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POLICY BRIEF - 35

COVID-19, Trade and India - Policy Issues in Leveraging the Opportunities

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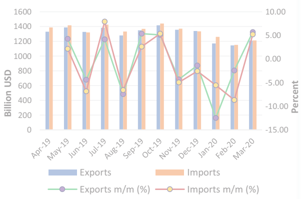
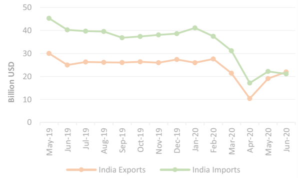
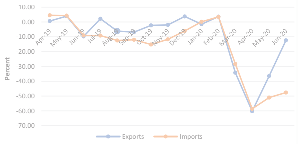
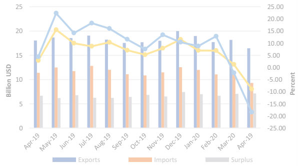
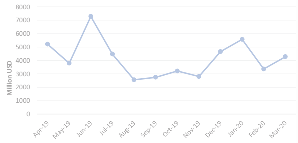










Background

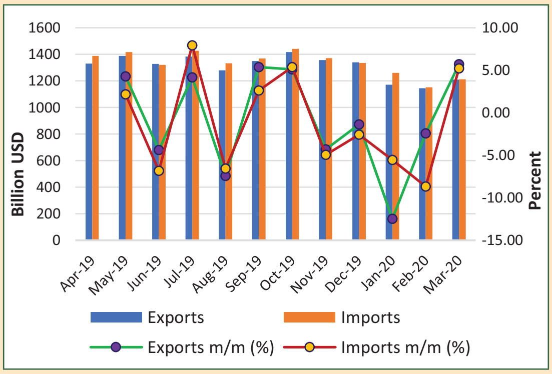
Initially, COVID - 19 was perceived as a problem of China, if not, maybe a problem of Asia, but soon it became a pandemic and, as of now, almost all the countries have experienced the resultant economic crisis due to the pandemic. This, in turn, in the last two quarters, has overstrained many segments of the economy, including trade, which is acclaimed as an engine of growth. Global trade has slumped in the first quarter of this year as many countries have experienced a sharp decline in their trade. According to CPB World Trade Monitor, the global trade volumes fell by 4.3%, year-on-year, registering consecutive declines in the first three months of this year. The overall decline in world trade was 2.5% between January-March, 2020. Global industrial production also has decelerated by 4.2% in the same period. WTO predicts a fall in world trade between 13-32% in 2020 due to the pandemic, which would be experienced by all regions, affecting the sectors with complex value chains the most. In this context, this policy brief examines how the engines of growth have been affected in India and what kind of policy coordination is required in the pandemic Economy, where Government of India (along with many states) is aiming to tap the crowding out of investment from China and emerge as the next superpower of Asia. The analysis is carried out taking the monthly data for the period April 2019-June 2020. We used data retrieved from UNCOMTRADE, World Bank, Ministry of Commerce and Industry, and Department for Promotion of Industry and Internal Trade, Government of India. For product-wise analysis, we have taken HS codes at the two-digit level.

Staggering Pace of the Engines of Growth

Global trade started to decelerate after December 2019 and recovered slowly in March 2020 (Figure 1). One of the major contributing factors is the drastic fall in the trade value of China, which is the largest contributor to global trade in these months.

Indian exports and imports started to decelerate after February, both in absolute terms and year-over-year growth, but slightly recovered in May (Figure 2). This downtrend is mainly attributable to the global slowdown, current COVID-induced recession, cancellation of orders, lockdowns in many countries and supply chain disruptions. In June 2020, India exported goods worth USD 21.91 billion which is 12.40 percent lower than the previous year, whereas imports stood at USD 21.11, with a negative growth of 47.60 percent compared to last year (Figure 3).

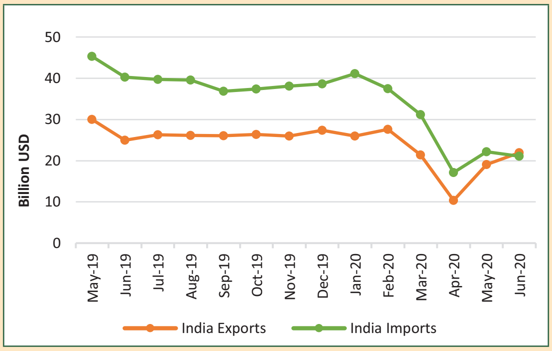
Figure 1: Trends in Global Trade between April-2019 and March 2020



Source: UNCOMTRADE as on 14.07.2020

India's merchandise trade deficit is also continuously falling since February 2020 and almost after two decades, India experienced a trade surplus of USD 0.8 billion in June 2020. This is mainly due to a huge fall in imports of petroleum and crude oil, and gold and silver and recovery in exports, thanks to the stimulus packages and revival in economic activities due to the reopening of global economies (Jethmalani, 16th July 2020). The fall in imports of crude oil and petroleum, the largest import product is due to slowdown in sales and commercial activities and transportation caused by regional lockdowns, and a lower price of oil in the global market. The fall in gold and silver is due to slowdown in social events and a change in consumer sentiments on saving caused by the pandemic (Chandorkar, 20th July, 2020). Uncertain employment situation and changed consumption habits and pattern also have contributed to fall in demand for capital and consumer goods.

Figure 2: Trends in India's Trade between April-2019 and June 2020



Source: Ministry of Commerce and Industry, Government of India

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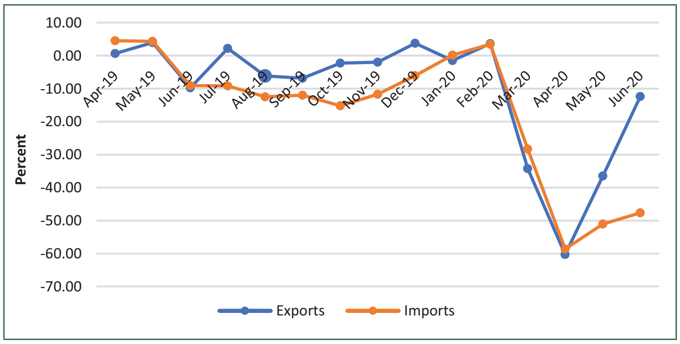
Figure 3: Trends in Growth Rates of Exports and Imports (year-on-year)



Source: Authors' calculations based on data obtained from the Ministry of Commerce and Industry, Government of India.

Mineral fuels, gems and jewellery, organic chemicals, machinery and mechanical appliances, pharmaceuticals, and automobiles together contribute about 40% of India's exports (Table 1). Within this, pharmaceutical products have replaced automobiles and emerged as a leading category in March 2020. India's increased pharma exports after the outbreak of the pandemic and a surge in the global demand for generic drugs to reduce healthcare costs have created a trade opportunity for India, which can be expected to continue. Between April 2019 and March 2020, pharma exports registered a positive growth of 2.39 percent while total exports have declined by 17.56 percent. Mineral oils, gems and jewellery, and organic chemicals experienced a significant decline in exports during this period. With respect to import basket, products that contribute about 70 percent of India's total imports (Table 1) have registered negative growth in the last fiscal. Between April 2019 and March 2020 India's total imports fell by 26.47 percent, and between January and March 2020, it was 24.24 percent. Gems and jewellery is the least-affected sector for the same period.

Trade in Services

Compared to merchandise trade, trade in services has not been affected much by the pandemic, though there is a slowdown in the sector. The major sectors affected are hotel and restaurant, and transport. Between April 2019 and April 2020, India's services exports fell from USD 18.06 billion to USD 16.45 billion with a growth rate of 8.91 percent (Figure 4). The fall in exports between January 2020 and April 2020 was 13.37 percent. Compared to exports, imports of services experienced a much steeper decline.

Trends in FDI

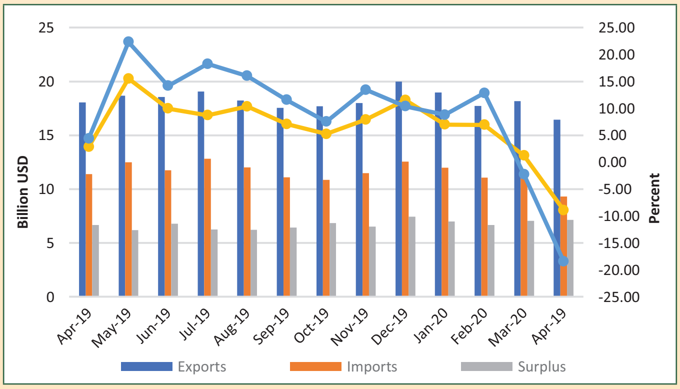
FDI inflows registered a record growth of 13% in the financial year 2019-20 to reach USD 49.98 billion in March 2020 (Figure 5). Including reinvested earnings, the figure shows 18% growth in the same period, which could be attributed to crowding out of investment from China to elsewhere and also aggressive policy measures taken by both central and state governments. The 'Make in India' initiative of the central government has also contributed

Table 1: Product Composition of India's Trade Basket

Products	Apr-19*	Jan-20*	Mar-20*	Growth (%) Apr-19 to Mar-20	Growth (%) Jan-20 to Mar-20
Exports					
Mineral oils	3.69	3.28	2.58	-30.23	-21.52
Gems and Jewellery	2.89	2.89	2.03	-29.73	-29.86
Machinery and mechanical appliances	1.66	1.63	1.47	-11.69	-10.07
Organic Chemicals	1.69	1.49	1.25	-25.82	-15.79
Pharmaceutical products	1.20	1.41	1.23	2.39	-13.01
Total Exports	26.04	25.83	21.46	-17.56	-16.9
Imports					
Mineral oils	13.97	14.73	11.69	-16.35	-20.67
Gems and Jewellery	6.44	3.34	2.86	-55.57	-14.46
Electrical machinery and equipment	3.92	4.18	2.89	-26.26	-30.85
Machinery and mechanical appliances	3.56	3.74	2.56	-28.15	-31.53
Organic chemicals	1.87	1.74	1.26	-32.5	-27.68
Total imports	42.39	41.14	31.17	-26.47	-24.24

Source: Authors' calculations based on data from the Ministry of Commerce and Industry, Government of India
* Values in billion USD

Figure 4: India's Trade in Services



Source: Ministry of Commerce and Industry, Government of India

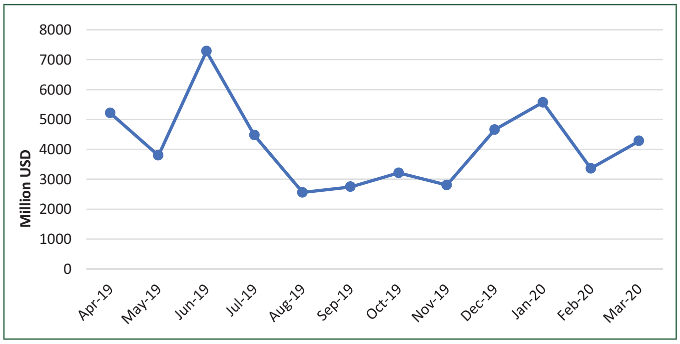
Table 2: Trends in Bilateral Trade with Top Trading Partners

Month	Exports*			Imports*		
	USA	UAE	China	USA	UAE	China
Apr-19	4.11 (15.77)	2.36 (9.06)	1.43 (5.50)	3.35 (7.90)	2.30 (5.41)	5.32 (6.54)
May-19	4.93 (16.53)	3.49 (11.69)	1.55 (5.19)	3.99 (8.54)	2.52 (5.40)	6.04 (12.94)
Jun-19	4.28 (17.08)	2.12 (8.45)	1.18 (4.72)	3.40 (8.29)	2.57 (6.26)	5.91 (14.40)
Jul-19	4.44 (16.93)	2.44 (9.29)	1.41 (5.38)	3.06 (7.57)	2.31 (5.70)	6.19 (15.30)
Aug-19	4.52 (17.39)	2.26 (8.70)	1.46 (5.62)	2.96 (7.86)	2.22 (5.89)	6.37 (16.91)
Sep-19	4.41 (16.96)	2.28 (8.77)	1.36 (5.25)	2.81 (7.46)	2.51 (6.67)	6.44 (17.09)
Oct-19	4.63 (17.65)	2.38 (9.07)	1.46 (5.57)	2.77 (7.30)	2.35 (6.19)	5.51 (14.50)
Nov-19	4.26 (16.53)	2.39 (9.28)	1.59 (6.18)	2.78 (7.22)	2.73 (7.08)	5.13 (13.31)
Dec-19	4.67 (17.22)	2.41 (8.90)	1.47 (5.41)	2.59 (6.55)	3.10 (7.83)	5.01 (12.66)
Jan-20	4.44 (17.20)	2.12 (8.22)	1.51 (5.83)	2.85 (6.92)	3.16 (7.68)	6.02 (14.64)
Feb-20	4.69 (16.94)	2.93 (10.59	1.12 (4.04)	3.04 (8.10)	2.49 (6.65)	4.44 (11.85)
Mar-20	3.72 (17.32)	1.66 (7.75)	1.07 (4.96)	2.06 (6.60)	2.01 (6.43)	2.88 (9.25)

Source: Authors' calculations based on data from the Ministry of Commerce and Industry, Government of India
Note: * values in billion USD; Values in brackets are percentage shares in total exports/imports

its bit in attracting FDI. Mauritius is the top investor in India followed by Singapore (Table 3). The service sector attracted 17% of the total FDI inflows in the financial year 2019-20 followed by computer software and hardware. Maharashtra attracted 30% of FDI inflows followed by Karnataka (18%). Mumbai and Bangalore, being the investment destinations for the top FDI categories and the state support, have been mainly responsible for the highest FDI inflows in these states.

Figure 5: Trends in India's FDI Inflows



Source: Ministry of Commerce and Industry, Government of India

Table 3: Top Investors, Sectors and States of India's FDI Inflows

Top Investing Investors	Top Sectors	Top States
Mauritius (30%)	Services (17%)	Maharashtra (30%)
Singapore (21%)	Computer Software and Hardware (10%)	Karnataka (18%)
Netherlands (7%)	Telecommunications (8%)	Delhi (17%)
Japan (7%)	Trading (6%)	Gujarat (11%)
USA (7%)	Construction Development (5%)	Jharkhand (8%)

Source: Department for Promotion of Industry and Internal Trade, Government of India

Doing Business, Trade Facilitation and Trade

The US-China trade war had already created tensions at the global level invoking the protectionist era. COVID-19 has also resulted in a huge mistrust and has aggravated this problem, affecting even foreign investments in China. Developed countries are trying to reduce their dependence on China. With China's integrity being questioned across many countries of the world after the outbreak of COVID-19 pandemic and developed countries mulling over shifting their manufacturing base out of China, many developing countries, including India, have started competing to attract a larger chunk of this capital flight. In the light of 'Make in India' and the recent call for Atmanirbhar Bharat (Self-reliant India), two things have become a priority for India: One, attracting foreign investments to create job opportunities and ignite the economy, two, promoting 'desi' products and create global branding for Indian products under the tag 'vocal for local'. Its success ultimately depends on the policy environment, the ability of the Indian firms to exploit this opportunity to create positive consumer sentiments both within India and overseas. In the current COVID-19 world of mutual mistrust, the biggest challenge for India lies in retaining the existing markets and capturing new markets. This is not easy, as there are many competitors in South and Southeast Asia trying to snatch this opportunity. If so, what margin of differences exist in institutional setup, which perhaps encourage trade and investment in an open economy, if India really plans to turn pandemic into an opportunity to make a mark in the global map, what kind of reforms are required and how soon this can be achieved? These questions need to be understood within the framework of Doing Business (DB), while doing so authors are completely aware of the limitations associated in the methodology of its computation. The earlier study by Tantri and Kumar (2018) argues that it is much costlier for a trading partner to trade with India than with China, which obviously gives a competitive edge to an exporter in China over the Indian exporter. For the latest available year (2020) India and China's DB ranks are 63 and 31 respectively (Table 4). China definitely fares better than India in the majority of the indicators except in obtaining construction permits, getting credit and protecting minority investors. Vietnam, which is emerging as one of the competitors for India in the Covid-19 world, has a close margin with DB ranking. Thus, India's attempt to attract foreign investment, bypassing China and Vietnam, depends on the kind of aggressive measures taken by both the economies.

Table 4: DB Rankings of India, China and Vietnam (2020)

	Overall DB Rank	Starting Business	Dealing With Construction Permit	Getting Electricity	Registering Property	Getting Credit	Protecting Minority Investors	Paying Taxes	Trading Across Borders	Enforcing Contracts	Resolving insolvency
India	63	136	27	22	154	25	13	115	68	163	52
China	31	27	33	12	28	80	28	105	56	5	51
Vietnam	70	115	25	27	64	25	97	109	104	68	122

Source: World Bank, 2020

Table 5: Starting Business in India, China and Vietnam - A Comparison

	Procedure (number)	Time (Days)	Costs
India	10	18	7.2
China	4	9	1.1
Vietnam	8	16	5.6

Source: World Bank, 2020

Table 6: The State of Trading Across Borders in India, China and Vietnam

	Time to Export		Costs to Export		Time to Import		Costs to Import	
	Documentary compliance (hours)	Border compliance (hours)	Documentary compliance (USD)	Border compliance (USD)	Documentary compliance (hours)	Border compliance (hours)	Documentary compliance (USD)	Border compliance (USD)
India	12	52	58	212	20	65	100	266
China	9	21	74	256	13	36	77	241
Vietnam	50	55	139	290	76	56	183	373

Source: World Bank, 2020

Policy Stimulus during the Pandemic

A quick glance at measures taken by the government in the last couple of months does show a good start. For instance, the Central Board of Indirect Taxes and Customs undertook several trade facilitation measures such as exemption of customs duty on ventilators, personal protective equipment, COVID-19 testing kits and related inputs, provisional clearance of goods under trade agreements without the requirement of originally-signed certificates of origin and allowing electronic certificates, temporary relaxation in terms of submitting undertakings instead of customs bonds for the clearance of goods, and introducing electronic copies of bills of entry and gate passes to importers and customs brokers (CBIC, 2020). A single, dedicated helpdesk for Covid-19 related queries has been set up on the CBIC website to facilitate quick answers to issues being faced by traders. Prior to the beginning of the outbreak in India in February 2020, the CBIC introduced 24/7 customs clearance at all customs formations till June 30, 2020, to prepare for possible disruptions, surges and delays in the supply chain on account of shutdowns in China during that period. The Foreign Trade Policy 2015-2020 has also been extended by one year, which means benefits under all export-promotion schemes, except the Service Exports from India Scheme, have also been extended for one year, and exemptions from payments of IGST and compensation cess on imports made by export-oriented units (EOUs) has also been extended by one year (PIB, 2020).

Besides this, many states have geared up to revive the economy and also to attract the crowding out of investment from China. For instance, the Government of Kerala has decided to set up two committees- an industrial advisory committee and an economic revival committee (Business Standard, 2020). The Karnataka Government constituted a Special Investment Promotion Task Force on May 11, 2020, to identify the possible sectors to attract investments from other countries that wish to relocate from China post the pandemic. 'Udyog Bandhu', the existing investment promotion agency in Uttar Pradesh, is going to be strengthened through the establishment of a new Investment Promotion and Facilitation Agency to further improve investments in the state and to facilitate job creation for close to 1.5 million returning migrants. (The New Indian Express, 2020). For redressal of grievances due to Covid-19, the Government of Haryana has set up a special online portal for reporting any issues.

Besides this, many industry-specific measures are taken up to revive the sector. For instance, the central government has decided to decriminalise certain Companies Act violations, including minor defaults such as delays in holding annual general meetings, shortcomings in CSR reporting, filing defaults, in order to unclog criminal courts. Environmental clearances, that were to expire between March and April 2020, have been extended till June 30, 2020. (Invest India, 2020a). At the industrial level Rs. 3,000 crore over five years has been allocated to developing three mega bulk drug parks in India. Telangana has provided for reimbursements of stamp duty, fixed power cost, GST and costs involved in skill training of local manpower in the pharmaceutical and life sciences industry. It also announced a capital subsidy of 25 percent to be given to handlooms and textiles units (ibid). Also units in the electronics and electrical machinery industry will receive full reimbursement of net SGST along with investment and transport subsidies in that state (ibid). In Maharashtra, as immediate relief from the pandemic, tariffs in the industrial and commercial sector has been reduced by 10 to 15 percent. Karnataka, which is the leading state in the aerospace sector, exempted local manufacturers in the aerospace and defence sector from the nationwide lockdown by permitting them to resume manufacturing activities with immediate effect (Invest India, 2020b).

Policy Suggestions for Leveraging the Opportunities

Sector-specific Measures

The history of economic policymaking in the past has shown that sector-specific approach is far more rewarding than a one-size-fits-all approach. For instance, China, is acclaimed for undertaking a sector-specific approach when it comes to promotion and facilitation of trade through SEZs than one-size-fits-all policy adopted by India since reforms. Resultantly, SEZs had contributed significantly in transforming the Chinese closed economy into open and more resilient, whereas in India it could not take off as expected despite two decades of its operation. This, among others, definitely calls for having a systematic intervention at key strategic/ leading exporting sectors of the country and also across states than having a uniform policy.

Institutional Reform with Better Coordination and Cooperation Across Different Ministries

There is a need for systematic coordination and cooperation (horizontal and vertical) across different ministries and agencies/actors, which has been blamed for underperformance of several export promotion policies in India, including SEZs. Bringing out many institutional reforms and boosting the infrastructure of the economy will not only facilitate to compete with China and Vietnam but also serve to kick-start the staggered trade pact of India with USA, UK and Canada.

Trade Surplus and Demand Push

India's trade surplus seems to be a welcoming trend from current account deficit perspective but reveals the stagnated or weak demand side of the economy, which needs to be investigated further in order boost the economy by addressing the deep-rooted issues besides encouraging supply-side expansion. However, this evidence is not enough to portray a gloomy picture of the economy as the biggest fall in imports are mainly in petroleum and crude oil, and gold and silver, which may be temporary.

Striking a Balance between Growth v/s Development Parameter

The policy approach, besides boosting the growth of the economy, should protect the environment and labour and thereby never get into the trap of growth with a race to the bottom. Because many Indian states, in their haste to attract foreign investment from all over the world, have been undertaking various labour reforms without addressing other structural problems hindering the industrial expansion in their state, which are though welcomed by industrial bodies but objected by Trade Unions as they affect the decent work and working life of workers. For instance, the Uttar Pradesh government has decided to exempt all businesses from all but four labour laws - the Building and Other Construction Workers Act, Section 5 of Payment of Wages Act, Workmen Compensation Act and Bonded Labour Act, for the next three years to encourage investments. The Madhya Pradesh government has made several amendments to its labour laws to promote ease of operating businesses and to attract new investments. Other states that have decided to increase working hours from 48 to 72 hours per week include Punjab, Haryana, Rajasthan, Himachal Pradesh and Gujarat. While Punjab and Haryana will be paying overtime rates, Himachal Pradesh and Gujarat will be paying regular wages. State governments' approaches to go over the board to attract foreign investment, while competing with others, are seriously threatening the safety and welfare of the laborers. If these are not addressed on time, it may result in chaos and unrest in the economy, which perhaps may push the engine of growth in reverse gear. The corresponding impacts may require a longer time to introduce course correction measures than the situation pandemic has brought forth.

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