Time to move beyond subsidies

India’s export promotion schemes face an uncertain future after the United States Trade Representative (USTR) decided to challenge their legality in the World Trade Organisation (WTO). The complaint of the USTR is that India is violating its commitments under the Agreement on Subsidies and Countervailing Measures (SCM Agreement) using five of the most used export promotion schemes, namely, the export-oriented units scheme and sector-specific schemes, including electronics hardware technology parks scheme, merchandise exports from India scheme, export promotion capital goods scheme, special economic zones and duty-free import authorisation scheme.

The main argument of the USTR is that India’s five export promotion schemes violate Articles 3.1(a) and 3.2 of the SCM Agreement, since the two provisions prohibit granting of export subsidies. Until 2015, India had the flexibility to use export subsidies as it is among the 20 developing countries included in Annex VII of the agreement that are allowed to use these subsidies as long as their per capita Gross National Product (GNP) had not crossed $1,000, at constant 1990 dollars, for three consecutive years. This provision applicable to the Annex VII countries was an exception to the special provisions provided to the developing countries (the so-called “special and differential treatment”) for phasing out export subsidies. Except Annex VII countries, all other developing countries were allowed a period of eight years from the entry into force of the WTO Agreement, i.e. 1995, to eliminate export subsidies.

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That India had crossed the $1,000 GNP per capita threshold in 2015 became known when the WTO Secretariat produced its calculations in 2017. An interpretation provided in a 2001 report of the Chairman of the Committee on Subsidies and Countervailing Measures, which is also considered as the document providing the methodology for implementing Annex VII of the agreement, says that countries like India must eliminate export subsidies immediately upon crossing the above-mentioned threshold. In the Doha negotiations, India and several other Annex VII countries sought an amendment of the agreement so as to enable them to get a transition period.

In a submission made in 2011, India, along with Bolivia, Egypt, Honduras, Nicaragua and Sri Lanka, argued that the Annex VII countries should be eligible to enjoy the provisions applicable to the other developing countries, namely, those that had GNP per capita above the threshold. The latter set of countries was required to phase out their export subsidies within eight years of joining the WTO. Additionally, they were allowed to enter into consultations with the Committee on Subsidies and Countervailing Measures, not later than one year before the expiry of the transition period, to determine if there was a justification for the extension of this period, after examining all of their relevant economic, financial and development needs. But this proposal, like all other proposals made as a part of the Doha Round negotiations, remains unaddressed.

It needs to be pointed out that this is not the first time that the U.S. has put India’s export promotion schemes under the scanner; although this is the first instance when its Trade Administration has initiated a WTO dispute involving these schemes. In 2010, the U.S. had questioned the export incentives provided to the textiles and clothing sector as a whole, arguing that this sector had a share in global trade exceeding 3.25% and had therefore become export competitive. The U.S. pointed out that according to Article 27.5 of the SCM Agreement, any Annex VII developing country which had reached export competitiveness in one or more products must gradually phase out export subsidies on such products over a period of eight years. There was, therefore, considerable pressure on the Department of Commerce to consider its future strategies regarding export promotion schemes.

It was perhaps the pressure that spoke when the Foreign Trade Policy (FTP) of the National Democratic Alliance government unveiled in 2015 did some serious introspection about the future of export promotion schemes, the first time that any government had done so. The policymakers recognised that the extant WTO rules and those under negotiation were aimed at eventually phasing out export subsidies. The FTP took this as a pointer to the direction which export promotion efforts in the country must take in the future: a movement towards more fundamental systemic measures and away from incentives and subsidies. A similar note was sounded in the mid-term review of the FTP released in December 2017. This document was significant also because the Indian government showed its awareness that the country was at the verge of losing the benefits of being an Annex VII country.

Contrary to the pronouncements made in the FTP, the government has continued to increase its outlays on export promotion schemes. In 2016-17, the total outlay on export promotion schemes was 58,600 crore, an increase of more than 28% in three years. During this period, the largest export promotion scheme in place currently, the Merchandise Exports from India Scheme (MEIS), was introduced to promote exports by offsetting the infrastructural inefficiencies faced by exports of specified goods and to provide a level playing field. The scheme initially covered 4,914 tariff lines and was subsequently increased to cover 7,914 tariff lines. In recent months, there has been a two-fold expansion of the scheme: one, to enhance the MEIS rates of ready-made garments from 2% to 4%; and two, to increase the MEIS benefits for all labour-intensive and MSME sector products by 2%. These expansions in the scope of MEIS increased the total outlay on the scheme to nearly 60% over the level in 2016-17.

The utility of export subsidies to promote exports has long been questioned. While the real impact of these subsidies has never been clearly measured, what has been quite evident is they have benefited the rent-seekers. There is, therefore, a strong case for the government to invest in trade-related infrastructure and trade facilitation measures, which can deliver tangible results on the export front.

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The India-Japan economic relationship remains underwhelming in relation to strategic ties

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