CARE Ratings
Professional Risk Opinion

Economics

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Foreign Trade Perspectives

The trade deficit for the first 7 months of the year was $ 77.7 bn, which though the lowest in the last 5 years is also associated with a sharp decline in growth in both exports and imports. Hence, while a lower trade deficit is good for the balance of payments as it lowers the current account deficit and to that extent puts less pressure on the capital flows in balancing the external account, there are concerns over growth in exports.

Table 1 below provides information on trends in foreign trade for the last five years for the first 7 months of the year. The value of exports at $ 154 bn was the lowest in this time period declining by 17.7% this year. Imports too have been impacted with the decline being sharp at 15.3% in FY16 so far. Growth in both exports and imports has been negative since January 2015. The trade deficit has been moving upwards on a month on month basis crossing $ 10 bn a month in all months except October where there was moderation to (-) $ 9.8 bn.

Low global commodity prices have been the main driver of volumes of trade and have had a mixed effect on all economies. While low crude oil prices have definitely benefited large importers, exporters of commodities especially of minerals and metals have also been affected. Broadly speaking three factors have driven these trade numbers:

- Low world economic growth, as major regions continue to face this challenge which in turn has impacted their demand for imports.
- Low global commodity prices have depressed the value of goods traded across frontiers. Hence, where volume levels have been retained, the value of exports has been impacted.
- Currency movements have varied across countries driven by both domestic factors as well as competitive action by governments to let their currencies decline. The Yuan depreciation was one trigger, while the expected Fed hike in interest rates has affected currencies of emerging markets. Hence in a market that is not growing significantly there has been fierce price competition from other emerging markets especially to the extent that prices affect the demand for imports.

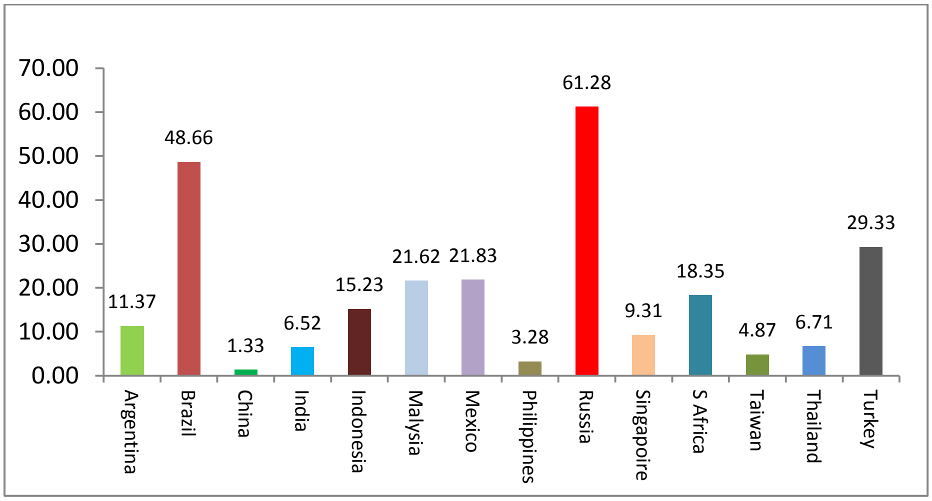
Table 1: India's foreign trade: April-October ($ bn and % growth)

	Exports	Imports	Trade balance	Growth Exports	Growth imports
2011-12	178.0	285.0	-107.0	44.6	36.7
2012-13	168.5	280.2	-111.7	-5.3	-1.7
2013-14	181.6	267.4	-85.8	7.8	-4.6
2014-15	187.4	273.7	-86.4	3.2	2.4
2015-16	154.2	232.0	-77.7	-17.7	-15.3

Source: CMIE

The depreciation in the rupee did not have a significant impact on our exports in terms of export competitiveness. The rupee was a better performing currency in relative terms which also carried the disadvantage of loss of price competitiveness on account of being relatively stronger. The graph below shows how various currencies depreciated vis-à-vis the dollar based on averages for the two 7 –months periods in 2014 and 2015.

Chart 1: Currency Depreciation: Apr-Oct (2015 over 2014) %



Source: Pacific Exchange Rate Services

Impact on GDP

Exports as a percentage of GDP at current prices were 23.1% while that of imports was 25.5%, with the trade deficit being 2.3% of GDP. With the deficit narrowing down, the GDP growth rate will receive some upward thrust. But the direct impact of growth in exports on GDP will be limited as growth is still dominated by internal factors.

Exports composition

The composition of exports in Table 2 shows that engineering goods, gems and jewelry, chemicals, textiles and readymade garments and refinery products are major constituents. Petro products are an important part of our exports and had a share of around 21% last year, which came down to 12.4% primarily as the value declined more on account of the depressed prices of crude oil.

All the major components except readymade garments had witnessed a decline in exports i.e. negative growth, reflecting low demand conditions for our exports.

For some of these conventional products, where demand tends to be relatively inelastic, competition from countries like Bangladesh and China could have impacted the relative attractiveness of our exports. In case of engineering goods and chemicals, slower growth in the importing countries would have affected demand for the same. In general, growth in exports would be driven primarily by demand conditions in the importing countries while price factor on account of depreciation will play a secondary role.

Table 2: Commodity-Wise Composition of Exports April-September ($ bn and %)

Exports	2014	2015	Share	Growth
All commodities	***161.2***	***132.7***	***100.0***	***-17.7***
Petroleum & crude products	***33.6***	***16.4***	***12.4***	***-51.2***
Non-POL	***127.5***	***116.2***	***87.6***	***-8.9***
Agricultural & allied products	***19.3***	***15.4***	***11.6***	***-20.2***
Ores & minerals	***1.3***	***0.9***	***0.7***	***-28.5***
Manufactured goods	***105.4***	***98.7***	***74.4***	***-6.3***
Leather & leather manufactures	***3.3***	***2.9***	2.2	-9.8
Chemicals & related products	16.4	16.4	12.4	-0.1
Engineering goods	34.5	30.2	22.8	-12.4
Electronic goods	3.7	3.2	2.4	-11.8
Textiles (exc readymade garments)	9.0	8.6	6.5	-4.0
Readymade garments	8.4	8.6	6.5	2.3
Other manufactured goods	30.2	28.7	21.7	-4.8
Gems & jewellery	20.9	19.8	14.9	-5.5

Source: CMIE

To gauge the importance of the demand factor, the destination of our exports is presented in Table 3 below. The top 20 countries in our exports list accounted for around 60% of our total exports and the top 10 had a share of 44%. The demand side of any economy is best captured by growth in GDP and typically a fast growing economy would be witnessing increased demand for imports. The same holds when economies slow down when demand for imports becomes less buoyant.

Table 3: Main export destinations (%)

World	Share	Growth	World	Share	Growth
USA	13.5	-5.1	Japan	1.7	-15.6
UAE	10.0	-8.5	Belgium	1.6	-13.9
Hong Kong	4.1	-9.9	Netherlands	1.5	-31.0
China	3.0	-18.9	France	1.5	-4.5
UK	3.0	-5.6	Vietnam	1.4	-24.9
Germany	2.3	-10.3	Malaysia	1.4	-16.4
Saudi Arabia	2.3	-47.5	Italy	1.3	-21.0
Singapore	2.2	-34.1	South Africa	1.3	-36.2
Bangladesh	1.8	-15.2	Turkey	1.3	-26.3
Sri Lanka	1.8	-15.7	Nepal	1.3	-19.0

Source: CMIE

The impact of the global slowdown on Indian exports can be gauged from the fact that there has been a slowdown in growth of most of these countries. Only two of the top 10 countries, USA and Bangladesh are to witness an increase in growth in GDP this year relative to 2014. The others are expected to grow at a slower rate indicating thereby that demand for imports in general would have been affected in these countries.

Composition of imports

Table 4 below provides information on the shares of various commodities in our imports along with the growth rates.

Table 4: Imports composition ($ bn and %)

Value in bn $	2014	2015	Share	Growth
All commodities	**234.1**	**200.4**	**100.0**	**-14.4**
Petroleum crude & products (POL)	**82.4**	**48.1**	**24.0**	**-41.6**
Non-POL	**151.7**	**152.3**	**76.0**	**0.4**
Agricultural and allied products	**11.0**	**11.1**	**5.5**	**0.6**
Ores and minerals	**13.1**	**10.5**	**5.2**	**-19.6**
Manufactured goods	**122.5**	**124.8**	**62.3**	**1.9**
Leather and leather manufactures	0.5	0.5	0.3	-0.6
Chemicals and related products	20.3	20.9	10.4	3.0
Fertilizers	3.3	5.2	2.6	59.3
Engineering goods	36.3	35.7	17.8	-1.7
Transport equipment	5.8	5.4	2.7	-6.1
Iron & steel	6.0	5.8	2.9	-3.3
Ferrous and non-ferrous metal products	7.3	7.1	3.5	-3.8
Non-electrical machinery	9.3	9.8	4.9	4.6
Electrical machinery	3.2	3.5	1.8	10.9
Electronic goods	20.0	21.9	10.9	9.7
Textiles (excl.rmg)	2.0	2.0	1.0	-2.0
Readymade garments	0.3	0.3	0.1	11.3
Other manufactured goods	43.1	43.5	21.7	0.9
Gold & silver	16.7	19.5	9.7	17.2
Gold	14.7	17.5	8.7	18.8
Silver	1.9	2.0	1.0	4.5
Paper board & manufactures	1.3	1.2	0.6	-8.5
Wood & wood products	1.6	1.3	0.7	-13.8
Artificial resins, plastic materials etc.	6.0	5.8	2.9	-4.3
Other commodities	**5.1**	**5.9**	**2.9**	**14.6**

Source: CMIE

The share of POL in total imports which used to be around 30-33% has come down to 24% during the first half of the year mainly due to lower crude oil prices. Gold still remains important accounting for 8.7%, but still lower than the level of 12-13% in FY14 when there was the foreign exchange crisis in the country. Engineering goods, electronics and chemicals are the other major components of imports.

In terms of growth in imports, the following are the observations:

1. POL and ores have witnessed negative growth. The lower dependence on import of ores is positive sign of greater recourse being sought to domestic supplies. In case of POL it is more due to fall in crude oil prices.
2. Within the category of engineering which also includes metals, electrical and non-electrical machinery have both showed positive growth. This is significant because even the IIP growth rates for these two segments were impressive with rates of 13.3% and 3.3% respectively indicating quite strongly the growth of the capital goods segment. More positively speaking, it does show signs of investment improving with both domestic production and imports supporting this activity.
3. Growth in import of fertilizers was high at 59.3% which supplemented growth in domestic production too with the IIP growth witnessing growth of 8% which came over a zero growth.
4. Growth in imports of both gold and silver has been positive with the former increasing by 18.8%. The government has introduced various schemes to monetize investment opportunities in bullion through sovereign bonds and deposits in November. It needs to be seen whether this would lead to lower demand for physical gold.

Concluding observations

Growth in imports of engineering goods does indicate that there is a positive scenario for capital goods as domestic production has also been growing in the first six months of the year. Exports continue to remain downbeat with negative growth mainly due to low demand conditions. Our major importing countries are generally not expected to grow at a higher rate in 2015 and hence prospects for the rest of the year would be subdued. Further while the rupee has depreciated, it is lower than that witnessed in other countries. Hence, the price advantage from a weaker rupee appears to be relatively moderated.

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