DISCUSSION PAPER

CUTS Centre for International Trade, Economics & Environment
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Review of Foreign Trade Policy 2009-2014

Introduction

The two main objectives of the previous Foreign Trade Policy (FTP) were: to double India's percentage share in global merchandise trade within five years; and use trade expansion as an effective instrument for economic growth and employment generation. The short term objective of the new FTP is to stop and reverse the declining trend in exports and provide extra support to sectors badly affected in the developed world. The policy objective is to achieve an annual export growth of 15 percent with annual exports targeted to reach US$200bn by March 2011. The objective is to return India to the high export growth path of around 25 percent per annum by 2014. It is also expected that India's exports will double by 2014. The policy's long term objective is to double India's share in global trade by 2020 (around 3 percent). All of these targets are to be achieved keeping in mind the overarching objective of generating and sustaining employment in labour-intensive export industries through the FTP.

These targets will be met through a mix of policies, namely fiscal incentives, institutional changes, procedural simplification, enhanced global market access and diversification of export markets. The three pillars of the policy that will help the government achieve these targets will be: improvement in infrastructure related to exports, reduction in transaction costs, and provision for full refund of all indirect taxes and levies.

This paper will mainly focus on the major changes in provisions that characterised the shift from the old to the new Policy. It will begin by looking at what special focus initiatives have been added to the Policy, in addition to initiatives in labour-intensive sectors such as agriculture, marine, leather etc. that are central to both policies. This is followed by a table which summarises the major changes in provisions in certain sectors such as handlooms, handicrafts and gems and jewellery etc. The paper will also describe the scheme specific changes as well as changes in provisions for Export Oriented Units (EOUs) and value added manufacturing. Other provisions in the new Policy will also be described, especially those extending support to exporters, and those relating to simplification of procedures and reduction of transaction costs.

The paper will then go on to look at the mentioned changes in provisions in light of recommendations made by CUTS International since 2005 through a project entitled *Grassroots Reachout & Networking in India on Trade & Economics (GRANITE)*. Some commentaries will also be looked at to present varying perspectives on the Policy by economists, representatives of export promotion councils (EPCs) and industries. A summary of highlights in terms of findings and policy recommendations will conclude the paper.

Special Focus Initiatives

The previous FTP identified initiatives for labour-intensive sectors such as Agriculture, Handlooms, Handicraft, Gems & Jewellery, Leather, Marine, Electronics and IT Hardware manufacturing Industries and Sports Goods and Toys sectors. The new FTP has continued the special initiatives for these sectors as well as come up with initiatives relating to the following fields:

- Market Diversification
- Technological Upgradation
- Support to Status holders
- Green Products
- Export Products from North East

Market Diversification

To insulate Indian exports from declining demand in its major target markets caused by the recession, the Policy is looking to diversify the country's exports to other markets such as Latin America, Africa, Oceania and parts of Asia. To help achieve this aim, 26 new countries have been included within the Focus Market Scheme (FMS), whose objective is to offset high freight cost and other externalities to select international markets with a view to enhance India's export competitiveness in these countries. Further, duty credit scrip (which provides credit for payment of import duty or other forms of export finance entitlement) for exporters has been increased from 2.5-3 percent of the value of exports under FMS.

Technological Upgradation

Technological upgradation of the export sector is being encouraged in order to enhance the competitiveness of exports, profitability of exported activities and to encourage exports of items that generate significant value added over the cost of inputs. The following facilities have been extended to enable this process:

- Export Promotion Capital Goods (EPCG) Scheme which offers import duty reductions on capital good imports in return for producers undertaking export obligations has been given a boost: The facility of duty free imports of capital goods under this scheme has been introduced for certain engineering products, electronic products, basic chemicals and pharmaceuticals, apparel and textiles, plastics, handicrafts, chemicals and allied products and leather and leather products. The existing three percent EPCG Scheme (that which facilitates capital good imports at an import duty of three percent) has been considerably simplified to ease its usage by exporters.

- To encourage value addition in manufacturing exports a minimum of 15 percent value addition on imported inputs has been stipulated as a requirement for availing of Advance Authorisation Scheme which permits duty free import of items which are to be physically incorporated in export items or others such as fuels which are to be consumed in the process of production of the export item.

- A number of products including automobiles and other engineering products have been included for incentives under Focus Product Scheme (FPS) which aims to encourage export of products characterised by high export/employment intensity by offseting infrastructure inefficiencies and other associated costs involved in marketing of these products.

Support to Status holders

To encourage existing exporters to expand their activities as well as encourage technological upgradation of export production, additional duty credit of one percent of the value of past export shall be granted on capital goods imports in the form of duty credit scrip. This facility shall be available for sectors dealing with leather products excluding finished leather), textiles and jute, handicrafts, engineering (excluding iron and steel and non-ferrous metals in primary and intermediate form, automobiles and two wheelers, nuclear reactors and parts, and ships, boats and floating structures), plastics and basic chemicals (excluding pharmaceutical products).

Green Products and Technologies

India aims to become a hub for production and export of green products and technologies. To achieve this, there will be promotion of development and manufacture of such products and technologies for export. However, associated modalities have not been spelt out. Initially, the focus will be on items relating to transportation, solar and wind power generation and other products.

Incentives for Exports from the North Eastern Region

- To boost export of products from the north-eastern States, notified products of this region would be incentivised under reward Schemes listed in Chapter 3 of FTP:

- Served from India Scheme (SFIS) whose main objective is to accelerate growth in export of services so as to create a powerful and unique 'Served From India' brand, instantly recognised and respected world over.

- *Vishesh Krishi and Gram Udyog Yojana* (VKGUY) whose main objective is to promote exports of:

    - Agricultural Produce or other products which add value to such produce,
    - Minor Forest Produce and their value added variants,
    - *Gram Udyog* Products,
    - Forest Based Products, and
    - Other Products, as notified from time to time.

- Focus Market Scheme elaborated above.

- Focus Product Scheme elaborated above.

- Status Holders Incentive Scrip whose objective is to promote investment in upgradation of technology by providing exporters credit of up to 1 percent of exports made during 2009-11 in specified sectors for payment of import duty.

Changes in sector specific provisions made through the new policy are summarised in Table 1.

Scheme Specific Changes

- Duty credit scrip entitlement under the Focus Product Scheme has been raised from 1.25-2 percent of the value of exports.

- Scope for products to be included for benefits under FPS has been widened and additional engineering products, plastic and some electronics have got a look in.

- MLFPS has been expanded by including products such as pharmaceuticals, textile fabrics, rubber products, glass

Table 1: Changes in Sector Specific Provisions made through the New Policy

Sectors	Provision added	Provision amended	Provision/clause deleted
Agriculture and Village Industry	To reduce transaction and handling costs, a system to enable export of perishable agricultural produce has been introduced. It will involve creation of multi-functional nodal agencies to be accredited by Agricultural and Processed Food Products Export Development Authority (APEDA).	The threshold limit expressed in terms of value of annual exports for notification of new towns of export excellence in these three sectors has been reduced from Rs 250-Rs 150 crore.	
Handlooms			Requirement of 'Handloom Mark' for availing benefits under FPS (to simplify claims under FPS).
Handicrafts	All handicraft exports would be treated as Special Focus products and entitled to higher incentives.		New Handicraft SEZs shall be established which procure products from the cottage sector and convert these into finished exports.
Gems & Jewellery	- Permission has been granted for import of diamonds on consignment basis for certification/ grading & re-export by the authorised offices/agencies of *Gemological Institute of America* (GIA) in India or other approved agencies. - Personal carriage of Gems & Jewellery products by individuals holding/participating in overseas exhibitions has been increased to US$5mn; the corresponding limit is now US$1mn in case of export promotion tours. - The length of the period within which import of unsold items is permissible has been extended to 90 days in case of participation in an exhibition in US. - In an endeavour to make India a diamond international trading hub, establishment of "Diamond Bourse (s)" is planned.		
Leather & Footwear	Re-export of unsold hides, skins and semi finished leather shall be allowed from public bonded warehouses at 50 percent of the applicable export duty.	Duty free import entitlement of specified items has been reduced from 5-3 percent of value of exports in the preceding financial year.	
Marine Sector	Imports for technological upgradation under EPCG in fisheries sector (except fishing trawlers, ships, boats and other similar items) exempted from maintaining average export obligation.		
Electronics & IT Hardware Manufacturing Industries			Hi-tech products of the Electronics and IT Hardware Manufacturing Industries Sector would be considered for inclusion in High Tech Products Export Promotion Scheme which also provides duty credit on the basis of previous year's export value.
Tea	Export of tea has been covered under *Vishesh Krishi and Gram Udyog Yojana* (VKGUY) scheme benefits	Minimum value addition for availing of advance authorisation scheme for export of tea has been reduced from the existing 100-50 percent. The limit on domestic sale of instant tea by Export Oriented Units has been increased from 30-50 percent.	
Pharmaceutical	Pharmaceutical sector is now extensively covered under Market Linked Focus Product Scheme (MLFPS) — pharmaceutical products would be now treated as focus products if exported to countries in Africa and Latin America and some countries in Oceania and Far East.		
Sports Goods and Toys	Duty free import of specified specialised inputs up to a maximum of 3 percent of the value of the preceding financial year's exports would be allowed.		

products, auto components, motor cars, bicycle and its parts etc. These would be treated as focus products when exported to 13 identified markets — Algeria, Egypt, Kenya, Nigeria, South Africa, Tanzania, Brazil, Mexico, Ukraine, Vietnam, Cambodia, Australia and New Zealand.

- A common simplified application form to avail of benefits under FPS, FMS, MLFPS and VKGUY has been introduced.

- Higher allocations have been provided for Market Development Assistance (MDA)[1] and Market Access Initiative (MAI)[2].

- Jaipur, Srinagar and Anantnag have been recognised as 'Towns of Export Excellence' for handicrafts; Kanpur, Dewas and Ambur for leather products; and Malihabad for horticultural products.

- Export obligation pertaining to import of spares, moulds etc. under EPCG Scheme has been reduced by 50 percent.

- Taking into account the recent trend of decline in exports, the facility of re-fixation of export obligation for any financial year marked by a reduction in exports from the previous year is now being provided for the entire 5 year policy period 2009-2014. A Directorate of Trade Remedy Measures will be set up to provide support to Indian industry and exporters, especially the MSMEs, for availing their rights through trade remedy instruments that offer protection from unfair trade practices such as dumping and subsidies.

- To impart stability to the Policy, Duty Entitlement Passbook (DEPB) Scheme[3] has been extended for one year till December 31, 2010. The DEPB rate shall also include a custom duty component on fuel as fuel is a consumable under Standard Input-Output Norms (SIONs).

Export Oriented Units

- EOUs have been allowed to sell 90 percent of their produce domestically as against 75 percent previously – only 50 percent of such domestic sales; would be eligible for 50 percent duty discount and all other such sales would have to be associated with full payment of all applicable duties.

Given that the global economy is still recovering from the recession, Board of Approvals (BoA) would consider, extension of block period by one year for calculation of Net Foreign Exchange earning of EOUs[4].

Value Added Manufacturing

- To encourage manufacturing exports characterised by value addition a minimum 15 percent value addition on imported inputs under Advance Authorisation Scheme has now been prescribed.

- Project Exports[5] and a large number of manufactured goods will be covered under FPS and MLFPS.

Support for Exporters

- Payment of customs duty for Export Obligation (EO) shortfall under Advance Authorisation/DFIA/EPCG Authorisation has been allowed by way of debit of duty credit scrips, whereas earlier the payment was only allowed in cash.

- Import of restricted items, as replenishment, shall now be allowed against transferred Duty Free Import Authorisations (DFIAs)[6], in line with the Duty Free Replenishment Certificate (DFRC)[7] scheme.

Simplification of Procedures

- The number of samples eligible for import by exporters has been increased from 15 to 50. Customs clearance of such samples will be based on declarations made by the importers taking into consideration limits on value and quantity of samples.

- Shipping Bills[8] applicable to one Export Promotion scheme can be converted for use in another within three months of issue instead of one, as provided for earlier.

- To reduce transaction costs, dispatch of imported goods directly from the port to the site has been allowed under Advance Authorisation Scheme for deemed supplies. At present, duty free imported goods can be taken only to the manufacturing unit of the authorisation holder or its supporting manufacturer.

- Disposal of manufacturing wastes/scrap will now be allowed after payment of applicable excise duty and before fulfillment of export obligation under Advance Authorisation and EPCG Scheme.

- Regional authorities have now been authorised to issue licences for import of sports weapons by 'renowned shooters'. Previously the Headquarters of DGFT had to be approached.

- The procedure for issue of Free Sale Certificate (allowing duty free sale of goods) has been simplified and the validity of the certificate has been increased from one year to two years. This will solve the problems faced mostly by the medical devices industry.

- Automobile industries having their own research and development (R&D) establishment will be allowed duty free import of reference fuels (petrol and diesel not manufactured in India) up to a maximum of 5 KL per annum.

- In response to demands for trade and industry sectors, the application and redemption forms under EPCG scheme have been simplified.

Reduction of Transaction Costs

- No fee shall now be charged for grant of incentives under the Schemes in Chapter 3 of FTP mentioned earlier

- Further, maximum fee for all other 18 Authorisations/ licence applications, is being reduced to Rs 100,000 from the existing Rs 150,000 for manual applications and Rs 50,000 from the existing Rs 75,000 for Electronic Data Interchange (EDI) applications.

- To further EDI initiatives, Export Promotion Councils/ Commodity Boards have been advised to issue Registration cum-Membership Certificates (RCMCs) through a web based online system.

- Electronic Message Exchange between Customs and DGFT in respect to incentive schemes under Chapter 3 will become operational by December 31, 2009. This will obviate the need for verification of scrips by Customs facilitating faster clearances.

- Double verification of shipping bills by customs for any of the DGFT schemes will be dispensed with for EDI ports, with effect from December 2009.

- In cases where the earlier authorisation has been cancelled and a new authorisation has been issued in lieu of the earlier authorisation, application fee already paid for the cancelled authorisation will now be adjusted against the application fee for the new authorisation, subject to payment of a minimum fee of Rs 200.

- An Inter Ministerial Taskforce will be formed to redress/ resolve problems/issues of exporters.

FTP 2009-2014 in Light of Recommendations Made Under CUTS' Implemented Project "GRANITE"

CUTS International had made some recommendations to the Director General of Foreign Trade (DGFT) for changes to the FTP, after engaging with many stakeholders, from the grassroots to top level policy makers under its flagship project entitled *Grassroots Reachout & Networking in India on Trade & Economics* (GRANITE). This project was implemented in 2007 and one of its main objectives is to make citizens' voices heard in the sphere of economic governance so as to enhance the government's accountability (at local, provincial and national level) on economic issues and help citizens make informed choices in regard to their livelihood. Thus, citizens' informed opinions were also communicated to policy makers working specifically on the National FTP with the objective of making the policy pro-poor and development, with focus on enhancing employment generation through trade. Analytical research, its dissemination as well as feedback to such research and associated issues led to the following recommendations by CUTS:

Simplification of Procedures

- Procedures need to be simplified through more use of automation and information technology.

- Better coordination among different government agencies dealing with exports and imports is essential.

- Modern best practice calls for a system, which ensures self compliance and maintenance of records (payment of tax, fees etc.) by exporters and importers for post transaction audits of records.

Reduction of Transaction Costs

India should take measures to reform and upgrade its customs systems and procedures in line with "best practices" and international standards. In spite of phenomenal growth in the Indian information technology sector, international trade is still largely administered through a paper-based system and face-to face contacts. India should make use of its internationally recognised IT sector to modernise customs procedures. The FTP should make sure that Kelkar Committee recommendations, which list best international practices on trade facilitation, are implemented. India can also try to replicate the system adopted by some of the developing countries, especially Southeast Asian countries, in this area.

Liberalisation of Regulator Framework

- The FTP 2004-09 has identified certain priority sectors to promote trade such as agriculture, handicrafts, leather etc. All these are labour-intensive activities and can help in employment generation in both rural and urban areas. Further, the five-year policy document also makes provisions to constructively engage states governments in export promotion. However, in the absence of a proper regulator the policy may not be able to achieve its desired objectives. The regulatory framework must enhance the country's ability to increase labour-intensive exports and thus achieve pro-poor objectives through trade.

- Promotional measures such as Market Access Initiative (MAI) and Market Development Assistance should be carefully directed to exploit hitherto untapped opportunities in those areas – for instance, organic farming, as there is a big market in developed countries for such products.

- The regulatory framework should be reformed and designed in a manner such that it works as a promotional agency rather an agency which puts up roadblocks and creates bottlenecks.

It is evident from the changes made to the FTP that CUTS' recommendations have been taken into serious consideration. To circumvent procedural bottlenecks which seem to add significantly to exporters' transaction costs, the new FTP is establishing an inter-ministerial taskforce which will oversee the Policy's implementation and take steps to enhance India's export competitiveness, especially taking into consideration the adverse impact of the global economic slowdown on Indian exports. In addition, an Inter-State Trade Council will be set up which will allow for closer interaction between Centre and States on a "regular and sustained basis".

However, it does seem that the reforms relating to transaction costs such as reduction or elimination of application fees and promotion of EDI connectivity have been somewhat insignificant till date. As a result, transaction costs still remain high because of a paucity of necessary infrastructure such as power and ports.

Views on FTP 2009-2014

- According to some experts, the export growth target of 20 percent p.a. is too low given that countries such as China have achieved growth rates of 30 percent. However, according to others, the export growth target set by the Policy seems ambitious.

- In addition, there is criticism that the government will not be able to push exports through fiscal giveaways, and the little relief offered "is directed at the labour-intensive sectors where little can be done till demand revives"[9]. On the other hand, some commentators feel that the Policy's objective to help labour-intensive export industries is somewhat inconsistent with its content, and that "the FTP tries to appease sectional interests of various commodities"[10].

- There is also criticism of the Policy's market diversification clause. It is said it will be difficult for Indian exporters to shift their focus from Western markets to the African and Latin American ones, which will not be able to create adequate demand for India's exports due to their own financial instability. The critics of this clause however, do not suggest an alternative. However, there are other views that the Policy's market diversification clause will in fact help Indian exporters explore untapped markets and realise their full potential.

- The Gems and Jewellery Export Promotion Council (GJEPC) has welcomed the initiatives taken by the policy, especially in regard to simplification of procedures for export of their products.

- There are concerns from apparel exporters over non-extension of MLFPS for garment sectors for exports to the EU and US after September 30, 2009. The Apparel Export Promotion Council chairman said that the apparel industry is asking for products like fabrics, silk products and home textiles (which are largely labour-intensive) to be included under the FPS to assist export growth[11].

- Another critique of the Policy is that markets covered by the FPS are at odds with the products covered. For example, including countries such as Vietnam and Cambodia as destination markets for Indian garments is unusual given that both these countries are net exporters of apparel. The exclusion of South Korea from FPS is also peculiar given the Comprehensive Economic Partnership Agreement (CEPA) signed with the country. There is a view that the Policy should have incorporated linkages established through concluded regional trade agreements while formulating the FMS list[12].

Conclusion

The main criticism of the new FTP seems to be that although it aims to help labour-intensive sectors, reduce transaction costs and in general help exporters through the global economic downturn, its provisions do not meet these objectives fully. For example, the provisions to reduce transaction costs do not take into consideration the significant linkage between high transaction costs and infrastructural deficiencies. Merely reducing application fees and implementing electronic payment systems will not lead to substantial and beneficial reduction in transaction costs for exporters. More emphasis needs to be placed on the improvement of existing infrastructure such as power, energy and transportation. In addition, the poor selection of markets for providing FPS incentives in regard to specific labour-intensive products without due regard for the opportunities generated through regional trading agreements would reduce the benefits from this initiative.

Endnotes

1 Under this scheme, financial assistance is provided for a range of export promotion activities implemented by EPCs and Trade Promotion Organisations on the basis of approved annual action plans.

2 Under this scheme, financial assistance is provided for export promotion activities on focus country, focus product basis.

3 This scheme allows for duty credit on imports required for export of a product.

4 Net Foreign Exchange Earnings of EOUs are meant to be calculated cumulatively in blocks of five years, starting from the commencement of production. Thus in the new policy, the block period will be extended to six years.

5 Project Exports is the setting up of overseas projects in the following four areas of engineering service: civil construction (structures/infrastructure), turnkey, process and engineering consultancy services, and project goods and project construction items (excluding steel and cement). Indian Project Exporters have executed a number of projects in a diverse range of markets overseas.

6 DFIA is issued to allow duty free import of inputs, fuel, oil, energy sources, catalyst which are required for production of export product.

7 Duty Free Replenishment Certificate is issued to a merchant-exporter or manufacturer-exporter for the import of inputs used in the manufacture of goods without payment of Basic Customs Duty, Surcharge and Special Additional Duty. However, such inputs are subject to payment of Additional Customs Duty equal to the Excise Duty at the time of import.

8 Shipping Bills are the main documents required by the Customs Authority for allowing shipment. They are usually of four types, with the major differences being with regard to the shipping goods being subject to certain conditions, such as: export duty/cess, free of duty/cess, entitlement of duty drawback, entitlement of duty credit under DEPB Scheme, and re-export of imported goods.

9 Editorial, *Too little aid for trade,* Hindustan Times, August 28, 2009, pp. 8

10 ET Debate, *Does FTP strategy encourage market diversification?* September 01, 2009 Available on: http://economictimes.indiatimes.com/Opinion/ET-Debate/Does-FTP-strategy-encourage-market-diversification/articleshow/4956956.cms?curpg=2

11 Business Line, *New trade policy to focus on labour-intensive exports,* August 10, 2009

12 *Ibid.*

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