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India's external sector during COVID-19

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India’s external sector has been a key component of the economic survey and in the current context of COVID-19, this chapter assumes importance. This chapter broadly presents India's trade pattern, a detailed account of the balance of payments, followed by the foreign exchange reserves, exchange rate and external debt and so on. This article is divided into three parts. First part presents the major trends in India's external sector as discussed in the economic survey is disused. In the second part, present the budget 2021-22 response to the observed trends in the economic survey and in the last part, some critical observations which have been missed in the survey and raises a few questions.

Sharp decline in India's merchandise trade

The global trade for the last few years shows a downward trend. There has been a concern of rising protectionist environment and growing tensions between the US and China trade. The COVID induced restrictions, both in terms of movement of people and movement of goods across the countries, had severe impact on merchandise trade. The initial estimates of the World Trade Organization (WTO) suggests that the impact of COVID on world trade could be as high as minus 32 percent. As the countries gradually eased the restrictions, the revised estimates of WTO in October 2020 shows that the world trade is expected to decline by 9.2 percent in 2020. The survey highlights significant regional variation in the COVID impact of trade. The effect is much severe for the advanced countries, especially in the US and other advanced European countries where the impact on exports is minus 12.2 percent. The striking feature is the resilience exhibited by Southeast Asian countries where export growth declined to two percent on account of the impressive performance of Vietnam, Taiwan and Malaysia. India on the other hand is one of the worst affected countries as the exports fell down to minus 16 percent in the first three quarters of 2020-21 (April to December). However, decline in imports outweigh the slow down in exports thus improving India's trade balance briefly.

The sectoral analysis of trade impact indicates a steep decline in non-petroleum oil and lubricants in the first two quarters of 2020-21 with some rebounding in Q3. Among all the traded commodities, drug and pharmaceutical products showed a favorable trade balance. The Survey carried out a very detailed analysis on the impressive performance of India's pharmaceuticals sector during the pandemic. It also shows that India's pharmaceutical sector’s share in the world has doubled in the last three to four years. Other commodities with favorable trade balance are textile, cotton fabrics and other agricultural products. On the other hand, the products which had a negative trade balance are crude petroleum, gold and electronic items, particularly the computer hardware and peripherals, and other a high-tech industry good like a craft and spare spacecraft parts.

Resilient service trade

The service trade remained relatively more resilient during the pandemic. The comparison of net service trade with Q1 and Q2 of 2019 to 2020 shows no severe decline despite a drastic decline in travel and remittances due to closure of borders and lockdown restrictions. This is because India's compositional net service is largely driven by the software exports which has not been severely affected.

Improvement in balance of payments: A short respite

The faster deceleration in merchandise imports as compared to exports along with resilient service trade improved India's current account balance. India has been having a 2.2% current account deficit for the last 10 years. But for the first time in last 16 years India shows a current account surplus in Q1 and Q2 of 2020-21. India's capital account improved on account of remarkable increase in the FDI inflows during April 2019 April to October 2020. The net FDI recorded an inflow of $27.5 billion, which is 4.8% compared to the last like first seven months of the previous financial year. The policymakers are coming to the conclusion that India is emerging as a favorable destination for FDI when the world is in crisis. However, India is not the destination for FDI as countries like Vietnam received much higher FDI during this period. In fact, it is Vietnam, which is attracting a lot of investment that is going out of China during the pandemic period. Favorable trade balance coupled with inflow of foreign investments has increased India's foreign exchange reserves making the country the fifth largest country in the world in terms of foreign exchange after China, Japan, Switzerland and Russia. Huge foreign exchange reserves provide a space for the government to invest in building the economy back from the crisis.

Budget 2021-22: Steps towards protectionism?

The response from the union budget to build a vibrant external sector is crucial for many reasons. India could aim at sustaining favorable trade balance by aiming at a rebuilding strategy that helps build competitive export sector. Especially, a strategy towards promoting domestic manufacturing and helping India upgrade in global value chains is need of the hour. The budget document leaves the reader a bit confused about the ideology of the government. In the context of Aatma Nirbhar Bharat, the budget proposes to remove exemptions on a lot of commodities. It eliminated 80 outdated exemptions and 400 old exemptions are being considered for removal. At the same time, it also increased the customs duty, particularly on agricultural products like raw cotton, raw silk and yarn and it also increased customs duty on some of the products of MSME sector. This could have implications paying high prices. The SME sector, as it has already been widely discussed had been severely affected by the pandemic. The budget is silent on the measures towards building. export competitiveness of this particular sector. One of the things that India could do is strengthening the already existing product linked incentive scheme. Similarly, India's logistic sector is very poorly ranked by the World Bank's logistics index. Improving India's logistics sector could improve export competitiveness. But unfortunately, we don't see anyone any of these items in the budget speech.