REMOVING QUANTITATIVE RESTRICTIONS: COMPETE OR PERISH

JUSTIN PAUL AND A. RAMANATHAN

There has been continuing debate about the costs and benefits of globalization, not only on worldwide basis, but also in reference to specific countries, such as India. It is evident that there has been a significant advance in India's external integration compared with its past record. With the reduction in import tariff rates and with the removal of 'Quantitative Restrictions' on imports, industrial units in India have been facing completion and challenge from imported products. Small-scale industries in India find it difficult to catch up in the race for better market share. On the other hand, 'Import Liberalization' has paved the way to Global markets where the consumer's sovereignty rule in its real sense. Although theoretical foundation for the link between free trade and higher growth is not solid, it may lead to exploitation of scale economies through better capacity utilization of inputs. Free flow of imports has also been catalystic to reducing the price level of many commodities and forcing domestic companies to compete with the Multinationals.

Quantitative Restrictions (QRs) on imports in India, which took the form of industrial licensing, have been gradually removed since 1996, and substantially removed (715 items) on 1st April, 2000. Indian economy became fully integrated with the world economy, with the removal of Quantitative Restrictions on imports (Restricted List, Special Import License and Canalized List), took on 1st April, 2001. Since 1994, tariff reform has brought the simple average of all rates down to a level lower than 35 percent with most of goods having a ceiling of 35 percent duty from 71 percent in 1993-1994. The process of tariff reform and reduction is ongoing, which has been strengthened by various governments after the establishment of World Trade Organization in 1995.

Justin Paul is Assistant Professor, Narsee Monjee Institute of Management Studies, Mumbai
A. Ramanathan is Professor of Economics, Indian Institute of Technology, Mumbai

Research on the impact of globalization suggests that there are links between the increase in the volume of foreign trade and trade liberalization programmes. (Bhattacharya, 2001; Anand 2000, Paul and Ramanathan 2000). Nayyar (1994, 1997) has examined the nexus between trade and industrialization in India. George (2001) has analysed the impact of EXIM policy on the Indian economy and the impediments to foreign trade and the globalization process. Studies (Kumar, 2001; Paul, 2001; Kausik and Paras, 2000; Vasudeva, 2001) have been carried out to examine the changes in import tariff rates and structure, removal of Quantitative restrictions, foreign exchange reserves and Balance of Payment relationship and the impact on industrial sector. Nayyar (2001) has examined the nature and extent of the external openness of the Indian economy and the impact of the paradigm shift in India's economic policy on foreign trade, tariff levels, and foreign investment. It has been suggested that there will be a marginal increase in import demand as a consequence of removal of the Quantitative restrictions on 1429 items. On the other hand, some studies have been published showing the adverse impact of QR removal on selected small scale industries, particularly watches and clocks, plastics, toys, ceiling fans, and diary products (Krishna 2001).

Industrial Production, Exports, Imports, and Growth

Openness to foreign trade is one of the central tenets of the industrialization strategy. Industrial growth is a pre–requisite for economic development. Trade liberalization measures undertaken by India under the aegis of World Trade Organization is expected to have significant impact on the industrial production and growth. Even though many aspects of globalization – capital flows, labour standards, environmental problems etc have captured world-wide attention, the driving force behind the global integration has been liberalization of trade in goods and services. The benefits of trade liberalization can be analysed as follows: First, when tariffs are lowered, relative prices change and resources are reallocated to production activities that raise industrial output. Second, larger long–run benefits accure as economies adjust to technological innovation, new production structures, and changing patterns of competition. With the establishment of World Trade Organization on 1st Jan 1995, and its ongoing attempts to promote free trade, exports and imports have become dynamic factors in the industrialization of the developing countries.

The Indian industry has not performed very well over the past two decades. During the post – reform period (1991-2001), the industrial sector has gone through significant structural change that has been induced by a continuous process of economic reforms. However, the industrial growth rate slowed down to 4.1, 6.6, and 5.7 percent in the year 1998-1999, 1999-2000, 2000-2001 respectively. (See Table 1).

Table 1: Growth rates – industrial production, exports and imports (in percent)

Year	Industrial Production	Exports (in USD million)	Imports (in USD million)
1990 - 1991	8.2	9.2	13.5
1991 - 1992	0.6	-1.5	-19.4
1992 - 1993	2.3	3.8	12.7
1993 - 1994	6.0	20	6.5
1994 - 1995	8.4	18.4	22.9
1995 - 1996	12.8	20.8	28
1996 - 1997	5.6	5.3	6.7
1997 - 1998	6.6	4.6	6.0
1998 - 1999	4.1	-5.1	2.2
1999 - 2000	6.6	13.2	11.4
2000 - 2001	5.7	20.6	14.4

Source: Compiled from Indian Economic Survey 2000 – 2001 & 1998 – 1999

Removal of Quantitative Restrictions and Impact

Quantitative Restrictions that were imposed on imports of 1429 items, have been taken away in two stages and items have been placed with Open General License (OGL) list. Items placed in OGL list imply free import. Under the GATT, imports have to be controlled only through tariffs or customs duties and not through Quantitative Restrictions such as quotas, licenses etc. all member countries need to abide by its provisions.

Table 2: Foreign exchange reserves and imports in India

Year ending on	Total FOREX Reserves at the end of financial year (US$ billion)	Total imports during the year (US$ billion)
31st March 1993	9.8	21.88
31st March 1994	19.3	23.31
31st March 1995	25.2	28.65
31st March 1996	21.7	36.68
31st March 1997	26.4	39.13
31st March 1998	29.4	41.48
31st March 1999	32.5	42.39
31st March 2000	38.0	42.20

Source: Compiled from Handbook of Statistics on Indian Economy, RBI, Mumbai, 2000 & RBI Annual Report 2000 – 2001

There are, however, some exceptions to this rule. One such exception is that a country can take resource to QRs on grounds of Balance of Payments (BOP) difficulties. It is under this exception that India has been maintaining QRs. Till 1993, our BOP situation had been quite uneasy. Since 1994-1995, there has been steady improvement in our foreign exchange (FE) reserve position (See Table 2).

In fact, India had been autonomously removing import controls ever since the late 1980s when there used to be a fresh list of items allowed to be imported under OGL (Open General License) every year. This process gathered momentum during the period 1995-1999. QRs on as many as 6161 tariff lines (or items) were already removed as on 31st March 1996. Since then, 1905 tariff lines for imports had been made free until the beginning of the year 1999-2000. India had plans to remove all the Quantitative Restrictions on the imports by 2003, but the Government was forced to take away with all Quantitative Restrictions in 2001 itself, after a dispute settlement between India and United States.

With the removal of Quantitative Restrictions on imports into India, consumers benefit as they get a wider choice of goods and services at a lower cost. Secondly, free trade brings down prices and helps in keeping the level of inflation flow, which is to the advantage of the consumer. Thirdly, the Government also benefits from higher customs duties on imports (e.g., things which were being bought in the markets abroad and brought into the country through various other channels can now be brought through legal channels, thus generating revenue for the country). A case in point could be that of freeing of gold imports that has resulted in gold now being imported through legal channels, with Government earning substantial revenue through customs duty. Fourthly, it would lead to easier access to imported raw material and capital goods for the domestic manufacturers leading to faster industrial growth.

Finally, competition from imports can lead to upgradation in the quality of even domestic products and increased productivity leading to increased competitiveness of the Indian domestic industry, which could help in pushing our exports. This means value for money for the consumers and may help in placing the domestic industry on a stronger footing to face international competition and to become global players. In a sense, therefore, removal of QRs can be viewed as not only a challenge but also an opportunity for the Indian industry to initiate steps for enhancing their competitiveness, given the fact that we had no alternative except to remove Quantitative Restrictions.

Removal of Quantitative Restrictions will have impact on prices. When the movement is from regulated regime to free trade environment, imports increase and the market share of domestic producers tend to decline. With the increase in imports, there is a possibility of depressing the domestic prices to the advantage of consumers. Competition from imports can lead to an increase in the quality of domestic products. Indian industry has to be on a sound footing to face the competition from the rest of the world, especially from MNCs. A large number of companies may sink and an equally large number which are quality conscious and competent may emerge as leaders. In the agricultural sector, farmers may not be able to compete with the imports of Diary products. The implications of the removal of Quantitative Restrictions can be summarized as follows:

A large number of companies may sink and an equally large number which are quality conscious and competent may emerge as leaders. In the agricultural sector, farmers may not be able to compete with the imports of Diary products.

- Removal of QRs means that an item can be imported without import license.
- Applied duties (tariffs) can be raised upto the bound tariff levels, wherever necessary, to protect the interests of the domestic industry including SSIs and agriculture.
- Apart from import duties, other measures can also be exercised to protect the domestic industry such anti–dumping duties in case of dumping of imported goods and safeguard measures in case of a surge in imports.

Impact on Small Scale Industries

Presently small-scale units have a value of plant and machinery below rupees 25 lakh. Krishna's (2001) study based on interviews with the owners of small scale industrial units, mainly watches and clocks, plastics, toys, ceiling fans, ice cream and bicycles (these item were put on OGL on 1st April, 2000) show that many tiny and small scale units have closed their plants and are presently importing. An extract from his paper is listed below

> "All tiny and small scale manufacturers of time pieces, wall clocks, alarm clocks, and watches in India have given up manufacturing activities and instead they have switched over to importing 'watch movements', fixing glasses on them, and selling them in the grey market. According to the President, All Indian Electronic Watch and Clock manufacturing Association, one lakh smuggled 'watch movements' are being sold per day in Delhi alone. (A 'watch movement' is the basic machinery of the watch; and for all practical purposes, it is the watch minus the case and glass). Another phenomenon that has adversely affected the small scale industrial units was under invoicing of imports by fake units, ever since the watches and clocks were placed on the OGL list."

Similarly, plastics, was placed on the OGL list for imports in India on 1st April, 2001. This affected the domestic production of polymers and plastic products. No import of raw material was possible because of the high protection given to indigenous raw material (polymers) producers. The import duty structure on plastic products and polymers is 67.08 percent (basic duty 35 percent, surcharge on basic customs duty 3.5 percent, additional duty 16 percent, and special additional duty 4 percent, for a total duty of 67.08 percent). However, the plastic items including bags imported from China are about 30 percent cheaper than those manufactured in India. Plastic bag manufacturers in India cannot compete with China. Hence, many units have closed in the years 2000 and 2001 and some are on the verge of collapse.

All QRs on imports have been removed in India since April 1, 2001. though the competition from imports brings about quality consciousness, some industries are adversely affected as has been the case of plastics. Being a developing country, consumers are price elastic in India. Hence, the Government and industrial associations like Confederation of Indian Industry; Chamber of Commerce etc. will have to take some action selectively in certain industries to redress the situation and to revive manufacturing activities. India's increased openness and integration with the world economy have been important factors in explaining the healthy growth in exports, and foreign investment recorded in the 1990s. Though the industrial growth showed a remarkable increase in the mid-1990s, it has slowed down to new low levels in the last two years.

To sum up, the current scenario has the following three aspects:

1. Opening up of our markets for global entry sent a shock wave among certain business circles.
2. Many industrial houses and business units are trying to catch up with the global catch word: 'Globalize or Perish'.
3. Some industries have identified globalization as the ultimate process for evolving a new business pattern to match the ever changing and highly demanding market environment. They are optimistic in achieving economies of scale.

References

Anand, Mukesh 2000, *'Does Trade Liberalization Lead to Loss of Comparative Advantage?'* Paper presented at the Conference on Industrialization in a Reforming Economy, Delhi School of Economics, 20-22 December.

Bhattacharya b, 2001, *'India Comes of Age'*, *Yojana*, May, Govt. of India, pp 4 – 8 Chadha, Rajesh 2000, 'Exim Policy changes', *Economic and political Weekly*, Vol 35, No.6, April 15-21

George, Leena 2001, *'Impact of New EXIM Policy'*, *Yojana*, June, Govt. of India.

Kaushik K.K. & Paras 2000 *'Trade Liberalization and Export Performance in India: a Statistical Verification'*, Foreign Trade review, April- June 2000 (Vol: XXXV, No.1).

Krishna, Nayyar 2001,*"Phasing Out of Import Licensing, Impact on Small Scale Industries"* Economic and Political Weekly, July 7.

Kumar, Nagesh 2001, *'Economic Reforms and Their Macro – Economic Impact'*. Economic and Political weekly, Vol 35, No.10, pp 803-812

Mehta, Rajesh (2000): *"Removal of QRs and Impact on India's Import"* Economic and Political Weekly, May 6, pp 1667-71

Nayyar, Deepak Ed (1997), *Trade & Industrialization,* Oxford University Press, Delhi

Nayar, Baldev Raj (2001), *"Opening Up and Openness of Indian Economy"* Economic and Political Weekly, September 15.

Paul, Justin (2000), *"Globalization, WTO and Foreign Trade: Challenges and Opportunities"*, Discussion Paper No.6, NMIMS, Mumbai

Paul, Justin (2001), *International Business Environment*, NMIMS Publication, Bombay

Paul, Justin, Sebastian V.J. and Ramanathan A 2000, *'Trade & Industrialization: An Empirical Study'*, July-December 2000, Foreign Trade Review, Journal of IIFT, New Delhi, pp 15-21, Vol 35, No. 2 & 3

Paul, Justin and Ramanathan A 2000, *'Sources of Industrial Growth in an Open Economy'*, Paradigm, Journal of IMT Gaziabad, Vol 4, No. 2, pp 21-29

Vasudeva P.K. (2001), *'Is Small Scale Industry Ready for a QR-Free Regime?'*, Economic and Political Weekly, Vol 36, No.1 January 6, pp 22-24