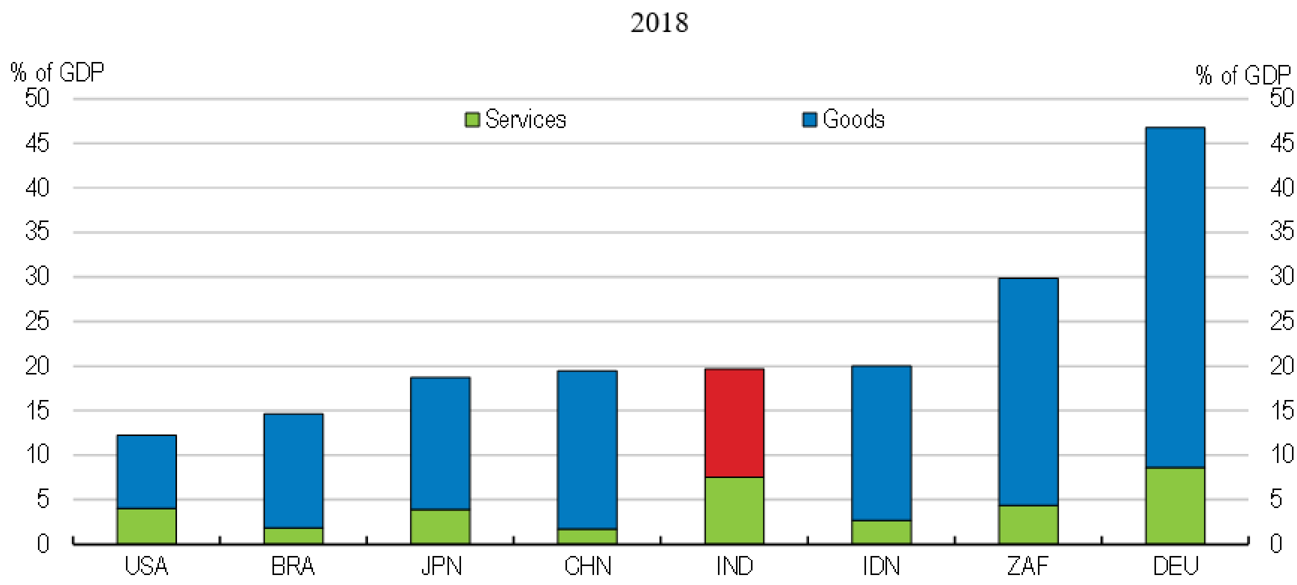
India’s export performance: the goods and services nexus

By Isabelle Joumard, India Desk, OECD Economics Department

The government aims at **making India an export hub**, to help boost job creation. The export-to-GDP ratio has risen fast since the early 1990s and now stands broadly at par with China (Figure 1). The large share of services in total exports however stands out: while India has performed very well in exporting IT services, exports of goods have lagged behind. Exports of labour-intensive manufacturing products could grow faster and contribute to job creation. The 2019 OECD Economic Survey of India discusses policies to make India’s exports more competitive.

Figure 1. India’s export-to-GDP ratio is relatively high, with a tilt towards services

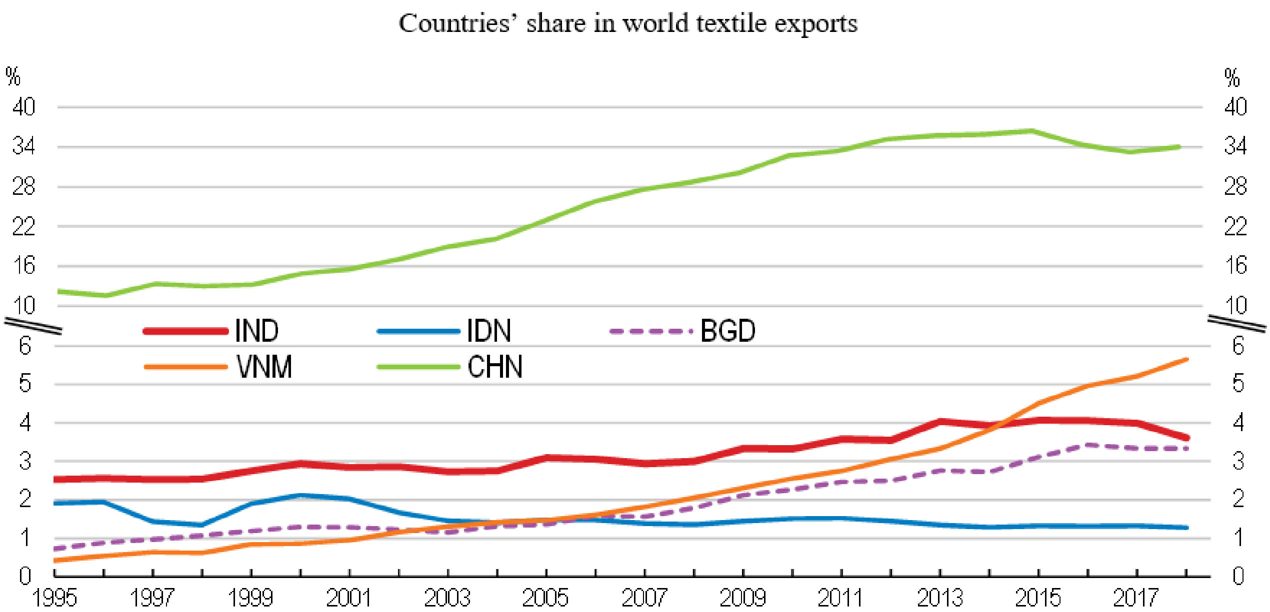


Source: World Bank, World Development Indicators database.

Performance of services exports has been stellar. India’s share of world services trade more than quadrupled from 0.5% in 1995 to 3.5% in 2018 and India has become a major exporter of business services, notably in the Information, Communication and Technology (ICT) sector. Medical and wellness tourism is also performing well, with patients seeking high-quality medical treatment at competitive prices in some Indian hospitals.

Exports of goods have displayed mixed results. India has gained market shares for some skill- and capital-intensive goods, including pharmaceuticals and refined oil. However, performance in exporting textiles, leather and agricultural products has disappointed. Looking at the labour-intensive components of the textile sector (including garment) provides an illustration: Vietnam now has a larger market share (Figure 2).

Figure 2. Exports of textile, garment and footwear: losing market share

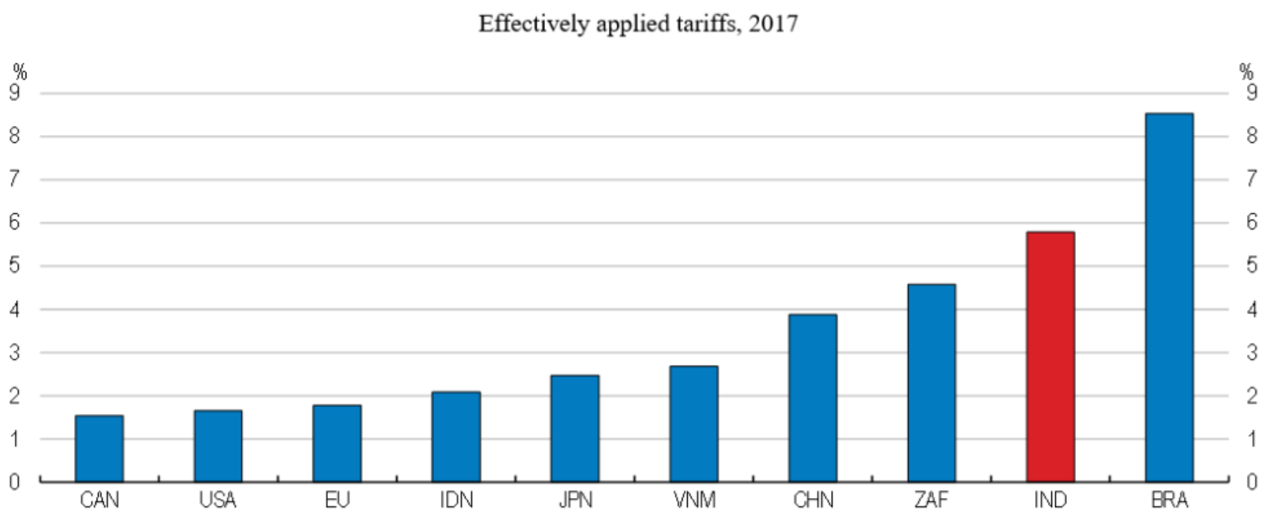


Note: Low-technology textile including garment and footwear.
Source: OECD calculations based on UNCTAD data.

Domestic factors partly explain the relatively low performance of labour-intensive exports. Labour regulations are more stringent for industries and large firms. This creates incentives for firms to stay small, making it difficult to exploit scale economies. Electricity prices are also relatively high and transport infrastructure bottlenecks persist despite recent improvements. This hampers the competitiveness of manufacturing goods which tend to be more intensive in energy and transport than services. The length and costs to acquire land, combined with relatively high financing costs, are further weighing on firms' competitiveness.

Barriers to trade also play a role. Import tariffs on goods declined substantially in the 1990s and 2000s. They have been raised again since 2017 and are relatively high (Figure 3). Expensive imports of intermediate products, due to import duties, can penalise Indian exporters if they do not receive the full compensation for the duties paid on inputs – this is often the case in a sector like the apparel sector where small enterprises account for the lion's share. The complexity of India's tariff structure further raises administrative and compliance costs. Overall, import duties run against the objective of making India an export hub.

Figure 3. Effectively applied tariffs are relatively high

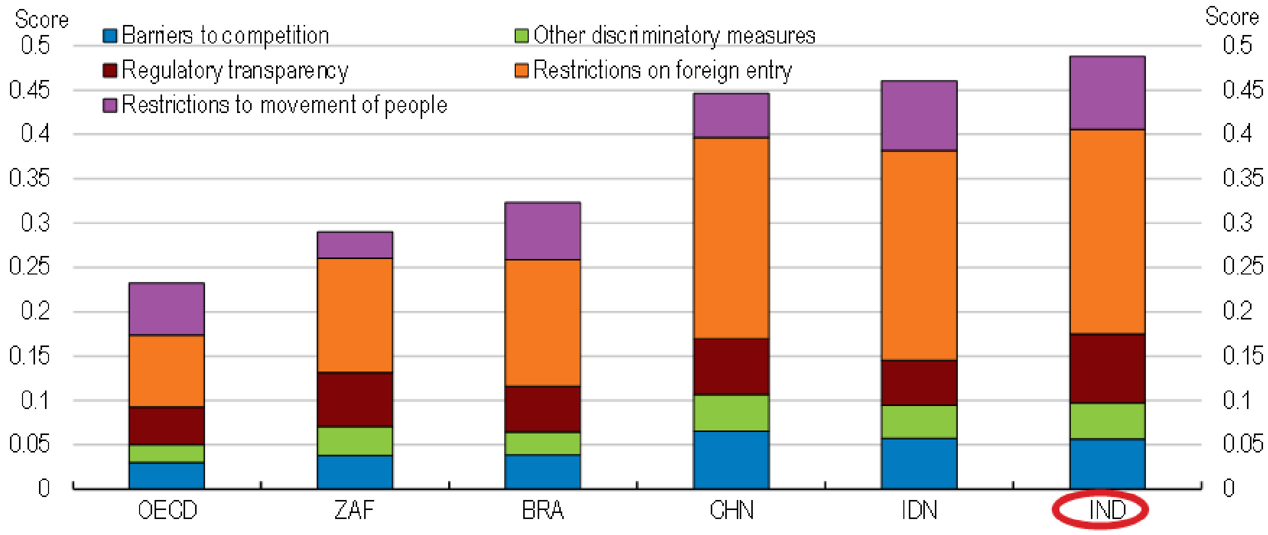


Note: Data show weighted averages of effectively applied tariffs, whereby the tariffs are weighted by the import value of each product.
Source: UNCTAD Trade Analysis Information System (TRAINS) data extracted from the World Bank, World Integrated Trade Solutions.

Trade in services also faces some restrictions, with local suppliers protected from foreign competition (Nordås, 2019; OECD, 2017). Only Indian nationals are allowed to practise as lawyers or architects. Services trade restrictions, as assessed by the OECD, are also relatively high in the banking, insurance, rail and air transport, and telecommunication sectors (Figure 4). Because services are key inputs for the manufacturing sector and support participation in global value chains, stringent regulations on services are weighing on manufacturing costs and thus on export performance.

Figure 4. Services trade restrictions, as measured by the OECD, are relatively stringent

OECD Services Trade Restrictiveness Index, 2018



Note: The STRI takes values between zero and one, one being the most restrictive. OECD refers to an unweighted average.
Source: OECD, Services Trade Restrictiveness Index database.

OECD simulations suggest that **India would be a major beneficiary of a multilateral reduction in barriers to services trade** (OECD, 2019b). Better priced services intermediates would foster a rapid expansion of production and job creation in the manufacturing sector. It would further support wages for low-skilled workers. Simulations also reveal that, even in the absence of a multilateral agreement, the economy would gain from a unilateral liberalisation of trade and investment (Joumard et al., 2020).

India could make exports a new growth engine. India's trade prospects are relatively positive as it has specialised in sectors which will likely be in high demand in the future (e.g. ICT services, pharmaceuticals and medical devices) and in fast growing destinations (with a large share of its exports to emerging market economies). To unlock its potential to seize market shares in the labour-intensive manufacturing segment, India should modernise labour and land regulations, address infrastructure bottlenecks and open up further the services sector to trade and investment. Better and less expensive services – financial, marketing, distribution, legal, transport, etc. – will increase competitiveness in the manufacturing sector, boost job creation and meet the aspirations of women and new comers on the labour market.

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