.72
1998-97	175.48	-93.01	-166.07	-169.49
1997-98	160.48	-163.9	35.72	-138.24
1998-99	109.44	-283.4	-81.73	-146.87
1999-2000	92.46	-157.6	-425.14	-163.75
2000-01	165.71	95.68	-342.45	-238
2001-02	134.72	-30.27	-389.5	-213.71
2002-03	170.45	5.34	-144.67	-189.6
2003-04	152.93	-197.86	318.04	-206.93
2004-05	387.9	-912.87	729.16	-223.75
2005-06	277.17	-1230.1	1115.82	-248.96
2006-07	376.49	-1741.3	1733.34	-295.15
2007-08	539.73	-2568.2	2902.38	-171.79
2008-09	550.94	-3625.1	2961.11	-253.84
2009-2010	383.29	-3598.2	3433.64	-276.64
2010-11	673.01	-4383.3	4759.77	-527.76
2011-12	1183.33	-6470.9	4769.25	-518.28

Source: (1) DGCI&S, Ministry of Commerce, Kolkata
(2) RBI, Government of India
(3) Economic Survey

Conclusion
From above one can find that trade liberalization has both the positive and negative effect on the Indian economy. Both the trade direction and composition has changed in favour of developing economy. Net factor income has been worsened by liberalization and trade policy.

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