2008-2009

INTERNATIONAL TRADE

Some facts that one must know

This document is the collection of facts that an MBA aspirant must know. However caution must be exercised while deriving interpretation from these facts. The complex interrelation between the cause and the effect must always be understood. Best of luck!

Career Launcher

Table of Contents

1. Introduction

Trade is as old as human history itself. Trade is *voluntary* exchange of goods or services[1] or both, with or without a medium of exchange called *money*. *Market* is mechanism that facilitates trade. When one gets goods for exchange of money it is called *buying* and reverse process is called *selling*.

The trade exits for many reasons, simplest of that is, if one cannot make a thing and it is available with someone else for exchange it with something of other person's interest. Some times its economical to purchase a thing rather then spent long time/effort in creating its own; in short, the specialization of labor is major reason for trade. Similarly, Trade exists between regions/countries because different regions have a comparative advantage in the production of some tradable commodity.

Trade should be distinguished from philanthropy, grant or gift where one gives away goods or money for the sake of human welfare and love.

1.1. What is foreign trade?

Foreign trade is the exchange of goods and services across the boundaries of the nation. As mentioned in the history of trade explained below, international trade has taken place throughout much of history (see Silk Road), but after the emergence of the nation states in the late 19th and 20th century its economic, social, and political importance has been on the rise in recent centuries. LPG (liberalization, privatization and globalization) coupled with Industrialization, advanced transportation, multinational corporations, and outsourcing are all have distinctly impacted international trade. Increasing international trade is basic to globalization.

The global trade has been divided into intra-country and across country trade. The character of two kinds of trade has shaped differently due to the emergence of policies, regulations and financial system that foreign trade has become a specialized branch of the economics. For nation states, its importance is immense and large efforts of foreign policy, aid policy and military policy are decided based on the requirement of the foreign trade of the nation.

Foreign trade has become a specialized area and several institutions have been created to generate, produce and manage and understand research. IIFT is an example of it.

[1] Trade involves goods and services both, so now onwards in this article, if not stated otherwise, whenever we say goods it means both goods and services

1.2. Why foreign trade

There are many theories that give the reasons behind the foreign trade. The basic question is why trade is necessary. Foreign trade came in to picture as a separate discipline because of the establishment of nation states. It has divided trade into national and international components.

David Ricardo has developed the most famous model on foreign trade, namely the, *comparative advantage*. Two or more nations trade because they have advantage in producing different commodities at a better cost and amount that is economical to purchase rather then make it yourself. In a Ricardian model, countries specialize in producing what they produce best. Unlike other models, the Ricardian framework predicts that countries will fully specialize instead of producing a broad array of goods. The above model can explain current foreign trade. We are not going into the deep and discussing other theories of foreign trade. Enthusiastic reader is suggested to go through models like Heckscher-Ohlin model, Gravity model and specific factor model.

1.3. History of trade

Trade is as old as communication, even older than that. We are briefly touching upon the history by mentioning the major events in the history of trade.

Trade begun when humans started exchanging the hunt or agriculture produce voluntarily. Traces of the long-range trade can be found in the ruins of Mesopotamia, ancient Egypt and Harappa civilization of Indus valley. From then onwards trade between Asia, Europe and North Africa has increased continuously. With every new invention in these parts of world, new items kept on adding and total trade kept on increasing. Spices, silk, gems and jewelry, swords and other metal products horses and other animals were the main items of long distance trade between these three continents.

However, the set back to foreign trade was the dark era that followed the great Roman Empire.

The fall of the Roman Empire, and the succeeding Dark Ages brought instability to Western Europe and a near collapse of the trade network. Nevertheless some trade did occur. For instance, there was a medieval group of Jewish merchants. They used to trade between the Christians in Europe and the Muslims of the Near East. Small regional trade was on during that time too. Cholas of South Indian kingdom was in trade with south East Asia through sea route. They controlled (albeit for small period) the Malacca strait and trade between china, East Asia and Middle East. In the north, the Moguls and Delhi sultanate had promoted the trade between India and Middle East. Vikings were active in trading between the Scandinavian region and mainland Europe. So even in dark ages the formation of linkages between different areas was on.

The enlightenment and the advent of sea routes bought new impetus to world trade. Vasco da Gama started the European Spice trade in 1498. Prior to his sailing around Africa, the flow of spice into Europe was controlled by Islamic powers, especially Egypt. The spice trade was of major economic importance and helped spur the Age of Exploration. Spices brought to Europe from distant lands were some of the most valuable commodities for their weight, sometimes rivaling gold. The discovery of new land (America) boosted the trade volume to the level world has not seen before. The main trading sea routes were trans-Atlantics and trans-Indian Ocean. The rise of European power was in the order in which countries have taken the sea trade seriously. Portugal in the 16th century, the Netherlands in the 17th century, and the British dominated trade in the East Indies in the 18th century. Spain was busy in looting gold from the Latin America.

The late 18th and 19th century was the era when new theories promoting free trade were proposed by the economist of the time. Adam Smith, David Ricardo and James Mill were the few names. There brief of their contribution is given in the in the section 12.

This century the trade saw major transformation. The two world wars and great depression, the rise of Japan followed by Korea, East Asian Tigers and later China were the major events. The formation of WTO and liberalization in India were the main events in the 90s and after, which will affect the future of world trade.

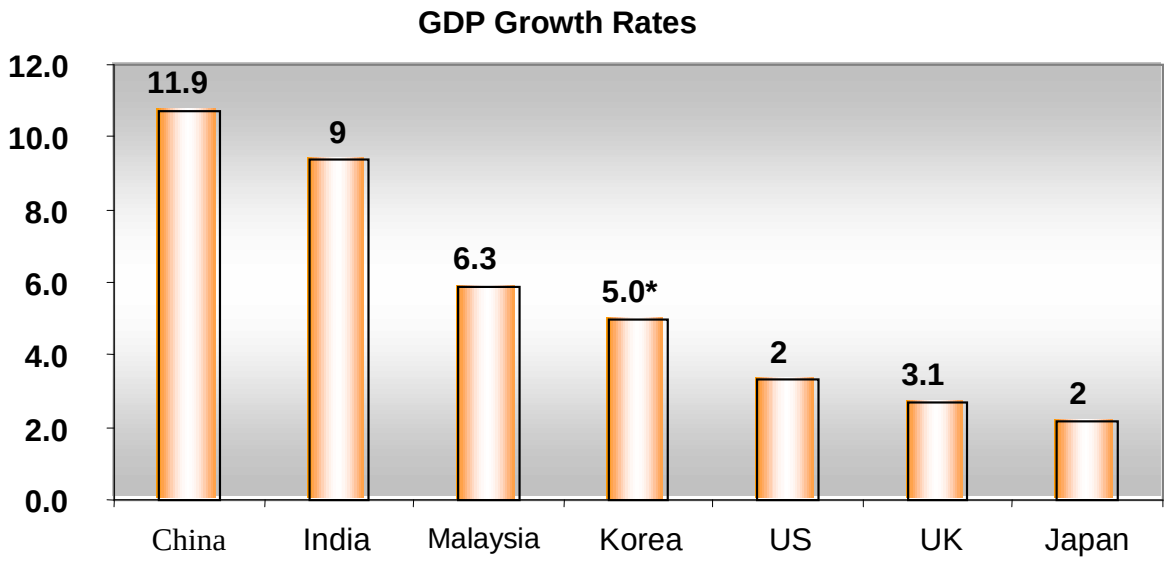
1.4. Shift of power to Asia

The purpose of including this topic here is that it has big importance in terms of its ability to shape the future of foreign trade. For India, Asia and rest of the world, the rise of Asia will decide how the trade in recent years has changed and how will it look like in the coming years. It will be cleared well, as the reader will go through the major trading regions of India in section of merchandise trade.
India, China, and other developing countries from Asia are giving the world economy the biggest boost in the whole of history. The facts below speak for it.

- Last year, for the first time, the combined output of emerging economies accounted for more than half of the world GDP (in PPP), with India and China alone accounting for nearly 1/4th.
- The share of world exports of the emerging economies was 43% against a mere 20% in 1970.
- They consumed over half of the world's energy.
- They hold 70% of the world's foreign exchange reserves.

In addition, as they integrate further into the global economy, obviously they would dominate the global economy. Importantly, since the emerging economies provide livelihood to 85% of the world's population, we could expect the spread of global gains to be more widespread than in any previous bouts of economic reforms.

India and China are growing almost 3 times as fast as Europe. China at 10.7% and India at 9.4% growth rate for the fiscal year 2006–2007 is much larger than US, UK or Japan. The difference can be deciphered with the bar chart below. The economy of India and China are bigger than the USA as estimated by purchasing power parity by the end of this fiscal year. Even when measured in Dollar terms, India and China will be bigger than USA in near future. (See BRIC report of Goldman Sachs for more details). These things are mentioned here so that reader can appreciate the rise of Asian economies and better predict the future of world trade in time to come. Following graph compares the growth rate of major economies[2].



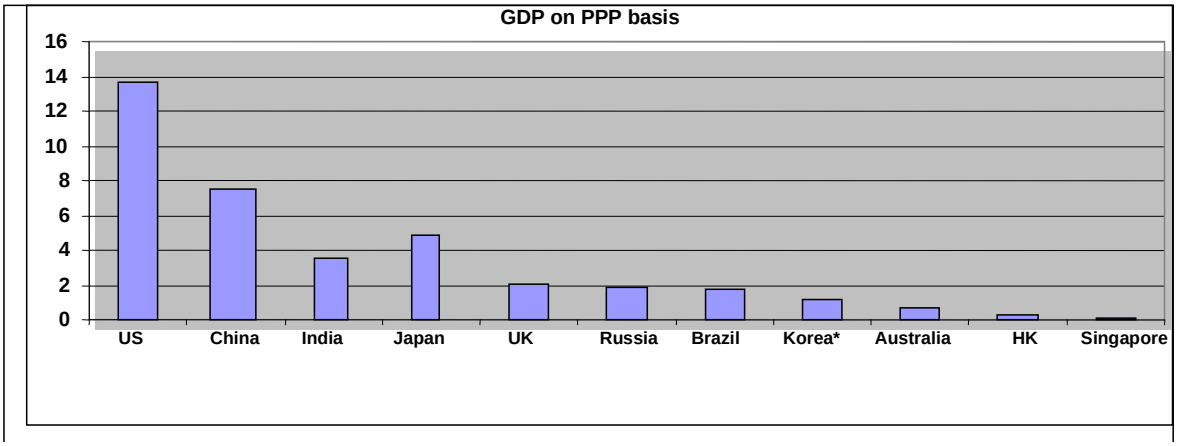
- *North Korea reported negative growth at –1.1%*
- *GDP figures expressed in percentage*

The PPP picture is brighter. Following graph tells that it is not far when we will catch up China and America[3].

---

[2] Source : International Monetary Fund, The Economist and the OECD

[3] *Estimates by IMF: World Economic Outlook, September 2007



**North Korea = $ 0.40 bn*

GDP ON PPP BASIS

COUNTRIES	GDP IN PPP BASIS (2007 est.)
US	$ 13.78 trillion
CHINA	$ 7. 099 trillion
INDIA	$ 2. 966 trillion
JAPAN	$ 4. 272 trillion
UK	$ 2. 13 trillion
RUSSIA	$ 2. 097 trillion
BRAZIL	$ 1. 849 trillion
KOREA	$ 40 billion – (NORTH KOREA) $ 1. 206 trillion –(SOUTH KOREA)
AUSTRALIA	$ 773 billion
HK	$ 293 billion
SINGAPORE	$ 227. 1 billion

2. Exchange systems

The single most important factor that gave a boost to the international trade is the evolution of exchange system. One can imagine how the international trade would look like if we still transact using the Barter system. The exchange system has seen the change form barter system to metal money, paper money, plastic money, virtual money and credit facility etc.

***Barter system**:* Barter is a type of trade that does not use any medium of exchange particularly money. In it, goods or services are exchanged for other goods and/or services. It is easy to have bilateral trade through it but multilateral trade is complex through it.

Barter is used in societies where no monetary system exists or in the economies where monitoring system is on the verge of collapse (hyperinflation etc). Recently the barter system has been seen in Zimbabwe. There inflation is so much that money loses its value in no time and barter is better way to manage trade. The food for work program ran by Indian government too has the traits of barter system. In Indian villages the barbers, cobblers and artisans are still paid in the form of crop produce, these all are the example of the barter system.

Money: Money itself must be a scarce good. Many items have been used as money, from precious metals, knives, shells, and cigarettes to entirely artificial money such as banknotes. Money is essentially a token (a faith) in other words, an abstraction. Paper currency is perhaps the most common type of physical money today. We talk a lot about De-mat accounts in the share market. Money was also the first thing that de-materialized. We never get the same paper money we deposit in the bank.

Money has few properties that make it better than the barter system. Unlike barter system it allows *divisibility*. If one has a cow and need 5 kg of rice certainly, he will not cut a leg of cow to get rice. The whole cow would be too expensive for exchange. Therefore, commodities do not have the divisibility which money has.
It also acts as *intermediary*. It is difficult to match the coincidence of wants of economic actors. It is difficult to have two people with both wants the things in others' possession. Money solves this problem by acting as intermediaries. Also unlike many commodities, money can be stored for the future.
Initially the things having some intrinsic value were the money. Examples of knives in china, pigs, seashells, cocoa beans were used as money. The roles that money played in trade are

i. Medium
ii. Measure
iii. Standards
iv. Store

Apart from acting as medium for exchange, money also helps in measure, setting standards for trade and can be stored for future.

***Fiat money**:* it refers to money that is not backed by reserves of another commodity. If a government, prints money at his will and the value of money is because of the government order or decree or *fiat* it is called the fiat money. If government print too

much of money (as for instance, in war times) it will result in long-term devaluation of money and inflation. In 1971 the US finally switched to fiat money indefinitely and it caused other nations currency to become fiat also.

Earlier the currencies were based on gold standard, which linked central banks, by a convention to redeem "hard currency" in gold. After World War II this system was replaced by the Bretton Woods ‘twins’ (the IMF and WB), which pegged currency of participating nations to the US dollar, which was redeemable nominally in gold. In the 1970s, this redemption ceased, leaving the system without a formal base and currencies of all major countries become fiat for indefinite time. Some consider the system today to be based on oil, a universally desirable commodity due to the dependence of so much infrastructure capital on oil supply. Since OPEC, prices oil in US dollars, the US dollar remains a reserve currency, but is increasingly challenged by the euro and to a small degree the Japanese yen. That is why many people believe that Iraq war has many other reasons apart from so-called WMD (weapons of mass destruction) issue.

Credit money: it is little difficult for a beginner to understand. Putting in simple words, if a bank gives credit of most of money deposited by the depositors, it actually increasing the money supply in the economy. At the same time, it does not have enough to pay back its depositors if they all come to ask for the payment. In simple terms, the bank is using depositor-creditor mechanism to increase the money supply.

John Maynard Keynes said that people hold money for three reasons

i. Transaction motive
ii. Precautionary motive
iii. Speculative motive

Money serves as medium of exchange but the receipts of money and payments of money lacks perfect synchronization. This gives rise to holding of money to carry day-to-day transactions. Precautionary need is to finance expenses on rainy days, like accident sickness or entertaining guests. When the prices of assets have uncertain, money can be hold for speculative purposes.

Some facts about money

- Income Tax was first introduced in Britain in 1799 to pay for a Royal wedding
- A $1 bill costs about 3 cents to make, and a $100 bill costs the same.
- 95% of the notes printed each year are used to replace notes already in circulation.

- Michael Jordan makes more money from Nike annually than all of the Nike factory workers in Malaysia combined and Tiger Woods' make more than entire labor force in Nike factories in south East Asia.
- Money (US $) is not made out of paper, it is made out of cotton.
- More of our fantasies are about money ... than sex.
- Money is the leading cause of disagreements in marriages.

Determinants of the value of the money: There are three important measures of the value of domestic money:

- The inflation rate, which determines the domestic value or purchasing power;
- The interest rate, or time value of money, which measures what savers get or borrowers pay; and
- The exchange rate, which measures the external value of the currency

The details about the exchange rate can be found in the section on foreign exchange.

3. Balance of Payments (BOP)

Out of many definitions, we are choosing the definition given by the IMF, "*The balance of payments is a statistical statement that systematically summarizes, for a specific time period, the economic transactions of an economy with the rest of the world. Transactions consist of those involving goods, services, and income; those involving financial claims on, and liabilities to, the rest of the world.*"

The BOP measures the payments that flow between any individual country and all other countries. It summarizes all international economic transactions for that country during a specific period, usually a year. The BOP is determined by the country's exports and imports of goods, services, and financial capital, as well as financial transfers.
It reflects all payments and liabilities to foreigners (debits) and all payments and obligations received from foreigners (credits). Balance of payments is one of the major indicators of a country's status in international trade, with net capital outflow.

The Balance of Payments for a country is the sum of the *current account* and *capital account* (sometimes called *financial account*). Ideally, the balance of payment should be zero, but it rarely is the case. BOP has direct impact on the foreign currency reserves of the country. If the BOP is positive, (negative) it resulted in the increase (decrease) of the reserves.
The Balance of Payments equation is given below:

$$\text{Current Account} + \text{Capital Account} = \text{Change in Official Reserve Account}$$

In short, BOP includes

i. Current accounts

- Merchandise
- Invisibles
- Unilateral transfers

ii. Capital Accounts

- Portfolio investment
- FDI
- Short term capital flows

The details of the items are given in the respective sections.

So it can be derived that a country can only consume more than it produces (imports more than exports) if it borrows from abroad (aid, debt or investment). This was the problem that plagued USA in the recent times, it has huge current account deficit and economists are worried about the long-term impacts of it. How long the USA will able to finance its excessive imports over exports.

BOP deficits/surpluses can be further divided into

Trade deficit (surplus)	**Merchandise trade**
GNP trade deficit (surplus)	Merchandise and invisible trade
Current account deficit (surplus)	*See next section*
Capital account deficit (surplus)	*See next section*
BOP deficit (surplus)	Errors and omissions

The BOP position of India is not very exciting. Since independence, India's balance of payments on its current account has been negative. Since LPG[4] in the 1990s, India's exports have been consistently rising, covering 80.3% of its imports in 2002–03, up from 66.2% in 1990–91. Since 2000-01, its balance of payments (current + capital account) has been positive. This is mainly due to large services export, tourism earning, remittances, increased foreign direct investment and deposits from non-resident Indians.

3.1. Current Account

Current account balance = (value of imports of goods and services + Returns on investments abroad) – (Value of exports of goods and services + return on investment outside the country)

Or simply,

Current account balance = Net value of export + Net returns on investments abroad

[4] Liberalization, privatization and globalization

Therefore, it includes merchandise, invisibles and unilateral transfers. Merchandise section records all the transaction in commodities. Invisibles records those in services (travel and tourism, banking, insurance, IT) income (repatriation of profits, dividends, interest on international debt) and wages and salary earned abroad. Unilateral transfer also considered the part of invisibles constitutes NRI remittances, private official gifts (Sachins' Ferrari given by Schumacher!), donations, grant and pensions. India has displaced China and Mexico to become top remittance receiving country in the world in 2007. We have received $24.7 billion[5].

Country	Remittances (2007) $ billion
India	$ 27
Mexico	$ 25
China	$ 25.7
Philippines	$17

Source : CIA fact Book 2008

Therefore, in nutshell, *Current account reflects the difference between the income a country earns from the rest of the world and the income rest of the world earns from that country*.

Apart from others things like aid, the *Balance of Trade* forms important part of the current account. The Balance of Trade is the difference between the monetary value of exports and imports in an economy over a certain period. A positive balance of trade (more export than import) is called trade surplus and its reverse is trade deficit. The balance of trade is can be divided into a goods and a services, it also called visible and invisibles component of trade.
USA has massive trade deficit. Year 1994 was the last year when USA has seen trade surplus, after it is in trade deficit. The situation become worse after the tenure of Bush junior and in year 2005 US had a trade deficit of more than $ 700 billion. It was more than the total GDP of India during that year.

Why so much of hula buloo about any country's trade deficit, in today's scenario America's. It can be explained with the simple reasoning that, if country America has a trade deficit because of large imports of consumer goods, other countries (gulf countries and China) accumulate cash from country America. That money can be used to purchase existing investment assets and government bonds within country America. As a result, the return from those assets will accrue not to citizens of America but to foreigners. The

[5] Times of India, Oct 22nd, 2008

consumption standard of future generations in America may therefore potentially decline because of the deficit.
Milton freedman is one economist (rather *Monetarist*) who least care about the trade deficits and have his own argument in the favor of trade deficits. He believed that deficits would be corrected by free markets as floating currency rates rise or fall with time to encourage or discourage imports in favor of the exports, reversing again in favor of imports as the currency gains strength.

As a rule current account is treated as net inflow of capital from abroad. Therefore, as a rule, BOP is zero and change in current account is reflected by corresponding change in the capital account.
Change in Current Account + change in Capital Account = 0

It is rarely zero and is reflected in the change in foreign exchange reserves (Forex) of the country, which is nothing but the change in the assets owned by the country. Change in forex in thus counted in capital account. Change in forex is referred as compensating, accommodating or financing transaction to distinguish it from both the capital and current account transactions.
Below is the list of major countries and their current account surpluses (figures in $ billions, 2007 estimates from the world fact book)

Rank	Country	Current Account Surpluses
1	China	179
2	Japan	174
3	Germany	135
4	Russia	105
5	Saudi Arabia	104
157	India	-26
158	France	-38
159	Australia	-42
161	UK	-58
162	Spain	-99
163	USA	-862

3.2. Capital Account

The capital account records all the inter country transactions that involves a change of ownership of an asset. It includes the two-way Portfolio investment, FDI and short-term capital flows.
The NRI deposits and loans from abroad (those given by WB, IMF and ADB[6]) are broadly part of part portfolio investment. It also includes FII[7]. The trade capital (sundry debtor/ creditor, trade advances of less than a year) arbitrage and speculative transactions in currencies go in to the short-term capital flow part of capital account.

Apart from the policy differences the capital account also based on the 'push' and 'pull' factors. The former includes factors such as low interest rates and low return on the capital invested, which push the capital out of the countries to the countries that offer more returns. The later are the factors that serve to attract capital into host country. It includes low cost of production, cheap labor, tax incentives, protection of property rights and financial market development. The recent flow of FII in the month of September and October can be examined and explained by the above reasoning. The readers should grapple why the out flow of FII happened in the end of the October 2007 (market saw biggest fall of 1600 pints within an hour) when rumors about banning the P (participatory) notes spread.

The differential in the interest rates (of government bonds, most 'safe haven' to invest money) in USA and Japan on one hand and India on the other gives the reason for flow of capital from USA/Japan to India. One can borrow virtually at zero cost in Japan and invest in India can earn 5-6% interest. Then why not entire money is flowing from Japan to India, think about it!

So in the end, are deficits bad?
Managers give one answer for all the questions, "It all depends." It is true that economic theory tells us that whether a deficit is good or bad depends on the factors giving rise to that deficit, but economic theory also tells us what to look for in assessing the desirability of a deficit.
If the deficit reflects an excess of imports over exports, it may be indicative of competitiveness problems, but because the current account deficit also implies an excess of investment over savings, it could equally be pointing to a highly productive, growing economy.

---

[6] World Bank, International Monetary Fund, Asian Development Bank

[7] Currently the investment in equity is less than 10% so no voting rights are enjoyed by and it is treated as FII. If investment is more than 10%, so foreign party enjoys the voting rights and investment is treated as FDI

3.3. Full Account Convertibility

There is lot of debate has happening in the recent times whether India should go for full account convertibility, which includes both the capital account and current account convertibility. India already has current account convertibility in place.

Convertibility is the monetary policy issue, which a nation needs to decide, it has broad implications. Convertibility on one hand encourages the foreign investors to invest as it allows them to carry out their profits and send back the money invested as per need. However, it also poses the threat of capital flight. It is something similar to what south East Asia witness during the 1997 crisis.

India after opening up if its economy in early 1990s has opted for full current account convertibility and her capital account is only gradually opened since then. This means that all the transactions in the current account of the balance of payments (BOP) are free for execution as far as foreign exchange is concerned (but it subjected to trade restrictions, if any) but many transactions that fall into the capital account of the BOP still need approval from the authority. In other words, it allows residents to make and receive trade-related payments — receives dollars (or any other foreign currency) for export of goods and services and pays dollars for import of goods and services make sundry remittances, access foreign currency for travel, studies abroad, medical treatment etc

There is no formal definition of capital account convertibility (CAC). The Tarapore committee set up by the Reserve Bank of India (RBI) in 1997 to go into the issue of CAC defined it as the freedom to convert local financial assets into foreign financial assets and vice versa at market determined rates of exchange.

To put is simply, capital account convertibility (CAC) -- or a floating exchange rate -- means the freedom to convert local financial assets into foreign financial assets and vice versa at market-determined rates of exchange. This means that capital account convertibility allows anyone to move freely from local currency into foreign currency and back.

It was an effort to find fiscal and economic policies that would enable India's transition to globalized market economy. The reasoning for capital account convertibility was so that foreign investors could invest without barriers.

Current Indian situation:

The target were set and then moved to later dates because of global crisis and indecisiveness of the government. East Asian crisis in 1997, Dot com bubble in 2000, elections in 2002 and the opposition of left thereafter has forced government to keep on

shifting the implementation of CAC. Buoyed by the very comfortable build-up of forex reserves, the strong GDP growth figures for the last two quarters and the fact that progressive relaxations on current account transactions have not lead to any flight of capital, on Friday the government announced further relaxations on the kind and quantum of investments that can be made by residents abroad. These relaxations are to be reviewed after six months and if the experience is not adverse, we may see further liberalization and in the not-too-distant future full CAC.
Finance minister feels that the deficits should be brought under control before the country should go for full account convertibility. By 2010, we can hope to see the implementation of full account convertibility in India.

4. External trade

External trade includes imports and exports of both the goods and services. Because of the different nature of the two, we are discussing them separately. Next section we are doing detail analysis of merchandise trade, followed a discussion on trade in services. The discussion is mainly India centric. The recent available data is being used and to judge the trend past two years of data is compared and past year growth rates are shown at most of the places.
During past fifty years, numerically the growth of India's import and export seems to be good but when compared to the other countries we have performed very poorly. It is also reflected in our continuously declining share in the world Ex/Import.

India which is 12th largest economy when measured in dollar terms; 16th largest importer and 28th largest exporter. It shows how close the Indian economy is. Small countries like Taiwan, Singapore and city of Hong Kong are bigger importer and exporters than India.

It can be largely because of socialist and *swadesi* (import substitution) policies adopted by the governments before 1991.

The major importing countries of the world are listed below. We can see where India stands viz-a-viz other major nations of the world.

World largest Importers (world fact book, 2007 Estimates)

Rank	Country	Import value ($ billions)
1	USA	1.968 tn f.o.b.
2	Germany	1.075 tn f.o.b
3	China	904.6 bn f.o.b
4	UK	621.4 bn f.o.b
5	France	600.9 bn f.o.b
6	Japan	573.3 bn f.o.b
16	India	230.5 bn f.o.b
17	Russia	223.4 bn f.o.b

The major exporting countries of the world are listed below. We can see where India stands in comparison to other major nations of the world.
World largest Exporters (world fact book, 2007 estimates)

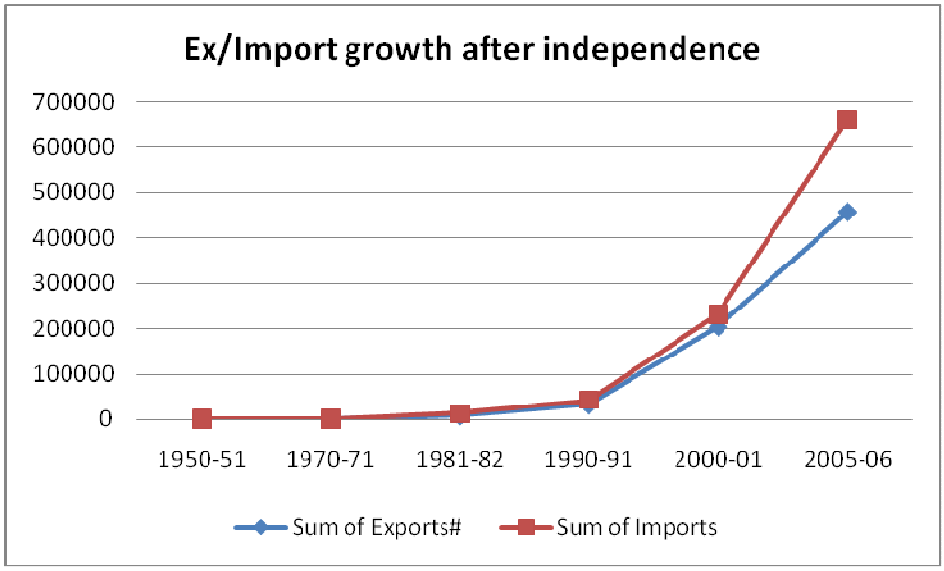
Rank	Country	Export value ($ billions)
1	Germany	**$ 1. 354 trillion f.o.b.**
2	USA	**$ 1. 148 trillion f.o.b.**
3	China	**$ 1. 22 trillion f.o.b.**
4	Japan	**$ 678. 1 billion f.o.b.**
5	France	**$ 546 billion f.o.b.**
11	South Korea	**$ 379 billion f.o.b.**
12	Russia	**$ 3555.5 billion**
13	Singapore	**$ 302. 7 billion f.o.b.**
28	India	**$ 151. 3 billion f.o.b.**

Source: CIA world Fact Book estimates 2008

Let us see how the Indian ex/import has grown over the years. In rupees terms it seems to be a phenomenal increase. However, when compared to the benchmark (developing nations of East Asia) we have done extremely poorly in external trade area.

Exports/Imports and Trade Balance of India[8]			
(1950-51 to 2005-06)			
(Rs. in Crores)			
Year	Exports	Imports	Trade Balance
1950-51	606	608	-2
1970-71	1535.3	1634.2	-98.9
1981-82	7805.9	13607.6	-5801.7
1990-91	32558	43193	-10635
2000-01	203571	230873	-27302
2005-06	456418	660408	-203992

The graph below summarizes the countries Ex/import performance post independence. The values here are in rupee crores.



During this period country saw a countinous decline in its share to total world trade. We were closed to the opportunity presented by the external world. We were dependent on the jute and cotton industry whose demand was largely inelastic and with natural polymers came there use was limited. Margaret Thatcher started privatization in 1970s, China libralized in 1980s and we were way behind it observing our hindu rate of growth (3% growth rate pre1991). The story of indian ex/imports is a story of missed opportunity. Thanks to LPG post 1991 and india joining the WTO India is again started to regain its long due position in international trade. Since 1991 India's export growth rate is consistently above worlds average export growth rate, leading to improvement in the India's share in world trade. India's share in world merchandise export is almost 1%

[8] Ministry of Commerce & Industry and Department of Economic Affairs

by the year 2007 and in serives we are shy away from 2%. The story till now is summurizes below.

Table 1: Indicators of India's Export Growth, 1950-2005
(US $ millions)

Period	Average Annual Growth Rates[a]				India's Share in World Exports, Averages		India's Exports of Goods and Services (Per Cent of GDP), Averages
	Goods		Services [b]		Goods	Services	
	India	World	India	World			
1950-59	0.22	6.30	3.78	NA	1.39	NA	NA
1960-69	3.58	8.77	1.78	NA	0.90	NA	4.21
1970-79	17.97	20.41	26.61	NA	0.54	NA	5.20
1980-85	2.39	-0.86	3.79	0.36	0.47	0.81	6.05
1986-90	17.76	12.36	10.47	14.14	0.48	0.63	6.29
1993-97	13.30	10.56	14.10	9.22	0.60	0.59	10.50
1999-01	10.26	4.09	9.52	3.07	0.66	1.07	12.52
2002-05	25.29	17.58	45.36	15.16	0.81	1.64	17.19[c]

4.1. Merchandise trade

The merchandise trade of the country has increased over the years. The graph in the previous page shows India's progress after the independence. With new impetus are given, and India's emergence as global manufacturing hub provides huge opportunity for Indian merchandise growth in the future.

Before going into the detail analysis of the export let have a look on export and imports as a percentage of countries GDP. It can be seen that china (and economies like Singapore, Honk Kong and UAE) is integrated more with the world.

Country	GDP ($ billions)	Export, import, total trade ($ billions)	Total trade as percentage of GDP
USA	13210	1024, 1869, 2893	22%
China	2680	974, 778, 1752	61%
Japan	4367	590, 524, 1114	25.5%
India	1000	126, 191, 317	31.7%
Brazil	1000	137.5, 91.4, 229	22.9%

The values of Japan and USA should be looked with care. It is not that they are isolated and thus the percentage of trade to GDP is low. Actually, the service trade and invisible component is much larger that is not reflected in merchandise trade.

For better understanding the international trade is discussed under different

- Commodity wise
- Region wise (EU, ASEAN, Africa etc)
- Top trading partners

- Focused analysis of trade with two major trading partners USA and China

Commodity wise:

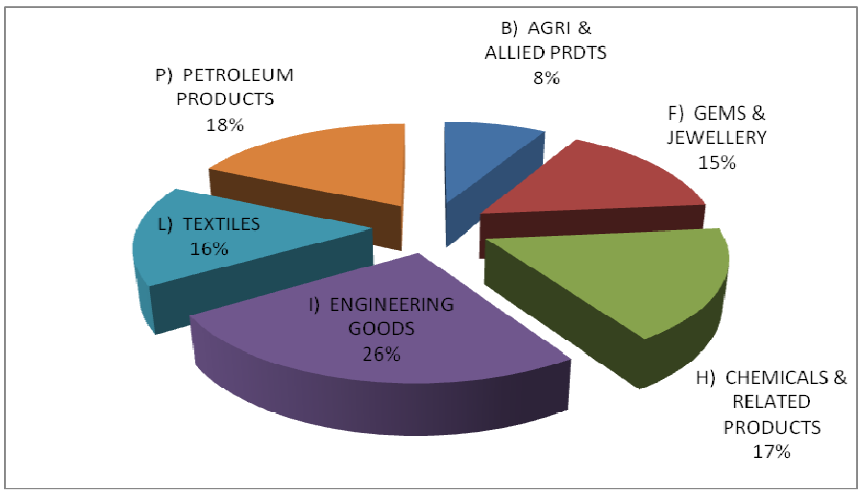
The commodity wise analysis of the merchandise trade is given below. Form the table it can be seen that bulk imports forms the largest component of the import, followed by machinery. The import of machinery reflects that the country is undergoing phase of rapid expansion of its productive capacities. The import of pearls and precious metal has a special place because it resulted in the value added exports later. Something similar is happening with crude oil also. As the country is becoming the refinery hub of the Asia, more and more re-export of crude will happen from the country after the value addition through refining.

Indian import during the last two years and growth rate is given in the table below.

Dated: 27/12/2008[9]				
Values in US$ Billions				
Commodity	**Apr-Mar 2007**	**Apr-Mar 2008**	**%Growth**	**%Share**
Bulk Imports	**84,076.71**	**112,108.78**	**33.34**	**44.59**
Pearls, Precious & Semi-Precious Stones	**7,481.67**	**7,976.56**	**6.61**	**3.17**
Machinery	**26,709.22**	**45,175.03**	**69.14**	**17.97**
Project Goods	**1,794.52**	**1,293.54**	**-27.92**	**0.51**
Others	**65,541.98**	**84,885.25**	**29.51**	**33.76**
Total	**185,604.11**	**251,439.17**	**35.47**	**100**
	Exchange Rate: (1US$ = Rs.)	***45.2849***	***40.2607***	

[9] Data Source: DGCIS, Kolkata

To have a feel of the share of different **import** commodities, the pie chart is given below.



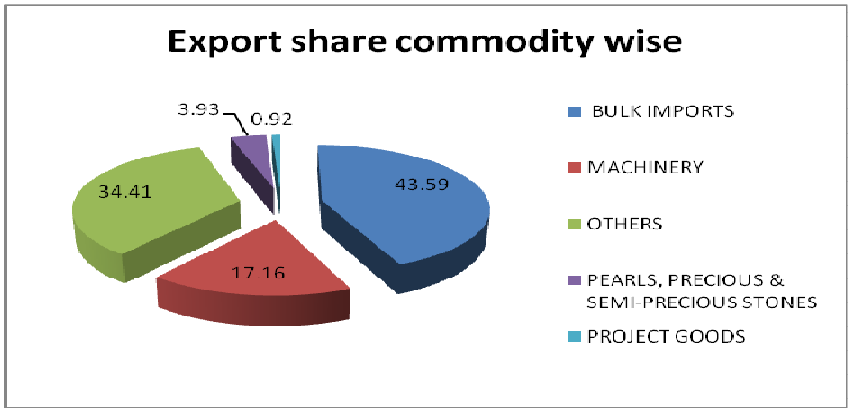
Indian export basket is quiet broad based. Engineering goods, Gems and jewlery, chemical and relaed products and petroleum are major export item. These all refelecrs the value addition capability and high tech mature industry of the nation. The export basket is much different than it used to be after independence. During 50's the jute and cotton products are main export comoodities. Textile deserve a specila mention here. Textile never able to come to its full potetial. After the dismatelling of MFA (multi fiber arrangement not *agreemnt*) textile export was thought to be increse by leaps and bounds but nothing of that sort happen and most of the advatgaes were cornered by china. Bagladesha vietnam and pakistan are givng tough competition to indian textile exports. The tremendous growth rate of engineering goods and petroleum priducts tells the story of future. In future indian exports will contitute of high value commodities more.

Indian export during the last two years and growth rate[10] is given in the table below:

[10] Data Source: DGCIS, Kolkata

Dated: 27/12/2008				
Values in US$ Millions				
Commodity	Apr-Mar 2007	Apr-Mar 2008	%Growth	%Share
Plantation	869.72	970.29	11.56	0.6
Agri & Allied Prdts	8,688.26	13,510.90	55.51	8.29
Marine Products	1,766.82	1,720.45	-2.62	1.06
Ores & Minerals	6,997.02	9,119.79	30.34	5.6
Leather & Mnfrs	3,014.33	3,502.50	16.19	2.15
Gems & Jewellery	15,964.52	19,678.68	23.27	12.08
Sports Goods	126.65	134.11	5.89	0.08
Chemicals & Related Products	18,407.32	22,347.12	21.4	13.72
Engineering Goods	26,471.29	33,709.56	27.34	20.69
Electronic Goods	2,935.36	3,498.15	19.17	2.15
Project Goods	137.45	145.07	5.55	0.09
Textiles	16,427.34	18,474.31	12.46	11.34
Handicrafts	437.65	508.24	16.13	0.31
Carpets	927.26	942.74	1.67	0.58
Cotton Raw Incl Waste	1,348.75	2,202.00	63.26	1.35
Petroleum Products	18,664.09	28,363.06	51.97	17.41
Unclassified Exports	3,078.84	4,077.19	32.43	2.5
Total	126,262.68	162,904.16	29.02	100
Exchange Rate: (1US$ = Rs.)	*45.2849*	*40.2607*		

To have a feel of the share of different **export** commodities, the pie chart is given below



Region wise:

If we see the region wise trade of commodities with India. We can say that Asia and ASEAN are the largest trading regions with India. Europe is distant second which closly folowed by the America. The recent increase in the dominance of Asia is due to three factors

- High growth rate of asian region
- Look east policy of government (lot of PTA were signed)
- High price of crude oil

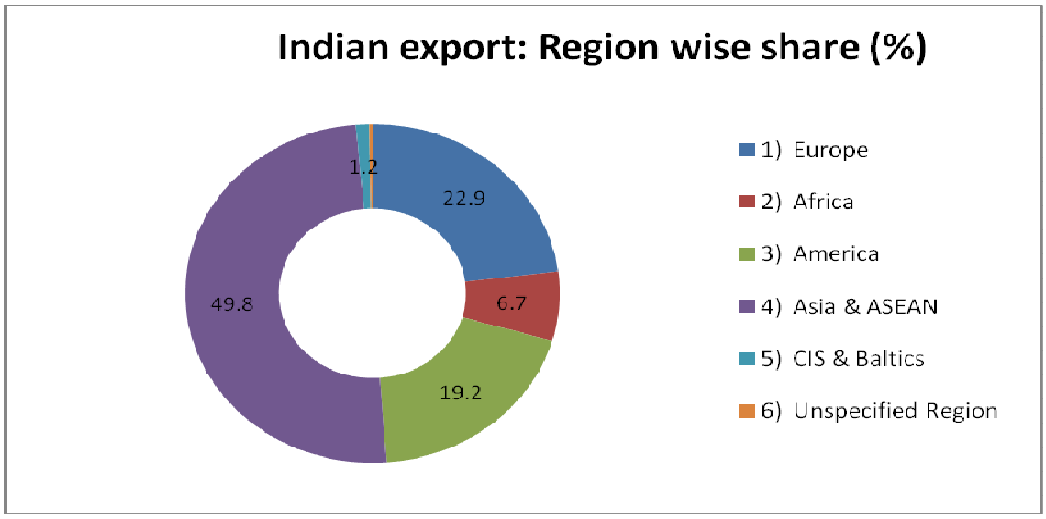
In asia west asia and east asia including japan are the major partners. The growth rate with africa is tremedous, but the base is low. Trade with europe is growing slowly. Future griwth will come from the regions like africa and asia.

The table below shows the region wise export[11] data.

[11] Data Source: DGCIS, Kolkata

Dated: 27/12/2008				
Values in US$ Millions				
Region	Apr-Mar 2007	Apr-Mar 2008	%Growth	%Share
1) Europe	28,848.19	37,238.63	29.08	22.86
1.1 EU Countries (27)	26,784.99	34,490.16	28.77	21.17
1.2 Other WE Countries	1,982.77	2,642.41	33.27	1.62
1.3 East Europe	80.43	106.06	31.87	0.07
2) Africa	8,404.97	11,540.64	37.31	7.08
2.1 Southern Africa	2,816.32	3,607.46	28.09	2.21
2.2 West Africa	2,441.48	3,474.93	42.33	2.13
2.3 Central Africa	203.31	257.38	26.59	0.16
2.4 East Africa	2,943.86	4,200.87	42.7	2.58
3) America	24,225.63	27,635.05	14.07	16.96
3.1 North America	19,960.96	21,977.28	10.1	13.49
3.2 Latin America	4,264.68	5,657.77	32.67	3.47
4) Asia & ASEAN	62,955.23	84,196.80	33.74	51.68
4.1 East Asia	1,488.86	1,409.11	-5.36	0.86
4.2 ASEAN	12,603.86	16,376.24	29.93	10.05
4.3 WANA	23,038.29	30,357.15	31.77	18.63
4.4 NE Asia	19,359.80	26,437.06	36.56	16.23
4.5 South Asia	6,464.42	9,617.24	48.77	5.9
5) CIS & Baltic's	1,476.95	1,737.62	17.65	1.07
5.1 CARs Countries	191.41	232.19	21.3	0.14
5.2 Other CIS Countries	1,285.55	1,505.44	17.1	0.92
6) Unspecified Region	351.7	555.41	57.92	0.34
Total	126,262.68	162,904.16	29.02	100
Exchange Rate(1US$ =Rs)	*45.2849*	*40.2607*		

The doughnut diagram below shows share of different regions in total Indian exports. Clearly, the Asia region dominates the large part of it.



Asia and ASEAN are the largest source for indian import. The dominance of the Asia region is even bigger than it was in the case of exports. The oil is critical factor. Has India has large oil import which largely sourced from the middle east reagion, it increased the over all share of asia in India imports. Again Europe is distant second and America is lagged behind.

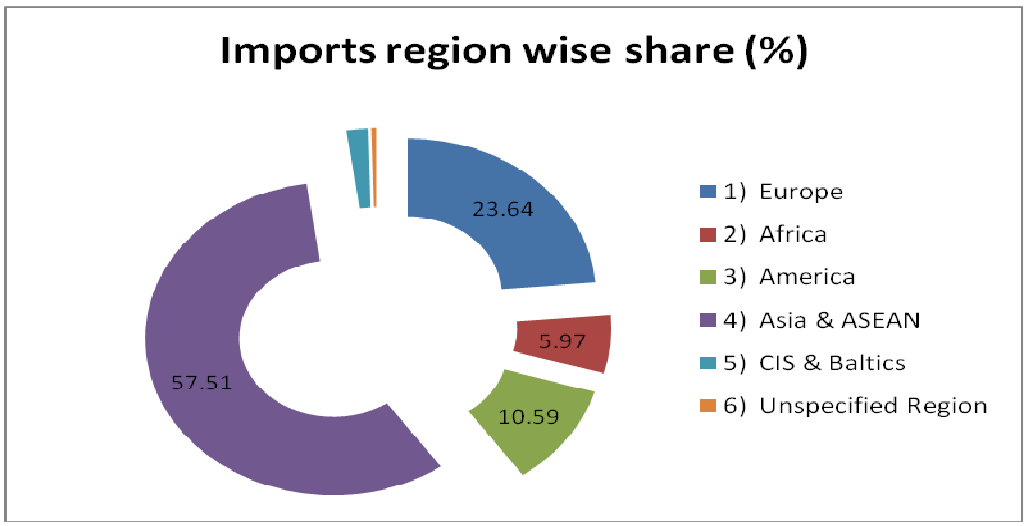
The imports from africa has gone almost 3 times of previous year value. The import from asian region is more than doubled duirng the same period.

The table below shows the region wise import[12] data

[12] Data Source: DGCIS, Kolkata

Dated: 27/12/2008				
Values in US$ Millions				
Region	Apr-Mar 2007	Apr-Mar 2008	%Growth	%Share
1) Europe	40,085.02	51,600.45	28.73	20.52
1.1 EU Countries (27)	29,809.06	38,413.67	28.87	15.28
1.2 Other WE Countries	10,216.51	13,151.02	28.72	5.23
1.3 East Europe	59.45	35.76	-39.85	0.01
2) Africa	11,376.70	14,941.72	31.34	5.94
2.1 Southern Africa	2,922.04	4,833.03	65.4	1.92
2.2 West Africa	8,192.67	9,740.54	18.89	3.87
2.3 Central Africa	29.01	48.98	68.84	0.02
2.4 East Africa	232.98	319.18	37	0.13
3) America	19,618.75	29,549.33	50.62	11.75
3.1 North America	13,502.98	22,991.48	70.27	9.14
3.2 Latin America	6,115.78	6,557.85	7.23	2.61
4) Asia & ASEAN	109,821.71	149,767.27	36.37	59.56
4.1 East Asia	7,579.67	8,377.05	10.52	3.33
4.2 ASEAN	18,089.64	22,663.48	25.28	9.01
4.3 WANA	51,152.33	71,881.82	40.53	28.59
4.4 NE Asia	31,493.89	44,733.52	42.04	17.79
4.5 South Asia	1,506.17	2,111.40	40.18	0.84
5) CIS & Baltics	3,860.17	3,778.33	-2.12	1.5
5.1 CARs Countries	142.85	112.03	-21.58	0.04
5.2 Other CIS Countries	3,717.31	3,666.30	-1.37	1.46
	841.75	1,802.06	114.09	0.72
Total	185,604.11	251,439.17	35.47	100
Exchange Rate:(1US$=Rs)	*45.2849*	*40.2607*		

For better comprehension, the doughnut diagram below shows the share of different reasons.



Top trading countries:
Since the WTO is not grathering pace as was expected, countries are increasingly strucking the bilateral trade agreements. The imprtance of trading partner is enormous in the present world. Indian's major trading partners are USA, china, Saudi Arab, UAE, and singapore. UK and gernaby are main trading partners in the EU region.

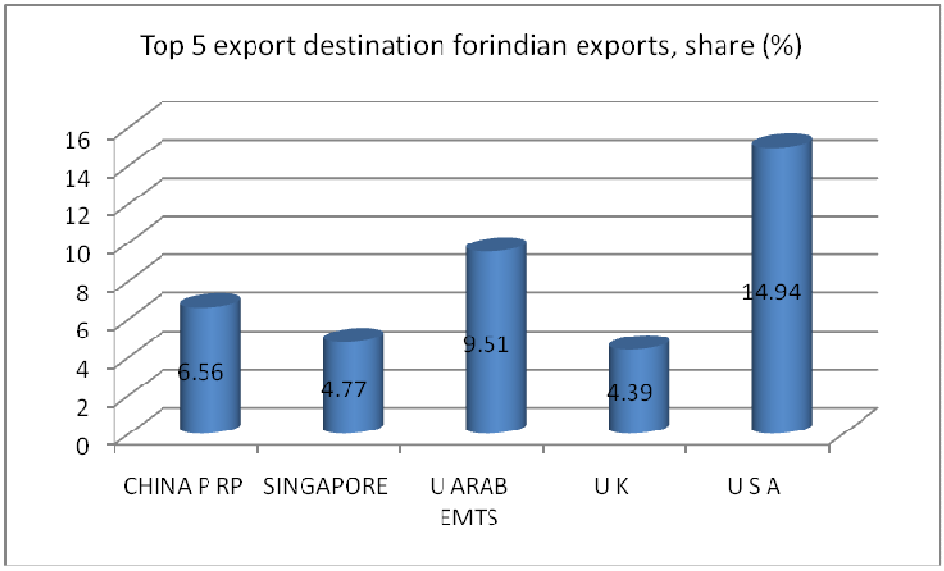
The growth rate of trade with china was special during last few years. From almost no where china has emered to become 2nd largest trading partner. Given the rapid increase in trade between the two countries it will soon beocme the largest trading partner of India.
Still the USA is largest destination of merchandise export from the India. UAE is second larget destination. UAE don't consume the indian export but re-export them to Africa, middle eastern countries and pakistan. It causes the value loss for bth pakistan and India. Much can be saved for two countries had the ships go directly from mumbai to Karachi.
Singapore is another major destination that re-export indian commodities to ASEAn and china region.

Top 5 country export[13] destination from indain goods are given in the table below.

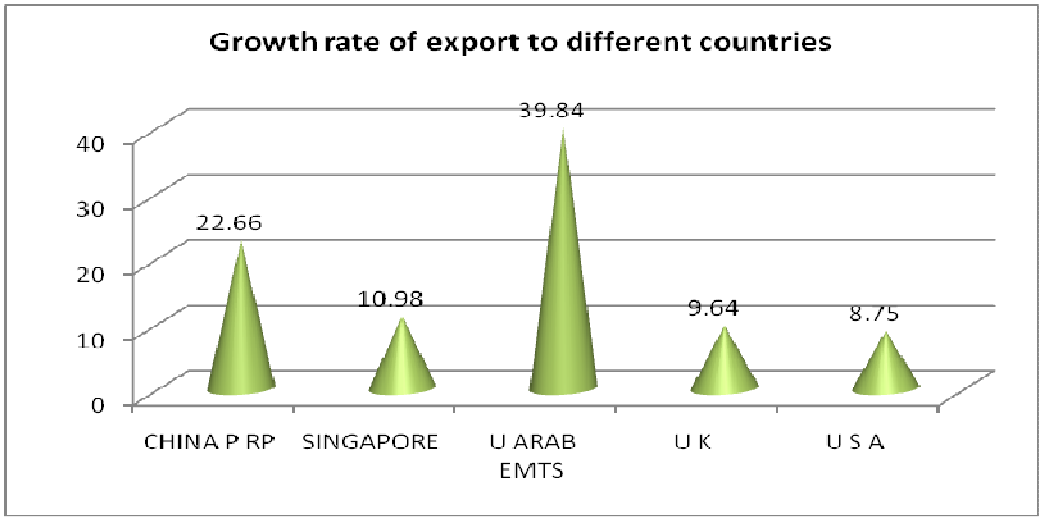
[13] Data Source: DGCIS, Kolkata

Dated: 27/12/2008					
Values in US$ Millions					
Rank	**Country**	**Apr-Mar 2007**	**Apr-Mar 2008**	**%Growth**	**%Share**
1	U S A	**18,851.42**	**20,712.03**	**9.87**	**12.71**
2	U ARAB EMTS	**12,022.77**	**15,626.91**	**29.98**	**9.59**
3	CHINA P RP	**8,287.48**	**10,828.78**	**30.66**	**6.65**
4	SINGAPORE	**6,064.19**	**7,367.54**	**21.49**	**4.52**
5	U K	**5,613.63**	**6,698.22**	**19.32**	**4.11**
	Total	**126,262.68**	**162,904.16**	**29.02**	**100**
	Exchange rate(1US$=Rs)	***45.2849***	***40.2607***		

The share of these countreis are given below. USA dominate followed by the UAE.



The growth rate of export to UAE and china is the highest. The cones below shows the growth rate of export to top five export destinations.



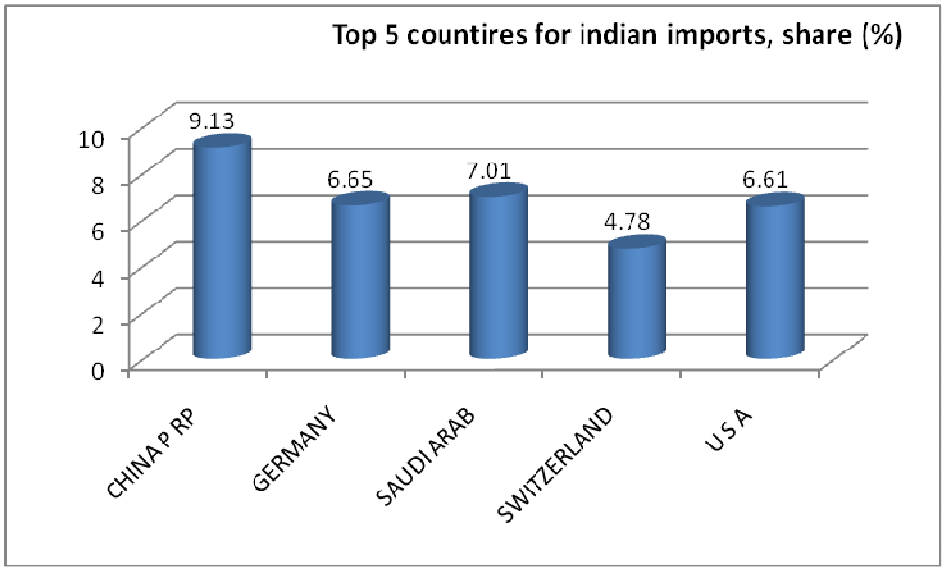
The largest source for imports is China. Electronics goods, low value and high volume items, plastic products, toys, tiles and lot many things are beign imported from china. China still not the source of high tech engineering goods. These are supplied by Germany and to little extent Japan. Saudi Arab is source of crude oil. Switzerland is source of electrical transmission, pharmacheuticals and confectionary.

Top 5 country import[14] sources for indain are given in the table below:

Dated: 27/12/2008					
Values in US$ Millions					
Rank	**Country**	**Apr-Mar 2007**	**Apr-Mar 2008**	**%Growth**	**%Share**
1	CHINA P RP	**17,447.01**	**27,102.38**	**55.34**	**10.78**
2	SAUDI ARAB	**11,726.96**	**21,019.29**	**79.24**	**8.36**
3	GERMANY	**13,373.44**	**19,401.13**	**45.07**	**7.72**
4	U S A	**8,650.77**	**13,470.50**	**55.71**	**5.36**
5	SWITZERLAND	**7,621.85**	**10,915.34**	**43.21**	**4.34**
	Total	**185,604.11**	**251,439.17**	**35.47**	**100**
Exchange Rate: (1US$ = Rs.)		***45.2849***	***40.2607***		

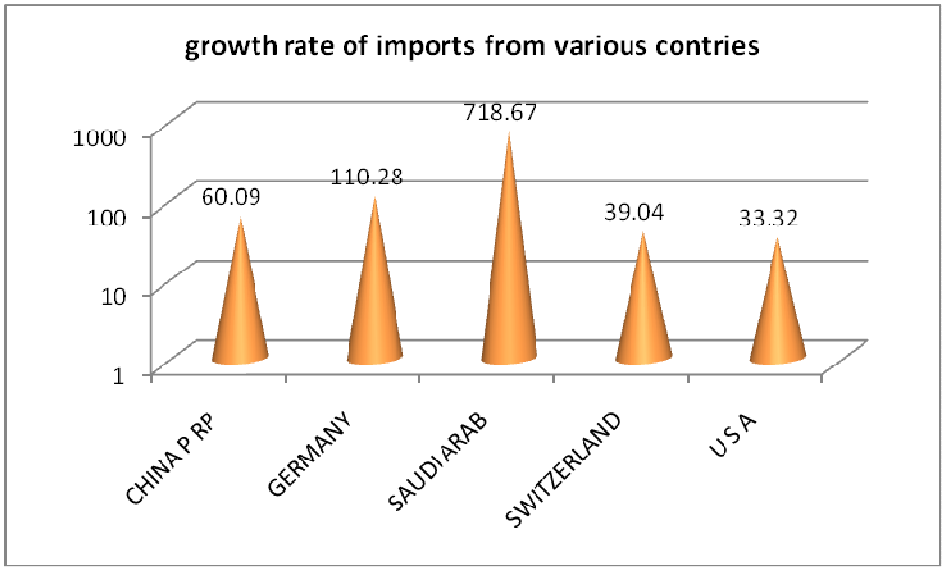
The share in Indian imports can be judged by the following bar chart. China leads by good margin. USA, Saudi Arab and Germany, all have nearly equal share.

[14] Data Source: DGCIS, Kolkata



Be careful in examining the next graph, here Logrithmic scale (for Y axis) is used as the growth rate of imports from different countires are differ by wide margin. If carefuly observed the growth of imorts from Saudi Arabia is much more than any other country. The import growth rate from Saudi Arabia is more than 700%. This increase can be attributed to rapid rise of crude oil prices in the international markets.

The growth rate of imports from Saudi Arab and Germany is the highest. the increase in imports from Germany is mainly of heavy engineering goods that are used to setup the manufacturing industires in the country. So one can feel exited when ever the imprts form Germany increased. The cones below shows the growth rate of export to top five export destinations.



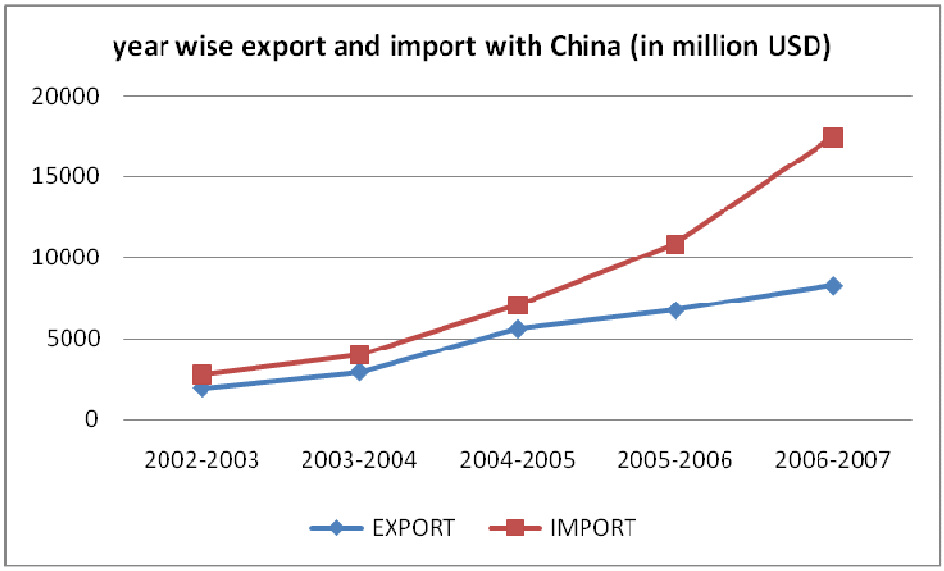
Detailed country wise analysis (USA and China):
I have included a comprehensive analysis of the trade with USA and China. These two natons are major trading partners and big economies of the world. Indian trade relation and volume of trade with the two nations will be crucial from growth of international trade of India.

China:
Trade figures with China are given below. The last four year growth rate in total trade are

Values in million USD					
\Year	**2002-2003**	**2003-2004**	**2004-2005**	**2005-2006**	**2006-2007**
EXPORT	1,975.48	2,955.10	5,615.88	6,759.10	8,293.97
%Growth		49.59	90.04	20.36	22.71
%Share	3.75	4.63	6.72	6.56	6.56
IMPORT	2,792.04	4,053.23	7,097.98	10,868.05	17,460.66
%Growth		45.17	75.12	53.11	60.66
%Share	4.55	5.19	6.36	7.29	9.4
TOTAL TRADE	4,767.52	7,008.33	12,713.86	17,627.15	25,754.62
%Growth		47	81.41	38.65	46.11
%Share	4.18	4.94	6.52	6.99	8.25
India's Trade Balance	-8,692.70	-14,306.65	-27,981.49	-46,075.19	-59,387.85

47%, 81%, 39%, and 46%. It shows how fast the two way trade with the china is incresing. The china has emerged from no where to become the second most important trading partner after USA. Indian exports area always lower than import, so we have consistent current account deficit with the china. The trade deficit has to brouth lower by increasing our export to China. the major export items to china are iron ore and steel. We import wide variety of products from china ranging from toys to telecom equipments.

The trend in ex/import with china can be seen in the grapth below. Its shows widining of the trade deficit with China.



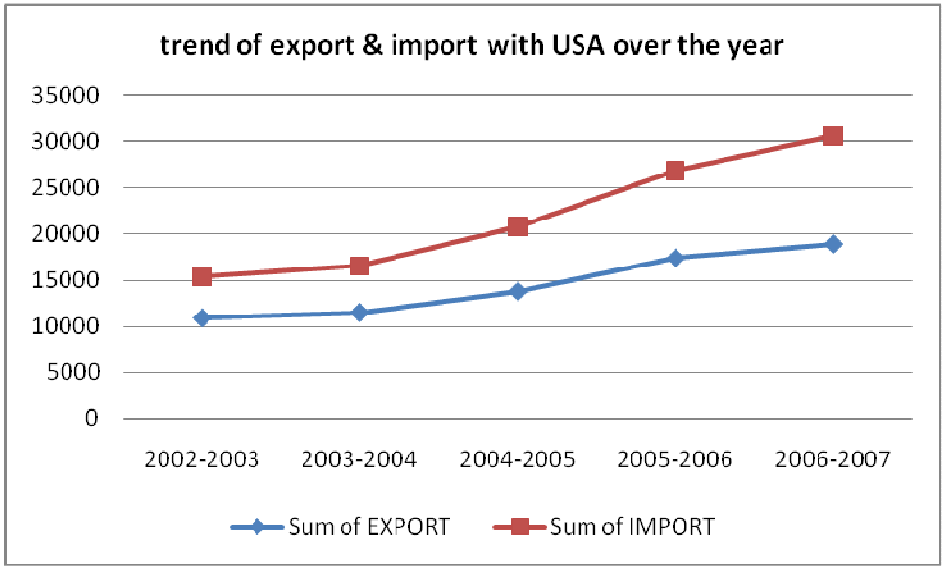
USA

Trade figures with China are given below. The last four year growth rate in total trade are 7.7%, 25%, 29%, 14% which are lower when compared to over all increase in the Indian trade. So USA is slowly lossing the percentage in the Indian trade. Even if the growth rate is less than that of china, but given the size of US economy and size of bilateral trade US will remain one of the main partner in trade.

Dated: 21/10/2007 Values in US$ Million

\Year	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007
EXPORT	10,895.76	11,490.11	13,765.75	17,353.06	18,866.17
%Growth		5.45	19.81	26.06	8.72
%Share	20.67	18	16.48	16.83	14.93
IMPORT	4,443.58	5,034.86	7,001.35	9,454.74	11,736.13
%Growth		13.31	39.06	35.04	24.13
%Share	7.24	6.44	6.28	6.34	6.32
TOTAL TRADE	15,339.34	16,524.97	20,767.10	26,807.81	30,602.30
%Growth		7.73	25.67	29.09	14.15
%Share	13.44	11.64	10.65	10.63	9.8
TRADE BALANCE	6,452.18	6,455.25	6,764.40	7,898.32	7,130.04
India's Trade Balance	-8,692.70	-14,306.65	-27,981.49	-46,075.19	-59,387.85

The exports to USA are greater than import from it, so India has trade surplus with the USA. The graph below shows the trend of the ex/import with USA.



The two interesting areas that one should know are petroleum and arms trade. These two areas were in news during past few months. Thus, a brief description has given below.

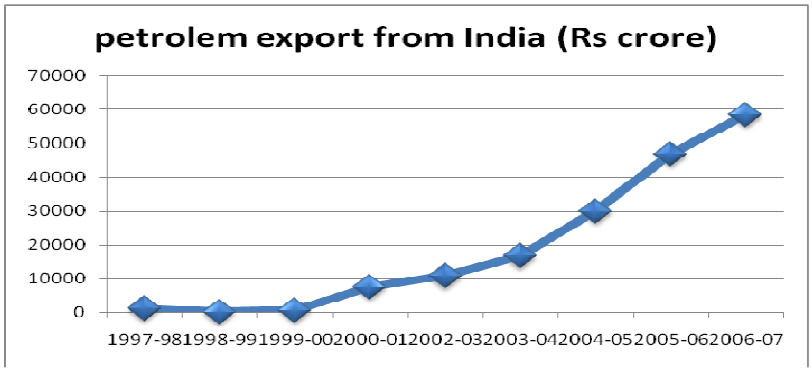
Petroleum export: The fastest growing item in the Indian export basket is refined petroleum products. It is refreshing to see that India a crude oil deficit country has start exporting petroleum products at such a large scale. It is a sign that Indian manufacturing and trade has come out of an age. The refinery margins are higher in India, the cost of refining the crude in lowest. Thus, currently only refineries in India are operating at close to 100% capacity. Indian diesel is exported as far as US and as unlikely market as Pakistan.

The ASSOCHAM Study for the period financial year 1999-2000 to 2006-07 has found that petroleum products exported by India have been growing at a whopping rate of 73 per cent for last three years[15].

India is likely to become a net exporter of petroleum products worth $ 497.01 billion by fiscal 2012-13 in the wake of their exports growing at a much faster pace than imports despite crude prices touching an all time high. The following graph shows the rise of petroleum export from India[16].

[15] http://www2.irna.ir/en/news/view/line-22/0710169852012343.htm (ASSOCHAM study on petroleum trade)

[16] Source: Ministry of Petroleum & Natural Gas, Govt. of India



Arms trade: Without the mention of the arms trade, the discussion of merchandise trade cannot be said to be completed. The arms industry is a massive global industry and business, which manufactures and sells weapons and military technology and equipment. Defense companies produce arms mainly for the armed forces of States. Products include guns, ammunition, missiles, military aircraft, military vehicles, ships, electronic Systems, and more. The arms industry also conducts significant research and development

It is estimated that yearly, over 1 trillion dollars are spent on military expenditures and arms worldwide. In 2004, over $30 billion were spent in the international arms trade (a figure that excludes domestic sales of arms) Many industrialized countries have a domestic arms industry to supply their own military forces. Some countries also have a substantial legal or illegal domestic trade in weapons for use by its citizens. USA is world's largest arms exporter followed by Russia, Germany, France and UK[17]. USA exported close to $ 8 billion in 2006. The arms sell by major countries are given in the table below.

Country	Export (2006) $ billions
USA	8
Russia	6.6
Germany	3.8
France	1.5
UK	1.06

India has consistently figured among top three arms purchaser in the world. China, Saudi Arabia and UAE are other major arms purchasing countries. Data on arms purchase is not available easily. Estimates told that India has purchased $8 billion worth of arms during the period of 1999-2002. The amount is easily be doubled by now. NDA government followed by the UPA government has struck many mega (multi billion) deals in the defense area. Russia, France, Israel and USA are main exporting countries to India.

[17] Stockholm International Peace Research Institute

4.2. Services trade

Trade in Services refers to the voluntary exchange of an intangible, called service, between a producer and consumer. If the trade in services takes place between entities that are based in different countries then it is called International Trade in Services. WTO has defined four modes of international trade in services. The details are mentioned in WTO section.

Time has come when the services will form the main pillar of export. Already the 55%[18] of GDP, services are set to dominate the export arena too. The advent of the digital age, and the large number of young and educated populace fluent in English, is gradually transforming India as an important 'back office' destination for global companies for the outsourcing of their customer services and technical support. India is a major exporter of highly-skilled workers in software and financial services, and software engineering. Other sectors like health services, biotechnology services, telecommunication, aviation and tourism are showing strong potentials with higher growth rates.

According to the estimates made by Federation of Indian Chambers of Commerce and Industry (FICCI), India's export of services is expected to touch $310.9 billion by 2011/12, powered by the booming software, consultancy, engineering and tourism sectors[19]. Services exports could even surpass merchandise exports, which are expected to more than double to $305.5 billion in the next five years.

India exported goods worth $112.4 billion during 2005-06 while export of services was $71.6 billion. Services exports are estimated at $91.5 billion in 06-07, and merchandise exports was $126 billion. Therefore, it can be seen that services export is catching up the merchandise export fast.

[18] To be precise it was 53.8% in year 2005
[19] Reuters, April 05, 2007

	Services	Merchandise
Growth rate for past 5 years	28%	22%
Value (06-07) $ billion	91.5	126
Future value (2011-12) $ billion	311	305.5

During the year 2006/07, a buoyant service exports helped India cut current account deficit of the country. As given in the earlier tables the merchandise trade deficit is large, but current account deficit is small thanks to surpluses earned by the services export.

Why services export is such a big opportunity for India.

- Services are already more than 50% (close to 55%) of GDP
- Unlike merchandise export, Services exports are not bogged down by infrastructural issues.
- The large English speaking population presents huge opportunity
- Low wage, high quality labor availability
- Good Intellectual property Rights (IPR) protection makes it safe
- Its part of WTO, democratic society and accounting and legal standards are close to what followed in west make it easy to operate and served from India.
- The edge in manufacturing can be copied easily, is it equally easy to copy the competitive advantage in services export! Think.

IT and BPO: services export from India is synonymous with IT and BPO industry. Moreover, why it should not be. If china is 800 pound gorilla in the manufacturing, India is 500 pound beast in services.

India accounts for 65 per cent of the global market in offshore IT services and 46 per cent of the global BPO market in 2004-05. With only 10 per cent of the potential market tapped so far by all the countries put together, the potential for further growth is very large. With annual growth of over 25 per cent, these two can generate export revenues of US$60 billion by 2010. Software exports reached US$ 17.2 billion in 2004-05. Employment in the sector grew by 30.1 per cent per year between 1999-00 to 2003-04. Revenue from exports of software, services and business process outsourcing (BPO) will reach about $40 billion for the fiscal year that ends next March 31, 2008[20]. By 2008, the industry is projected to grow from 4.1 per cent of GDP in 2004-05 to 7.0 per cent of GDP and account for 35 percent of total exports.

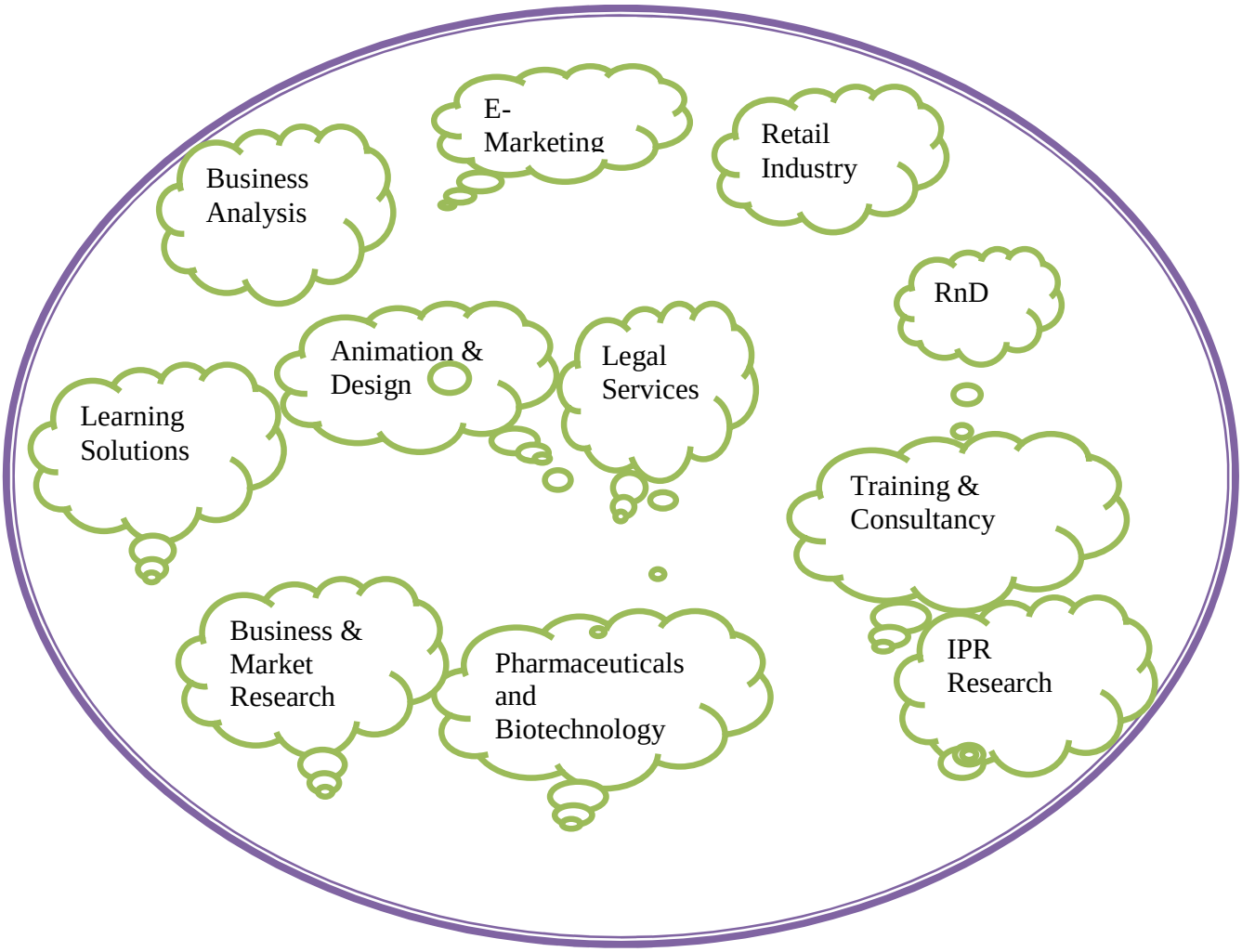
[20] Data released by the National Association of Software and Services Company (NASSCOM)

Year	Export ($ billion) approx. figures
2004-05	17.5
2005-06	22
2006-07	33
2006-07 (estimated)	40
2009-10 (estimated)	60

There are many barriers to be over come to achieve this target. Achieving high growth in software exports will require deep and enduring innovation across multiple dimensions, like business model innovation; focusing on new service lines, like infrastructure off-shoring and knowledge innovation; developing Internet Protocol based solutions, systematic talent enhancement, better technology and research capabilities.

KPO: Knowledge Processing Outsourcing is popularly known as a KPO. Information is Knowledge. Today's economy is Knowledge economy. Knowledge processing is a continuous process of creation and dissemination of information by bringing together the information industry leaders to create knowledge and see meaning in information and its context. This Information driven Knowledge outsourcing in known as Knowledge Processing Outsourcing or KPO.

To sustain the edge and first mover advantage in the business services export, BPO industry should increasingly become a knowledge process outsourcing (KPO) industry. It should leverage on the high quality human capital that exists in the country in a wide range of fields – in engineering, architecture, medicine, law, accountancy, finance, management, and entertainment. Following diagram encompasses the emerging KPO opportunities in different sectors:



Others: Besides software in which India has already made an impact, there is good potential for exports of many other professional services, like super-specialty hospital; satellite mapping; printing and publishing; accounting, auditing and book-keeping services.

A new development in services exports is the explosive growth of business services, including professional services. This is reflected in the growth of miscellaneous services excluding software, which grew by 216 per cent to US$16.3 billion in 2004-05, and 181 per cent in the first half of the current year to reach a level of US$15.4 billion and surpass even the value of software services exports. The enormous opportunities for further

growth of these services make WTO negotiations in services all the more important for India

5. Trade policy

Trade policy is a comprehensive document that guides the administrators to take decisions that helps in achieving the trade target set by the country. It is not just for increasing the country's export.

While increase in exports is of vital importance, trade policy aims to facilitate those imports that are required to stimulate Indian economy. Coherence and consistency among trade and other economic policies is important for maximizing the contribution of such policies to development.

Current trade policy which formulated by the UPA government is for the five year period of 2004 to 2009. It is essentially similar in spirit to earlier policy 2002-2007. The earlier policy, instead to be carried until 2007, was stopped in 2004 and new policy is framed for entire period of UPA governments. The details of the policy are given below.

5.1. EXIM policy 2004-09[21]

Objectives

Trade is not an end in itself, but a means to economic growth and national development. The primary purpose is not the mere earning of foreign exchange, but the stimulation of greater economic activity. The Foreign Trade Policy is rooted in this belief and built around two major objectives. These are:

- To double our percentage share of global merchandise trade within the next five years; and
- To act as an effective instrument of economic growth by giving a thrust to employment generation

Strategy

Trade policies have formed the detailed strategy for achieving above objectives. The brief of the strategies adopted is given below:

- Unshackling of controls and creating an atmosphere of trust and transparency
- Simplifying procedures and bringing down transaction costs.
- Neutralizing incidence of all levies and duties on inputs used in export products, based on the fundamental principle that **duties and levies should not be exported**.
- Facilitating development of India as a global hub for manufacturing, trading and services

[21] EXIM policy document 2004-09

- Identifying and nurturing special focus areas that would generate additional employment opportunities, particularly in semi-urban and rural areas, and developing a series of 'Initiatives' for each of these
- Facilitating technological and infrastructure up gradation of all the sectors of the Indian economy, thereby increasing value addition and productivity, while attaining internationally accepted standards of quality

The **thrust sectors** identified in the policy are:

- Agriculture
- Handlooms
- Handicrafts
- Gems and Jewelry
- Leather and Footwear

Apart from it, the export promotion schemes were planned for achieving the ambitious target set by the policy. Few of the important components of export promotion schemes are

- Target plus scheme to accelerate growth of exports
- Vishesh krishi upaj yojna for agro-exports
- EOUs shall be exempted from Service Tax in proportion to their exported goods and services.
- A scheme to establish Free Trade and Warehousing Zone is introduced

The policy also talked about the SEZ. The details of the

6. World Trade Organization (WTO) related issues

Facts file of WTO. (See Next Page)

World Trade Organization :

Location: Geneva, Switzerland
Established: 1 January 1995
Created by: Uruguay Round negotiations (1986-94)
Membership: 149 countries (on 11 December 2005) (Saudi Arabia is the last member)
Budget: 175 million Swiss francs for 2006
Secretariat staff: 635
Head: Pascal Lamy (Director-General)

Functions:
• Administering WTO trade agreements
• Forum for trade negotiations
• Handling trade disputes
• Monitoring national trade policies
• Technical assistance and training for developing countries
• Cooperation with other international organizations

The details and definitions about the WTO as an institution, its role and responsibilities has discussed in detail in the section on major international financial institutions (section 11). The major issues to be discussed in WTO are agriculture, services and goods. They are

- Negotiations on goods trade (NAMA)
- Agreement on Agriculture (AOA)
- Negotiations on services

These three are explained below.

6.1. NAMA

NAMA stands for **Non-Agriculture Market** Access. In the Doha rounds the negotiations were held for a reduction or elimination in tariff peaks, tariff escalation, high tariffs and non-tariff barriers, particularly on goods that are of export value and therefore of interest to developing countries. Because the tariffs in agriculture are very emotional and complex issue (considering the subsidies involved), Countries decided to go ahead with NAMA. The importance of the NAMA is reflected by the fact that 90% of worlds merchandise trade is covered under the NAMA.

All those products that are not covered by the Agreement on Agriculture or the negotiations on services come under NAMA. In practice, NAMA products include manufacturing products, fuels and mining products, fish and fish products, and forestry products.

6.2. WTO and agriculture

The negotiations for WTO Agriculture Agreement were held in the 1986–94 during Uruguay Round. It was a significant first step towards fairer competition and a less distorted sector. It includes specific commitments by WTO member governments to improve market access and reduce trade-distorting subsidies in agriculture. These commitments were implemented over a six-year period (10 years for developing countries) that began in 1995. Participants have agreed to initiate negotiations for continuing the reform process one year before the end of the implementation period, i.e. by the end of 1999. These talks have now been incorporated into the broader negotiating agenda set at the 2001 Ministerial Conference in Doha, Qatar.

The AoA (Agreement on Agriculture) has three central concepts: domestic support, market access and export subsidies.

Domestic support (subsidies) in USA and EU: In agriculture, related issue the most debated issue is that of domestic support in agriculture. The provision of the WTO agreement on the domestic support measures aims at discipline trade distorting support to farmers. This is to be achieved by the quantification of domestic support. As per agreement, all domestic support should be reduced by 20%. The domestic support measures are characterized into different boxes. The brief descriptions of the boxes are given below.

- Blue box: it includes direct support to producers under the production-limiting program. It means the farmer will get money for not producing on his/her field. It is ironical that in one part of world many dies of hunger and at some other part farmer is paid to not produce.
- Green box: it includes measures that have either no or minimal effects on production. Measures like price support to producers and support involving transfers from consumer kept under this box. R&D, extension services, marketing and promotional services and infrastructure services comes under this box.
- Amber box: it includes the domestic support policies that distort the market price, like minimum support price, direct payments, and non-exempt subsidies.

6.3. WTO and trade in services

One must have heard that the negotiations are on for various modes of trade in services. Here we are deciphering it

- Mode 1: (**Cross border trade**) it involves delivery of a service from the territory of one country into the territory of other country. *Like offshore model of IT industry. TCS office in Bangalore serving American express client in USA.*

- Mode 2: (**Consumption abroad**) it covers supply of a service of one country to the service consumer of any other country. *Like medical and health facilities provided for foreigners coming to India*.
- Mode 3: (**Commercial presence**) *like office of Indian company TCS in USA serving American express*.
- Mode 4: (**movement of persons**) *like Indian IT person travelling to USA to serve American Express.*

India's efforts have been to get binding commitments in cross-border supply of services (Mode 1) and movement of natural persons (Mode 4). In Mode 4, India has been pushing for clear prescription of the duration of stay and removal of the Economic Needs Test.

Indian is trying big time to establish itself as a services hub of the world. The details of the services export are given in the section on services export. WTO negotiations can play a major role in this regard. There is a need to negotiate both multilaterally and bilaterally, issues like the National Health Service Systems in European countries like UK which virtually deny market access; lack of coverage of medical expenditure incurred abroad by US medical insurance companies; need based quantitative limits; need to be natural persons; and accreditation rules. Similarly, in the case of accounting, auditing and bookkeeping services, market access limitations, which are mainly in the form of licensing, accreditation, in-state residency and state level restrictions in countries like US, have to be negotiated.

6.4. Important rounds of WTO negotiations (Singapore & Doha)

Two very important rounds that have lasting impact on liberalization of world trade are Doha and Singapore round of negotiations. Their impact on a developing country like India is still bigger as the items of discussion in these rounds like Agriculture affect the livelihood of 70% of the population.

Singapore round (1996)

At the WTO Ministerial Conference held in Singapore in 1996, the decision was taken to set up three new working groups to consider the following topics: trade and investment, trade and competition policy, and transparency in government procurement.

- Trade and Investment
- Competition
- Labor standards and
- Environment
- Government procurement

Trade and investment issue talks about the intra-company cross border trade. Intra-company cross border trade is estimated to be 1/3rdof total trade trade. It tried to

demystify the relationship between trade and investment. However, many developing countries were opposed to starting negotiations on a multilateral investment agreement, as they feared that an international set of rules would hinder them in implementing national business and development policies.

Competition issue was intended to prevent the price collusion and monopoly power. Some countries opposed it on the ground that such rule will undermine a country's sovereign power to act against multinationals.

Labor standards were proposed to be set in each country to prevent child labor and to give rights to the MNCs operating in the developing nations to hire and fire at will.

Environment cause was set up with the intention to protect the environment. America and EU, which is the biggest polluter on the earth, were talking about the environment. It was an effort to acquire another instrument to protect their markets from the import from developing nations.

The **government procurement** issue proposed the complete impartiality and transparency in the government. Governments are one of the biggest purchasers in developing nations. So through this clause developing nations government will not able to do preferential buying from domestic industries.

To know how India responded to these Singapore round proposals, see the next section on Doha round.

Doha Round (2001)

Doha round comprises of many ministerial meets happened at different places in the subsequent years, starting from year 2001 at Doha. The negotiations are still on and currently world is witnessing a deadlock with developed nation at one side and upcoming developing nation on the other side. Most prominent voices in the developing side are that of India, South Africa and Brazil.

Timeline of Doha round: Doha round has seen following negotiations

- 2001 Doha
- 2003 Cancun
- 2004 Geneva
- 2005 Honk Kong

The Doha round will be remembered for the strong stance taken by the India (by the minister of commerce Murasoli Maran). India walked out of the conference saying that until implementation issues of Uruguay round are addressed India will not discussed the Singapore issues. The India wanted the issue freeing agriculture trade (domestic subsidies given to farmers of rich countries). India wanted developed nations to open up their market for goods from developing nations and non-tariff barrier tools like anti dumping etc should not be used to keep the commodities from developing nations at bay.

The walk out by India posed a threat that India might get isolated at that stage of negotiations. However, the stance taken by India was logical and just and in the benefit of developing nations. Due to it, developing nations came to India's side and developed world has to agree to India's demands. Following the things won by India during 2001 Doha round

- No binding to source life saving drugs only from western MNCs, now India can supply its cheap drugs to aids affected nations in Africa and Caribbean.
- Farm subsidies in western nations came up for discussion, it pave the way to reduce them.
- In the area of services, the restriction on the movement of people was removed. Now India software engineers can go to the places.
- USA agreed to review its anti dumping rules.

The others decisions taken were

- Registration of products like wine and basmati rice knwn by the region
- Progress on NAMA issues

Doha round is still far from completed. India kept is hard stance in the subsequent ministerial meetings. In Cancun 2003, India was represented by Arun Jaitley, and in Geneva 2004 and Honk Kong 2005 by commerce minister Kamal Nath. India has made it clear that WTO is trade negotiation body, not a world government, so better that WTO should not interfere in the sovereign issues like labor and government procurement. In the issues of environment, America was beaten comprehensively when its dual nature came in public by its response to Kyoto protocol.
Cancun was the last effort to revive Singapore issue by the developed nations but they failed to do so, resulted in the failure of Cancun talks. In Geneva, talks again failed but there developed nations formally give up the Singapore issues.

The current impasse is due to both the developed nations and developing nations are not ready to yield ground for the negotiations. Now India has again taken lead when it has shown willingness to yield little provided west reciprocates. Prime Minster and commerce minister indicated it. As per original plan Doha round has to be completed by 2004 but it still not. Doha has become the longest round in the history of WTO. India's stand is that Doha should be treated as '*market ac*cess' round. G20 group of developing nations want it to be a '*development round*'.

6.5. Other WTO related issues (TRIPs, TRIMs, MFA)

Three most discussed issues in relation with the WTO are of TRIPs (trade related intellectual property rights), TRIMs (Trade Related Investment Measures) and MFA (multi fiber arrangement).

- TRIPs

- TRIMs
- MFA

The brief description of these three is given below.

Trade related intellectual property rights (TRIPs)

To understand TRIPS, one must know what the intellectual property means. WTO defines the intellectual property as; *Intellectual property rights are the rights given to persons over the creations of their minds. They usually give the creator an exclusive right over the use of his/her creation for a certain period.*

Therefore, Intellectual Property Rights are the assurance given by the government to protect the innovation. It is through granting monopoly over production and marketing. General Agreement on Tariff and Trade (GATT) state: "*members shall provide for the protection of plant varieties by patents or by an effective sui generics system or by a combination thereof*".

Patent is a concept directly related to the TRIPs. It is an important area under TRIPs agreement. A patent is usually granted for any

- Novel (new) inventions whether products or processes
- Involving an inventive step
- Capable of industrial application

The idea of patent is to grant the inventor a limited monopoly over his intellectual creation for a limited period.

Other issues addressed by TRIPs are

- Copyright and Related Rights
- Trademarks
- Geographical Indications
- Industrial Designs
- Layout-designs (Topographies) of Integrated Circuits
- Protection of Undisclosed Information

The copyright is given wide areas ranging from the area of cinematography to software code and other artistic expressions.

Trademarks are owner's mark that distinguishes its product from others products. To copy it or to produce very similar to it prohibited under TRIPS.

Geographical indicators are interesting one. Only the wine produced in Champagne region of France can be called 'champagne'. Similarly a Scotch whisky and Indian Basmati rice. It prevents any other region to produce a generic product like champagne or basmati rice and market it like original champagne.

Last three also protect the proprietary information in different fields of industrial design, electronics and information processing.

The TRIPS agreement seems to be discriminatory to protect the interest of developed countries or the patent holders. Further, the agreement carries some unfavorable effects to developing nations like India. The major points of concern for developing nations are:

- bio-colonization,
- Monopolies of MNCs, and
- Loss of traditional plant breeds and varieties, bio-piracy and exploitation on India medicinal

There are people who argue on the other side. It will promote innovation, research, and development among Indian companies. After 2005, in the product patent regime pharmaceutical companies are indulge in development of new molecules. Many people feel that India holds a lot of promise in the liberalized trade regime and the agreement would bring the favorable changes to the Indian economy.

India has made much amendment in the previous IP regime and many modifications were made to fit in Indian legal system with the compliance rule of WTO. Below we have listed few of the new legislations passed by the country

- The Trademarks Act, 1999
- The Patent Act, 1970 as Amended by **The Patents (Amendment) Act, 2005**
- The Copyrights Act, 1957
- The Designs Act, 2000
- The Geographical Indication of Goods (Registration and Protection) Act, 1999
- The Protection of Plant Verities and Farmers Rights Act, 2001
- The Semiconductor Integrated Circuits Layout – Design Act, 2000
- The Biological Diversity Act, 2002

Trade related Investment Measures (TRIMs)

In the late 1980s, there was a significant increase in foreign direct investment throughout the world. Developing countries countries receiving foreign investment imposed

restrictions on foreign investment these restrictions were to protect domestic industries and to prevent the outflow of foreign exchange reserves (foreign exchange shock).

Examples of these restrictions are

- local content requirements (which require that locally-produced goods be purchased or used),
- manufacturing requirements (which require certain components be domestically manufactured),
- domestic sales requirements,
- technology transfer requirements,
- export performance requirements (which require that a specified percentage of production volume be exported),
- foreign exchange restrictions, remittance restrictions,
- Employment restrictions

Many of these restrictions are prohibited under the TRIMs agreement, thus limiting the power of national government to act against the foreign investment by the MNCs. The reason given is that many of these measures distort trade and WTO is all about liberalizing the trade.
Uruguay round produced a detailed agreement on TRIMs. Detailed legal framework has been set and Article III and Article XI mentions violations of TRIMs.

Certain exceptions are provided and period was specified for countries to abolish TRIMs. Developed countries had a period of two years in which to abolish such measures; in principle, developing countries were given five years and least-developed countries were given seven years. The period for developing nations like India ended in the 1999. The proposal was that the transition period might be extended for developed and least developed countries. The Agreement also requires a standstill on existing TRIMs and prohibits the adoption of new TRIMS during the transition period.

Multi Fiber Arrangement (MFA)

Be careful its arrangement not agreement. Even Prime Minister Manmohan Sign commit this mistake!
Since 1974, the Multi-fiber Arrangement (MFA) has governed world trade in the textile and apparel industry. The MFA provided the basis on which industrialized countries (US, Europe) restricted imports from developing countries. Quotas have been negotiated each year on a country-by-country basis, assigning the quantities of specified items, which can be exported from developing countries to the developed countries.
This is gross violation of open market philosophy proponed by the developed nations. MFA is the symbol of double standards practiced by these countries. It has only to protect

domestic textile industry in developed nations and few middle-income countries like Mexico.

At the GATT Uruguay Round, it was decided to bring the textile trade under the jurisdiction of the World Trade Organization. The Agreement on Textiles and Clothing provided for the gradual dismantling of the quotas that existed under the MFA. This process was completed on 1 January 2005. However, large tariffs remain in place on many textile products.

So the MFA has expired by January 1, 2005. Life without MFA would be easy. However, initial turmoil would be there. On the one hand, many poor countries that have benefited from quotas will be forced to compete with producers elsewhere. China has gained most from a quota-free world. India has not able to gain it supposed to gain, thanks to rising rupee, less support from government, hindering infrastructure and policies, and tough competition from china.

Domestic industry in USA has damaged a lot and Mexico lost a lot, India shown only some the modest gain.

6.6. Impact on India

Since the establishment of the WTO, India's trade, including the pharmaceutical products, has been growing continuously, both in the merchandise goods category as well as in commercial services. The total merchandise goods exports of India have increased from US$ 26.33 billion in 1994-95 to US$ 102.7 billion in 2005-06 (provisional), whereas total merchandise imports (excluding petroleum products) grew from US$ 22.72 billion to US$ 105.1 billion (provisional) during the same period. The export of pharmaceutical products has increased from over US$ 854.51 million in 1999-2000 to US$ to 2444.06 million in 2005-06. Similarly, India's total commercial services trade increased from US$ 14.06 billion in 1994 to US$ 80.58 billion in 2004.

India also has been pursuing its national interests by forging coalitions of developing countries on various negotiating issues such as G-20 on Agriculture, G-33 on Special Products and Special Safeguard Mechanism under Agriculture negotiations, NAMA-11 in respect of Non-Agricultural Market Access negotiations, 'Friends of Mode 4' in services and 'Friends of Geographical indications' in trade-related intellectual property rights. India has also been playing an active role in strengthening various developing country coalitions by bringing together G-20, G-33 and G-90 groups of countries in a broad alliance to reinforce each other’s positions on issues of mutual interest. On the domestic front, country does monitor the imports of sensitive items. It can intervene in a WTO compatible manner to protect the interests of all domestic stakeholders.

7. Regional trading arrangements

The deadlock in the WTO negotiations has caused a spur in the RTA (regional trade agreements and FTAs (free trade agreements).

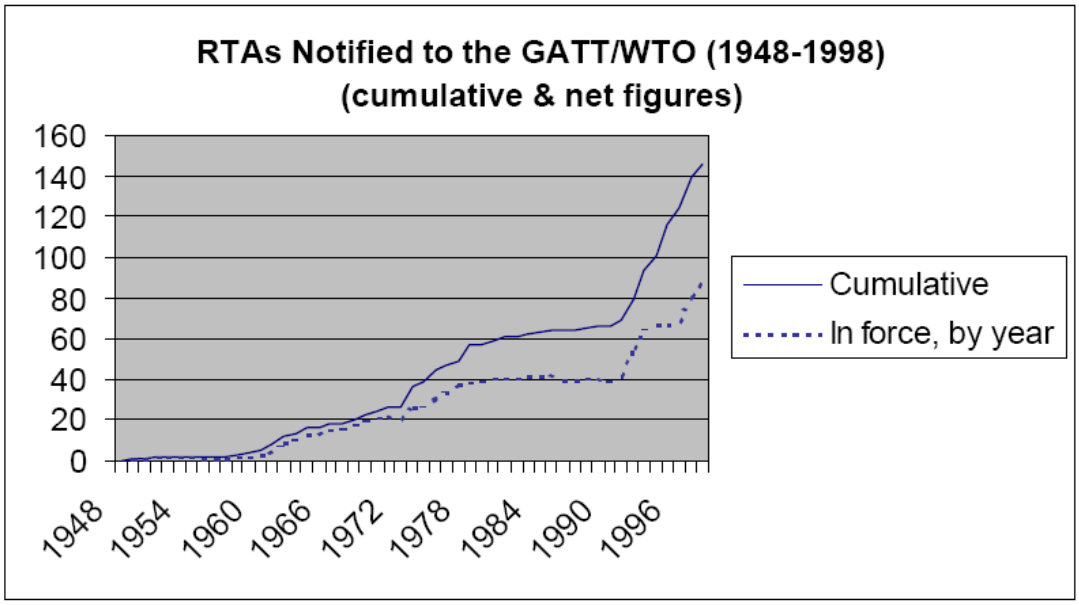
Regional trade agreement is between the more than two countries situated in the same geographical area. Examples are

- NAFTA
- SATFTA
- ASEAN
- EU
- MERCOSUR

Free trade agreement is between two countries or a country with another group of counters. There are various name/classification for FTAs, depending upon the needs of the partners or the level of freeness (openness) in the trade. If one, visit the commerce ministry website he will find different terms like PTA (preferential Trade agreement), Framework agreement, FTA and Comprehensive Economic Cooperation Agreement (CECA).

To remove confusion these all are essentially the trade agreements aims to liberalize the trade between India and its trading partners. With time, the degree of openness and needs of negotiations has caused the emergence of different formats. Now government has decided to make the CECA as the guideline for future free trade negotiations.

It is also noticeable that many of these new agreements are inter-linked. As per estimates, the countries of the European Union and Mexico belong to more than 10 regional agreements. Brazil, Colombia, Venezuela, Chile and some Central American countries belong to between 5 and 10 such agreements. Most other WTO members belong to at least one agreement. The main exceptions to this pattern were Hong Kong, China; Japan; Macau and Mongolia. Now Japan and China are entering into FTAs with ASEAN. The growth in RTAs from 1950 to mid 90s is shown in the graph below. The rise during post 1990 can be seen.



The recent news items were that India is ready to for FTA with EU and India wants to sign FTA with ASEAN before the year-end of 2007. These two news items shows the eagerness on the part of government to go forward with the FTAs.

The brief description of these RTAs and FTAs are given below.

RTA	Year of est.	Member countries
ASEAN	1967	Indonesia, Malaysia, Philippines, Singapore, Thailand, Brunei Darussalam, Vietnam, Lao, Myanmar
NAFTA	1994	USA, Mexico, Canada
SAFTA	1994	India, Pakistan, Nepal, Sri Lanka, Bangladesh, Bhutan, Maldives
MERCOSUR	1991	Brazil, Argentina, Uruguay and Paraguay

7.1. ASEAN

The Association of South East Asian Nations (ASEAN) encompasses 10 South East Asian countries. Its key position in the Asia-Pacific region, its dedication to peace and stability in the region and its important economic weight has made ASEAN an important player in the world arena. It is the European Union of South East Asia.

ASEAN was established on August 8, 1967 in Bangkok, Thailand with the signature of the Bangkok declaration by the five original member nations (Indonesia, Malaysia, Philippines, Singapore, and Thailand). In 1984, Brunei Darussalam was admitted as the sixth member. In 1995, Vietnam also joined ASEAN. Lao People's Democratic Republic and Burma/Myanmar became members in 1997. Cambodia joined in 1999. The Member countries that make up ASEAN have a combined GDP of 656 billion € (2002),
There are large economic disparities between the ASEAN members. With a population of some 503 million people, they make up one of the largest regional markets in the world.

7.2. NAFTA

In January 1994, Canada, the United States and Mexico launched the North American Free Trade Agreement (NAFTA) and formed the world's largest free trade area by economic size. The Agreement has brought economic growth and rising standards of living for people in all three countries. In addition, NAFTA has established a strong foundation for future growth and has set a valuable example of the benefits of trade liberalization.
Under NAFTA, all non-tariff barriers to agricultural trade between the United States and Mexico were eliminated. In addition, many tariffs were eliminated immediately, with others being phased out over 5 to 15 years. All agricultural provisions will be implemented by the year 2008. For import-sensitive industries, long transition periods and special safeguards allowed for an orderly adjustment to free trade with Mexico.

7.3. MERCOSUR

Mercosur is a RTA between Brazil, Argentina, Uruguay and Paraguay, founded in 1991, later updated in 1994. Its purpose is to promote free trade and the fluid movement of goods, peoples, and currency in south and Latin American countries.
Venezuela applied for membership, but its entry hasn't been ratified by Paraguay nor Brazil, although it was ratified by Argentina and Uruguay

7.4. SAFTA

Here is our own RTA. This RTA is for south Asia region. SAFTA stands for South Asian Free Trade Area**.** The Agreement on the **SAFTA** was signed on 6 January 2004.

It is an agreement reached at the 12th South Asian Association for Regional Cooperation (SAARC) summit at Islamabad, Pakistan. It creates a framework for the creation of a free trade zone covering India, Pakistan, Nepal, Sri Lanka, Bangladesh, Bhutan and the Maldives. The framework agreement on SAFTA envisions zero customs duty on the trade of practically all products in the region by end 2012. The SAARC Preferential Trading Arrangement (SAPTA), with concessional duty on sub-continent trade, went into force on 1 January 1996.

7.5. PTA (of India)

PTA stands for Preferential Trade Agreement. It is a bilateral effort between the two countries to liberalize and open up the trade. Below are listed few of the PTAs India has signed with other countries. PTA with Mercosur is with the group of South American nations.

- India-Chile PTA
- India-MERCOSUR PTA
- India-Afghanistan PTA
- India-Sri Lanka FTA

India has trade agreements with china, Maldives, Nepal, Bhutan, Bangladesh, Japan, DPR Korea, Korea, Myanmar and Mongolia etc. frame work agreements with ASEAN, Thailand and Chile are also in place.

7.6. Comprehensive Economic Cooperation Agreement (CECA)

CECA is new frame work on which India is planning to negotiate its future bi-party trade agreements. India has first signed this agreement with Singapore. Its detail study and impact on the Indian economy was accessed in the process, now the agreement can be said to be matured and its impacts on Indian economy are understood to large extent. Government is planning to go ahead and struck this agreement with many countries. The negotiations with Japan and Thailand are on and time frame for the implementation has been decided. With these two countries, by the year 2009 the agreement should have come under effect. Efforts are on with USA and china for the same agreement.

The objectives of this Agreement are

- To strengthen and enhance the economic, trade and investment cooperation between the Parties;
- To liberalize and promote trade in services in accordance, including promotion of mutual recognition of professions;
- To establish a transparent, predictable and facilitative investment regime;
- To improve the efficiency and competitiveness of their manufacturing and services sectors and to expand trade and investment between the Parties, including joint exploitation of commercial and economic opportunities in non-Parties;
- To explore new areas of economic cooperation and develop appropriate measures for closer economic cooperation between the Parties;
- To facilitate and enhance regional economic cooperation and integration, in particular, to form a bridge between India and the Association of Southeast Asian Nations (“ASEAN”) region and serve as a pathfinder for the India-ASEAN free trade agreement; and

8. Foreign investment

Foreign investment is the purchase of Indian asset by a non-Indian. It is classified as FDI and FII depending upon the nature of asset purchased and duration of holding the asset. The details of the two are given below.

8.1. Foreign direct investment (FDI)

Foreign direct investment (FDI) is an investment made by any entity into the economy of some other country where he acquires the lasting interest through the purchase of assets in that foreign economy.

Foreign Direct Investment (FDI) flows are usually preferred over other forms of external finance because they are non-debt creating, non-volatile and their returns depend on the performance of the projects financed by the investors. FDI also facilitates international trade and transfer of knowledge, skills and technology.

India is one of the best places to start a business[22]. Recently in the AT Kearney India has displaced the US to become the second-most favored destination for foreign direct investment after China. India is also named as the top reformer in South Asia as per annual Doing Business Report issued by the International Finance Corporation (IFC).

India is in the reckoning. The figures appear to be improving by the day. While FDI equity flows were US$ 5.5 billion in 2005-06, it increased almost three times to US$ 15.7 billion in 2006-07, representing a growth rate of 184 per cent. With this, the cumulative FDI inflows in to the country since 1991 reached US$ 54.6 billion. Further, the Government seeks to double the FDI inflow to US$ 30 billion this fiscal in order to maintain a growth rate of 9 per cent per annum over the next five years

With the opening of the retail slowly foreign retailers such as Wal-Mart have started to enter the Indian market (*Wal-Mart source $17 billion of material from china every year*). At the same time, a number of United States transnational companies such as General Motors and IBM are rapidly expanding their presence in India, as are several large Japanese TNCs such as Toyota and Nissan

The principal sources of FDI between 1991 and March 2007 have been in the following order

[22] Global services location index by AT Kearney

Rank	Countries
1	Mauritius
2	US
3	UK
4	Netherlands
5	Japan
6	Germany
7	Singapore

The following table shows the highest FDI receiving states in the country during the period from year 2000 to 2003.

State	FDI ($ millions) year 2000-03
Delhi	2982
Maharashtra	2732
Tamil Nadu	747

STATEMENT ON COUNTRY-WISE FOR FDI INFLOWS From APRIL 2000 to SEPTEMBER 2008

Sector	AMONUNT OF FDI INFLOWS	In US $	%age to total FDI inflows
Metallurgical industries	106, 620.23	2552.55	3.34
Fuels (Power & Oil Refinery)	119, 142.27	2,762.05	3.73
Electrical equipment (Incl S/W & Elec)	55,798.07	1,292.50	1.75
Telecommunications	255,009.48	5,795.99	7.99
Chemicals (other than fertilizers)	79,565.28	1,811.36	2.49
Drugs & Pharmaceuticals	61,419.01	1,401.60	1.92
Services Sector	666,249.	15, 633.61	20. 87

[1] Indian finance and investment guide http://finance.indiamart.com/investment_in_india/fdi.html

It can be seen from the above table that the principal sectors attracting FDI during this period have been electrical equipment, services, telecommunications, transportation, fuels, chemicals and construction (in that order).

As of now, the data cannot be shown here, but telecommunication is ahead of other sectors in attracting FDI. Steel sector has shown much promise but the real investment yet to be flowed. The petroleum refinery is one industry that is attracting some big tickets investments from the likes of Mittals.

Foreign Direct Investment (FDI) is permitted through the following forms of investments:

- Financial collaborations
- Joint ventures and technical collaborations

- Capital markets via Euro issues
- Private placements or preferential allotments

In the following industrial sectors, FDI is not permitted[23]:

- Arms and ammunition
- Atomic Energy
- Railway Transport
- Coal and lignite
- Mining of iron, manganese, chrome, gypsum, sulphur, gold, diamonds, copper, zinc.

Finally the factors hindering the FDI in India are

- Infrastructural hassles
- Indian Bureaucracy
- Diverse Market

8.2. Foreign Institutional investment (FII)

Currently the investment in equity is less than 10% so no voting rights are enjoyed by and it is treated as FII. If investment is more than 10%, so foreign party enjoys the voting rights and investment is treated as FDI[24]. The limit of 10% is fixed arbitrary and on the belief that this signifies the distinction between the no role and role in the management f in the company. From the point of view of a country receiving such capital, FDI is more stable than PI (including loans) as the former is harder to reverse than the later.

Only registered foreign institutional investors (FIIs) can invest in Indian securities/stocks. An FII, or a foreign institutional investor, is an entity established to make investments in India. Therefore, these FIIs need to be registered with the Securities and Exchange Board of India (Sebi). A FII can be pension funds; mutual funds; insurance; investment trusts; banks; or a foreign government agency; charitable trusts etc.

There is debate on how good FII investment is when compared to FDI. Are FII going to stay in India for long term or will fly away creating an East Asian type crisis. People like Ankeleswar Aiyar of TOI always insist that FII are not short-term loans and going to stay for long. The reason given behind is that if the FII want to take away money from the equity the sharp fall in the share prices will not allow them to cash on the securities and run away.

[23] Indian finance and investment guide http://finance.indiamart.com/investment_in_india/fdi.html
[24] GS Gupta, 2004, Macroeconomics, TMH publisher

Recently FIIs have injected a whopping $18 billion into India in 2007 until October. The subprime crisis in the west and attractive returns from Indian equities has attracted lot of funds in the recent times. It has caused the share market to redefine its peak.

The following entities proposing to invest on behalf of broad based funds are also eligible to be registered as FIIs:

- Asset Management Companies
- Investment Manager/Advisor
- Institutional Portfolio Managers
- Trustees

8.3. Hedge finds

Hedge funds, which invest through participatory notes, borrow money cheaply from Western markets and invest these funds into stocks in emerging markets. This gives them double benefit: a chance to make a large profit in a stock market where stocks are on the rise; and a chance to make the most of the rising value of the local currency.

For past few years, hedge funds have consistently given higher returns over other avenues of investment. It coupled by the increasing regulatory efforts by the governments of different countries, to keep an eye over investment and flow of money. Because of higher returns and tighter regulatory environment, the popularity of hedge funds has increased tremendously.

It is proved by the fact that the amount of money that is under management of hedge funds has gone up by four times between 1996 and 2004. It is expected to further triple between now and 2010 to over $2.7 trillion. Public funds, endowments, and corporate sponsors have all increased their allocations to hedge funds

Hedge funds charges are different from other brokerages firms. As per a study done by Morgan Stanley's prime brokerage unit, the majority are charging a 1.5 per cent management fee and 20 per cent of profits.

8.4. P notes

The recent noise about the Participatory Notes (P Notes) has made them a high probability question during the interviews of any B school.
It is very simple. Any foreign individual cannot invest in Indian market. Only registered FII can do so. So FII has developed an instrument call P notes a way for non-registered foreign entities to invest in the Indian share market.

We all need to know that P notes are the instruments issued by FIIs to overseas investors, who wish to invest in the Indian stock markets without registering themselves with the market regulator, the Securities and Exchange Board of India.

So P notes can be used by the hedge funds that are not registered with Sebi to invest in Indian securities. Indian based brokerages buy securities / stocks in India and then issue P notes to foreign investors. Any dividends or capital gains collected from the underlying securities go back to the investors.

Finance ministry and Indian regulators (Sebi and RBI) are not happy about P notes because they have no way to know who owns the underlying securities. Hedge funds were largely blamed for triggering the East Asian Crisis. Therefore, regulators fear that hedge funds acting through P notes will cause economic volatility in India's exchanges. Left parties also putting pressure on the government to ban the P notes in Indian Stock market. However, it would not be that easy. Almost more than 30% of FII investment in Indian securities in through P notes only[25].

Hedge funds were largely blamed for the sudden sharp falls in indices. Unlike FIIs, hedge funds are not directly registered with Sebi, but they can operate through sub-accounts with FIIs. These funds are also said to operate through the issuance of participatory notes.

8.5 External commercial borrowings (ECBs)

Similar to borrow from the domestic market companies can borrow from the international market. The lower rate of interest on loans in the international market is increasingly making it more attractive to borrow from outside the country

External Commercial Borrowings (ECB) as defined (by the RBI) to include

- commercial bank loans,
- buyer’s credit,
- supplier’s credit,
- securitized instruments such as floating rate notes, fixed rate bonds etc.,
- credit from official export credit agencies,
- Investment by Foreign Institutional Investors (FIIs) in dedicated debt funds
- Commercial borrowings from the private sector window of multilateral financial institutions such as IFC, ADB, AFIC, CDC etc

[25] Other estimates are that nearly 50% of the foreign investment in equity is through P notes. These different figures show how opaque the P notes investment is.

Companies are free to raise ECB from any internationally recognized source like banks, export credit agencies, suppliers of equipment, foreign collaborations, foreign equity - holders, international capital markets etc.

Government policy seeks to keep an annual cap or ceiling on access to ECB. This means that total sanctioned amount for all applicants within a year cannot exceed that limit.

Year	ECB ($ millions)
01-02	2652
02-03	4234
03-04	8175

The major borrowers for ECB are, power, telecom, petroleum, roads and ports and railways.

8.6 Non-resident deposits

In simple words, to exploit the interest rate differential (Indian banks offer higher interest rate than foreign banks) the non-residents deposit money in India. That is non-resident deposits.

Expatriate deposits, traditionally, have been a key source of stable inflows for the capital account. In the post liberalization years, non-resident deposits remained an important and relatively stable source of capital flows. After reaching a peak of US$3.3 billion in 1996-97, such deposits slackened somewhat during the later years of the decade of 1990s, but recovered to reach a record level of US$3.6 billion in 2003-04. Thereafter, however, for the first time since 1990-91, non-resident (NR) deposits became net outflows in the year 2004-05. Total outstanding amount in the non-residents deposits were at US$35.1 billion at end-March 2006[26].

9. Foreign Exchange

In the discussion of international trade, the foreign exchange must have a mention. Foreign exchange is one of the critical factors deciding the import and export attractiveness of the country. It also affects the balance of payment situation of the country. Two things to be discussed under it are

- Exchange rate
- Foreign exchange reserve

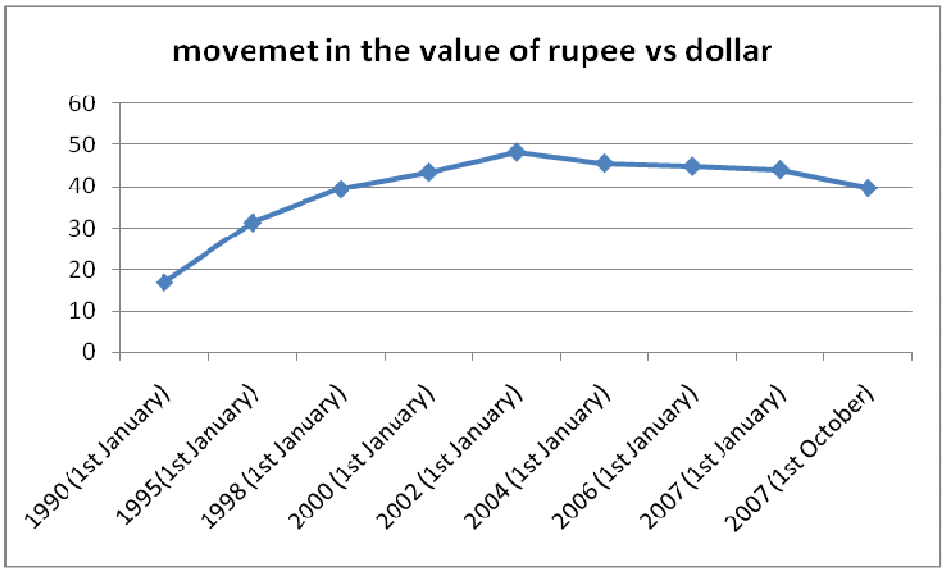
[26] Indian budget 06-07 http://indiabudget.nic.in/es2006-07/chapt2007/chap617.pdf

9.1. Exchange rate developments

Rupee has seen the large fluctuation in its value post 1990. The value of rupee as moved one way, i.e. downwards. However, post 2005 the trend reversed and since then rupee has appreciated by almost 20%.

Year	Value of 1$ in rupee[27]
1990 (1st January)	16.96
1995(1st January)	31.37
1998 (1st January)	39.4
2000 (1st January)	43.55
2002 (1st January)	48.28
2004 (1st January)	45.68
2006 (1st January)	44.95
2007 (1st January)	44.16
2007 (1st October)	39.7

The movement is better captured by the graph below[28]



The impact of exchange rates:

The impact of exchange rate is the changes on the realizations or costs in the economy. As all commodity kind of goods produced and sold in the country - ferrous and non-ferrous metals, basic and petrochemicals, and so on, are priced according to import parity.

[27] Compiled by the author from newspaper archives
[28] Generated by the author from newspaper achieves

The exchange rate affects their prices too the exchange rate can be used as an anti-inflation measure. However, it could have rather unwelcome repercussions on growth, employment and the current account balance.
The undervalued currency (when official exchange rate is lower than market determined rate) makes the export cheap and imports costlier. An overvalued currency (when official exchange rate is higher than market determined rate) makes the import cheap and export costlier. Countries like china consistently keep the currency to boost exports from the country. India has moved to the area where Central Bank (RBI) quasi manages the exchange rate. It allows the movement of the currency in the band defined and intervenes only when there is excessive volatility in the market.

9.2. Foreign exchange reserves

Foreign exchange (Forex) reserves are the foreign currency deposits held by a nation (through its central bank). It includes apart from foreign currency other assets that can be exchanged into foreign currency at ease. So it includes

- foreign currency
- gold
- SDRs
- IMF reserve position as this total figure is more readily available

These are assets of the central banks, which are held in different reserve currencies majorly in dollars followed by euro and in little amount in pound and yen.

The forex reserve serves many purposes like

- Control excessive volatility in currency exchange rate
- Protect the monetary system from shock (like sudden capital flight and depreciation of rupee)
- It allows central bank to purchase the issued currency
- Exchanging its assets (forex) to reduce its liability

As shown in the balance of payment part the change in the forex reserves is reflection of balance of payment situation of the country. If the BOP is positive, the forex reserves will increase.

The large forex reserves are strength on hand but it has its own down side. It is the cost nation has to pay to reduce the risk. The cost is that forex is a low productive or unproductive asset. There is a cost involved in holding bigger reserves.

Now a day countries are finding the innovative ways to increase the returns of their forex reserves. The excessive component of the forex reserves is invested in other assets through some investment arm of the government. UAE's $875 billion Abu Dhabi

Investment Authority, Singapore through Temasek Holdings and GIC are already doing it. India is also planning to create its own investment firm from its forex reserves.

The forex reserves of various countries are given in the table below.

Rank	Country/Monetary Authority	billion USD (end of *month*)	Change in year 2007
1	China	$ 1905 (Sept) [1]	+32.9%
2	Japan	$ 997 (August)	+8.7%
3	Russia	$ 484.7 (November 2008) [2] [1]	+56.8%
-	Eurozone	$ 430 (November)	+16.6%
4	Taiwan	$ 282 (August) [2]	+2.7%
5	India	$ 247 (Nov) [2]	+64.4%
6	Brazil	$ 208 (Dec) [3]	+105.9%
7	South Korea	$ 201 (Nov)	+9.7%
8	Singapore	$ 175 (July)	+19.1%
9	Hong Kong	$ 158 (August)	+14.6%
10	Germany	$ 137 (August)	+20.3%

[1] Forex figures changes every week. Reader should take them as indication of reserve size. All the figures are for the months of September and October and taken from Wikipedia.

10. Contribution of major economists (in area related to foreign trade)

10.1. Adam smith

The major contribution by the Adam Smith was the invisible hand mentioned in his book the wealth of the nations. Moreover, he is generally ignored as a trade theorist in textbooks.

In the area of international trade Adam smith proponent the free trade and oppose the restriction in trade (*policy of mercantilism*).

Adam Smith had pointed to increased trading as being the reason for the flourishing of not just Mediterranean cultures such as Egypt, Greece, and Rome, but also of Bengal (East India) and China.

His theories explain the great prosperity of the Netherlands after throwing off Spanish Imperial rule, and declaring Free Trade and Freedom of thought. It had made the Free Trade/Mercantilist dispute the most important question in economics for centuries.

10.2. Ricardo

The Ricardian model focuses on **comparative advantage** and is perhaps the most important concept in international trade theory. In a Ricardian model, countries specialize in producing what they produce best. Unlike other models, the Ricardian framework predicts that countries will fully specialize instead of producing a broad array of goods. In addition, the Ricardian model does not directly consider factor endowments, such as the relative amounts of labor and capital within a country.

10.3. Milton Freedman

Milton freedman is one economist (rather Monetarist) who least care about the trade deficits and have his own argument in the favor of trade deficits. He believed that deficits would be corrected by free markets as floating currency rates rise or fall with time to encourage or discourage imports in favor of the exports, reversing again in favor of imports as the currency gains strength.

If country America has a trade deficit because of large imports of consumer goods, other countries (gulf countries and China) accumulate cash from country America. That money can be used to purchase existing investment assets and government bonds within country America. As a result, the return from those assets will accrue not to citizens of America but to foreigners. The consumption standard of future generations in America may therefore potentially decline because of the deficit.

10.4. Peter F Drucker

Unlike Milton freedman or Ricardo who addressed the issue of international trade directly, Peter F Drucker addresses it indirectly. Drucker thoughts do say something about the international trade though not directly.

His study of multinational corporations does incorporate the elements of international trade. He criticized the communist and socialist tendency of excessive protectionism. In his books (like The Age of Discontinuity), one can find the praise for free trade and laissez faire. He has introduced the terms like knowledge economy and thus implicitly introduced the trade in knowledge industries. Decades after his mention KPO industries have become a fast growing industry in India.

11. International financial institutions

The major financial institutes that one must have an idea about are WTO, World Bank and International Monetary fund (IMF). The brief description of these institutions is given below.

11.1. WTO

The World Trade Organization (WTO) is the only global international organization dealing with the rules of trade between nations. At its heart are the WTO agreements,

negotiated and signed by the bulk of the world's trading nations and ratified in their parliaments. The goal is to help producers of goods and services, exporters, and importers conduct their business. It formed on Jan. 1, 1995, as successor to the General Agreement on Tariffs and Trade (GATT), which since 1947 had regulated tariffs worldwide.
When established WTO aimed to regulate the following subjects

- Tariffs on trade in manufactured goods and agriculture
- Services
- Intellectual property
- Food
- Government Purchasing

These agendas bought are based on certain principles that form the tenet of the WTO. The WTO philosophy has based on five main principles that this organization strive to achieve in the world trade.

- Nondiscrimination
- Reciprocity
- Binding and enforceable commitments
- Transparency
- Safety valves

The last two points were of major contention and India in the leadership of Murasoli Maran opposed it in the Doha round of trade.
Key principles include ``national treatment," which requires member nations to regulate imported goods in the same way as domestic goods; ``most favored nation," which obligates nations to give equal treatment to all other member nations; and elimination of quotas, such as requiring the United States to end its politically sensitive apparel and sugar quotas by 2005.

Rules force nations to open their banking, insurance and telecommunications industries to foreign competition. U.S. firms have benefited greatly.

Copyrights, trademarks and patents are crucial for the U.S. computer, software, entertainment and biotechnology industries, which lose billions of dollars each year from pirated goods.

The Sanitary and Phytosanitary Standards (SPS) agreement covers food safety issues from pesticide regulations to product labeling and genetically engineered foods. Critics say SPS rulings undermine safety standards -- for example, a ruling this year against the European Union's ban on hormone-treated U.S. beef.

The WTO bans nations and their states or provinces from giving preference to local industries in government purchasing of goods and services.

The above two points were seen as the instrument in the hands of developed nations to bend the rules in their favor. India leads the developing nation and opposes them. We were successful in safeguarding the developing nation's interest in the process.

The politics of the negotiation forms a very interesting reading. One should read more material on negotiations and discuss in-group issues like, the formation of India, SA and Brazil alliance and concept of LDC (least developed nations).

GATT and WTO rounds of negotiations often confuse people. Here is the brief time line of the rounds held. The summary of the topics being discussed also given.

	Place	Time line	Subjects covered
Seven rounds	Geneva to Tokyo	1945 to 1973	Tariffs, non-tariff measures, "framework" agreements, Anti-dumping
Eighth round	Uruguay Round	1982 to 1995	Tariffs, non-tariff measures, rules, services, intellectual property, dispute settlement, textiles, agriculture, creation of WTO, etc
	Doha Round	2001 to now	Tariffs, non-tariff measures, agriculture, labor standards, environment, competition, investment, transparency, patents etc

11.2. Bretton Woods institutions (World Bank and IMF)

The World Bank is a group of international organizations responsible for providing finance to countries for purpose of development of the nations post WWII (World Bank), and to alleviate the balance of payments problems (IMF). They famously called the Bretton Woods Twins. Both institutions have their head quarter on the same street.

Fifty years ago in 1944, the World Bank[29] conceived at Bretton Woods in America. Two years later, in 1946, it was born. With its brother institution, the International Monetary Fund (IMF), it now affects virtually every country in the world. Those in richer countries contribute through taxes and more than half the countries in the world borrow, many extensively.

Presently the World Bank has four main sections. The governments of 176 countries currently own the IBRD, the largest, including all 15 of the republics, which formed the Eastern European block. This is a four-fold increase of membership over the 44 countries, which conceived of the institution in 1944. The IBRD makes loans only to creditworthy borrowers and has suffered no losses on the loans it has made. Throughout that whole time, it has made a profit. A substantial part of that income goes to strengthen its reserves, and to fund the International Development Association (IDA), the Agency set up within the Bank in the 1960s to lend to developing countries4. In addition, some of the funds are loaned in the world market.

The World Bank sections are (four main and two additional):

- International Bank for Reconstruction and Development (IBRD) commonly called **World Bank**.
- International Monetary Fund (IMF),
- International Centre for the Settlement of Investment Disputes (ICSID), responsible for settling disputes between governments and foreign investors
- International Development Association (IDA), responsible for providing long-term interest-free loans to the poorest of developing countries
- International Finance Corporation (IFC), responsible for providing finance to support private ventures in developing countries
- Multilateral Investment Guarantee Agency (MIGA), responsible for providing political risk insurance to promote foreign direct investment into emerging economies

On the web site of IMF, it said about itself that, "an organization of 185 countries (Montenegro being the 185th, as of January 18, 2007), working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty".
Its current president is Rodrigo Ratto from Spain.

[29] More correctly the International Bank for Reconstruction and Development (IBRD),

Its job is to oversee the global financial system by observing exchange rates and balance of payments, as well as offering financial and technical assistance. Its headquarters are located in Washington, D.C., USA, next to World Bank.
IMF has faced lot of criticism. For eastern Asian crisis in 1997, IMF had to bear a lot of criticism. It had thrown all the praises on the economies of Thailand, Indonesia and South Korea before these nations fell into the crisis. IMF did not provide them timely assistance and did not warn them before hand. The details of East Asian crisis are in the last section.

There is a unwritten understanding between EU and USA. The World Bank chief is form USA and IMF chief is from EU (Spain)

12. SEZs

India was one of the first in Asia to recognize the effectiveness of the Export Processing Zone (EPZ) model in promoting exports, with Asia's first EPZ set up in Kandla in 1965. With a view to overcome the shortcomings experienced on account of the multiplicity of controls and clearances; absence of world-class infrastructure, and an unstable fiscal regime and with a view to attract larger foreign investments in India, the Special Economic Zones (SEZs) Policy was announced in April 2000.

The SEZ Act, 2005, supported by SEZ Rules, came into effect on 10th February, 2006, providing for drastic simplification of procedures and for single window clearance on matters relating to central as well as state governments. The main objectives of the SEZ Act are:

- generation of additional economic activity
- promotion of exports of goods and services
- promotion of investment from domestic and foreign sources
- creation of employment opportunities
- development of infrastructure facilities

The SEZ Rules provide for different minimum land requirement for different class of SEZs. Every SEZ is divided into a processing area where alone the SEZ units would come up and the non-processing area where the supporting infrastructure is to be created.

SEZ rules ensure simplified procedures for development, operation, and maintenance of the Special Economic Zones and for setting up units and conducting business in SEZs. Single window clearance for setting up of an SEZ is the target, but practically file need to take approval from many sitting behind the window.

The major incentives and facilities available to **SEZ developers** include-

- Exemption from customs/excise duties for development of SEZs for authorized operations approved by the BOA.
- Income Tax exemption on export income for a block of 10 years in 15 years under Section 80-IAB of the Income Tax Act
- Exemption from minimum alternate tax under Section 115 JB of the Income Tax Act
- Exemption from dividend distribution tax under Section 115O of the Income Tax Act
- Exemption from Central Sales Tax (CST)
- Exemption from Service Tax (Section 7, 26 and Second Schedule of the SEZ Act)

Land allocation in SEZ: According to section 5(2) of the SEZ rules, while at least 50 percent of the land area needs to be earmarked for developing processing area for sector specific SEZs, the minimum processing area requirement for multi-product SEZs is only 25 percent. It is noteworthy that while the minimum land area requirement for sector specific SEZs is 100 hectares, and for multi-product SEZs, it is 1,000 hectares. Therefore, while a developer of a sector specific SEZ of 1,000 hectares is required to develop at least 500 hectares of processing area, the developer of a 1,000- hectare multi-product SEZ is required to build only 250 hectares of processing area. This is a clear anomaly.

The processing area of SEZs should not be less than 50 percent. Further, 25 percent of the non-processing area should be dedicated for infrastructure development. Building of residential and commercial complexes should be permitted over 25 percent of the total land area. The SEZ rules should be suitably amended in this regard. After the amendment in 2006, the limit has been increased from 25% to 35% of total area. The present rules after the amendment are shown below[30]

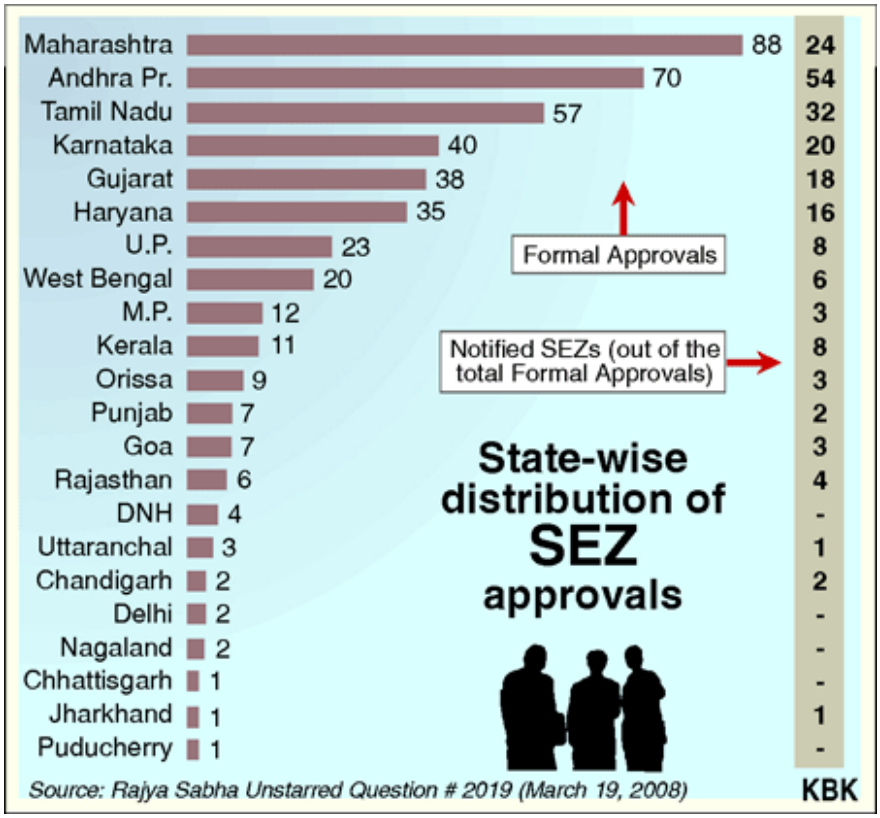
Category	*Minimum Processing area Requirement*
Multi – product SEZ	Increased from 25 percent to 35 percent. The Central Government may on a recommendation from the Board of Approval relax the requirement to 25 percent for reasons to be recorded in writing
Sector Specific SEZ	At least 50
A standalone Free Trade and Warehousing Zone	At least 50

Few states like Maharashtra, Gujarat, Tamil Nadu, AP and Karnataka are actively pursuing the SEZ policy. It will enhance the regional imbalance that already exists between the east and southern India in particular. For instance, Bihar has yet to approve

[30] Commerce ministry website

a single SEZ. West Bengal and Orissa are facing stiff resistance from local farmers. *Nandigram*, *Singur* and POSCO are example of how tough to get land for industrial purpose in these states. The states wise SEZ approved and notified are shown in the table below. The regional disparity is visible in the statistics shown below.

State-wise distribution of SEZ approvals AS on April 2008



STATES	FORMAL APPROVAL GRANTED (2005)	SEZ NOTIFIED UNDER SEZ ACT (2005)	FORMAL APPROVAL GRANTED (2008)	SEZ NOTIFIED UNDER SEZ ACT (2008)
Andhra Pradesh	**44**	**26**	**70**	**54**
Gujarat	**19**	**7**	**38**	**18**
Harayana	**19**	**7**	**35**	**16**
Karnataka	**27**	**14**	**40**	**20**
Kerala	**10**	**6**	**11**	**8**
Maharashtra	**47**	**13**	**88**	**24**
Orissa	**5**	**-**	**9**	**3**
Tamil Nadu	**25**	**16**	**57**	**32**
West Bengal	**7**	**1**	**20**	**6**

The current performance and near future predictions are very optimistic. After the last year growth of more than 50%, this year government expecting a two folds increase in the export from the SEZs. It means that SEZ engine is just start gathering pace now.

The impact of the government policies can be seen from the data given below. It shows the export earnings from few major SEZs.

No.	Name of the SEZ	Exports 2005-06	Exports (2006-07)
1	Kandla Special Economic Zone	1101.18	1482.66
2	SEEPZ Special Economic Zone	9192.22	11897
3	Noida Special Economic Zone	5670.76	6893
4	MEPZ Special Economic Zone	1858.85	2462.4
5	Cochin Special Economic Zone	696	1037.52
6	Falta Special Economic Zone	524.95	998
7	Visakhapatnam SEZ	612.71	715
8	Surat Special Economic Zone	2337.67	5198.94
9	Manikanchan Special Economic Zone	510	1018

10	Nokia Special Economic Zone	--	1649.661
11	Flextronics SEZ	--	161.54

Exports from the functioning SEZs during the last three years are as under-

Year	Value (Rs. Crore)	Growth Rate (over previous year)
2003-2004	13,854	39%
2004-2005	18,314	32%
2005-2006	22 840	25%
2006-20007	34,615	52%
2007-2008	66,638	92%

Projection of Exports from Central Government SEZs for the period 2007-08

Name of the SEZ	Projection of Exports for 2007-2008 (Rs. Crore)
Kandla Special Economic Zone	1500
SEEPZ Special Economic Zone	11000
Noida Special Economic Zone	7000
MEPZ Special Economic Zone Cochin Special Economic Zone	2500 1250
Falta Special Economic Zone	1500
Visakhapatnam Special Economic Zone	800
Surat Special Economic Zone	5500 (Rs. Crore+C25)
Manikanchan Special Economic Zone	1200
Nokia Special Economic Zone	9046.26

The predictions made by the commerce ministry are very rosy. There estimates say that the current investment of Rs. 43123 crores already happened and it has generated the employment for 35053 persons. Ministry further estimates that by December 2009 SEZs would attract the investment of Rs. 2,59,159 crores and would generate the employment of 17,43,530 additional jobs.

If all the 341 that got the formal approvals becomes operational, the expected investment and employment would be of Rs. 3,00,000 crores and 4 million additional jobs respectively. The summary is given in the table below[31]

[31] Commerce ministry website

SUMMARY
Current investment and Employment
Expected investment and Employment

Employment and Investment in Special Economic Zones

(As of 30th November 2007)

(a) Current Employment in the SEZs:
i) In the 7 Central Government SEZs 1, 81,494persons

New generation SEZs:

ii) SEZs notified under the SEZ Act 2005 **59356 persons**

iii) 12 private/State Government new generation SEZs set up/notified prior to SEZ Act 2005 35477 **persons (most of**

the employment

Generated after 2004-05)

Sub-total of (ii & iii) **94833 persons**
Total employment (i, ii & iii): **2,76, 307 persons**

(b) Current Investment (Private):

i) In the 7 Central Govt. SEZs (private investment only) Rs. 4638.98 crore

New generation SEZs:

ii) 12 private/State Government new generation SEZs set up/notified prior to SEZ Act 2005 Rs. 2638 crore

iii) SEZs notified under the SEZ Act 2005 Rs. 52,354 crore

Sub-total of (ii & iii) Rs. **54831** crore

Total Private Investment (i, ii & iii): Rs. 59631.2 cr.

(c) Expected Investment and Employment:

Expected employment **in new generation** Special Economic Zones:
• By March, 2008: 100,000 direct jobs
• By December, 2009: 22, 30,277 additional jobs

Expected investment **in new generation** Special Economic Zones:

• By March, 2008: Rs.100, 000 cr. including FDI of US $ 5 – 6 billion
• By December, 2009: Rs. 2, 85,279 crore

Source: Commerce ministry website

The future hot SEZ are Navi Mumbai SEZ developed by Mukesh Ambani and his close associate Anand Jain. A huge SEZ planned by the reliance group in Haryana, somewhere in Delhi Jaipur highway.

SEZ related important data

13. Other topics of interest

An MBA aspirant must be versed with the subprime crisis of 2007 and East Asian crisis of 1997. The Crisis and depressions are the time when new opportunities emerge and necessary corrections happen in economy. However, these are never without costs. Many businesses are failed and many companies go bankrupt in these crisis. A brief about the East Asian crisis and subprime crisis is given below. Enthusiastic readers should also read about great depression on 1930s.

13.1. East Asian Crisis (1997)

The East Asian economic crisis is the most important economic event in the region of the past few decades.
The crisis started in Thailand with the financial collapse of the Thai baht caused by the decision of the Thai government to float the baht. At the time, Thailand had acquired a burden of foreign debt that made the country effectively bankrupt even before the collapse of its currency. The drastically reduced import earnings that resulted from the forced devaluation then made a quick or even medium-term recovery impossible without strenuous international intervention. As the crisis spread, most of Southeast Asia and

Japan saw slumping currencies, devalued stock markets and asset prices, and a precipitous rise in private debt.

Indonesia, South Korea and Thailand were the countries most affected by the crisis. Hong Kong, Malaysia, Laos and the Philippines were also fairly hurt by the slump. Mainland China, India, Taiwan, Singapore and Vietnam were relatively unaffected. Japan was not much affected by the crisis but was going through its own long-term economic difficulties. However, all of these Asian countries saw their currencies fall significantly relative to the United States dollar, though the harder hit nations saw extended currency losses.

Though there has been general agreement on the existence of a crisis and its consequences, what is less clear were the causes of the crisis, its scope and resolution. There is no unanimity about its root causes or about the solutions. The differences of views are being debated in academic and policy circles.

In the first phase of the crisis, as it spread from Thailand to Malaysia, Indonesia, the Philippines, then to South Korea, the international establishment (represented by the IMF) and the G7 countries placed the blame squarely on domestic ills in the East Asian countries.
Another view and more accepted is the developments of the global financial system, with the combination of the following features has caused the financial crisis in South-East and East Asia:

- Financial deregulation and liberalization across the world (as the legal basis);
- The increasing interconnection of markets and speed of transactions through computer technology (as the technological basis); and
- The development of large institutional financial players (such as the speculative hedge funds, the investment banks, and the huge mutual and pension funds)
- Currency depreciation and debt crisis

13.2. Sub Prime Crisis (2007)

Sub Prime is any loan that does not meet *Prime* guidelines. In USA and other western economies the loan given and the credit charged is depending upon the credit worthyness of the borrower[32]. Sub-prime loans posed bigger risks and thus the interest rates charged on it are higher than the conventional rates. Some people take sub-prime loans with

[32] If an entity mid fico score is below 620 and you have any mortgage defaults within 12 months or recent then the entity is considered *"sub prime"* from lending pupopose

higher rates (even if they have better credit scores) for reduced documentation requirements, not having to pay off collection accounts etc.

Subprime lending encompasses a variety of credit instruments, including subprime mortgages, subprime car loans, and subprime credit cards, among others. The term subprime refers to the credit status of the borrower (being less than ideal), not the interest rate on the loan itself.

This is part of the "crisis". The underwriting standards got so poor they were giving everyone with a pulse a loan.
Other point of view on crisis is that there really is not a *subprime crisis*. Right now, there is *liquidity crisis* on Wall Street. Because so many subprime loans are in default, Wall Street investors are no longer supplying money to market, which lenders use to lend out repeatedly. It resulted in subprime crisis.

Whatever be the reason, it has resulted in biggest treat of recession after dotcom bubble of year 2000. All major banks have suffered huge losses in it and the house market in USA suffered a meltdown.