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"Impact ofForeign trade on Economic Development"

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Abstract

International trade, as a major factor of openness, has made an increasingly significant contribution to economic growth. International trade has experienced rapid growth together with its dramatic economic growth which has made India to target the world as its market. This research discusses the role of international trade in India's economic growth. It starts with a review of conceptions as well as the evolution of India's international trade regime and the policy that India has taken in favor of trade sectors. In addition, India's international trade performance is analyzed extensively. This research has evaluated the progressive effects of international trade on India's economic growth through examining improvement in productivity.

The purpose of the paper is to study and evaluate the Impact of Foreign Trade on the development of Indian Economy and to provide a thoughtful investigation.

For the purpose of the study, secondary data information is used and the paper is divided in three parts. Firstly itdeals with the Impact of foreign trade pre and post liberalization. Secondly it discussesGDP in boosting economic development of our country. Thirdly it consists of concluding section; it discusses what was actually anticipated from foreign trade and how it manifested in the present economic scenario.

Key words: GDP, International Trade, Economic Development

INTRODUCTION

India’s international trade has experienced rapid expansion together with its dramaticeconomic growth which has made the country target the world as its market. The stablepolitical system, vast natural resources and abundant skilled labor in India have madeit a modern global factory. Discussions of the role that international trade plays inpromoting economic growth and productivity in particular, have been ongoing sinceseveral decades ago. A core finding from the comprehensive literature shows thatinternationally active countries tend to be more productive than countries which onlyproduce for the domestic market. Due to liberalization and globalization, a country'seconomy has become much more closely associated with external factors such asopenness. Thus, conducting a study on the effects of international trade on economicgrowth is of great significance in this globalized era. It helps policymakers map outappropriate policies by determining the source of productivity growth with respect tointernational trade.

Since the initiation of economic reforms and the adoption of the open door policy,international trade and India’s economy have experienced dramatic growth. India’sintegration into the global economy has largely contributed to its sustained economicgrowth. Some of the industries with comparative advantages began to acquire a highlevel of specialization, and India has achieved a high growth rate of GDP, as well as anenormous inflow of hard currency and increase in employment. Additionally, India’sparticipation in international trade has also contributed to improvement in productivityof domestic industries and advancement of technology. On one hand, large imports ofmachinery goods in the early 1990s had an immediate impact on productivity throughthe application of technology embodied in them. On the other hand, the level of scienceand technology in India increased dramatically due to the effect of “learning bydoing.”

REVIEW OF LITERATURE

Ferrantino et al (1997) discussed the relationship between trade liberalization and economic growth. At theoretical level trade liberalization positively affected the economic growth but there are controversies among theorist about the time lag that require for complete affect of TL. While on other hand empirical literature investigated that there is a strong positive linkage between trade liberalization and economic growth especially in the rapidly growing countries.

The impact of service sector liberalization on output growth is examined by **Mattoo, et. al. (2001).** The study used per capita GNP growth, vectors for controlled growth and trade in services as main variables. The model is based upon cross country growth regression. Results finally demonstrate that services sector liberalization also has positive impact on GDP growth.

The advancement of trade liberalization process in China and its impact on growth is estimated by **Lardy (2003).** The basic focus of this paper is to investigate the impact of trade liberalization on manufacturing sector. This paper analyzes that basic evolution towards liberalized economy started in 1970s and there exist strong positive correlation between trade openness and economic growth in China.

The impact of liberalization on the growth of Bangladesh is estimated by **Khan. (2007).** The empirical findings of this paper explain that physical capital and real interest rate have significant impact on long run economic growth while financial liberalization negatively affected the growth.

Yasmeen (2009). Mincerian earning function is used for data analyses. The finding of study shows that gender gap and educational qualification are most important determinants of wage. Trade liberalization does not cause any danger to the wage market and does not increased labor productivity in the case of Pakistan. The association between trade openness and inflation is explained by Hsin-Yi Lin (2010). Panel data of 106 countries from 1970-2007 is used and findings illustrate a negative consequence between trade openness and inflation at higher inflation rate.

The causality between trade liberalization, human capital and economic growth in Pakistan is analyzed by **Chuhdhary et al (2010).**Granger causality is used for estimation. Results of this study revealed that in long run relationship between economic growth human capital and trade liberalization is significant and positive while in short run labor force also significantly contribute in growth.

Causal relation between Foreign Direct Investment, export and economic growth in Pakistan is analyzed by **Iqbal et.el. (2010).** Export, import, FDI and GDP growth are important variables of study. VAR and modern cointegration tolls are used for estimation. Results indicate that in long run positive relationship exist between the variables of study. Both trade and FDI play important role in growth of economy.

The link between trade liberalization economic growth and inflation is investigated by **Jin (2003)**. The studied analyzed the data before economic crisis of 1997/98 in Korea. Findings of the paper show negative impact of trade liberalization on growth due to crowding out of domestic investment. Inflation also negatively associated with increased openness.

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OBJECTIVE

1. To Study the importance of foreign trade in the world of Indian market.
2. To examine the relationship between Indian foreign trade and economic development of India.
3. To study the impact of foreign trade on Indian economy.

RESEARCH METHODOLOGY

Research methodology employed is descriptive to some extent, exploratory to a certain degree and partially causal. Secondary sources of data are used. The data and all relevant information for this study has been collected with the valuable assistance of various Books, Magazines, Research Articles, Newspapers, Research Journals and online resources etc. Data published by various institutions such as Government of India, World Bank, CGAP, Reserve Bank of India, NABARD, State Level Bankers Committee (SLBC), etc are used for the objective of the present paper.

INDIAN FOREIGN TRADE OVERVIEW

Foreign trade in India began in the period of the latter half of the 19th century. The period 1900-1914 saw development in India's foreign trade. The augment in the production of crops as oilseeds, cotton, jute and tea was mainly due to a thriving export trade. In the First World War, India's foreign trade decelerated. After post-war period, India's exports increased because demand for raw materials was increased in all over world and there were elimination of war time restrictions. The imports also increased to satisfy the restricted demand. Records indicated that India's foreign trade was rigorously affected by the great depression of 1930s because of decrement in commodity prices, decline in consumer's purchasing power and unfair trade policies adopted by the colonial government. During the Second World War, India accomplished huge export surplus and accumulated substantial amount of real balances. There was a huge pressure of restricted demand in India during the Second World War. The import requirements were outsized and export surpluses were lesser at the end of the war. Before independence, India's foreign trade was associated with a colonial and agricultural economy. Exports consisted primarily of raw materials and plantation crops, while imports composed of light consumer merchandise and other manufactures. The structure of India's foreign trade reflected the organized utilization of the country by the foreign leaders. The raw materials were exported from India and finished products imported from the U.K. The production of final products was discouraged. For instance, cotton textiles, which were India's exports, accounted for the largest share of its imports during the British period. This resulted in the decline of Indian industries. Since last six decades, India's foreign trade has changed in terms of composition of commodities. The exports included array of conventional and nontraditional products while imports mostly consist of capital goods, petroleum products, raw materials, intermediates and chemicals to meet the ever increasing industrial demands. The export trade during 1950-1960 was noticeable by two main trends. First, among commodities which were directly based on agricultural production such as tea, cotton textiles, jute manufactures, hides and skins, spices and tobacco exports did not increase on the whole, and secondly, there was a significant boost in the exports of raw manufactures such as iron ore. In the period of 1950 to 1951, main products dominated the Indian export sector. These included cashew kernels, black pepper, tea, coal, mica, manganese ore, raw and tanned hides and skins, vegetable oils, raw cotton, and raw wool. These products comprised of 34 per cent of the total exports. In the period of 1950s there were balance of payments crunch. The export proceeds were not enough to fulfill the emerging import demand. The turn down in agriculture production and growing pace of development activity added pressure. The external factors such as the closure of Suez Canal created tension on the domestic financial system. The critical problem at that moment was that of foreign exchange scarcity. One of the most important phenomena in post war economic history has been the enormous expansion of world trade. India trade grew poorly from 1950 to 1980 as compared with world. Trade. India entered into planned development era in 1950‘s and at that time Import Substitutionwas a major element of India‘s trade and industrial policy. In 1950 India‘s share in the total world trade was1.78%whichreducedto 0.6% in 1995. In 1993, India rank 33rd in top exporting countries and 32nd in top importing countries. NaturalResources of the country are not evenly divided amongst public and private sector business enterprises. During 2003-04India's share in the global trade was 0.8%, in 2005 it was 1.0%. The PC Alexander Committee (1978) was the firstcommittee to review and recommend on Import –Export Policies and Procedures. This committee recommended thesimplification of the Import Licensing procedure and provided a framework involving a shift in the emphasis from―control to development‖. In 1980 Tandon Committee gave recommendations on export strategies in eighties .In theExport Import policy of 1978-79, for the first time in India's History decentralization of some licensing functions tookplace and the powers of regional licensing authorities was enhanced. Export Oriented Units were set up under the EOUscheme introduced in early 1981. The export and Import Bank of India (website) was set up in 1982 to take over theoperations of international finance wing of the IDBI. Other major objectives were to provide financial assistance toexporters and importers. In the Trade Policy of 1985-88 some measures were taken based upon the recommendation ofAbid Husain Committee 1984. This committee envisaged ―Growth Led Exports, rather than Export Led Growth. Therecommendation of this committee stressed upon the need for harmonizing the foreign trade policies with other domesticpolicies. This committee recommended announcement of foreign trade policies for longer terms. The export import passbook scheme was introduced in 1985 as per recommendation of Abid Hussain Committee. In 1985 Visvanathan pratapSingh Government developed a 3 year Exim policy. Tax Reform Committee chaired by Raja J Chelliah suggestedminimizing the role of quantitative restrictions and reducing the tariff rates substantially. Export Processing Zones wereset up to push up export In order to liberalize imports and boost exports, the Government of India for the first timeintroduced the Indian EXIM Policy on AprilI, 1992. In the light of the reform policy objectives successive governmentshave been taking various trade reforms. Successive annual Union Budgets have also extended a number of tax benefitsand exemptions to the exporters. These include reduction in the peak rate of customs duty to 15 per cent; significantreduction in duty rates for critical inputs for the Information Technology sector, which is an important export sector; grantof concessions for building infrastructure by way of 10-years tax holiday to the developers of SEZs; Facilities and taxbenefits to exporters of goods and merchandise; reduction in the customs duty on specified equipment for ports andairports to 10 per cent to encourage the development of world class infrastructure facilities, etc. A number of tax benefitshave also been announced for the three integral parts of the _convergence revolution'the Information Technology sector,the Telecommunication sector, and the Entertainment industry. In order to bring stability and continuity, the ExportImport Policy was made for the duration of 5 years. However, the Central government reserves the right in public interestto make any amendments to the trade Policy in exercise of the powers conferred by Section-5 of the Act. Suchamendment shall be made by means of a Notification published in the Gazette of India. Prior to 2004, the Foreign TradePolicy was called EXIM Policy. The Foreign Trade Policy, 2008-2009 (_FTP‘) was finally announced by the Hon‘bleMinister of Commerce and Industry, Smt. Nirmala Sitharaman on April 1, 2008. The FTP has been announced in thebackdrop of several measures initiated by the Government of India such as _Make in India‘, _Digital India‘and _SkillsIndia‘, among others. The FTP, introduced with a view to double India‘s share in world trade by the year 2020, rationalizes the general provisions regarding imports and exports and promotional measures offered by the Commerce Ministry and also offer mechanism for resolving quality complaints and trade disputes.

The principle objectives of the EXIM POLICY 2008-2009 policy are:

1. To facilitate sustained growth in exports of the country so as to achieve larger percentage shares in the global merchandise trade.
2. To provide domestic consumers with good quality goods and services at internationally competitive prices as well as creating a level playing field for the domestic producers.
3. To stimulate sustained economic growth by providing access to essential raw materials, intermediates, components, consumables and capital goods required for augmenting production and providing services.
4. To enhance the technological strength and efficiency of Indian agriculture, industry and services, thereby improving their competitiveness to meet the requirements of the global markets.
5. To generate new employment opportunities and to encourage the attainment of internationally accepted standards of quality.

INDIAN FOREIGN TRADE NEW ERA

IMF in its World Economic Outlook (WEO) released in April 2008 has projected economic growth rate for 2008 and 2009 to be at 3.5%and 3.8% respectively. The new Foreign Trade Policy will focus on ways to boost India‘s exports and reduce dependence on imports, a government official said on Monday. ―India — being part of WTO — cannot only think in terms its export promotion without equally supporting import substitution. ―Therefore, the focus of the new policy would be to vigorously promote both exports and imports with significantly substantial focus on exports, industry body PHDCCI said, quoting Additional Director General of Foreign Trade (DGFT) Sumeet Jerath. Mr. Jerath said the policy (FTP 2008—09), to be announced by the new government post general elections. India‘s overall exports fell short of the $325 billion target in 2008—09. They touched $312.3 billion.

Mr. Jerath said: ―It would be the attempt of the policy makers to take India‘s share in global trade to over 5 per cent from current level of 2 per cent in the next five year period. ―He also informed the industry chamber‘s members that the DGFT‘s second committee report on reducing transaction cost is ready. He said, .(it) suggests a way forward as to how the new government should tackle the issues relating to higher transaction cost to enable exporters achieve the desired level of exports to both developed and developing economies. ―On the pharma sector, he assured the industry that new government will make sure that the domestic industry gets a fair deal in other countries. "The focus of the foreign trade policy is to support services and exports along with improving the ease of doing business. The new trade policy will boost exports and create jobs while supporting Make in India and Digital India,"

CONCLUSION

With the Liberalization, Privatization and Globalization of the Indian economy and following liberal foreign trade, there had been changes in the business environment. With the development of science and technology there is a change in the nature of the Indian economy. There had been increase in the trade volume in the India‘s international trade, and the exports from India also have increased.

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