India's Foreign Trade and Current Account Deficit: Challenges Ahead

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Abstract

Current Account Deficit is one of the major macroeconomic problems facing India. In this paper, we have tried to investigate the trends in foreign trade and current account deficit in the context of India. The balance of payments in India has come under pressure recently with the current account deficit (CAD) reaching a historical record level of 4.2% of gross domestic product (GDP) in 2011-12.We have also analyzed the performance of India's foreign trade. One of the major indicators of a country's external performance is its trade account in general and current account in particular. Imbalances in current account might predict future changes in a managed foreign exchange regime; therefore sustainability of the current account has become the major concern of not only the policy makers, but also the central banks and the market analysts of the emerging economies.

Keywords: *Current Account Deficit, Foreign Trade, Exports, Imports.*

Introduction: The Current Account of the country constitutes the balance of trade (exports minus imports of goods and services), net factor income (such as interest and dividends) and net transfer payments (such as foreign aid). The balance of trade is the most important part of the current account. And a current account surplus is associated with trade surplus. However, for the few countries with substantial overseas assets or liabilities, net factor payments may be significant. Positive net sales to abroad generally contribute to a current account (CA) surplus and negative net sales may indicate a CA deficit.Net transfer payments are very important part of the current account in poor and developing countries as workers' remittances, donations, aids and grants and official assistance may balance high trade deficits.

As per IMF's World Economic Outlook January, 2013, the volume of world trade (goods and services) in 2012 slowed down to 2.8 per cent compared to the 5.9 per cent achieved in 2011. As per IMF projections, growth in the volume of world trade is expected to rise to 3.8 per cent in 2013. The IMF has put its growth projections of world output at 3.5 per cent in 2013. The advanced economies are expected to grow at 1.4 per cent while the emerging and developing economies to grow at 5.5 per cent in 2013. The projected growth rates in different countries are expected to determine the markets for our exports. As per WTO's International Trade Statistics, 2012, in merchandise trade, India is the 19th largest exporter in the world with a share of 1.7 per cent and the 12th largest importer with a share of 2.5 per cent in 2011.

Literature Review:

Manpreet Kaur, Surendra S. Yadav, and Vinayshil Gautam (2012) Analyzed and examined the causal relationship between FDI and current account. The investigation of this relationship is crucial for country like India where current account deficit is one the major macroeconomic problems.

T.P. Bhat (2011) The pre-reform period did not see much of structural changes in the foreign trade particularly, the export sector. However, there has been some significant changes in import, specifically high imports of petroleum products and machinery and equipments. The post-reform period witness significant changes in the trend, pattern and structure of external trade.

Aviral kumar tiwari (2012) examined the long-run relationship between oil and non-oil exports and imports, in order to see whether the current account deficit in India is sustainable. To achieve our objective we have carried out co integration analysis with structural breaks (as unit root analysis of both variables shows that these variables have been subject to structural changes). Interestingly, we found that there is a strong evidence of a long-run relationship between non-oil exports and imports and no evidence in the case of oil exports and imports. This implies that a foreign trade deficit is sustainable in the Indian context for non-oil commodities but not for oil commodities.

Mark, Theodore, Abhijit (2007) conducted an investigation into the sustainability of the Indian current

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account over the study period 1950-2003. It is argued that a necessary condition for current account sustainability is that exports and imports are co integrated.

Objectives:

1) To see how India's trends of exports and imports have differed in last 5 years.

2) To see how did trends of exports and imports affect the CAD in India.

Data and Methodology:

This study is based on secondary .the data required for the study has been collected from the DGCIS Kolkata. This study employs annual Indian data for imports, exports and the current account over the study period 2004-2013. Data are expressed as a percentage of GDP and in gross values as well. The required data for imports and exports expenditure, net interest payments on debt and GDP are obtained from International Financial Statistics and the Reserve Bank of India. We have taken secondary data and have used tools of bar diagram and pie chart to enrich the given statistics.

Trends of Export and Import and Their Growths in India:

Table 1

Year	Exports	% growth	Imports	% growth	Trade balance
2004-05	3,75,340	27.94	5,01,065	39.53	-1,25,725
2005-06	4,56,418	21.60	6,60,409	31.80	-2,03,991
2006-07	5,71,779	25.28	8,40,506	27.27	-2,68,727
2007-08	6,55,864	14.71	10,12,312	20.44	-3,56,448
2008-09	8,40,755	28.19	13,74,436	35.77	-5,33,680
2009-10	8,45,534	0.57	13,63,736	-0.78	-5,18,202
2010-11	11,42,922	35.17	16,83,467	23.45	-5,40,545
2011-12	13,20,836	15.56	21,32,198	26.65	-8,11,362
2012-13	14,46,627	9.52	24,36,564	14.27	-9,89,938

Source- DGCIS Kolkata Values in Rs, crores

Interpretation: Exports have been growing every year. But at the same time it is noticeable that imports are growing as well. Growths of imports have been considerably more than growth of exports every year. This leads to trade deficit or Current account deficit. As noticed in 2009-10 growth of imports were negative leading to decrease in imports but growth of exports that year was negligible too. Despite a lower trade deficit, current account deficit in the second quarter of 2009-10 was almost at the same level as last year, mainly on account of lower net invisibles surplus. "The invisibles surplus, however, continued to be driven by private transfers and software exports," the RBI said in its data released on balance of payments (BOP).Oil Imports declined in 2009 as compared to 2008 hence contributing to lower merchandise imports. Currently the statistics says that trade deficit is pretty high, and the highest since last 8 yrs time. The CAD recorded a remarkable percentage of GDP which was more than 6%.That was one of the reasons for FDI norms being finalized.

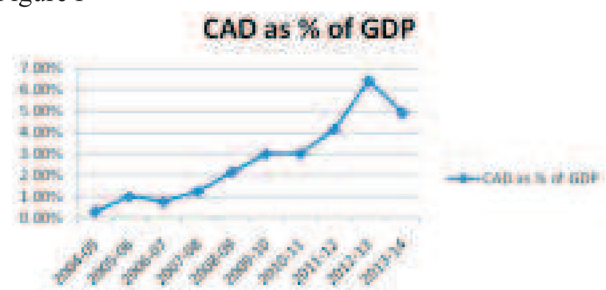
CAD since 2004-05 as % of GDP:

Table 2

Years	CAD as % of GDP
2004-05	0.3%
2005-06	1%
2006-07	.75%
2007-08	1.25%
2008-09	2.15%
2009-10	3%
2010-11	3%
2011-12	4.15%
2012-13	6.4%
2013-14(Nov)	4.9

Source- DGCIS Kolkata

Figure 1



Interpretation: The highest current account deficit was above 6% of GDP reported in Q4 2012-13. The estimates show that it will be difficult to match this highest reading of current account deficit. The growth in export of goods and services will have to be higher and growth in imports lower and matched by a high growth in remittances. The trends arrived from GDP estimates show it could be a negative surprise for the economy. The lowest was during 2006-07 where India had a GDP growth of double digits, above 10%, which eventually decreased because of the global economic crisis. Currently the Reserve bank of India has been successful to reduce the CAD and has got it down to 5% approximately. Foreign Direct Investment plays an important role in it.

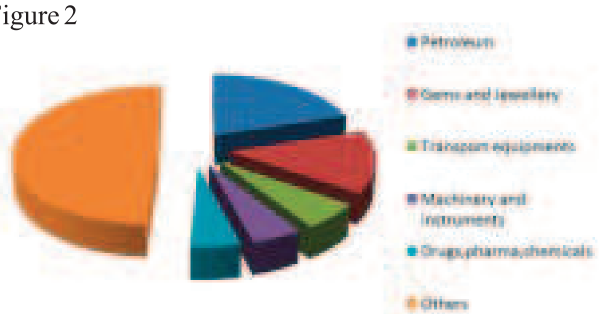
Share of Top Five Commodities in India's Exports 2012-13:

Table 3

Petroleum	20.20%
Gems and Jewellery	14.40%
Transport equipments	6.10%
Machinery and instruments	5.10%
Drugs,pharma,chemicals	5.00%
Others	49.20%

Source- DGCIS Kolkata

Figure 2



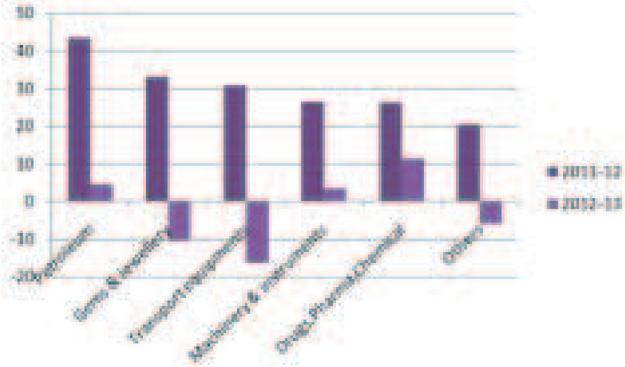
Top Five Commodities of Exports by Growth (April-January) 2011-12 And 2012-13:

Table 4

Export commodities	2011-12	2012-13
Petroleum	43.56	4.57
Gems & Jewellery	33.08	-10.31
Transport equipments	30.79	-16.24
Machinery & instruments	26.51	3.53
Drugs,Pharma,Chemical	26.38	11.34
Others	20.43	-5.89

Source- DGCIS Kolkata

Figure 3



Interpretation: As we have compared the growth of exports here we see a pretty much negative impact of our growth in exports. Petroleum, machinery & instruments and drugs have recorded pretty much negligible growth but other items like gems and jewellery, transport equipments etc have constituted to negative growth.

Exports of Other Commodities Showed Negative Trend since Last Year's Time Constituting to Our Increasing CAD: Export of Plantation crops during 2012-13 (April–January), decreased by 9.95 per cent in US $ terms compared with the corresponding period of the previous year. Export of both coffee and tea registered negative growth in exports.

Agriculture and Allied Products registered a growth of 27.57 per cent with the value of exports increasing from US $ 21353.59 million in the previous year to US $ 27240.35 million during the current year.

Exports of Ores and Minerals registered a negative growth of 35.48 per cent over the same period of the previous year.

Export of Leather and Leather Manufactures recorded a negative growth of 2.22 per cent during 2012-13.Export of engineering goods registered a negative growth of 5.05% .Export of electronic goods registered negative growth of 4.55% since last year's time. Export of textiles recorded negative growth of 5.56% and readymade goods on average negative growth of 10%.Cotton yarn /Fabrics recorded positive growth of 6.38%.Exports of handicrafts declined by about 16%.

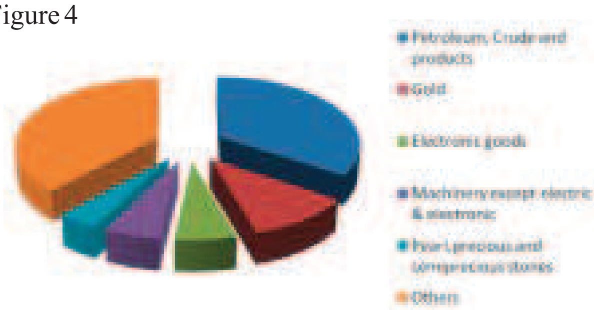
Share of Top 5 Commodities in India's Imports:

Table 5

Petroleum, Crude and products	34.40%
Gold	11.10%
Electronic goods	6.30%
Machinery except electric & electronic	5.70%
Pearl, precious and semiprecious stones	4.30%
Others	38.20%

Source- DGCIS Kolkata

Figure 4



The import performance by growth of top five principle commodities in 2012-13, with the corresponding period of previous year.

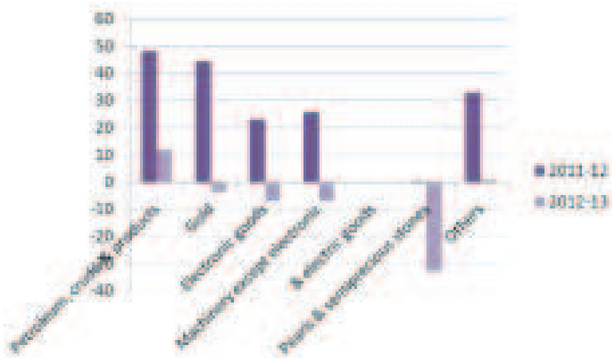
TOP 5 Commodities of Import by Growth:

Table 6

Export commodities	2011-12	2012-13
Petroleum, crude & products	48.2	11.8
Gold	44.4	-3.7
Electronic goods	23.1	-7.1
Machinery except electronic & electric goods	25.7	-6.9
Pearls & semiprecious stones	0.4	-32.8
Others	32.9	0.8

Source- DGCIS Kolkata

Figure 5



Interpretation: Except petroleum crude and products growth has been negative in all importing commodities. In petroleum as compared to last year as well growth has been less but positive. Technically importing commodities have reduced but assumingly reduction in export growth has been more than reduction in import growth leading to persistent Current account deficit. Imports of Fertilizers registered a negative growth of 19.80%.Imports of petroleum and crude oil products registered a positive growth of 11.80%Imports of pearls and precious and semiprecious recorded a considerable decline of 32 % approx. Import of capital goods recorded a negative growth of 6% on average approx. Import of medicines and pharmaceuticals registered a growth of 4.21%.Coal,coke and briquettes registered negative growth of 10% approx, Import of gold and silver also decreased registering a negative growth of 9.32%.

Conclusion: Reserve bank of India has been successful to reduce the CAD which had gone very high during the 1st quarter of this year. Now RBI has reduced it for more than 1.5% of GDP. Due to employment of many FDI, norms and decrease in import of gold due to implementation of high import duty which reduced the internal demand for gold considerably.

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