FOREIGN TRADE
AND
FOREIGN EXCHANGE
(For Students of MBA/MMS for Paper of International Finance)

O.P. Agarwal
B.K. Chaudhuri

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FOREIGN TRADE AND FOREIGN EXCHANGE

(For Students of MBA/MMS for Paper of International Finance)

O.P. AGARWAL
Diplomas in Cooperation/Industrial Finance,
Chief Manager(Retd.), General Manager’s Office, Bank of Maharashtra, Mumbai.

(Late) B.K. CHAUDHURI
Dy. Chief Officer, Methods & Systems (Retd.),
Former Faculty Member, Staff Training College,
United Bank of India, Kolkata.

SEVENTH REVISED EDITION : 2015
DEDICATION

Dedicated to Prof. (Dr.) Ramesh G. Bapat, M.Com., Ph.D.,
Vrushali Apartment, Shivaji Nagar, Pune - 5 and
Shri Bhanu Pratap Bansal, Retired Banker r/o Dal Bazar,
Lashkar - Gwalior (M.P.), my college friends, who
inspired/encouraged and motivated

O.P. Agarwal
Changes and amendments in business are normal and changes in foreign exchange and foreign trade are essential. The changes have been unprecedented in the state of Liberalisation. The liberalisation initiated and continued by the Central Government, the keen competition in the manufacturing/marketing of products and the rapid increase in export of services, have, all combined, changed the entire picture of the Indian economy. This has thrown up several challenges and the important among them is the need of trained professionals in international trade and economics. The important lesson export control/management does not depend on any preconceived notions. Export manager should always be pragmatic and of open mind.

I have endeavoured my best to incorporate all the latest changes in the foreign trade especially the new foreign trade policy 2009-2014, cap on Bank’s bulk deposit norms 2013, changes in hedging rules to increase to aid volume in July 2012, and new restrictions and norms for restricting current account deficit in foreign trade.

I am grateful to the learned professors and students/readers for their overwhelming support extended to the earlier editions of this book. I deem that this new edition would meet all the expectations of the readers/faculties. Constructive suggestions for the quality improvement of the book would be honoured with deep sense of gratitude.

Last but not the least, I thank my wife Mrs. Veena O. Agarwal M.A. (Eco.) for sparing me, from my social duties, to complete this book.

Date: 7.7.2015

O.P. Agarwal
704/11-D Springleaf Building,
Lokhandwala Complex,
Kandivli (East), Mumbai - 400 101
There is no dearth of books on foreign exchange in India today. Why, then, yet another treatise on the same subject? For one thing, the subject of foreign exchange is a rather difficult one, for it is highly technical and strictly governed by regulations which change frequently. For another, it is perhaps the most comprehensive one. Finally, it is practical and of immediate application to foreign exchange problems.

The present volume is a detailed study of banking operations in foreign exchange, and covers, at the same time, the theories underlying these operations as well as the Exchange Control Regulations embodied in the Foreign Exchange Regulation Act of 1973, the Exchange Control Manual of 1978 and subsequent circulars of the Reserve Bank of India. A copy of the English rendering of Uniform Custom and Practice for Documentary Credit, 1974, which is Brochure No. 290 of the International Chamber of Commerce, Paris, has been given in the Appendix.

As in my Practical Banking, which deals with loans and advances and other aspects of Indian banking, I have appended to each chapter of this book some of the important questions set on the subject of Finance of Foreign Trade and Foreign Exchange at the CAIIB examinations for the past 15 years or so. The present volume will, I am confident, prove to be a quite useful handbook on foreign exchange in theory and practice, not only for the bank people, but also for those who are engaged in foreign trade.

I take this opportunity to record by grateful thanks to Shri Piyush K. Naha, Superintendent, International Branch, United Bank of India, Kolkata, for his ungrudging assistance, and to Shri D.K. Bannerjee, Superintendent, Foreign Exchange Department, Central Bank of India, Kolkata, for making some very valuable suggestions which have been incorporated in the present volume.

B.K. Chaudhuri

7/4 Mitra Colony,
Kolkata - 700 034
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**APPENDIX**

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### Structures

On completion of this chapter, you will understand the following:

1.1 Foreign Trade

1.2 Foreign Trade: Meaning

1.3 Dumping

1.4 Balance of Trade

1.5 Balance of Payments – Meaning – Accounting

1.6 Disequilibrium

1.7 Correcting the Deficit

1.8 Foreign Contracts

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1.10 Most Favoured Nation Clause

1.11 Euro-Money

1.12 Methods of Foreign Trade

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1.14 Role of Exim Bank

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1.16 Off-Shore Banking Operations

1.17 LIBOR

1.18 European Currency Unit (ECU)
1.1 FOREIGN TRADE

The foreign trade of a country refers to its imports and exports of merchandise from and to the other countries under contracts of sale. No country in the world produces all the commodities it requires. On the contrary, a country may produce more of those commodities, in the production of which it has a greater or comparative advantage, and may not produce or may produce smaller quantities of those in the production of which, it has a greater or comparative disadvantage. The commodities which a country produces at an advantage, it exports, while those in producing which it has greater disadvantage, it imports. This happens under what in economic terms is called the Law of Comparative Cost or Advantage. Further, the price at which goods are traded between two countries depends on the extent and sufficiency of demands for the goods to be imported and exported; this is expressed in economic terms as the Law of Reciprocal Demand.

Foreign trade is of paramount importance for all the countries for their economic growth and provides a better quality of life to its citizens. The total foreign trade transacted by all the countries in the world economy as a whole, it is estimated that the total foreign trade in goods and services in 2001, amounted to US $15020 billion, which was 33% of total world economy. The Information Technology (IT) industry, which has touched life at all points and at all levels, has certainly affected manufacture/production/and commercial services in India. It has given a jump for many industries/business and even Government to leap-frog into the new millennium by many innovations and clever use of this new technology, U.S.A. was having a GDP $10171 bn in 2001 amounts to a little over one third of the total world economy.

1.2 FOREIGN TRADE: MEANING

Trade is the exchange of goods and services between a purchaser and a seller. If the purchaser and the seller are the residents in the same country and purchases and sells goods and/or services then such business is called as Inland Trade.

But when the residents of two or more different countries do the transactions of sale and purchase of goods or services, such trade is said to be foreign trade and transactions are known as foreign trade transactions. Such trade is also known as International Trade. International trade consists of transactions between residents of different countries.

The features of foreign trade are:
(a) involvement of different monetary units.
(b) imposition of restrictions in import and export by various countries.
(c) imposition of restrictions on release of foreign currencies.
(d) existence of multiple regulations, legal practices and rules in different countries.

Foreign Trade is of 2 types: (a) Import (b) Export

If the seller is abroad (across the borders) and the buyer is in the home country, trade is known as Import trade, while when the seller is in the home country and the purchaser is abroad, the trade is known as Export. What is import for one country is export for other country and vice-versa. Foreign Trade can be divided into 2 more types according to visibility; viz.:

Visible and Invisible: Visible Trade is one which can be seen, i.e., Trade of goods, Merchandise. Transfer or Exchange of Goods is visible while, exchange of services between the purchaser and seller is invisible. It is not visible but it actually takes place, i.e., shipping, transfer of technical know-how, insurance, transportation, fees of the professional experts, bank charges, commission, exchanges interest, etc., are invisible.

General Equilibrium Theory of International Trade: It was first developed by Eli Heckscher (1879-1952), and later refined by fellow Swedish Economist, Bertil Ohlin (1899-1979) in 1933. Heckscher - Ohlin trade theory explains the existence and pattern of International Trade based on a
comparative cost advantage between countries producing different goods. Ohlin accepts Ricardo’s view that the comparative Cost Difference is the basis of international trade. In 1919, Prof. Heckscher pointed out that the international trade is caused due to the differences in the comparative costs, resulting from the difference in relative scarcity (i.e. relative prices), of the factors of production in the two countries. According to Ohlin, the differences in the factor prices are due to the differences in the factor endowments in different countries and the differences in production functions for different commodities. Hence, Ohlin’s theory can be called factor endowment theory. For instance, a country, which has abundant labour and scarcity of capital, will specialise in the production of labour-intensive goods and export them and vice-versa. The prices of factors are determined by the supply of factors and the demand for them. Hence, given the demand, in a capital-abundant country, the rate of interest will be lower and in a labour-abundant country Y, the wage rate will be lower. So the capital-intensive commodity ‘X’ will be cheaper in country X and the labour-intensive commodity ‘Y’ will be cheaper in country Y. Ohlin explains this with reference to Australia and England. In Australia, the supply of land is abundant and cheap, while the supply of labour and capital is scarce and dear. Therefore, Australia specialises in the production of goods requiring a larger amount of land and a little amount of capital. On the other hand, in England, the supply of capital is abundant and the supply of labour is scarce. So, England specialises in the production of goods requiring a larger amount of capital and/or little amount of labour. So, Australia exports land-using products to England and imports capital-intensive goods from England and England exports capital-intensive goods to Australia and imports land-using goods from Australia. Therefore, trade takes place between any two countries because of the differences in factor endowments and their international immobility.

1.3 DUMPING

A part from the export of goods under contracts of sale, goods may also be sold in foreign markets by a process known as ‘dumping’. The word originated from the practice followed by manufacturers who sent their unsold goods for sale at prices below their cost of production to markets in which they did not normally sell, in order to maintain the price in their own markets. However, the word has now come to mean the practice of selling different prices in two markets, with a view to maintaining home prices and/or capturing foreign markets.

Dumping may be sporadic, predatory or persistent. When a manufacturer finds himself with distress goods on his hands, which he wants to dispose of in a foreign market at low prices, without harming his normal markets, or when he regards the cost of goods as already sunk in foreign markets and wants to cut his losses abroad by selling the goods for whatever the may fetch, the dumping is sporadic. Predatory dumping refers to selling at a loss abroad, in order to gain access to markets and then driving out the competitors, to reap near-monopoly benefits by raising the prices. When a producer consistently sells at a lower price in one market than in another, the practice so followed is called persistent dumping.

In all these cases, the sales in foreign markets are effected at prices which are lower than the domestic prices. Sale of Chinese calculators in Indian markets is a burning example in 2014-15. When a manufacturer sells abroad at a higher price than at home, the practice followed is called reverse dumping.

1.4 BALANCE OF TRADE

The difference between a country’s imports of merchandise and its exports thereof, is referred to as its balance of trade’. When the exports of merchandise of a country exceeds its imports, it is said to have a favourable balance of trade, and when its imports of merchandise exceed its exports, it has an unfavourable or adverse balance of trade.

Balance of Trade: Meaning – Causes of Reduction/Increase in Balance of Trade — Corrective Measures

Meaning: Balance of Trade means position of imports and exports of a country as against other countries. This is also called the net difference between the value of commodities, imported and exported.
When the exports of a country exceeds the imports of goods, it is said to have a *surplus*, *positive* or *favourable* balance of trade. But when imports of goods and services exceeds the exports of goods and services, it is said to have a *deficit*, *negative* or *unfavourable* or *adverse* balance of trade position.

When a country exports commodities it gains foreign exchange. If the imports exceeds exports; it results in net payment by the country of foreign exchange to other countries from its reserves or borrowings from other countries. It may be known that imports and exports, during any period of time, are seldom equal, the balance of trade will not be ordinarily balanced.

### Amount in US $ Million

<table>
<thead>
<tr>
<th>Year</th>
<th>Current A/c Deficit % of GDP</th>
<th>Fiscal Deficit %</th>
<th>GDP Growth %</th>
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<tbody>
<tr>
<td>2010-11</td>
<td>2.7</td>
<td>–4.9</td>
<td>8.4</td>
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<td>2011-12</td>
<td>4.2</td>
<td>–5.8</td>
<td>6.5</td>
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<tr>
<td>2012-13</td>
<td>4.4</td>
<td>–5.5*</td>
<td>5.5</td>
</tr>
<tr>
<td>2013-14</td>
<td>4.1</td>
<td>–5.0</td>
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*Source:* *But rose to 6.7% at the end of March 2013.*

### Trade Deficit Touches a Record High of $19.6bn

Trade deficit touched a record $19.6 billion in October 2011 as exports fell below the $20 billion mark for the first time in a year and imports maintained their momentum.

According to preliminary data released by the commerce department on 8-11-2011, export growth moderated to 12.4% in October 2011 with the value of shipments out of the country estimated at $19.9 billion.

“In any sector, it is the lowest in the last three months, deceleration is uniform,” commerce secretary said while warning that the “picture is not going to be rosy for the next six months”.

In contrast, imports surged 36.7% to $39.5 billion on account of a steep rise in oil, gold and coal imports. According to numbers compiled from the commerce department and Bloomberg database, trade deficit in October in significantly higher than the previous monthly record of $15.7 billion seen in August 2008 and May 2011.

Trade deficit over the next few months is going to narrow as local producers adjust to the changing demand situation and lower import of inputs.

According to data available with the commerce ministry, export volumes have continuously declined from $29.4 billion May, although imports have not seen a decline of same magnitude (see chart). From a peak of 82% in July 2011 export growth has been slowing every month. It moderated to 44.25% in August 2011, 36.36% in September and is estimated at 12.4% in October 2011.

But given the high growth rates witnessed in the first half of the financial year, exports in April–October are estimated to have increased around 46% to $179.8 billion.

Although, Khullar said the government remained “cautiously optimistic” about reaching the $300 billion export target for the current financial year, the asking rate has shot up since shipments out of the country would have to be worth $24 billion a month between November 2010 and March 2011.

Already, the impact of the problems in Europe is showing on sectors such as electronic goods where contraction was witnessed in October. Engineering and petroleum exports too grew by 2.6% and 9.4%, respectively.

<table>
<thead>
<tr>
<th>Year</th>
<th>Export</th>
<th>Import</th>
<th>Trade Deficit</th>
<th>Year</th>
<th>Export</th>
<th>Import</th>
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<td>17.7</td>
<td>28.9</td>
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<td>25.6</td>
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<td>21.4</td>
<td>27.8</td>
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<td>May’11</td>
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<td>45.1</td>
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Foreign Trade

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<td>29.1</td>
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<td>11.8</td>
<td>14.4</td>
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Figures in $ bn

Source: Dept of commerce.

Hard Fact on Easy Money

Every explanation for market behaviour rests on a series of factors. But here’s a factor cited by everyone pretty much all the time these days: quantitative easing (QE).

QE — central banks increasing the size of their balance sheet and using the money to buy up assets — has been deployed by the US, European and Japanese central banks to revive their domestic economies.

Whether or not QE is responsible for the mild uptick in advanced economies, that the gush of liquidity can perk up emerging economy stock markets is almost taken for given by many pundits. Others worry that the liquidity can push up inflation.

India’s economy managers seem to take QE — or the amount of foreign participation in equity markets — seriously as well.

But pundits and economy managers in India should take a pause. QE isn’t all that it’s built up to be in terms of an explanation for market behaviour. And a buzzing market is the wrong priority for policymakers.

Missing the Mark

So, what has been the Indian experience since QE? Yield-seeking foreign investors should arrive in droves to arbitrage the growth (and returns) that may be achieved in India when their home country offers zero interest rates. But this hasn’t quite happened in our equity markets.

Here’s the data: in rupee terms, the Nifty is up a measly 4% per annum for the last three years, while in dollar terms, the returns are a negative 2% compounded. This much-touted “liquidity” driver does not seem to have excited equity markets.

Liquidity infusion is supposed to increase asset prices, cause inflation and lead to currency appreciation.

In India, stock prices were up about 8% per annum since June 2007, real estate prices increased on average 10% per annum, and inflation (CPI) has been in the same ballpark, while currency had depreciated! Real returns from almost all asset classes seem zero or negative. Only gold — as a hedge against currency depreciation — has held firm.

Strengthen Infrastructure

Can we blame inflation on foreign inflows? Over the last few years, M3 — a measure of money supply — has grown about 16% per year. This fell to 14.2% in the first quarter of 2011-12 year, and post QE3, is now at 12.6%. So, foreign inflows don’t seem to have raised money supply.

The Economic Survey has identified that there are over ` 7.5 lakh crore worth of projects stuck in India due to policy issues — mining, environment and land acquisition being major problems.

Inflation has mostly been caused by policy inaction leading to supply constraints and also by some policy action — increase of administered prices, energy and food in particular.
The Indian economy needs serious investment in infrastructure. Long-term infrastructure projects are best financed by long-term capital at low interest rates.

The global environment offered India just such an opportunity. This was India’s best chance to increase productive capacity of the economy, and allow growth without inflation.

Lack of focus on “enabling” policy prevented investment in core sectors. In a world, where increasing inflation is the target of most central banks, home-made inflation seems to be our own doing.

What could happen if liquidity were to tighten and if rich-economy central banks were to reverse the easy money policy? Well, if the above is true — not a whole lot!

Interest rates would rise, as would global inflationary expectations. Since most currencies are engaged in competitive devaluation, the relative effect of currency movements would be neutralised.

Real interest rates in India may actually rise — leading to higher savings, lower dependence on foreign inflows and better capital allocation.

Money is not a commodity that remains constant. When dealing with QE-induced money flows, the question “where will the money go” is nonsensical.

The money can remain on the balance sheets of banks — as happened in the initial stages of QE1 and QE2. It can also be lost when asset prices fall — like when the real estate bubble in the US burst.

**Remove Roadblocks**

Investment activity should be, and largely is, based on expectations of future returns. If QE3 works, it is possible that developed markets will provide greater opportunities to investors than emerging markets.

A case in point is the new high that the US equity markets have reached — while emerging markets like India remain below their all-time highs. Trying to guess the timing or direction of money flows is a fruitless activity. Pundits should know this.

India’s economic managers, too, would do well to look at measures that would remove constraints in the real economy rather than focusing on financial markets.

Financial markets are meant to serve as the barometer of investment outlook — fiddling with the barometer does not change the underlying reality of a poor investment climate. Never mind the easy money.

India’s economic managers would do well to look at measures that would remove constraints in the real economy rather than focusing on financial markets.

There are two factors for variation in balance of trade position, viz.:

1. **External Factors**
   (a) The sudden rise in prices of essential commodities of import like edible oil, sugar, machinery, drugs and medical equipments, etc.
   (b) Migration from countries where Indians are target for violence. This affects the inward remittances.
   (c) Position of world-wide inflation or recession in the developed countries like U.S.A., Germany, Japan, France, England, etc., with whom regular foreign trade is carried out.
   (d) Trade restrictions imposed by the developed countries as regards limit of quantities of imports, restrictions under other bilateral agreements.
   (e) Continuous upsurge of US Dollar (as happened in April 2012) onward after November 2008, when the price of one Dollar gone over `68 (in Sept. 2013). This had pushed up the price of the items imported especially gold/edible oil/crude oil pulses etc..

2. **Internal Factors**
   (a) Domestic shortage of agricultural and industrial products.
   (b) Low industrial and agricultural production due to high production cost.
(c) Absence of hi-technology or obsolete technology.
(d) High consumption of internal productions making it unable to export.
(e) Increasing tendency in population growth, which compels consumption of domestic production and even ever-increasing imports for minimum necessities.
(f) Inadequate knowledge of export-markets of Trade Information Systems like JETRO in Japan, KOTRA in Korea, CETDC in Hong Kong and STDB in Singapore, to keep prompt track of business information overseas.
(g) Neglect of export profitability.

Corrective Measures: To come out of the above unfavourable balance of trade position, certain corrective measures are required —

1. Export Promotions: The Government should take adequate steps to encourage exports, reduce the cost of production, improve the quality of goods and make the price of export goods competitive in the international market.

2. Import Restrictions: Presently, our economy is a Liberalized Economy. Even then the Central Government should take such steps which restrict the imports, make it costly by imposing heavy duty on goods imported, ban the items of less importance, fix quota for essential items of imports, allow import against licence only.

3. Finance: The deficit in the balance of payments by borrowings overseas, take all proper measures to increase exports.

4. Monetary Measures: The R.B.I., as a monetary authority, should adopt a policy of credit squeeze, put restrictions on bank credits, make costly by raising bank rate (8.50% w.e.f. 4th April 2013), base rate which is 9.05–10% in 2015, put restriction on the bank for lending and reduce their capacity to extend credit facilities by imposing certain economic measures that is Selective Credit Control and/or open market operations.

5. Fiscal Measures: To take drastic steps to curtail public expenditure, budgeting for surplus, levying lower rate of taxes and recover taxes speedily. In June 2012 Central Government has opted for curtailing public expenditure, even then current account deficit reached to 6.7% of GDP in March 2013.

1.5 BALANCE OF PAYMENTS — MEANING — ACCOUNTING

Meaning: The balance of payment of a country is a systematic record of all the trade transactions, visible and invisible imports and exports during a given period. A country must pay for its import of goods and services and in turn for its export of goods and services it receives payment from other countries. The balance of payment is a difference between international transfer of funds for a country’s imports and exports during a certain period of reference. Balance of payment includes the imports and exports of merchandise and services inflow and outflow of capital, interest and dividends on account of foreign investments, tourist income and expenses, gifts, donations, etc.

Thus, balance of payments is more comprehensive than balance of trade. Balance of payments includes balance of trade and other invisible items of foreign trade.

It should be clear that a country with a deficit in balance of trade need not necessarily have deficit in balance of payments or vice-versa. The deficit in balance of trade may be more than offset by surplus in the invisible trade, resulting in surplus of balance of payments.

Current A/c deficit as of GDP during the last 4 years has been (in billion dollars) as:

<table>
<thead>
<tr>
<th>Year</th>
<th>Deficit</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008-09</td>
<td>2.3bn</td>
</tr>
<tr>
<td>2009-10</td>
<td>2.6bn</td>
</tr>
<tr>
<td>2010-11</td>
<td>2.6bn</td>
</tr>
<tr>
<td>2001-12</td>
<td>3.66bn</td>
</tr>
</tbody>
</table>
The balance of payment accounting has two types of accounts, viz., Current Account and Capital Account.

The Current Account Sec. 2(J) FEMA Act, 1999 includes private and Government merchandise, invisible items like:

1. Foreign trade, services, short-term banking and credit facilities.
2. Payments as interest on loans and net income from investments.
3. Remittances for living expenses of parents, spouse and children residing abroad, and

While the capital account transactions include private long and short-term assets, banking transactions and official loans, amortisation, IMF and reserves and monetary gold contingent liabilities [Sec. 2(e)].

When a country has a favourable balance of payment position over the years, inflow of foreign capital takes place, the country’s currency becomes strong as country’s foreign exchange reserves are accumulated.

1. **Definition:** The balance of payment of a country is a systematic record of all the economic transactions between the residents of that country and the residents of foreign countries during a given period of time.

   An economic transaction is an exchange of value, that is, an act which involves payment and receipt of money in exchange for some economic goods or services or assets. An international economic transaction evidently involves such transfer of title to goods or assets or rendering of services from the residents of one country to the residents of another. As to who are the residents of the reporting country is more or less arbitrarily decided by it.

2. **Contents:** The balance of payments thus, includes the imports and exports of merchandise and services, inflows and outflows of capital; interest and dividends on account of foreign investments, tourist income and expenditure, gifts, donations, etc. Further, since it is not always possible to have sufficient information to effect a complete record of international transactions, an item for “Errors and Omissions” is added to the balance of payments, to strike a balance between the two sides of the accounts.

3. **Use:** The most important use of the balance of payments for most countries is that it describes, in a concise fashion, the state of international economic relations of the country, as a guide for its Government’s in framing its monetary, fiscal, exchange and other policies.

4. **Broad Divisions:** The balance of payments is broadly divided into:

   (a) Balance of payments on current account, i.e., the balance of payments concerning the imports and exports of merchandise and services; and
   (b) Balance of payments on capital account, i.e., the balance of payments which includes the transactions of the balance of payments on current account and reflects the changes in the foreign assets and liabilities of a country.

5. **Balances within the Total:** For purposes of analysis, the items of the balance of payments are classified into different groups. There are at least five separate types of balances, viz.:

   (a) Merchandise/trade balance, i.e., the balance of imports and exports of merchandise;
   (b) Current account balance, i.e., the balance of imports and exports of merchandise and services;
   (c) Basic balance, i.e., the current account balance plus long-term capital;
   (d) Net liquidity balance or balance on regular transaction, i.e., basic balance plus errors and omissions plus short-term, non-liquid capital flows; and
   (e) Official transactions balance, i.e., net liquidity balance plus liquid liabilities to foreigners.

6. **Illustration:** A specimen of the balance of payments with imaginary figures is given below:
### India’s Overall Balance of Payments in 2006-07/2012-13

<table>
<thead>
<tr>
<th>Description</th>
<th>2006-07 (April to Sept)</th>
<th>2012-13 (till 13.3.2013)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Current Account</td>
<td>– 10.3</td>
<td>– 19.29</td>
</tr>
<tr>
<td>B. Capital Account</td>
<td>18.9</td>
<td>203.71</td>
</tr>
<tr>
<td>C. Errors &amp; Omissions</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>D. Overall Balance</td>
<td>8.6</td>
<td>223</td>
</tr>
</tbody>
</table>

Source: DNA Newspaper

### 1.6 DI SEQUIL BRUUM CURRENT A/ C DEFICIENCY (CAD)

The debit and credit items in a balance of payments seldom balance. As a result, the balance of payments is either in surplus or in deficit. When a country happens to have a favourable balance of payments over the years, inflows of foreign capital takes place, provided that the rates of interest prevailing there are high and there is confidence in the country’s currency: that is, no devaluation of that country’s currency is apprehended. When, on the other hand, a country has an unfavourable balance of payments, its foreign exchange resources get depleted.

**CAD: A Slippery Slope**

Just when the Reserve Bank of India appeared to have won the three-year battle against inflation, a new front on a record current account deficit has opened up. Baby steps are being taken, but a failure to contain it will have worse consequences.

### Causing Worry Lines

| **The 25 bps reduction in key interest rate is not the beginning of a journey to a paradise of low-cost funds regime** |
| **Inflation may have eased to a three-year low, but there are concerns over the external sector. The historically-high CAD is an obstacle for policy makers** |
| **The government has raised import duty on gold to 6% to lure away buyers. But rising crude prices was a worry in 2013-14** |
| **Raising of debt investment ceiling for foreigners to $75 billion, from $65 billion has also helped, but it is also a worry** |
| **It may take time for fiscal consolidation to reap benefits for the economy** |
| **Govt allowing oil companies to deregulate diesel prices. may be too little, too late** |
The frequency with which a topic comes up in a discussion indicates the significance of it. By that yardstick, current account deficit takes the centre stage at the Reserve Bank of India policy making as inflation and fiscal deficit are pushed to the background.

The former central bank Governor Duvvuri Subbarao referred to the current account deficit, the excess of spending overseas over earnings, at least 22 times in a call with economists on 30 January 2013. That is up from five times during a similar call after the second quarter monetary policy in October 2013. Alarm bells are ringing, but not loudly as yet.

The 25-bps reduction in key interest rates is not the beginning of a journey to a paradise of low-cost funds regime. Inflation may have eased to a three-year low and finance minister P. Chidambaram may be more convincing than ever in containing the fiscal deficit, but it may not yet be enough to return to the ga-ga years of growth miracle.

External imbalances could put a spoke in economic revival. Just like an individual who keeps funding his consumption disproportionate to his earnings runs me risk of the lender shutting me tap, international investors who have been kind to the nation could do the same. “An out-of-control current account deficit can easily hit both growth and inflation by raising concerns among foreign investors and by forcing a sharp depreciation of the currency,” says Jahangir Aziz, chief Asia economist at JP Morgan. Chase, who forecasts the December 2013 quarter number at 6.5% of the gross domestic product.

“For the year as a whole, CAD is unlikely to fall below 4% of GDP as continued high gold demand and higher imports driven by modest recovery that most of us are expecting will keep the overall import growth pretty strong.”

Imports have always been strong, thanks to distorted pricing of oil products and the economic mess that drove investors to gold when they wanted to preserve their earnings from getting eroded by high inflation. While oil is an indicator of economic expansion, gold is a drain on the economy with wealth going into un-productive purposes that get locked up in vaults.

Chidambaram had raised the import duty on gold to 6%, which accounted for 10% of trade deficit. The government had belatedly permitted oil companies to raise the prices of diesel, one of the two major components of subsidised fuel, the other being cooking gas.

At this point, both the measures appeared to be too little and too late. The global liquidity wave is lifting asset prices, including commodities, again. Benchmark Brent crude oil prices have risen $5 per barrel since the government started taking baby steps on diesel prices in mid-January 2014. Official import of gold may have slowed, but that has opened up the door for smugglers of the precious metal with customs officials catching huge quantities at regular intervals these days.

“While higher duties will probably reduce demand somewhat, unless fundamental causes of increased gold demand are mitigated, the effect is unlikely to be sustained,” says Saugata Bhattacharya, economist at Axis Bank. That leaves the nation with one choice to set right the external economy –
exports which depends on consumption demand in the West. The US economy contracted in the December 2013 quarter and consumer confidence in Europe is sliding, thanks to the unemployment rate of more than a fifth in countries such as Spain and Greece.

While oil is an indicator of economic expansion gold is a drain on the economy with wealth giong into fet locked up in vaults

“The CAD may stay elevated in the near-to-medium term without the prospect of any quick recovery of exports,” says Siddhartha Sanyal, economist at Barclays. “The Imports Bill will likely depend critically on global commodity prices as the imports volume for critical imports such as oil is unlikely to soften quickly.”

Indian exports have plunged for eight straight months. Indian services, which have been a pillar for nearly two decades, are cracking. Services exports have slowed sequentially over the last three quarters. But, imports are still on the rise, worrying policy makers.

“There is also another concern about CAD, which is not so much discussed, which is the quality of CAD,” Subbarao said. “If we had a high current account deficit because we were importing capital goods. But, if we are having a high current account deficit because we are importing a lot of diesel where demand is not price-elastic and we are importing a lot of gold, then that is a concern.”

India has been lucky. The Federal Reserve, the European Central Bank, which have been printing unlimited money since 2008, is now joined by the Japanese central bank. India has received $25,519 crore in portfolio flows in January 2014, against $26,925 crore, a year before.

Raising of the debt investment ceiling for foreigners to $75 billion from $65 billion had also helped. But it is also a worry. A lot of this is hot money and could reverse at a short notice, jolting the currency market. “Much of the recent FII investment under the G-see limits has flown into short-term T-bills, enhancing refinancing risks to external debt,” RBI’s economic review said. “Concern’s about the sustainability of India’s external sector have increased.”

When all is not well, the governor went ahead with the lowering of interest rates that could manifest in a higher demand, and in fact worsen the external sector imbalance. None other than a top RBI executive admits to that.

“In a slowing economic growth, a high trade deficit is a matter of concern, and (will) show some imbalance,” says Deepak Mohanty, executive director at RBI. “So partly, it could be that a lot of domestic production is getting substituted by imports.”

The quarter point reduction in interest rate may not lead to a rush by entrepreneurs to put up new projects. But it is aimed at pushing demand. If the demand expectations materialise with economic factors not in place as it happened in 2011 when a premature pause in interest rate increase had to be reversed, the central bank’s reaction may not be different this time either.

Five years of economic mis-management has complicated policy decisions. It is no more a straight case of inflation and interest rates. As we saw the governor latch on to the government, bringing down fiscal deficit to ease rates, it may now be time to see improvements in the current account deficit number. “We will take into account, what the current account deficit is. It will not be driven just by the inflation number or the inflation trajectory,” Subbarao said on his monetary policy stance. “The current account deficit has implications for inflation) and, therefore, for the conduct of monetary policy.”

This concern eliminates the possibility of lowering interest rates in the near future. Economists penciling in a 100-150 bps cut in interest rates are now forecasting half that.

Just as the 6-7% economic growth rate looks to be the new norm, so may be the interest rates for some years to come. These may be the new normal.
1.7 CORRECTING THE DEFICIT

If a country happens to have a persistent deficit in its balance of payments, its Government has perforce to intervene and adopt measures to correct the position. Such measure includes:

1. **Import Curtail:** When imports are restricted, the balance of payments position no doubt improves; but when imports consist of raw materials for the manufacture of export goods, it may not be wise to restrict such imports. It may, in such circumstances, be a more prudent policy to finance the deficit in the balance of payments by borrowing abroad in the hope of repayment by increased exports, provided that the foreign lending is not tagged, *i.e.*, is not made on condition that the borrowing should be utilised in purchases in the lending country. Import restriction is effected through such measures as imposition of tariffs, fixing of quotas, allowing imports only against licences. Tariffs are import duties levied on goods entering the country and are usually expressed as a percentage of the value, or as an amount of home currency per unit of the goods imported. Tariff’s, thus make imports dearer and are intended to discourage imports. Quotas refer to limits fixed in respect of the total quantities or values of commodities to be imported, and import licences are issued until the quotas are exhausted. The allocation of licences is usually based on certain factors, such as priority in consideration of the needs of the country’s economy, export-orientation of the goods to be imported, imports made previously by the applicant, etc.

2. **Export Promotion:** The export promotion policy of a Government — the Government of India is no exception — may take the form of reducing the rate of interest chargeable by banks on export finance, guaranteeing bank advances to exporters by way of packing credit and export-bill purchases, providing insurance cover for exports, allowing duty drawbacks or cash incentives to exporters, abolishing export duty, if there be any, etc.

3. **Monetary Measures:** If there is excessive purchasing power with large cross-sections of a country’s population compared with the available supply of goods and services, and if the consequent demand for them causes imports to rise, the monetary authorities, *i.e.*, the Central Bank of the country, may adopt a policy of credit squeeze; that is to say, borrowings by banks from the Central Bank are made costlier by raising the bank rate; lendings by banks are restricted by a reduction in their lending resources by raising the statutory liquidity ratio (SLR), and/or by open market operations by the Central Bank.

4. **Fiscal Measures:** These relate to a Government’s revenue and expenditure and include budgeting for a surplus by pruning its own expenditure, levying high taxes, extending the areas of taxation, etc.

5. **Devaluation:** Devaluation, refers to a reduction by the Government in the country’s official rate of exchange between its own currency and other currencies. This is effected by reducing the par value of the currency in terms of gold. If the currency of a country is overvalued in terms of other currencies, its exports decline and imports increase, resulting in a persistent deficit in its balance of payments. Devaluation is the main corrective measure which is employed to set right such fundamental disequilibrium. It makes the country’s exports cheaper and imports dearer, and thereby, stops further drain on the country’s foreign exchange resources. On the other hand, the extra exports after devaluation may leave a smaller supply of goods for domestic consumption, as a result of which incomes may exceed the supply of goods, leading to inflation, *i.e.*, rise in prices, which may eventually offset the benefits of devaluation.

The *revaluation* of a currency refers to an increase by the Government of the country in the value of its currency in terms of other currencies. This is done by increasing the par value of the currency in terms of gold. When the currency of a country is undervalued, which is indicated by the relative cheapness of its goods and ever-increasing foreign exchange reserves, a revaluation of its currency may be desirable, if imports are to be encouraged and/or exports are to be made dearer.
1.8 FOREIGN CONTRACTS

1. Terms: Goods are traded between two countries under contracts of sale/purchase agreed upon by the buyers and sellers. Such contracts not only specify the quality, quantity, price and the period of supply of the goods to be bought and sold, but they also stipulate the mode of delivery, the terms of payment of freight and insurance charges, and the mode of payment for the goods.

2. Mode of Delivery: Delivery may be actual or constructive. Where the goods are physically delivered to the buyer, the delivery is actual. Where documents of title to goods, such as Bills-of-Lading, and not the goods, are handed over to the buyer, the delivery is constructive. In foreign trade, delivery is always constructive.

3. Freight and Insurance: In foreign trade, certain abbreviations are used to indicate whether freight – i.e., charges for the transportation of goods from one country to another by ship or air or by post – should be prepaid, and whether the shipment should be covered by insurance, and if so, who should bear the charges. These are:

(a) c.i.f.: These letters stand for cost, insurance and freight, and when included in a contract of sale/purchase, mean that the goods, apart from being of the agreed quality and quantity, should be invoiced at the agreed price, and placed in good packing condition on board or a vessel, taking the usual route in one shipment, unless otherwise provided in the contract, on or before the specified date; that the required freight should be prepaid and that the shipment should be fully covered by insurance by the seller. The seller should also see to it that the Bill-of-Lading is a clean shipped ocean one and is accompanied by a marine insurance policy, and not a certificate of insurance, as a certificate is not normally a good delivery under a c.i.f. contract. He should also obtain, when called upon to do so, such other documents as consular invoice, certificate of origin, etc., and pay export duties and other charges, if any payable. The charges are borne by the seller, of course, on behalf of the buyer, and being included in the invoice price of goods sold, are ultimately passed on to the buyer. When freight is prepaid, the bill of lading is marked Freight Paid. Under this contract, payment is to be made by the buyer on presentation of the shipping documents, and in the event of the shipment being lost in transit, the value thereof is recoverable from the insurance company. The seller has, therefore, to see to it that the documents relating to the shipments are strictly in terms of the credit.

(b) c & f.: The two letters stand for cost and freight, and when included in the terms of a contract of sale, mean that apart from pricing, quality, quantity, and shipment of the goods as under a c.i.f. contract, freight should be prepaid and the expenses therefore, should be borne by the seller, even if the amount being added to the invoice price of the goods sold is ultimately passed on to the buyer. In a c & f. contract, insurance is the concern of the buyer, and the seller is under no obligation to insure the goods while they are in transit.

(c) f.o.b.: These letters stand for free on board. In an f.o.b. contract, the buyer names the vessel and specifies the date by which the goods are to be shipped and the seller has to see to it that the goods are placed in a properly packed condition on board the named vessel by the time specified and that a clean shipped bill of lading is issued. The responsibility of the seller ceases the moment the goods sold are placed on board the ship which is to carry them to the buyer’s country, but at the same time, he loses his right of lien or stoppage in transit of the goods. All expenses incurred in placing the goods on board the ship are borne by the seller and included in the invoice price, while the freight is payable and insurance is to be arranged at his own expense by the buyer.

(d) f.a.s.: These letters stand for free alongside ship, and imply that the seller is responsible for the delivery of the goods within the specific time alongside the ship which will carry them to their destination, and that the expenses incurred in placing the goods on board the ship are on account of the buyer and insurance is to be arranged and premium, freight, etc., are to be paid by him. The seller must provide a clean ship’s receipt and should, if necessary,
assist the buyer in obtaining the documents issued in the country of origin and/or the documents relating to the shipment.

4. Mode of Payment

(a) OD/DP: The contract of sale may stipulate payment on demand (OD) or documents against payment (DP); that is to say, the buyer, i.e., the drawee of the bill of exchange covering the goods sold, should pay for the goods purchased on presentation of the bill of lading, etc.

(b) DA: The contract of sale may be on DA terms, which means that the documents of title to the goods sold will be delivered to the drawee (i.e., buyer), on his acceptance of the relative bill of exchange, while the payment is to be made by the drawee/acceptor on maturity, i.e., after the expiry of the tenure of the bill, i.e., the period for which the bill is stated to run before maturity.

(c) VP/COD: VP stands for value payable and COD for cash on delivery. These abbreviations are usually used in international trade when goods are despatched by post parcel. The letters COD are also used in the case of shipment by air. They imply that the post parcel would be delivered to the addressee (buyer), by the postal authorities only against the payment of the value thereof in cash.

1.9 INTERNATIONAL TRADE AGREEMENTS/INSTITUTIONS

WTO (GATT) was the abbreviation of the World Trade Organisation which was signed at Geneva by 23 countries in 1947, effective January 1948. It is a world organisation, designed to bring about the maximum possible rate of growth in world trade by reducing tariff barriers among the member countries. There have since been a number of sessions of the GATT, and the member countries have, on several occasions, reduced the level of tariffs amongst them by mutual agreement, such as the “Kennedy Round” of negotiations concluded in 1967.

The “Kennedy Round” was the world’s biggest-ever tariff-cutting deal, and gave a new boost to trade among the developed and developing countries. Under the influence of the WTO, the “beggar thy neighbour” policy of the 1930’s has been abandoned, resulting in a great expansion of world trade. The WTO also applies to quota restrictions and other import controls.

WTO constitutes a code of conduct covering the totality of the member countries. WTO is meant for the world-trade without any barriers. It believes in negotiations and throughout it, WTO works for reduction of and elimination of barriers of trade. Over the period of 58 years, custom tariffs have been reduced from about 40% to an average of 5% of the price of imported products. The WTO is the principal international body in world-trade. It constitutes a code of conduct to which 80% of the world trade has been covered. The trade problems of the developing nations has been a major pre-occupation of WTO. It has successfully governed international awareness. It makes the trade problems of the developing countries and have caused for relief and drawn attention of the developed nations towards such problems of the developing countries and forced them to provide solutions to it. The WTO’s code of conduct, its effectiveness and legal validity has on several occasions deterred Governments in imposing trade restrictions in general or particular against some countries.

In September 1986, ministers of 100 countries got together in Uruguay Seaside resort of Punta-del-este and began 8th round of negotiations to build a bigger, brighter and better world trading-order. The round of talks concluded on 15th December, 1993. It concerned matters like:

1. Reducing specific trade barriers and improving market access tariffs, non-tariff measures, tropical products, natural resources-based products, textiles and clothing, agriculture.
2. Strengthening WTO disciplines.
   Trade Related Investment Measures (TRIMS)
   Trade in services.
**Implications of WTO on Indian Trade:** Mr. Arthur Dunkel, former Director General of GATT, submitted comprehensive documents on 20 December, 1991, which was commonly known as Dunkel Proposal or Dunkel Draft. India signed this Pact on 15 April, 1994 along with 124 other countries. Its special features were:

1. Aims at removing non-tariff barrier to trade of agricultural commodities.
2. The ordinary Customs Duties shall be reduced by 36%, within a minimum rate of reduction of 15% for each tariff between the year 1993 to 1999.
3. Every country will have to import minimum 3% of their corresponding domestic consumption.
4. Reduction in export subsidies on Agriculture Products shall be reduced by the developing countries at 24% of budgetary outlay and 16% quantitative outlay with above requirements. India’s world trade could gain US Dollars 1.25 billion.

**TRIPS:** As per arrangements, all export subsidies are proposed to be abolished. This is a very controversial subject.

**TRIPS:** The Indian Patents Act would be required to be amended within a period of in between 5 to 10 years. The patented drugs will become costly.

**Services:** Telecom, Hotel, Construction, Computer and Medical services will be open to foreign firms. This will enable the free movement of skilled workers from India.

**Textile & Clothing:** Quantitative Restrictions (QR), on textile imports from India by European countries, viz., U.S.A., Canada could be phased out within 10 years. Tariffs on such imports by European Community are proposed to be reduced. This would boost the Indian exports.

**Agriculture:** Due to reduction in subsidies by the member countries, the prices of agro-products are expected to go up and Indian exporters can fetch better prices. Due to the seed patenting, the Indian farmers can get a better quality. Indian farmer’s fear is that the prices of seed would be very high. GATT was transformed into a new organisation which was named as the World Trade Organisation (WTO) w.e.f. 1st January, 1995.

There was general opinion about Uruguay Round Agreement and the provisions of the TRIPS, in particular, were not largely in the interests of the developing countries, on the contrary India and the other developing countries had more to lose than gain from walking out of the GATT on this issue. Under the terms of agreement, India was to meet all obligations till year 2005, of the TRIPS agreement. But India has to accept applications for product patents on pharmaceuticals and agriculture chemicals. The second obligation is that the Government has to give exclusive marketing rights for 5 years to holders of product patents issued in another WTO member country. The biggest impact of the TRIPS Agreement is that after 2005 year, India will have to provide patent protection to pharmaceutical products, in addition to production processes under India Patents Act, 1970.

Dr. Arthur Dunkel, former Director General of General Agreement on Tariffs and Trade (GATT), introduced the Dunkel Draft which resulted is setting up of the WTO to monitor international trade and to facilitate the process of globalisation. In the meeting of the WTO in December 2005, there was strong opposition by India, in addition to other developing agricultural countries against curtailment of subsidies on products. The opposition continued in meetings of July 2008/July 2011 and March 2013.

India, as a member signatory to the Agreement, has received significant tariff concessions from several other member countries, and has also been able to pursue a policy of quantitative import restrictions to conserve her slender foreign exchange reserves.

What is of great concern to India and many developing countries is the tendency of the developed countries to drag in may *Extraneous* issues into the WTO, which indirectly would affect their exports. One such move was to bring into the WTO the need for uniform labour standards among the members. The issue was that with liberalisation of trade, developing countries whose wages are comparatively LOWER, would have an edge in the competition with the developed countries. The main contention of the developing countries was the reduction of the agricultural subsidies, as well as high tariff barriers of the
developed countries, who could not give any commitment on reducing them. The developing countries were also against the introduction and discussion of new issues (referred to as Singapore Issues), without a prior resolution of the various issues raised by the developing countries earlier.

Cancun Meet is to be remembered for the ability of the developing countries to hold together, despite the severe pressure being exerted by the global economic powers. Multilateral trade negotiations were conducted on more even terms for the first time in WTO. India/China and Brazil stood together in this effort. Hence, the sum and substance of WTO negotiations are that India has to oppose any unfair demands in the ministerial discussions and show solidarity with other countries which do so, while at the same time, continue negotiations indirectly with the countries to improve our trade.

**WTO Delhi Meet to Shape Geneva Talks**

After more than eight months of inaction, it was time again for trade ministers to huddle up and strategies on how to move the stalled WTO negotiations. WTO director-general Pascal Lamy, who has been steering the Doha round since September 2005, was a key driver at the informal New Delhi meet. In an exclusive pre-ministerial telephonic chat with Anmiti Sen before setting off for the Capital, Mr. Lamy gives an insider’s view on where exactly the Doha talks are poised and why he is optimistic about the talks getting wrapped up by the end of 2010.

**Though the New Delhi ministerial is an informal one, key ministers are going to sit across the table first time since the talks broke down in Geneva in July 2008. What are your expectations?**

It is an informal gathering that is different from what happens in Geneva, where the negotiating and decision-making processes have to involve each and every constituency. Here, we are not going to take decisions on substance that are taken by the larger membership. But it is a very useful occasion. We are grateful to Mr. Anand Sharma for having taken the initiative. The meet will give guidance to ministers on how the negotiations can get moving in Geneva given the fact that 20% of the deal remains to be done.

**Are you saying only 20% of the issues need straightening?**

Everybody knows what remains to be done, where the remaining 20% difficulties are. The question we have to address now, given the 2010 deadline agreed upon by trade leaders, is how do we work out the negotiating process in Geneva so that the remaining issues are settled within the time period. It has to be a mix of multilateral and bilateral contact. The Delhi meet will test the political signals we have received from countries, including India, that all want to go in the right direction.

**What gives you hope that talks are going to move now?**

Given the harshness of the economic crisis and the huge importance of pushing back the protectionist pressures that are appearing here and there, although not in a big way, there is this feeling among members that the best thing is to keep opening trade and conclude the round. All this needs a more concrete translation, and hence the necessity of organising a process here. The rather large number of ministers gathering in Delhi is a good occasion to do that.

**Will members agree to make the December texts on agriculture and Nama the starting point of the negotiations?**

I am not saying everybody is 100% in agreement with the text. There are a number of issues that are open, that still have to be changed. However, the conventional wisdom is that we start from where we are.

**There have been talks that differences on the trigger level on increasing import tariffs for developing country farmers have been sorted out. Your views?**

I wouldn’t go as far as to say it is in our pocket. But I think, compared to last July, the case for developing countries to protect their farmers against import surges is dear, and the case on the side of exporting members – a large number of them developing countries – that it should not impinge normal trade flows is also dear. It is now a case of finding the right numbers and architecture by making both sides understand the other side’s constraints.
**Save Doha Round, Save the WTO**

The World Trade Organization (WTO) has been deeply paralysed over the last three years, due to the impasse over the Doha Round. There is an interesting debate in the international press on whether the Doha Round is effectively dead and, if not, whether it is useful to keep it alive in its comatose situation. In the eyes of sceptics, the Doha Round is long past its’ use – by date and its agenda of little relevance in a rapidly – changing global economy. Going by this view, the WTO would do well to jettison the round and start afresh with work on issues that are more relevant. On the other side, it is argued that aborting the round, billed as Development Round when it was launched in 2001, would have serious consequences for future global cooperation on economic issues.

At the heart of the impasse are related developments in the global economy over the last decade:

1. Changes powered by new communication technologies and fuelled by widespread liberalisation have altered the structure of the global manufacturing process and the direction and composition of trade flows. The fragmentation of manufacturing along widely – dispersed regional and global value chains is increasingly challenging the market dominance of incumbents.

2. The economic and financial crises in developed countries over the last decade stand in stark contrast to the persisting high growth trajectories of the emerging economies. This development has altered the political economy of the discourse in the WTO. Unlike the past, developing countries of all shades are better organised to canvass their positions. Though a welcome development, it also means it takes longer to build consensus around issues being negotiated.

3. In the US, persisting high unemployment levels and an uncertain recovery have made it difficult to build political consensus on a Doha deal that does not include major concessions by emerging economies on ‘new’ market access for US businesses. At the same time, the US is reluctant to cede ground on its defensive interests.

4. Regional trade deals have emerged as a strong counterpoint to the multilateral process. Proponents argue that they are easier to conclude more closely reflect trading realities and serve multiple objectives. The remarkable and rapid integration of the east Asian economies illustrates how regional initiatives can lead to substantial improvements in competitiveness.

5. For many developing countries, issues that concern their poor such as food security and commodity price volatility are high on their negotiating priorities. There are deep divisions on such issues within the WTO and strong outcomes are unlikely.

The cumulative impact of these developments is waning global support for the round from business and other interests. That is a shame because on the basis of the results so far, it can safely be said that this round has more to offer than any previous round in terms of market access in all areas, reduction of distortions in farm trade, stronger rules to ensure fairer trade, new disciplines on trade facilitation at the border, etc. The outcomes will significantly enhance global trade flows and make them more predictable and transparent.

The impasse has raised questions on the WTO’s role in a changed global economy. It is obvious that the WTO can no longer be the central platform for trade liberalisation taking place around the world. Instead, it must focus on capturing this liberalisation through multilateral bindings. It also has to focus on areas in which regionalism cannot deliver, by developing global rules. It is unproductive to think of regionalism and multilateralism as binary opposites. Their complementarities have to be explored, and the WTO has to multilateralise regional liberalisation.

**Regionalism and multilateralism are not binary opposites. The WTO has to find a way to multilateralise regional liberalisation.**

It is clear that even with the best political will (in June 2011) Doha Round cannot be concluded in 2011. It cannot be deferred to next year either because, in 2012, the US will be busy with presidential elections and China with the leadership transition after the 18th Party Congress. The only realistic strategy is to identify less controversial issues for closure this year, keeping the more contentious ones, such as market access issues, aside for continuing consultations. Selecting the less difficult issues for early completion would not be easy but, given the necessary political commitment, this can be achieved.
The next few months will be a defining period for Doha Round and for the WTO. Unless, it can find a way out of the hole it has pushed itself into, the WTO faces a deeply uncertain future. It is also unrealistic to expect the tired, crisis-ridden economies of the US, Europe and Japan to provide the leadership to steer the WTO in this difficult phase. Emerging economies of Brazil, China, India, Indonesia, Mexico and South Africa acting in concert with other like-minded countries will have to step in with a vision of what kind of organisation the WTO should be in future in order for it to be able to address the challenges of the 21st century.

WTO Panel Seeks Talks on New Issues

But Report does Not Find Favour with India

A panel appointed by the World Trade Organisation (WTO) Chief Pascal Lamy on 24-4-2013 recommended sweeping changes, including special treatment for developing and poor countries, pushed for inclusion of new issues such as investment, currencies and climate change in the multilateral body’s programme, besides reiterating the need to conclude the Doha Round talks.

It has also suggested that the existing system of across-the-board flexibility to developing and poor countries be replaced with a needs-and-capacity-based approach that could be time specific. This may result in countries such as India getting the same treatment as the developed countries. Indian officials immediately attacked the report saying it is not in the country’s interest. “It is not WTO’s report. It is WTO director general’s (Pascal Lamy) report. We will oppose thee proposals,” said an official. Others too, opposed the move with some going to the extent of accusing the panel of pushing the rich nations’ agenda.

Lamy, however, backed the suggestions. “It offers food for thought to members on what they should do in the medium to long-term.” If the recommendations are accepted, the bilateral trade deals, which have mushroomed in recent years as the Doha Round talks have made little progress, would be impacted. “The multilateral system will remain deficient until a real set of disciplines is established to facilitate convergence of PTAs (preferential trade agreements) with the multilateral trading system,” the report said.

In other words, it could mean that countries such as India that cut import duty on cars or wine and spirits under a trade pact with, say the European Union (EU), would allow the import of the products on payment of same customs duty from all WTO member countries. The change in the trade architecture is meant to check PTAs becoming the dominant way of doing business. After all, there are 300 such agreements that the 159 WTO members have signed and several are under negotiation. On an average, any member belongs to 13 separate PTAs and is negotiating at least one agreement.

For Indian policymakers, the new issues that are currently “no go” areas are a bigger concern. The panel has given a list of nine areas – competition policy international investment, currencies, trade finance, labour, climate change, corruption and integrity, Aid-for-Trade and international economic rules that it believes are relevant to the global trading system. Some the of the developed countries such as EU members had earlier tried to get subjects such as competition, investment but had to back off.
India Cut Duty on Singapore Imports

539 products covered under the agreement

On 20-12-2007, India decided to reduce or eliminate duties on the import of 539 products from Singapore, a move aimed at expanding trade between the two nations.

India and Singapore had decided to amend their Comprehensive Economic Co-operation Agreement (CECA), to make the duty changes, the Commerce Ministry said in a statement in New Delhi. Duties on 307 products eliminated in five equal cuts between 15th January, 2008, and 1st December, 2011. The 307 products include base metal, excluding gold and platinum w.e.f. Feb. 2013 machinery and mechanical appliances, chemicals and textiles.

India will eliminate duties in nine equal cuts on 97 other products and cut duties to 5% for 135 products by December 2015. The Comprehensive Economic Co-operation Agreement was signed by Singapore’s Prime Minister, Lee Hsien Loong and his Indian counterpart, Manmohan Singh in June 2005.

Since then, Singapore’s exports to India rose 26.5% to $3.4 billion in the fiscal year 2006 and 63% to $5.5 billion in 2007.

(i) European Economic Community (EEC): The European Economic Community, also referred to as the European Common Market (ECM), came into being with the Treaty of Rome, signed in 1957 by six countries of Europe, viz., France, Germany, Italy, Belgium, Holland, and Luxembourg. The treaty provides for free movement of goods, persons, services and capital among the member countries, and has led to the establishment of a Customs Union amongst them, in order to correct the disequilibrium in the balance of payments. The members have abandoned separate external tariffs amongst themselves and the Customers and Economic Union so created, is by implications a political association, a block of non-communist countries of Europe.

There was much speculation about the future of India’s trade with the United Kingdom, that it should the latter prefer to join the Common Market, since Indian exports entered the U.K. without any tariff or quota restriction by virtue of the Indo-British Trade Agreement of 1939. However, the U.K. joined the Community in January 1973, thus terminating the trade agreement with India.

(ii) UNCTAD: The letters stand for the United Nations Conference on Trade and Development. This is a forum of the United Nations Organisation, aiming at international economic co-operation in the areas of trade and aid. The Conference has a permanent organ, The Trade and Development Board, by way of its executive body. The UNCTAD is held every four years to seek ways to end disparities between the rich and poor nations. Total numbering 192 as on 31.1.2012. There have so far been four conferences — the first at Geneva from March to June 1964; the second at New Delhi in February-March 1968; the third at Santiago, Chile, in April 1972; and the fourth at Nairobi in May 1976. So far, the success of the conference in achieving its objects has been very limited Bilateral Free trade agreements held in Brueks Bmsels on 6.12.2007 between India and European Union.

Main Activities of UNCTAD

1. Trade and Commodity for diversifying production
2. Investment technology and Enterprise development to familiarise governments with investment environment
3. Macroeconomic policies, debt and development financing for providing computer based debt management and financial analysis.
4. Transport customs and IT in building training networks and organising training in all areas of international trade.
5. Special Programmes for least developed land blocked developing end small is and developing countries is exacquing the links between development strategies and portlyy reduction.
(iii) **OPEC:** The letters stand for Organisation of Petroleum Exporting Countries. The organisation, which consists of Iraq, Iran, Saudi Arabia, the U.A.E., Kuwait, Algiers, Libya, Nigeria, Indonesia, Venezuela, Equador, etc., aims at protecting the interests of the member countries by controlling the prices of petrol and petroleum products.

These countries export oil and in return import consumption goods, capital goods, raw materials, etc., from the countries which buy oil. But for reason such as the fall in the value of the dollar, rise in the prices of commodities in oil-importing countries, etc. — the real income from the export of oil, the OPEC countries contend, has considerably declined. To make up for the erosion in their real income, they have suggested that the prices of oil be linked to the prices of 20 to 30 key commodities, which they need to import from the oil-importing countries; these have been termed index-linking of prices.

The prices of oil have been raised several times, and the price rise has hit the importing countries very hard, particularly the developing countries like India. The short-term effects of the pricing policy on India has been the high cost of imported oil, which has resulted in disequilibrium in her balance of payments. India has, therefore, been compelled to intensify her oil exploration efforts, as she has done in Bombay High, with a view to minimising her need for importing oil but ever than 80% crude oil is imported in India.

(iv) **Petro Dollars:** The recent rises in the prices of oil in January 2008, have led to a huge accumulation of currencies at the disposal of the oil-exporting countries of Western Asia and other places. The surplus currencies have been invested by the owner countries, many of which have linked their own currencies with the US dollars, in deposits with American banks and/or in shares in multinational concerns in the U.S.A. Such deposits in dollars in the U.S.A. are referred to as oil or petro dollars.

The petro dollars are used by the U.S.A. to finance the development programmes of the West Asian countries which, in turn, use them to make payments for their imports from the U.S.A., while the U.S.A. again uses these dollars in purchasing oil. Thus, petro dollars are in circulation over and over again.

These dollars may be made available to the deficit countries to help them tide over difficult periods

(v) **Asian Clearing Union:** The Asian Clearing Union (ACU), was established on 9th December, 1947, with the Reserve Bank of India, the Bangladesh Bank, the Bank Markazi of Iran, the Nepal Rastra Bank, the State Bank of Pakistan and the Central Bank of Sri Lanka and Myanmar as the founder members. The Union of Burma Bank joined the Union in April 1977. Its head quarters is at Teheran, Iran, and its operations are conducted by a Board of Directors and a Manager.

The Union has been established with the following objects:

1. To facilitate payments for current international transactions within the ESCAP (United Nations Economic and Social Commission for Asia and the Pacific) region;
2. To reduce/eliminate use of extra-regional currencies to settle transactions by promoting the use of the participants’ currencies;
3. To effect, thereby, economies in the use of foreign exchange and a reduction in the cost of making payments for such transactions; and
4. To contribute to the expansion of trade and promotion of monetary co-operation among the countries of the area.

The Union is a mechanism for settlement of payments on a multilateral basis between the participating countries, i.e., Bangladesh, Myanmar, India, Nepal, Pakistan, and Sri. Lanka, providing thereby a partial solution to the two major payments problem experienced by these countries, viz., foreign exchange shortage and inconvertibility of their currencies. The clearing operations, which were originally optional, commenced on 1st November, 1975.

In the beginning, the transactions routed through the ACU, used to be settled by the Central Banks of the member countries. Since 1st October, 1980, the settlement is being done by the banks authorised to deal in foreign exchange in those countries. These banks can open/maintain accounts with/on behalf of their correspondents in the member countries in Sri Lankan Rupee, Pakistani Rupee, Iranian Rial, Myanmar Kyat and Bangladesh Taka. These accounts designated, ACU Clearing Accounts, are kept
distinct from other accounts. The funding of, and disposal of surplus balances in these accounts, are to be arranged through the respective Central Banks.

All instruments of payment, such as demand drafts, mail and telegraphic transfers, bills of exchange drawn under irrevocable letters of credit, should be expressed in the currency of either of the participating countries. There is, however, no bar to making contracts in any international currency by the exporters or importers in the member countries.

(vi) So far as India is concerned, all eligible payments between India and the other member countries except Nepal are required, since January 1984, to be settled through the ACU. The payments, excluded from settlement through the ACU are the payments on account of:

1. Travel,
2. Contracts made under loans from an International Financial Institution like the World Bank,
3. Export/import transactions under bilateral lines of credit between the Government of India and that of any other member country, and
4. Deferred payments facilities extended by one member country to another member country.

Payments between Nepal and India are not eligible to be settled through the Union.

A Memorandum of Procedure (ACM), to be followed by the designated banks in India, for the purpose of handling the transactions to be cleared through ACU, has been drawn up by the Reserve Bank, even though the Exchange Control Regulations for the time being in force govern the payments and receipts cleared through the Union. An application for remittance is in payment of goods imported, and on Form A2, if the remittance is for any other purpose.

The accounts of the ACU are kept for settlement purposes in a common unit of account designated as the Asian Monetary Unit (AMU). The value of one AMU is equivalent to one Special Drawing Right (SDR), as valued from time by the International Monetary Fund.

There were till the end of November 1983, two accounting periods for the settlement of ACU transactions in every calendar month: first to fifteenth was the first period and sixteenth to the end of the month was the second period. Since 1st December, 1983, the accounting periods are three: (i) from the first to tenth, (ii) from eleventh to twentieth, and (iii) from twenty-first to the last date of the month. Settlement was, and still is, to be made at the end of each two-monthly settlement period. At the end of a settlement period, each participant is notified of its net position and accrued interest, and of the amounts it will have to pay to, or receive from, other participants. Payments are to be made in US dollars, or in any other mutually acceptable currency, within four working days of the receipt of the notice. Accordingly, receipts and payments channelled through the ACU are deemed to have been received or paid in US dollars or any other convertible currency.

Non-residents of Indian nationality or origin, working or residing in any member country, except Nepal are eligible for the facility of remittance relating to Non-Resident (External) (NRE) Account through the ACU. This account can be funded by remittances in any permitted currency, or in the currency of the country from where the remittance originates, or in Indian Rupee out of the Rupee balance held in an account of a bank, in any erstwhile country in the External Group.

On receipt of a remittance in ACU currency, the Rupee equivalent thereof, is to be worked out at the bank’s appropriate buying rate, based on the Reserve Bank’s rate for buying the currency from it. In this case of an FCNR Bank account, the Rupee equivalent worked out as above should be converted into Pound Sterling or US Dollar, as the case may be, at the bank’s TT selling for the currency.

A withdrawal from either of these accounts or repatriation of the fund held therein is permitted when done in the manner prescribed for these accounts. When the repatriation is desired in an ACU currency, the procedure prescribed for settlement of transactions passed through the ACU should be followed.

The Reserve Bank purchases spot, and forward for delivery up to six months on monthly option basis, the currencies of the countries participating in the ACU (except Nepalese Rupee), to enable the participants to dispose of the surplus balances in their accounts in these currencies accumulated as a result
of transactions cleared through the ACU, and to give forward cover facilities to exporters in these currencies.

The Reserve Bank sells only spot (and not forward) the participant’s currencies (except Nepalese Rupee), for funding the accounts maintained in the countries concerned. The banks can quote their buying and selling rates for the currencies, by loading the prescribed margin to the Reserve Bank’s spot and forward buying rates and spot selling rates.

The benefits accruing from the ACU are:

1. Appreciable savings of the liquid foreign exchange reserves for some of the member countries, derived from the multilateral settlement of the net position of the claims arising over a period of time.
2. Reduction of the working balances (including short-term borrowings) in the foreign exchange, the banks in the member countries so long needed to maintain in London and/or New York for settlement of intra-regional transactions in Pound Sterling or US Dollars.
3. Elimination of the need for double conversion of currencies and thereby, savings in the cost of settlement; and
4. Curtailment of the time needed before for settlement of transactions by the elimination of the intermediary correspondents in London or New York.

Pact would allow European car-makers to export their surplus capacity to India: SIAM

Indian automakers fear that a proposed Free-Trade Agreement (FTA) between the European Union and India could end up benefiting European carmakers at their expense, Society of Indian Automobile Manufacturers (SIAM) says.

“We are of the opinion that a free-trade agreement with EU would allow a one-sided advantage and allow the European auto industry to export their overcapacity to India,” says SIAM president S. Sandilya.

The current talks with EU centre on a 50% reduction of tariff of all cars from 60% import duty to 30%. Additionally, a quota of big cars of over 1500cc is also being negotiated that may allow EU to export these vehicles at 10-15% duty to India.

The industry is concerned that free import under reduced tariff may allow India to became a big lucrative market of cars made in the EU. In 2011-12, the Indian automobile industry achieved a turnover of `2,64,000 crore, of which vehicle exports revenue was around `32,000 crore.

Automotive trade, already favours the EU. In 2010-11, EU exported $3.4 billion worth automotive products to India including $400 million worth of Completely Built Units (CBU) of car. According to government data, the rest were Completely Knocked Down cars (CKD), unassembled cars are classified as auto components that are tooled in small factories into fully built cars.

In the same year, India exported cars worth $1.7 billion to the EU. A majority of these were hatchbacks. It did not export any CKDs. The difference between the two countries is that India’s exports to the EU are limited to small cars with an average price of €6,000-7,000 each, while the cars being exported by the EU are large luxury sedans & SUVs, each costing €20,000 and above.

Analyst’s tracking the sector say this difference loads the trade hugely in favour of the EU even without the FTA being operational. “If duties on car CBUs are reduced under the FTA, this trade imbalance in favour of EU will be further enhanced at the cost of domestic production and value addition,” says Deepesh Rathore, India MD of Delhi-based automotive think thank IHS Global Insight.
The auto industry accounts for 4% of the country’s GDP and employed 13 million people in 2005. The government’s 10-year Automotive Mission Plan aims to bring this up to 10% of the GDP and 25 million additional jobs by 2016. In comparison, Germany has 22% of GDP coming from its auto industry.

Automakers fear the ongoing FTA negotiation may impact future investment and employment generation. Already French carmaker Peugeot Citroen has pulled off its 4,000 crore investment from India looking to directly import cars under the FTA route.

Currently, each locally manufactured car in the country generates employment for 13-15 people, while CKD operations where components are assembled into a vehicle, employ 4-5 people. Employment in logistics, sales and service of these vehicles is additional to these figures.

“If we follow this local manufacturing that has made India today the sixth largest car manufacturer of the world, we have the potential to become the third largest car manufacturer by 2020 and the world leader in small cars by then. This could become a distant dream, if lower tariffs shift our core manufacturing out of India,” Sandilya warned.

SIAM, which represents 40 automotive vehicle and engine manufacturers in India, wants all CBU and engines to be kept in India’s negative list as was the case in earlier FTAs with Japan, ASEAN and South Korea.

1.10 MOST FAVOURED NATION (MFN) CLAUSE

This is a clause which is included in a commercial treaty between countries, for the purpose of extending concessions in trade to each other’s products. The essence of MFN is that if a member country gives tariff concessions to another member country, then the same concessions become applicable to all other member countries. Pakistan has been given MFN status by India in the year 2012 but Pakistan has not reciprocated even in 2015.

According to WTO principles, a member – nation of WTO must give the same most favourable treatment with respect to tariffs and related matters to other members, which it gives to any other member country. This non-discriminatory treatment ensures that any tariff reduction or other trade concession is automatically extended to all contracting parties of the WTO. However, there are some exceptions to the MFN principle:
(a) **Grandfather Clause:** Article 1 (2) permits contracting parties to continue with the preferences received or granted under different arrangements, which were in existence price to the formation of GATT. But, it prohibits any change in the margin of preferences granted or received. For example, the USA preferences to Philippines fall under this category as also Common Wealth Preferences. (b) **Customs Union and Free Trade Areas:** Article XXIV provides for the formation of Customs Union and Free Trade Areas. As per this clause, nations of the world (total nations as on April 2013 are 193) are allowed to form Customs Union and Free Trade Zones.

### 1.11 EURO MONEY

Euro money is a monetary system of eleven European countries, which started its functioning, since January 1999. This is the third strong currency after dollar (US). This is the money against which there is neither gold backing nor any natural Government. From January 2002, currencies of all eleven countries are converted into Euros. The 17 countries to such joint efforts are Italy, Germany Austria, Belgium, Finland, Ireland, Luxemburg, the Netherlands, Portugal and Spain and the other 5 mentioned nations which have not yet joined the Euros, due to economic and political reasons are, Great Britain, France, Denmark, Egypt and Sweden.

Conditions for this agreement are:
1. The countries have to keep their Budget deficit, below 3% of the Gross Domestic Product (G.D.P.).
2. Countries should have Government debts below 60% of G.D.P.
3. Inflation should not exceed 1.5%.
4. Rate of interest should not be more than 2%.

**Advantages to India:** India’s 80% export business is in US Dollars and European Union is having 20% share in exports of India, the cost of transactions to Indian exporters.

**Advantages to the World:** Euro would become very strong currency in the world economy and the world would be set free out of the influence of US Dollars. Looking to the number and economic progress of Euro, it would be weighy on Japanese Yens and US Dollars.

### 1.12 METHODS OF FOREIGN TRADE

Foreign trade may be carried on, that is, goods may be traded between the exporter and the importer, in any of the following three ways:

1. **On Open Account Basis:** This means that the goods may, where the credit status of the importer is high, be sent direct to him in expectation of payment in due course on presentation of the relative documents through a bank. Exports on this basis are not permissible in India.

2. **Bill of Exchange:** The exporter may draw bills of exchange on the importer for the value of the exports and collect the bills through a bank.

3. **Letter of Credit:** The exporter may agree to export the goods only against a letter of credit opened in his favour.

### 1.13 BANKING FACILITIES

To Indian merchants and manufacturers already engaged in, or intending to enter, foreign trade, banks can render assistance in a number of ways. For instance, to exporters and importers in India, a banker can provide the names, addresses and status reports as to the credit-worthiness and the ability to fulfill contracts of overseas buyers and sellers of goods they want to export to or import from.

Secondly, when an Indian exporter or importer goes abroad on a business tour for purposes of export promotion through on-the spot studies of the taste and preferences of foreign buyers, or of the manufacturing, packaging and advertising techniques followed, or for personal contacts with foreign sellers for
concessional terms, the banker can give instructions to his correspondents in the countries concerned to render such help and advice as the exporter or importer may need abroad.

Thirdly, the banker may, where required, provide the names and addresses of foreign firms and organisations which may be interested in joint ventures in India.

For importers in particular, the banker can collect import bills drawn on them and arrange remittances abroad in payment thereof. He can, if the overseas suppliers so demands, open on behalf of the importer, documentary credit in favour of the supplier, and arrange payment through his correspondent in the supplier’s country on presentation of the sight draft drawn under the credit, provided that the draft is accompanied by the relative shipping documents and other terms of the credit are complied with. If the importer fails to honour the import bills drawn under an L/C on presentation, the banker may grant credit to him by clearing and storing the goods imported and allowing partial deliveries against part payments. Or if the terms of the credit so stipulate, as in the case of a deferred payment credit, the banker may accept bills drawn under it on behalf of the importer and honour them on due dates, whether or not the importer deposits funds for such payments, and provide such exchange cover as is needed.

To exporters, the banker may render agency services by collecting their foreign bills covering the exports made by them and realising the process thereof in due course. He may allow packing credit to them to enable them to procure or manufacture the goods for export, and then on the shipment of exports, may extend short-term, post-shipment credit by negotiating the export bills. He may also extend medium or long-term export credit facility to an exporter by furnishing, on his behalf, financial or performance guarantee to foreign suppliers or Governments, or by executing bid bonds in favour of tenders-inviting foreign Governments or other authorities.

The banker may also provide to importers and exporters, information about exchange control regulations, import licence procedures to be followed, etc.

### 1.14 ROLE OF EXIM BANK

Various facilities offered to exporters/buyers credit/suppliers credit.

**Definition and Functions:** Export-Import Bank of India, is a public sector bank, established on 1st January, 1982, with the authorised capital of ` 2,000 crore and paid-up capital was ` 949.90 crores as on 31.3.2006 while Reserves were ` 1,77,030 crore. The object of establishing this bank is for providing financial assistance to exporters, facilitating, promoting foreign trade of India by co-ordinating the working of institutions engaged in financing export and import of goods and services, with a view to promoting the country’s international trade and for matters connected therewith or incidental thereto. It is also empowered to finance export of consultancy and related services, assist Indian Joint Ventures in the third world, conduct export market studies and provide international merchant banking services. EXIM Bank concentrates on medium and long-term financing.

The functions of the Exim Bank are:

1. To provide financial assistance to exporters and importers;
2. To act as the principal financial institution for co-ordinating the working of other institutions, engaged in the field of financing internal trade.
3. To undertake limited development and merchant banking activities in relation to export-oriented industries.

The important items of the Exim Bank are:

1. Granting loans and advances in and outside India for the purpose of export and import;
2. Refinancing loans and advances granted by banks and other notified financial institutions for export and import;
3. Re-discounting usance export bills of banks;
4. Providing investment finance to Indian companies towards their equity participation in joint-ventures established abroad; and
5. Granting obligations, jointly with banks on behalf of project exporters engaged in the execution of construction and turnkey contracts abroad.

To promote the exports of capital goods and projects on liberalised financing terms, the Exim Bank initiated in March 1983, two major steps by allowing:

1. Exporters to quote the price for orders on deferred payment terms in any hard currency, so that they may be more competitive in the foreign markets, and
2. Commercial banks to participate in export financing by only undertaking the risk involved in the contracts.

OBJECTIVES

The following objectives have been set up before EXIM Bank:

1. Granting Loans and advances in India, solely or jointly, with commercial banks to persons exporting or intending to export from India, goods including export of turnkey projects, civil construction services, etc.
2. Granting Loans and advances outside India as above.
3. Granting lines of credit to Governments, financial institutions and other suitable organisations in foreign countries to enable persons outside India to import from India goods including turnkey projects, civil construction contractors, other contracts and services, including consultancy services.
4. Issuing bid-bonds and guarantees and other similar facilities in India or abroad solely or jointly with the commercial banks, on behalf of persons exporting or intending to export from India, goods including turnkey projects, civil construction contracts or other contracts and services, including consultancy services.
5. Selling or discounting of export bills in the world markets.
6. Discounting of export bills negotiated or purchased by a scheduled bank or a financial institution or granting loans and advances against such bills.
7. Maintaining of foreign currency accounts with banks and correspondents abroad for purposes connected with the business of export-import bank.
8. Undertaking and financing of research, surveys and techno-economic studies in connection with promotion and development of international trade.
9. Providing technical, administrative and financial assistance to any exporter in India or any other person, who intends to export goods from India for promotion, management or expansion of any industry with a view to developing international trade.
11. Financing export of machinery and equipment on lease basis.
12. Granting of loans and advances to Indian Joint Ventures abroad.
13. Contributing to the bonds, debentures and stocks of a development bank or export bank of a foreign country.
14. Collecting, compiling and disseminating market and credit information in respect of international trade.
15. Opening Letter of credits (L.O.C) is different counties.

Supplier’s Credit: Under supplier’s or seller’s credit, funds are provided on deferred payment terms to Indian exporters of plant, equipment and related services which enable them to extend deferred credit to the overseas buyer. This programme covers project exports, which could be turnkey projects or construction projects.
The credit is provided by Exim Bank in participation with commercial banks where individual contract value is not more than ` 3 crore, banks may provide the credit and avail 100% refinance from the Exim Bank.

The exporter is desired to obtain an advance and down payment of atleast 15% of the contract value. Cash payment and deferred payments instalments, guaranteed repayment is secured by letter of credit as acceptable to Exim Bank. But where the importer is of a Government department or Public Sector Undertaking (PSU), a guarantee from the Government or promissory note is sufficient for the Exim Bank. In addition, to ensure regular release of foreign exchange by the Central Bank of the importer, a letter from the Central Bank of the concerned foreign country, giving an undertaking regarding prompt release of exchange towards the receivables may also be required.

The exporter is required to submit the projected quarterly withdrawal of the entire credit amount, well in advance of its utilisation. The Exim Bank will decide the withdrawal schedule and terminal date of its withdrawal, considering the delivery schedule under the export contract. The negotiating bank will submit all the disbursement requests along with copies, non-negotiable documents, required under the Letter of Credit (L.O.C). ECGC insures the exporters and in many cases, additionally, gives the guarantee to the negotiating bank.

**Buyers’ Credit:** Credit is extended by the Exim Bank to the buyers abroad to enable them to import engineering goods and projects from India on deferred credit terms. Similar to direct lending to exporters, the facility is to be secured by a letter of credit or bank guarantee or guarantee from the Government or promissory note from the Government. Exporters can be financed by any bank at the pre-shipment stage or post-shipment stage, by extending finance under pre-shipment packing credit facilities or by granting export bill discounting limit or negotiating export bills under post-shipment finance. Export trade also get financed under a buyer’s credit. In foreign trade, credit for long-term period is extended by the exporters, his banker to the buyer abroad, on his undertaking to pay the value of the goods being purchased by him, to the exporter in instalments at regular intervals within specific time say 3 to 5 years, etc.

Exim Bank directly enters into an agreement with the overseas borrower, outlining the terms and conditions of the credit covering the export contract.

**Various facilities to Exporters:** In addition to providing lending for supplier’s and buyer’s credit, following other facilities are provided by the Exim Bank:

1. **Consultancy and Technology Services Finance Programme:** Indian consultants, executing overseas contracts involving consultancy and technology services, wherein deferred payment terms need to be offered to the client, can utilise the facility. The credit will be extended by Exim Bank in participation with the commercial banks. The exporter is normally expected to obtain an advance/down payment of 25% of the contract value and remaining portion would be covered by credit under the programme. The currency of the credit would normally be Indian Rupees. Loans in other currencies can also be considered, if required. ECGC cover is also required to be obtained by the exporter.

2. **Overseas Investment Financing Programme:** Exim Bank provides financing, where an Indian company establishes a Joint Venture overseas and requires funds towards equity participation. The Joint Venture should have been approved by the Government of India, as well as the concerned authorities in the host country. Rupee funds are provided by the Exim Bank in the form of long-term credit, normally not exceeding 10 years. The equity shares issued to the Indian promoter are required to be pledged to the Exim Bank, together with a mandate/assignment in its favour, in respect of receivables arising from know-how/management fees, royalties, dividends, etc. on the investments. The Exim Bank may also stipulate as collateral security charges on the assets of the exporters.

3. **Pre-shipment Credit:** Credit is available to the eligible exporters to buy raw materials and inputs required to produce capital equipment that has to be exported. Exim Bank participates in the credit, if the requirement is for periods in excess of 180 days. Pre-shipment credit upto 180 days is available from the commercial banks.
4. **Export-Oriented Units (EOUs):** Units registered as 100% Export Oriented Units (EOUs) and units setup in Free Trade Zones (FTZ's) and Domestic Tariff Area (DTA) units, exporting of their annual sales are eligible for financial assistance from the Exim Bank for acquisition of land, building, plant and machinery and other miscellaneous fixed assets, along with margin money for working capital and preliminary/pre-operative costs. Re-finance is provided by Exim Bank in projects. There are two categories of exporting units firstly, 100% export-oriented units which get green cards for securing easy access to their inputs and secondly, units setup in the Free Trade Zones such as Kandla, Santacruz (Mumbai), Falta, Haldia (West Bengal), Chennai, Cochin and Noida (UP).

5. **Computer Software Exports:** Exim Bank is designated as an agency for facilitating speedy clearance and meeting foreign exchange requirements towards imports for computer software exports where export obligation of 35% of foreign exchange is undertaken. Exim Bank undertakes financial and technical analysis of software export proposals and monitors the progress of software exports. It arranges for clearance of imports and finance under one window.

6. **Export Marketing Fund:** Export marketing fund is a component of the World Bank Loan to India for industrial exports. Central Government has designated Exim Bank as the agency to manage the fund.

Private Sector Companies and Joint Sector Companies, who have the overall resources, capability, potential, top management commitment and an export strategy to penetrate and retain presence, particularly in the developed country markets and engaged in manufactured export or export of computer software are eligible for assistance. Activities eligible for assistance include desk research/overseas field market research/minor product adaptation/overseas travel/product inspection services/training/establishing overseas operations/travel to India by overseas buyers/front end promotional expenditure/research and development/equipment for plant modernisation/capacity expansion/tooling/Jigs and fixtures, and testing quality control equipment.

Finance is available in foreign currency up to 50% of the cost of the activity to grant finance.

7. **Export Product Development:** Under it, the firms undertake product development, research and development for exports.

8. **Project Preparatory Services Overseas:** Sectors which are considered include agriculture/agro industry/energy industry/water supply and sewerage/education/health. Maximum loan is `20 lakhs and grant is `10 lakhs.

**Assistance Terms and Conditions**

Exim Bank has been operating a lending programme for extending financial assistance to eligible industrial units, subject to the following terms and conditions:

1. The assistance may be direct in the form of a rupee term loan granted or deferred payment guarantee given by the Bank on its own account or in participation with a term-lending institution or a commercial bank, or it may be direct by way of refinance to a commercial bank providing finance to an eligible unit.

2. 100 per cent export-oriented units recognised as such by the Central Government or units in the free trade zones in India, either existing or to be set up, are eligible for the assistance for projects which call for capital outlay of over `2 crore. Commercial banks lending for projects costing up to `2 crore are eligible for refinance which will be 100 per cent of the loan granted.

3. The assistance rendered is usable for acquisition of fixed assets, such as land and building, plant and machinery, etc. for margin money, working capital, preliminary and pre-operative expenses, and/or for expansion/diversification of product or products.

4. No credit authorisation from the RBI or any reference to the IDBI is necessary.

5. The proposal is appraised in the light of the usual considerations, such as project viability, product marketability, etc. The usually acceptable debt-equity ratio of 1.5:1 may be relaxed in deserving cases.
Note: For a loan granted in participation no separation appraisal is made by the Bank, where the lending bank confirms that the project is technically, economically, and commercially viable and the borrowing unit has made firm arrangements for marketing their products overseas.

6. Interest is charged currently at the rate of 9% p.a., i.e., the rate applicable to the Bank’s supplier’s credits, on rupee term loans for acquisition of India-made plant and machinery, and at the rate of 12% p.a. when the loan is for acquisition of other fixed assets or imported machinery.

7. For refinance a spread of 1% p.a. is charged in favour of the lending bank where the effective interest charged by it does not exceed the Bank’s rate on finance provided directly.

8. For deferred payment guarantees, a guarantee commission at the rate of 1% p.a. is charged.

9. A commitment fee is charged on the undrawn loan amount during the availability period.

10. The loan is repayable in 10 years including the moratorium period.

11. The loan or guarantee is required to be secured by a first charge by way of mortgage/hypothecation of fixed assets supported, where considered necessary by the Bank, by personal guarantees of the promoters/directors.

12. Other conditions include promoter’s contribution of not less than 20 per cent of the project cost, appointment by the Bank of a nominated Director on the unit’s board of directors, monitoring of the composition of the unit’s board of directors, management set-up, payment of dividend, procuring/selling arrangement, etc.

13. The application for the loan or guarantee is to be made in the Bank’s printed form accompanied by a detailed project report, market survey report, and Government approval certificate where necessary.

14. Pending completion of the appraisal, a bridge loan, where necessary, may be granted.

15. Giving forfeiting service of export receivables to exporters without recourse to the Loan Portfolio reached to `65,563 crores at the end of 2012-13. LOC opened for $83.35 opened for $83.35 on dollars. At the end of 2012-13 Locs were available use for 75 countries amounting $8.57 bn dollars under 167 LOCs (ET 24.5.2012)

Total funded assistance under various programmes were given `1503.89 or in 2005-06.

1.15 FREE PORT/ FREE TRADE ZONE/ SPECIAL ECONOMIC ZONE

A free port is a port declared as such by the Government of the country in which it is located. At a free port, ships belonging to any country may load or unload cargo, without having to pay Customs or any other duties, barring of course the harbour charges. Similarly, an area or zone may be declared a free trade zone, with a view to getting the benefits of free trade with other countries.

There are no quantitative restrictions on imports into or exports from free port or a free trade zone. The imports into a free port or a free trade zone are, however, to be used within the port or the zone, any such import moving out to other parts of the country is subject to Customs Duty.

A free port or a free trade zone is also conducive to entrepot trade, i.e., imports not for domestic consumption but for re-export.

In India, the idea of establishing free ports or free trade zones was first mooted in 1957, by the Exports Promotion Committee. The objective was stimulation of exports. Manufacturing concerns situated in a free port or free trade zone will get the advantage of duty-free imports, such urgently needed things as capital goods, components and raw materials for end-products for exports, and in consequence, may be in a position to offer better terms of trade to the foreign buyers of their manufactures, achieving in the process increased exports. No doubt, exporters of certain specified goods residing in other places of the country get the benefit of cash assistance by way of refund in part or in whole of the import duties paid for raw materials for exports, but this involves initially a larger working capital and there are also procedural delays in getting the refund.
At the moment, there are two free trade zones in India, one at Kandla in Gujarat and the other at Santacruz in Mumbai. The Kandla Free Trade Zone (KFTZ), is the first such zone and till date the only multi-product processing zone in India. The facilities that the Government of India has extended to Kandla zone consist of:

1. The introduction of an OGL for the import of capital goods, raw materials, components, tools, jigs, fixtures, gauges, etc.
2. The provision of finance at concessional rates of interest, and
3. The exemption from Gujarat sales tax on sales made within the zone.

The Gujarat Housing Board has allotted 92 tenements to industrialists in this area and the number of units operating there is over 40 now.

The Electronic Export Processing Zone (SEEPZ) at Santacruz, Mumbai has had about 30 units set up in its area engaged in producing 100 percent export-oriented electronic equipment, components and consumable durables, such as radios, TV sets, integrated circuits, semi-conductors, remote control, X -ray equipment, etc.

Total number of SEFZs approved till oct. 2010 were 579 out-of which 54 SFZS approved were denotified during last 2 years. In sept. 2012 there ere 231 operational SFZs were in the country. And total software Technologies park number in Sept 2012 was 52 and their share in GDP was 7.5 %.

**Time to Make SEZs Attractive**

The government proposes to modify the special economic zone policy following increasing requests for SEZ denotification by developers who cite poor interest from exporters non-availability of skilled labour force and taxes. A look at SEZs’ share in total exports:

**While India’s exports grew 2.2 times during FV08-12, SEZs’ contribution increased more than five-fold....**

**Contribution of SEZ exports in total exports (FY08-FY13)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Exports (₹ Lakh Cr)</th>
<th>SEZ Exports (₹ Lakh Cr)</th>
<th>% SEZ Share (In brackets)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>6.56</td>
<td>0.67 (10.16)</td>
<td></td>
</tr>
<tr>
<td>2008-09</td>
<td>8.41</td>
<td>1 (11.86)</td>
<td></td>
</tr>
<tr>
<td>2009-10</td>
<td>8.46</td>
<td>2.21 (26.1)</td>
<td></td>
</tr>
<tr>
<td>2010-11</td>
<td>11.43</td>
<td>3.16 (27.64)</td>
<td></td>
</tr>
<tr>
<td>2011-12</td>
<td>14.54</td>
<td>3.64 (25.07)</td>
<td></td>
</tr>
<tr>
<td>2012-13</td>
<td>11.53</td>
<td>3.53 (30.63)</td>
<td></td>
</tr>
</tbody>
</table>

Yet, developers want to shut shop. It appears the Initial euphoria has fizzled out as the 2008 crisis worsened. No wonder the Board of Approval for SEZs approved 54 requests for denotification in the last two years.

Maharashtra Government has approved in Jan. 2013 a new Industrial Policy that allows investors in SEZs to convert these projects into Integrated Industrial Areas (IIA). Under this scheme, 60% of land must be used for primary production and the remaining 40% can be used for residential or commercial or allied purposes. In Maharashtra State, out of 146 SEZs notified only 17 are operational and 22 have been denotified.
Government Relaxes Norms for SEZs

Government made the special economic zones attractive for the investors by notifying relaxations in the minimum area requirements and easing the exit clause for developers on 12-8-13. In line with the announcement made by the commerce and industry minister in April 2013 the amendment in SEZ rules will allow SEZ developers to add one product category on each additional 50 hectares of land.

There will be no minimum area required for IT SEZs, but only a minimum built up area of 1 lakh square meters for the top-7 cities, 50,000 square meters for the next 15 cities and 25,000 square meters for the rest of the cities. “The idea is to give incentives to push these IT SEZs out of the big cities and explore the less dense cities.”

Multi-product SEZ’s minimum land requirement has been cut to 500 hectares from 1,000 hectares. Single product SEZ’s minimum land requirement has been cut to 50 hectares from 100 hectares. Multi-services SEZs will be treated on a par with single-product SEZs, with the minimum area being slashed to half from 100 hectare. This will allow multi-product SEZ developers with a minimum land requirement of 500 hectare to set up multi-services SEZ on an additional 50 hectare of land.

For SEZs to be set up exclusively for electronics hardware, agro-based food processing, biotechnology, handicrafts, the minimum area required will be 10 hectares.

Agro-based food processing SEZs are being introduced following demands by the agrarian states. SEZs allow duty-free imports or domestic procurement of goods and also provide 100% income tax exemption on export income for SEZ units for the first five years.

Positive Note
1. Amendment in SEZ rules will allow developers to add one product category on each additional 50 hectares of land
2. Multi-product SEZ’s minimum land need has been cut to 500 hectares from 1k hectares

Govt Plans Financial Centres within SEZs

Work in Progress center will offer services such as offshore banking, derivatives, currency trading as well as insurance and reinsurance

The government will soon put in place a framework for setting up of international financial centres (IFC) in the country, in an effort to capture some of the market for high-end financial services to Indian companies, an area in which the likes Singapore and Dubai tends to dominate.

These centres would be set up within special economic zones (SEZ). “We are working on the framework. Rules and regulations are in the works. An announcement is expected shortly,” said a senior government official. Essentially, international financial centres will offer services such as offshore banking, derivatives, currency trading as well as insurance and reinsurance.

“The RBI, Sebi and IRDA are working on rules required for international finance centres. These rules should be issued in a couple of months,” said Ramakant Jha, managing director and group CEO, Gujarat International finance Tec City
(GIFT), an upcoming finance hub. The commerce department and the finance ministry are also working on the framework that could be unveiled soon.

“We have proposed the RBI to change some guidelines around allowing offshore banking and currency convertibility at the GIFT city. This would require separate regulations as well as exemptions from the regulator inside GIFT,” said Jha.

“We hope a new set of guidelines by April 1 this year from the RBI as well as SEBI, If this happens we will see international exchange being operated from GIFT as well,” he added.

The government is also looking at changes to the taxation structure to facilitate creation of such centres that would provide listing platforms, banking and other financial services. These centres are expected to bring down cost of services on the back of tax benefits available to zones.

The government is keen to attract foreign investment back into the country and also prevent export of Indian securities market by changing rules and regulations. Nifty futures, for instance, are traded largely in Singapore.

In his first budget, finance minister Arun Jaitley had raised concerns over fund managers shifting base to other countries and made changes in the tax regime to encourage them to shift base to India. Bombay Stock Exchange (BSE) has already signed an agreement with GIFT to set up shop there.

In 2007 a report by Percy Mistry, had recommended far reaching changes in India’s legal and regulatory architecture to make Mumbai an international financial centre.

The report called for India to capture a chunk of the market for high-end financial services. In the first stage, as per the report, Mumbai could connect India to global IFCs.

Later it could even aspire to compete with the likes of London by attempting to capture financial services beyond those required by Indian companies.

The government feels locating these financial hubs within SEZs will also give a leg up to these enclaves that were envisaged as zones akin to China’s famous special economic zones such as Shenzhen, which are central to that country’s export boom.

### 1.16 OFF-SHORE BANKING OPERATIONS

Off-Shore banking is an altogether new system of banking which has come into vogue. This system is operated through the off-shore banking units of overseas banks, established in off-shore banking zones, similar to free trade zones, in under-developed countries.

The off-shore banking unit of an overseas bank is required to maintain a certain base as well as a certain level of liquidity. It is precluded from entering into competition with the banks, or from raising funds from the residents, of the host country. The funds of the unit have to be brought in from the parent bank or from the overseas money markets.

The funds of an off-shore banking unit are employed in financing capital-intensive local projects or in turnkey projects undertaken in foreign countries by the exporters of the host country. The funds may also be utilised in manufacturing in the off-shore zone goods out of raw materials, components and technical know-how imported duty-free into the area, taking advantage of the comparatively low cost of trained manpower in the host country. The goods so manufactured may be taken back to the parent country or exported to other countries. The profits made out of such banking operations may be repatriated, usually tax-free, to the parent bank. The operations of an off-shore unit of a foreign bank are, it goes without saying, subject to exchange control regulations current for the time being in the host country.

Off-Shore Banking Units are at present operating at such places as Bahrain, Singapore, Hong Kong, etc. There are 20 centres throughout the world.

The benefits that the host country may derive from allowing the establishment of an off-shore banking unit of an overseas bank in its domain are:
1. Inflow of interest-free foreign capital into the country;
2. Supply of capital from foreign sources to capital-intensive local industries;
3. Earning foreign exchange by way of payment for services rendered in converting raw materials into finished goods, etc.
4. Exemption from minimum reserve requirements;
5. Low or non-existent taxes and levies;
6. Entry is relatively easy, especially for large international banks, in contrast to the situation in neighbouring countries, which may strictly limit or prohibit the entry of foreign banks;
7. Licence fees are generally low;
8. Close proximity to the important loan outlets or deposit sources.

As per the policy declared by the RBI in 2002, the branches of Indian Banks located in the Special Economic Zones (SEZ), are called Off-Shore Banking Units, and are treated as foreign branches of Indian Banks located in India. Off-Shore Banking units would also be set up in all SEZs for the promotion of SEZ, as well as to cater to the needs of units located in SEZs.

The banks operating in India, both in the public or private sector as well as foreign banks, authorised to deal in foreign exchange, are eligible to set up Off-Shore Banking Units.

The banks having Off-Shore Banking Units have been exempted from maintaining CRR (4% w.e.f 4.4.2013) and SLR (21.50% w.e.f. 6.2.2015), on the business figures of these off-shore banking units. However, the Know Your Customer (KYC) guidelines (new KYC guidelines has been implemented from the year 2013) and the provisions of the Anti-Money Laundering Act is applicable to the off-shore banking units.

The sources for raising the funds would be only external. Further, these units will be allowed to deploy the funds by lending to units located in SEZ and the SEZ Developers. These units are also permitted to invest outside India. The Off-Shore Banking units set up in SEZs are also allowed 100% income-tax exemption for 3 years and 50% for next 2 years, under Section 80-LA of the Income-Tax Act, 1961.

Till the year July 2012, there were 584 approvals for Special Economic Zones (SEZs) in India. Some of these SEZs are located in Kolkata, Madhya Pradesh, U.P., Rajasthan, Gujarat, Karnataka, New Mumbai, A.P., Orissa, Kerala, Tamil Nadu, Jharkhand and Maharashtra State. Total sanctions till July 2012, there were 584 SEZs in India, and operational.

SEZs till July 2012 were only 158 Tax incentives have been taken out from 2010-11 like M.A.T, dividend distribution Tax. No service Tax on units located in SEZs or developer of such SEZs from 2.7.2013.

The response from Indian banks to off-shore banking is positive, reveals the development of these banks in the last few years in the field of international banking. A number of banks including State Bank of India, Indian Overseas Bank, Bank of India and Bank of Baroda have set up off-shore banking units for deposit-taking and final lending at places like Bahrain, Hong Kong, Colombo, Cayman Islands, etc.

The total exports in SEZ’s during April to June 2012 were ` 1.18 Lakh Cores. The total exports in the year 2011-12 were $245.9bn.

**IBU International Finance Ltd.**

The IBU International Finance Ltd., the first-ever international financial organisation, sponsored by a corporation of Indian nationalised banks, such as Indian Bank, Bank of Baroda and Union Bank of India, was established in Hong Kong and started functioning, with effect from October, 1980, as a deposit-taking organisation with off-shore and other activities. The organisation is eligible to accept deposits of Hong Kong dollars 50,000 and above.

The Sodhani Committee on Foreign Exchange Reforms (1996), recommended for allowing Indian banks and financial institutions to set up off-shore banking units, as it would prove to be cost-effective for
local institutions. These units can offer many services, including managing funds raised by Indian corporates through GDR issues.

1.17 LIBOR

The word LIBOR stands for London Inter-bank Offered Rate, used in connection with the lending operations in the currency market.

Interest is charged for each interest period at the base rate plus the spread negotiated between the borrower and the bank, acting on behalf of the syndicated banks. The interest rate is adjusted every six months, in accordance with the changes in the base rate. Some loan agreements provide for a minimum loan rate to take effect when the LIBOR plus the negotiated spread falls below the pre-determined level, while some others provide for an increasing spread in the later years of the loan. The Libor Rate on 30-9-2008 was 6.88% due to financial crises in USA whik on 30.11.2007 it was 5.34% only

1.18 EURO CURRENCY UNIT (ECU)

1. At present, the ECU has been recognised from January 2002, as a foreign currency, officially by Italy, France, Belgium and Luxembourg and de facto by the United Kingdom, Eire, the Netherlands, and Denmark and of late, Japan has also recognised the ECU as a foreign exchange. The Reserve Bank of India has granted the ECU, the status of approved currency for the purpose of foreign exchange transactions. Banks in India can freely open accounts abroad, denominated in ECU.

2. The ECU is a currency basket composed, according to the 'open basket' formula, of the 12 EMS currencies plus Pound Sterling and Greek Drachma in the following proportions:

<table>
<thead>
<tr>
<th>Currency</th>
<th>Proportion</th>
</tr>
</thead>
<tbody>
<tr>
<td>French Franc</td>
<td>1.3</td>
</tr>
<tr>
<td>Pound Sterling</td>
<td>0.0878</td>
</tr>
<tr>
<td>Italian Lira</td>
<td>140</td>
</tr>
<tr>
<td>Danish Kroner</td>
<td>0.219</td>
</tr>
<tr>
<td>Greek Drachma</td>
<td>1.15</td>
</tr>
</tbody>
</table>

The composition is not fixed, and the component currencies are authorised to fluctuate within +/- 2.5 per cent, excepting the Italian Lira, which may fluctuate within 6 per cent. Pound Sterling is as yet outside this mechanism. The weights of the components currencies are determined by economic criteria, which are reviewed every five years. Any change in the composition of the ECU, automatically affects all existing contracts.

The value of the ECU is defined in each of the constituent currencies on the basis of an official parity or central rate. As the Pound Sterling and the Drachma do not belong to the EMS, they have been given a fictitious parity. The central rates are used to establish a chart of bilateral cross-rates between the ECU currencies, and the Central Banks of the EMS countries, other than the Bank of England and the Bank of Greece have agreed to enforce these bilateral rates, subject to variations of 2.5 per cent on either side (Lira 6 per cent).

3. The ECU being a basket of currencies, the borrowers get the benefit of protection from any brusque exchange and the interest rates movement. They can also have the benefit of raising substantial amounts of weak currencies not normally available in the international market. Another attraction of the ECU borrowing is that the borrower is isolated from the North American, Japanese, and Swiss exchange rates movement. Interest is payable on short-term ECULOA NS at a rate of 2.5 per cent below the US Dollar rate for a year-and-a-half.

There is also an inter-bank deposit market in ECU for ECU 10 billion or more, for maturities up to one year or more. There is also an extremely active exchange market in ECU throughout Europe. The ECU is quoted against US dollars and cross-rates are calculated against other currencies with very narrow
spreads. Invoicing in ECU has the distinct advantage of minimising exchange risks due to the spreading of the same over the 10 constituent currencies, and of availability of fresh buyers in the case of exports to, and of fresh sellers in the case of imports from, the ECU countries where the original buyer or seller, as the case may be, defaults.

**QUESTIONS**

1. Explain briefly the meaning of balance of payments. What methods would you suggest for correcting an adverse balance of payments?
2. Discuss the importance in India for banks to have recourse to Dollar/Euro-currency markets to finance imports of capital goods. Briefly describe the nature, functioning and scope of such markets.
3. “One of the OPEC countries had advocated that oil prices should be index-linked, preferably to the price of 20 to 30 key commodities.” Explain what you understand by OPEC countries and index-linked prices. Why do you think such a pricing is advocated? What would be the short-term and long-term effects of such a pricing policy on India?
4. Explain briefly the assistance an Indian exporter can obtain from banks and other financial institutions in India.
5. Write short notes on:
   - Terms of trade;
   - Bilateral Trade Agreements;
   - S.E.Z.
   - CIF Contract;
   - Euro-Money;
   - Balance of payments;
   - UNCTAD;
   - COMECON;
   - WTO;
   - EEC;
   - ACU.
6. What, if any, was the case for establishment of a separate Exim Bank in India, and what are your own views on the subject?
7. Mention some of the important components of India’s Balance of Payments. What role can India’s invisible exports play in achieving a better Balance of Payments position?
8. What are the common contract terms used in international trade? Explain the significance of these terms as far as they affect the buyer and the seller.
9. Discuss the pre-requisites for the establishment of an ‘Off-Shore’ Banking Unit in India.
10. Describe the role of the Exim Bank in financing the international trade of India.
11. Define visible and invisible imports and exports. Discuss — ‘Trade surplus does not necessarily mean balance of payments surplus.’
12. Discuss C.A.D.