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Content

INDIA'S FOREIGN TRADE AND INVESTMENT

Sample Preview of the Solved Sample Question Papers

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QUESTION PAPER

June – 2024

(Solved)

INDIA'S FOREIGN TRADE AND INVESTMENT (M.C.O.-15)

Time: 3 Hours] *[Maximum Marks: 100*

Note: *Attempt any five questions. All question carries equal marks.*

Q. 1. "New foreign investment policy is described as a boon for attracting foreign capital in India." Do you justify the statement.

Ans. Ref.: See Chapter-2, Page No. 34, Q. No. 4.

Q. 2. Examine the directions of India's exports and the reasons of these trends. Explain the total export promotion organizations.

Ans. Ref.: See Chapter-4, Page No. 58, 'Direction of India's Foreign Trade' and Chapter-6, Page No. 95, 'Organizations Involved in Export Promotion'.

Q. 3. Critically examine the significance of foreign direct investment in Indian context.

Ans. Ref.: See Chapter-2, Page No. 30, Q. No. 6 and Page No. 35, Q. No. 7 and Page No. 36, Q. No. 8.

Q. 4. Examine the thrust areas of India's foreign trade for improvements.

Ans. Ref.: See Chapter-4, Page No. 61, 'Thrust Areas of Foreign Trade'.

Q. 5. Examine the impact of WTO regime on agricultural products and its exports.

Ans. The World Trade Organization (WTO) regime has had a profound impact on global agricultural trade, including agricultural products and exports. For countries like India and other developing nations, agriculture plays a critical role in the economy, employing a significant portion of the population and contributing to GDP. The WTO's Agreement on Agriculture (AoA) has influenced agricultural policy, export competitiveness, and domestic agriculture markets. Below is an examination of the impact of the WTO regime on agricultural products and exports, especially in the context of developing countries like India:

Key Features of WTO's Agricultural Framework

1. Agreement on Agriculture (AoA): The AoA is a major pillar of the WTO's agricultural policy, aiming to make agricultural trade more market-oriented. The agreement has three main components:

- **Market Access:** Reduction of tariffs and non-tariff barriers to create more transparent and fairer access to agricultural markets.
- **Domestic Support:** Restrictions on the level of domestic subsidies that distort agricultural production and trade.
- **Export Subsidies:** Gradual reduction or elimination of export subsidies that give competitive advantages to certain countries.

2. Sanitary and Phytosanitary Measures (SPS):

- The SPS Agreement sets guidelines for food safety and animal/plant health standards. While it allows countries to set their own standards, these must be scientifically justified and not used as disguised barriers to trade.

Positive Impacts of the WTO Regime on Agriculture and Exports

1. Improved Market Access:

- **Lower Tariffs:** The WTO regime has reduced tariffs and non-tariff barriers to trade, improving market access for agricultural exporters, particularly from developing countries. For instance, Indian agricultural products like rice, spices, and tea have found broader access to global markets as a result of liberalized trade.
- **Diversification of Export Markets:** With the opening of international markets, countries like India have been able to diversify their agricultural export destinations. This reduces dependency on a few trading partners and provides greater opportunities to tap into high-demand markets in Europe, the U.S., and Southeast Asia.

2. Boost in Export Competitiveness:

- **Global Standards and Quality Improvement:** The WTO regime, by enforcing compliance with international standards, has driven improvements in the quality and safety of agricultural products. Indian exporters, for example, have adopted better practices in food safety and processing, enhancing their competitiveness in international markets.
- **Trade Liberalization:** The liberalization of agricultural trade has enabled developing countries to leverage their comparative advantages. For India, its vast production of high-quality rice, spices, tea, fruits, and vegetables has gained significant traction in international markets.

3. Increased Agricultural Exports:

- In countries like India, agricultural exports have seen an uptick under the WTO regime. India's exports of agricultural products like basmati rice, non-basmati rice, seafood, and spices have increased in volume and value.
- **Emergence of New Markets:** WTO negotiations have helped open up new export markets for developing countries. For example, Indian products now find markets in Africa, Southeast Asia, and even Latin America, benefiting from reduced tariffs and trade facilitation measures.

4. Promotion of Fair Competition:

- The WTO's efforts to reduce or eliminate export subsidies, particularly by developed countries, have created a more level playing field. This is significant for developing countries like India, where farmers rely on global competitiveness rather than subsidies to succeed in export markets.
- **Reduction in Trade Distortions:** Through the WTO, there is greater scrutiny and reduction of trade-distorting domestic support (subsidies) provided by developed countries, which often made it difficult for developing nations to compete.

5. Encouragement of Reforms and Policy Adjustments:

- The AoA has pushed developing countries like India to reform their domestic agricultural policies, especially in areas like subsidy rationalization and the introduction of market-oriented reforms. Although these reforms have been slow and met with resistance, they have helped improve efficiency and competitiveness.

Negative Impacts and Challenges of the WTO Regime on Agriculture and Exports

1. Protectionism and High Tariffs in Developed Markets:

- **Limited Market Access:** Despite the AoA's goals of liberalizing trade, many developed countries still impose high tariffs and use tariff-rate quotas on sensitive agricultural products like dairy, sugar, and meat. This limits the ability of developing nations like India to expand their agricultural exports to these markets.
- **Non-Tariff Barriers:** While tariffs have been reduced, non-tariff barriers (NTBs), including stringent SPS measures, have emerged as significant hurdles. Developed countries often implement strict quality, safety, and health standards that developing countries find difficult to meet, acting as disguised barriers to entry.

2. Impact on Domestic Agricultural Policies:

- **Constraints on Domestic Support:** The WTO's restrictions on domestic subsidies (classified into 'Amber' 'Blue,' and 'Green' boxes) limit the ability of developing countries to support their agricultural sectors. For India, where farming is predominantly small-scale and farmers rely heavily on subsidies for inputs like fertilizers and electricity, this constraint poses significant challenges.
- **Food Security Concerns:** Many developing countries argue that the WTO's agricultural policies do not sufficiently address food security concerns. For example, India's public food distribution system (PDS) and minimum support price (MSP) system, which are essential for ensuring food security, may come under scrutiny under the WTO rules as they are seen as trade-distorting.

3. Subsidies in Developed Countries:

- **Unequal Playing Field:** Despite commitments to reduce subsidies, developed countries, especially in the EU and the U.S., continue to provide substantial domestic support to their agricultural sectors. These subsidies give their farmers a competitive edge over farmers in

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INDIA'S FOREIGN TRADE AND INVESTMENT

BLOCK 1: FOREIGN TRADE AND INVESTMENT

Overview of Foreign Trade

1

INTRODUCTION

Trade policy is one of several economic tools utilised in a growing nation like India to meet the needs of economic growth. India's trade strategy has two main goals: promoting exports and limiting imports to the amount of foreign currency that is available to the government. The lack of or severe scarcity of essential inputs, such as industrial raw materials, capital goods, and technology, is a nation like India's fundamental issue. Only imports can break the bottleneck. Imports can be financed in the short term by borrowing money, receiving foreign help, but in the long run, more export revenues are required to pay for imports. Therefore, the primary goals of trade policy are to promote exports and regulate imports using various tools and strategies. key policy changes have been made over time, reflecting the necessity and pressure for India to play a key role in global trade by taking an all-encompassing, holistic approach to the total growth of the nation's international commerce.

CHAPTER AT A GLANCE

AN OVERVIEW OF LEGAL FRAMEWORK FOR FOREIGN TRADE

A nation's international commerce is made up of the export and import of products and services, which results in an influx and outflow of foreign currency. While the overseas commerce Development & Regulation Act, 1992 and the Rules and Orders made thereunder control India's overseas commerce, the Foreign Exchange Management Act, 1999 regulates payments for export and import trade transactions in terms of foreign exchange. The Customs Act of 1962 governs the actual functioning of international trade transactions including export and import of products and services through a variety of means of transportation. A comprehensive plan of quality control and pre-shipment inspection is also in style under the Export (Quality Control and Inspection) Act of 1963 in order to present the image of the nation as a manufacturer and exporter of high-quality products and services. In addition, there are other additional laws and standards governing international trade.

Foreign Trade (Development and Regulation) Act, 1992

The international Trade (Development and Regulation) Act, 1992 addresses issues related to or incidental to international trade development and regulation by facilitating imports into and increasing exports from India. Under the authority of this Act, India issues its Export and Import Policy. By giving the Importer-Exporter Code Number, this Act also grants authorisation for import and export. The suspension and/or cancellation of the Importer-Exporter Code Number is also used as the maximum penalty for the commission of any offence, violation of any law, harm to the country's trade relations, or bringing disrepute to the country's credit or goods while conducting export-import trade transactions.

Foreign Exchange Management Act, 1999

Under the authority granted by the Defence of India Rules, the exchange control was instituted in India on September 3, 1939, as a wartime measure during the early stages of the Second World War. The Foreign Exchange Regulations Act, 1947, which went into effect on March 25, 1947, eventually superseded the emergency powers. The Foreign Exchange Regulations Act of 1973, often known as FERA, took the place of this Act after it underwent extensive revision in response to the shifting demands of the economy throughout the post-independence era. The Foreign Exchange Regulations (Amendment) Act of 1993 was created in response to the need for additional extensive amendments to the FERA as a result of the advent of the era of liberalisation of the external sector of the economy, industrial licencing, partial convertibility of the rupee, and full convertibility on current account. Foreign Exchange Management Act (FEMA), enacted in 1999, took the role of FERA.

The legislation governing foreign currency has been consolidated and amended with the help of FEMA. This Act's principal goals are to support the orderly growth and maintenance of India's foreign exchange market as well as to ease international commerce and payments. The FEMA provisions, which are periodically updated, are used by the Reserve Bank of India to create rules and regulations. The following are the main thorough Notifications containing the same:

(i) Foreign Exchange Management (Export of Goods and Services) Regulations, 2000;

(ii) Foreign Exchange Management (Current Account Transactions) Rules, 2000;

(iii) Foreign Exchange Management (Manner of Receipt and Payment) Regulations, 2000.

The Customs Act, 1962

On December 13, 1962, the Customs Act of 1962 became effective. The Sea Customs Act of 1878, the Land Customs Act of 1924, and the Aircraft Act of 1934 were all abolished.

This Act's main goals are to *(a)* control legitimate export and import trade transactions in accordance with national economic policies and objectives, *(b)* prevent smuggling, *(c)* collect money, *(d)* carry out tasks for other agencies, and *(e)* compile trade data. The First and Second Schedules of the Customs Tariff Act, 1975, which pertain to imports and exports, respectively, include information regarding the rate and kind of customs tax that may be imposed on each item, as determined by the Central government.

Export (Quality Control and Inspection) Act, 1963

In order to improve the export trade through quality control and preshipment inspection, the Export (Quality Control and Inspection) Act was passed in 1963. The Act gives the Government the authority to determine the kind of quality control or inspection as well as the commodities that may be required to undergo mandatory quality control and/or inspection prior to export. The Act forbids the export of products that are below standards or that do not adhere to the rules established by the Act. The following export categories are excluded, though: *(i)* Export Oriented Units (EOUs) and units situated in Free Trade Zones (FTZs), etc.; *(ii)* Star Export Houses; *(iii)* Exports made in reliance on a letter from a foreign customer declaring that no pre-shipment inspection by an authorised inspection agency is necessary: *(iv)* Items with the ISI mark or AGMARK.

The Government created the Export Inspection Council (EIC) and the Export Inspection Agencies (EIAs) on January 1, 1964, to ensure the efficient functioning of the Export (Quality Control and Inspection) Act, 1963. The EIAs are the organisations that actually examine the products and give the export-worthiness certifications, whilst the EIC serves as a body that advises the government on issues pertaining to quality control and inspection. Under the present Foreign Trade Policy, trade and industry are strongly encouraged to improve product quality in order to portray the nation as a manufacturer and exporter of high-quality goods on a global scale.

Other Regulations: The same laws, orders, regulations, technical requirements, environmental standards, and safety standards that apply to domestically manufactured items also apply to all imported goods.

IMPORTANCE OF INTERNATIONAL TRADE

The variety of economic resources present in many nations serves as the foundation of global commerce. Not all nations have the same manufacturing infrastructure thanks to nature. There are variations in the climate, the geological resources, the availability of labour, and the cost of capital. Each nation finds it profitable to specialise in the production of a few particular goods as a result of these distinctions. The exchange of excess output through international commerce promotes this specialisation. When overseas markets are more affordable for consumers to purchase goods from and more lucrative for sellers to sell their goods than the home market, there is international trade. Therefore, via international commerce, resources may be used more efficiently. The following are some discussions about the value of international trade:

***(i)* Greater availability of Goods and Services:** A nation can acquire the things that it cannot create or cannot manufacture as affordably as other nations through international commerce. As a result, a country's level of participation in international commerce greatly influences its level of prosperity. Consumers profit from trading internationally to the extent that they can find the best deals.

***(ii)* Better use of Country's Resources:** The best potential use of a nation's resources is made possible via international commerce. Numerous times, local industries rely on international marketplaces to sell their output. For instance, India's jute and tea industries rely heavily on export customers. The prosperity of Japanese business depends on exports. Even though the US is not heavily dependent on international commerce, more than 25% of the country's industrial and agricultural output is exported.

***(iii)* Division of Labour and Specialization:** Due to international commerce, the nation may export those goods in areas where it has a competitive edge. Likewise, if the nation finds itself in a difficult situation or in need of the items, it may import them. By concentrating more on beneficial items, the nation will be able to produce and export those goods in big quantities.

***(iv)* Enhances Competitiveness:** Opportunities for trading with other nations are provided through international trade. More products and services are exported and imported as a consequence. The nation must produce big volumes of goods or offer high-quality services in order to compete with the other participants in the new market. As a result, manufacturers and service providers may face intense rivalry. Such competition and strict quality control may increase the nation's overall competitiveness.

***(v)* Reduction in Costs of Production:** The entire cost of manufacturing decreases, when the lowest sources for capital goods and raw materials are used, which lowers costs.

***(vi)* Stability of Prices:** When a country notices that the price of a certain good is trending upward, it might boost its imports of that good to halt the upward trend. Similar to this, if a commodity's price declines owing to an excess of supply, the trend may be reversed by exporting the same. As a result, prices become more or less consistent around the world. Foreign commerce might be used to restrain monopolists' dishonest practises.

***(vii)* Greater Employment Opportunities:** Foreign commerce increases domestic agricultural and industrial production, which boosts employment levels in the nation.

***(viii)* High Rate of Economic Development:** Foreign commerce promotes quick economic growth and a greater rate of national income growth. In actuality, foreign commerce was viewed as a development driver. A lot of industrialised nations, like the USA, UK, and Japan, owe their success to the export of manufactured goods. Many emerging nations, like South Korea, Taiwan, Thailand, Singapore, and Hong Kong, have greatly profited in recent years from their active engagement in international commerce.

***(ix)* Contribution to Government Revenues:** The majority of governments levy taxes on imports and occasionally on exports as well. The State Exchequer receives considerable earnings from these charges.

***(x)* Helps in Balance of Payments:** To satisfy its needs, the nation imports a range of goods and services, including capital goods, petroleum products, etc. Import payments are done in foreign currencies. The nation makes money overseas through exporting goods and services. If export revenue exceeds domestic revenue.

***(xi)* Harmonious Relationship among Various Countries:** Foreign commerce has a significant role in bringing distinct nations together. It encourages friendly ties and cooperation between everyone. It may result in global economic integration, which then promotes political stability and increased international collaboration on sociocultural advancements. Thus, increased commerce can also lessen the chance of conflict. There will be a beneficial balance after paying imports.

FOREIGN TRADE AND ECONOMIC GROWTH

Foreign commerce has always served as an economic catalyst. The "outward-oriented growth strategy" adopted in recent years by the Newly Industrialising Economies of Asia, including Hong Kong, Singapore, Taiwan, Malaysia, Thailand, and South Korea, has allowed them to get past the limitations of being small, underdeveloped economies with few resources.

Contribution of Foreign Trade to Economic Development

Foreign trade contributes to economic development in a number of ways. These areas as follow:

1. The main purpose of international commerce is to find ways to import capital goods, without which no economic process can begin.

2. It enables for the flow of technology, allowing for rises in total factor productivity, as well as some short-term multiplier benefits for nations with a labour shortage.

3. Through it creates pressure for dynamic transformation.

(i) Competitive pressure from imports,

(ii) Pressure of competing for export markets, and

(iii) A better allocation of resources.

4. Exports provide greater capacity utilisation, expanded scale economies of scale, segregation of production patterns from local demand, and improved adoption of new technology.

5. These, in turn, assist in boosting the domestic firm' profitability without necessarily raising prices. Fig. 1.1 can be used to show this.

AC is the average cost curve in Fig. 1.1. The amount of output that will result in the lowest average cost per unit is Oq_1. The production level is just Oq, and the associated average cost is OC due to the domestic limitation. The company can run at maximum efficiency and cut the average cost by CC_1 if it can export qq_1 quantity. In such a scenario, exporting—even on a no loss, no profit basis—is advised since optimal capacity utilisation increases the profitability of the company's domestic activities. Both the profitability per unit and the overall profit from domestic operations will rise thanks to CC_1 and CC_1 QS, respectively. Exports therefore boost profitability without raising prices.

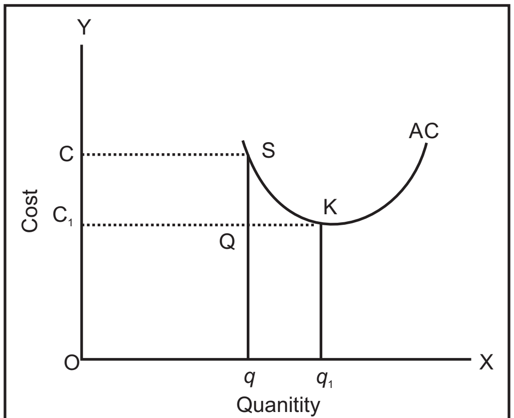

Fig 1.1

6. Most workers' welfare is improved by foreign commerce. It does so in at least four of the methods listed below:
   (i) Higher salaries result from larger exports;
   (ii) Workers benefit immediately from trade since lower imports benefit them as consumers;
   (iii) As the value of the products they create rises, it enables the majority of employees to become more productive;
   (iv) Trade accelerates the transfer of technology from the industrial sector to EEs, and this technology is biassed in favour of skilled labour;

7. Since "civilization" expanded by "mimesis", or simple copying, as historian Arnold Toynbee put it, increased trade openness has been significantly linked to a decrease in poverty in most emerging nations.

Level of Trade and Balance of Trade: The volume of commerce in a nation indicates how much of its output is exported. The percentage of exports to GDP is used to quantify this. It shows how interconnected an economy is. Some nations, like Germany, have a high degree of commerce about 50% of their entire production is exported. We can determine if a country has a trade surplus or deficit by looking at the balance of trade. A nation may have minimal trade yet a large trade imbalance. For instance, despite only exporting 14% of its GDP, the United States has a $540 billion trade imbalance.

A country's volume of commerce is significantly influenced by three factors:
   (i) the size of its economy,
   (ii) its geographic location, and
   (iii) its history of trade.

TRADE POLICY AND STRATEGY

All policies that have an impact on a country's trading conduct, whether directly or indirectly, are referred to as trade policies. The broad trade strategy that the nation has adopted, in turn, depends on the planners' broad development strategy for determining the specifics of the numerous policies. In its most severe version, this policy forbids the transfer of production elements to or from the outside, multinational enterprises, and the freedom of international communications. Such a severe sort of inward-focus is almost ever seen in any nation in the current global economy. The type of outward orientation that allows for the free movement of products, labour, money, multinational corporations, and open communications is the antithesis of this extreme form of inward orientation.

Arguments for Outward-orientation

Advocates of outward-orientation claim that being open helps to foster positive educational outcomes, the development of new ideas and approaches, the emergence of new organisational forms, etc. They hold that free trade, often known as the global market, promotes learning via commerce and implies successful dynamic transformation of the economy into greater standards of life. Free trade is a win-win situation because, notwithstanding differences in their domestic institutions and policies, all the trading partners stand to gain from increased production.

The pricing mechanism is interfered with, there are allocative and X-inefficiencies, there are distortions, and competitive businesses and industries are hampered by quotas and other quantitative constraints.

Arguments for Inward-orientation

In response to these claims, proponents of inward orientation argue that such policies foster local talent, self-reliance, domestic technical advancement, and an adequate range of goods while avoiding the negative impacts of external display. Inward-focus is promoted as an unavoidable policy due to the development disparities between developing and industrialised nations.

No general conclusions can be taken in this situation since the effects of these two types of tactics on employment growth, income creation, production growth, and income inequality might likewise be of various nature.

KEY ASPECTS OF INDIA'S FOREIGN TRADE

In 2020, India will account for 1.6% of global product exports and 4% of global commercial services exports. 2.1% of global exports of goods and services are made up of these items. While the percentage of global imports of goods is 2.1% and that of global imports of commercial services is 3.2%. 2.3% of all imported goods and services worldwide.