



Comments on India's Exports: The New Normal?

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Main Takeaways

- What's new?: Macro-level evidence, complemented by sectoral and firm-level analysis.
- Key findings
 - “Quiet” revolution as India’s exports shift from traditional items to new engineering, electronics and pharma.
 - External demand as the main driver of India’s exports but negligible roles of ER and relative prices is counterintuitive.
 - Important implications for future growth if weakness in global trade persists.

India's Exports: The Role of Trading Partners' Demand

■ Recent IMF research:

- IMF WEO (Fall 2016): cross-country analysis finds that weak investment accounts for up to $\frac{3}{4}$ of trade slowdown.
 - IMF India (2017): panel regression of EM exports with India's export elasticity to trading partners' demand close to 1.
 - IMF India (2015): industry-level analysis finds long-run coefficient on global demand close to 1.
- Post-2005 decline in demand elasticity other than electronics comes close to long-run elasticity of 1.

India's Exports: Role of Exchange Rates

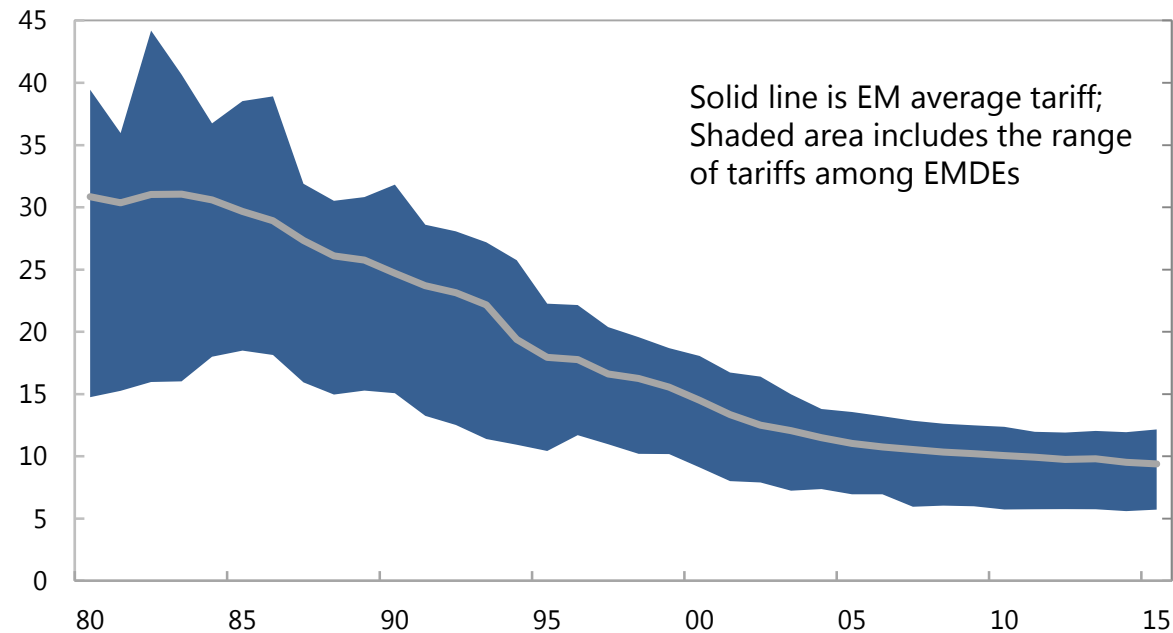
- Surprising that ER is not significant, though firm-level analysis suggests appreciation hurts higher domestic VA exporters.
- Other studies find price competitiveness matters.
 - IMF India (2015, 2017) estimates price elasticity of -0.2 to -0.3.
 - Distorted price signals hinder resource allocation and firm growth.
- *With possible secular stagnation in AEs, how to make exports more competitive and responsive to changing patterns of external demand?*

1. Remove Trade Distortions

- India's import tariffs are the highest among EMs.
- Food, agriculture and manufacturing remain highly protected.

Tariffs in Emerging Markets and Developing Economies

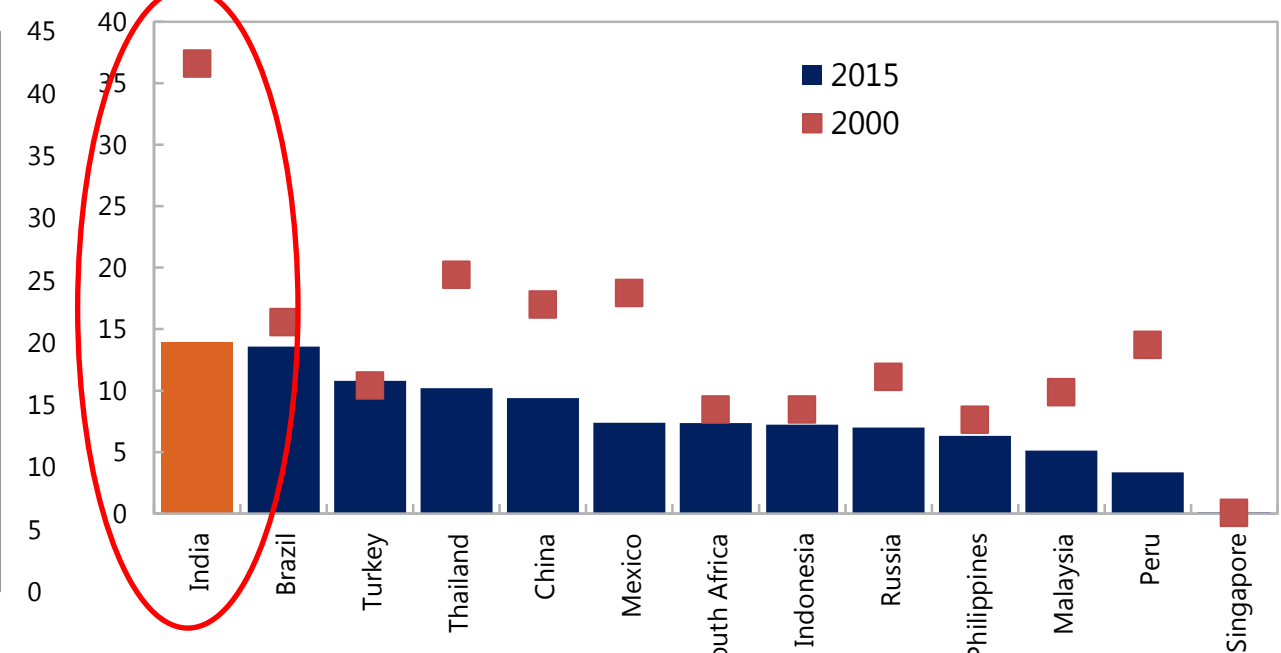
(In percent; simple average)



Sources: Chapter 2, October 2016, IMF, *World Economic Outlook*; and IMF staff estimates.

MFN Applied Tariff Rates

(In percent)

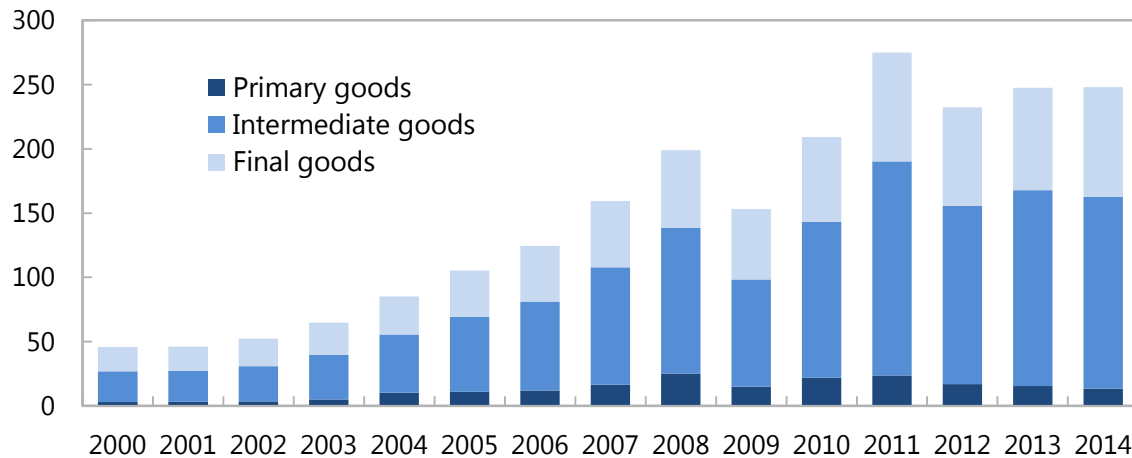


Source: WITS database.

2. Room to Expand Global Value Chain

- India has gradually integrated into the global value chain, but still room to do more.
- GST roll-out in July 2017 will also strengthen *domestic supply-chain linkages*.

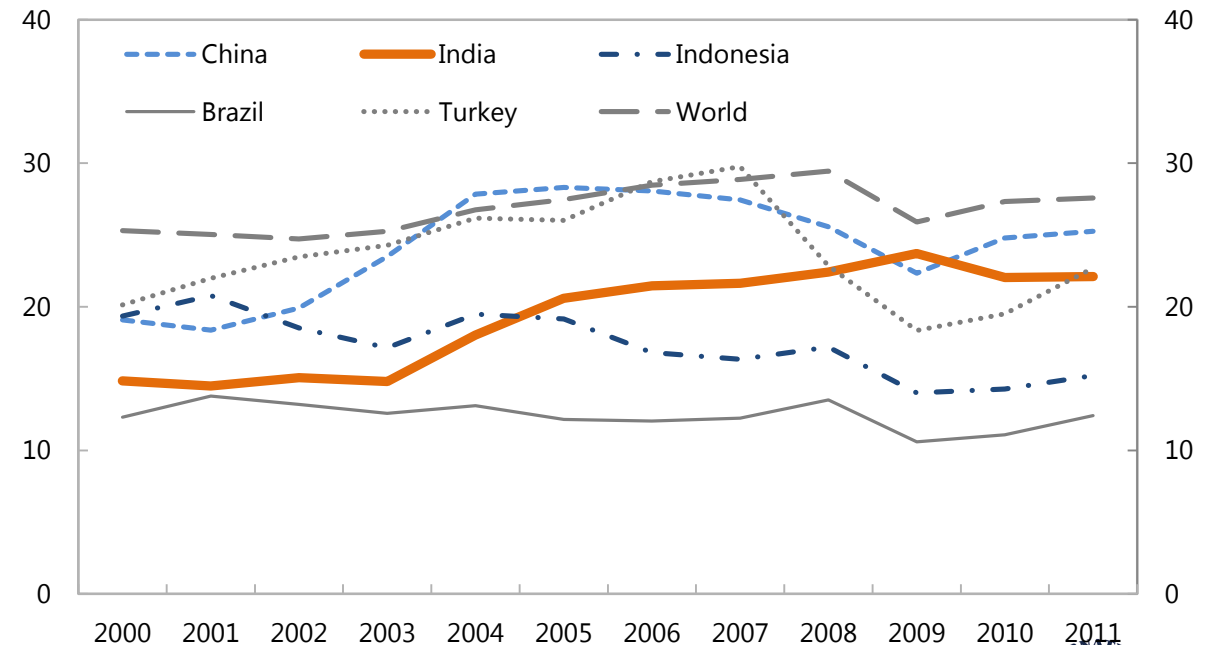
India: Merchandised Exports 1/
(In billion of US\$)



Sources: RIETI database, YES BANK.

1/ Export value based on BEC classification system in order to classify all of the trade goods by production stage. "Primary goods" are materials to be used for food and beverages and in industrial supplies. "Intermediate goods" are trade goods that represent the intermediate input along the path toward becoming the final product. These goods are manufactured goods (processed or assembled) that are produced from primary goods but still are not yet final products. "Final goods" is defined here as goods used by the producer (as the intermediate input) and goods consumed by households and the government.

Foreign Value Added
(In percent of total merchandised exports)



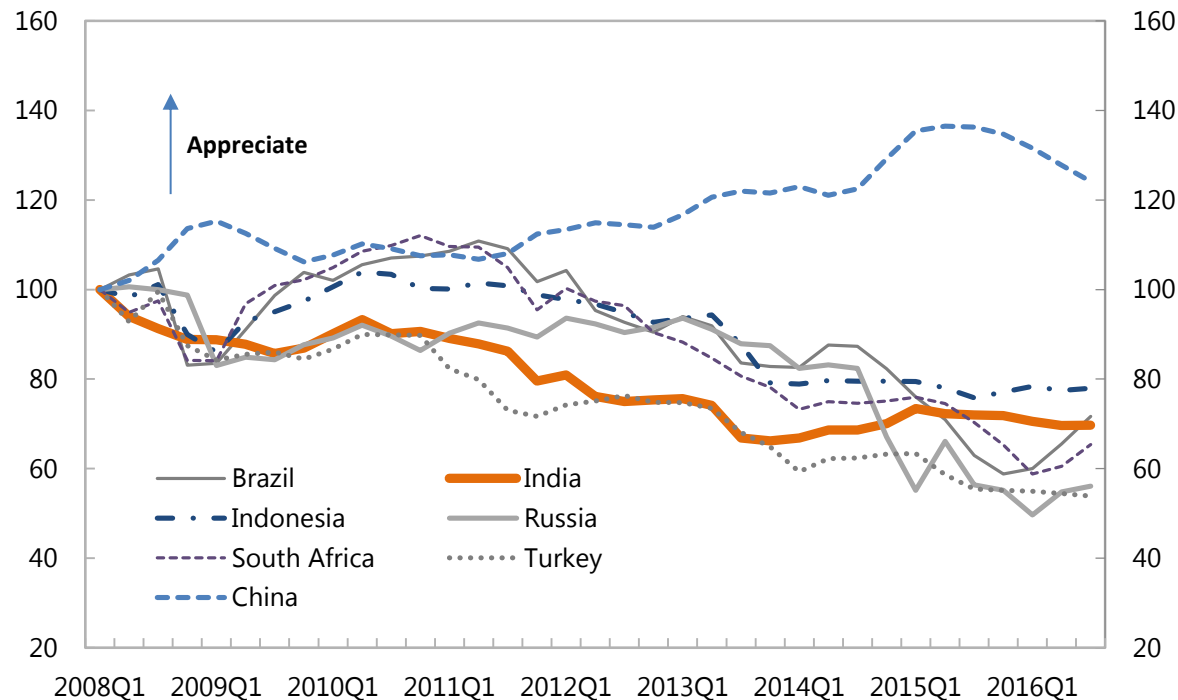
Source: Boddin (2016) based on World Input-Output Database



3. Protect Price Competitiveness

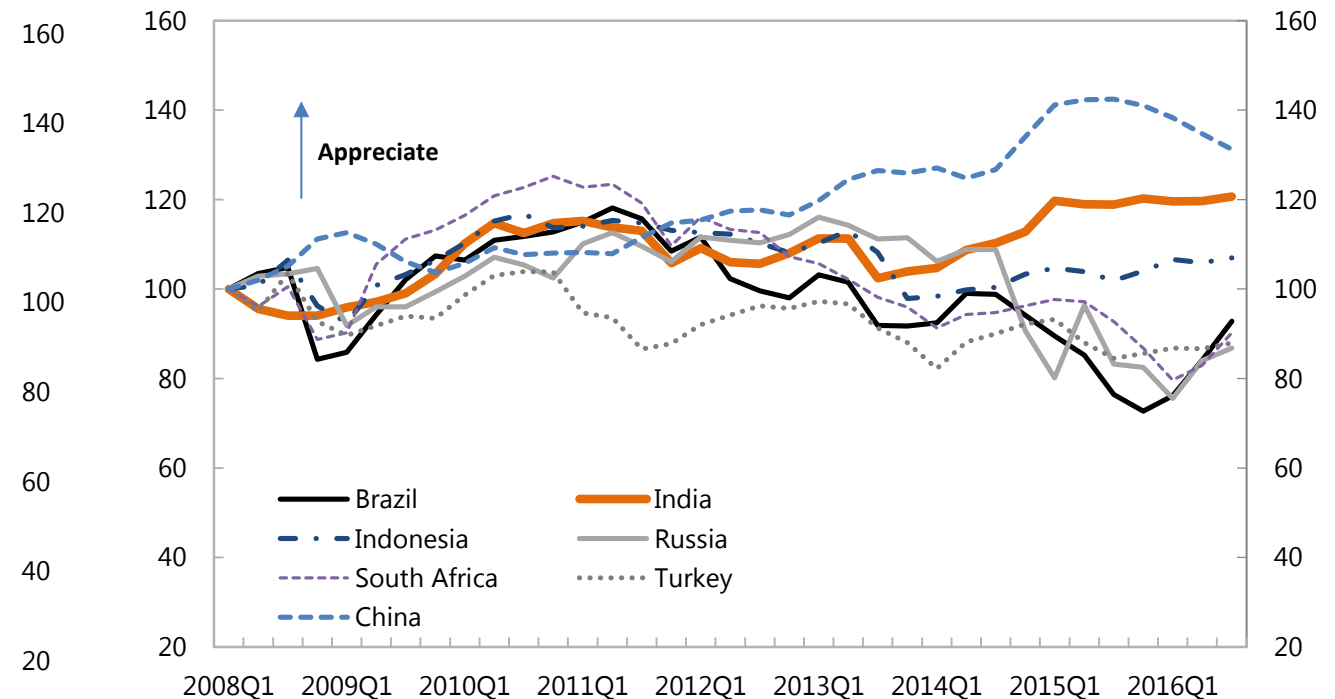
- Indian rupee appreciated in real terms against Asian peers.
- Higher inflation relative to partners erodes competitiveness.

Nominal Effective Exchange Rate
(Index, 2008Q1=100, trade partners' weighted)



Sources: IMF's INS database, IMF staff calculations.

Real Effective Exchange Rate
(Index, 2008Q1=100, trade partners' weighted consumer price index)



Sources: IMF's INS database, IMF staff calculations.

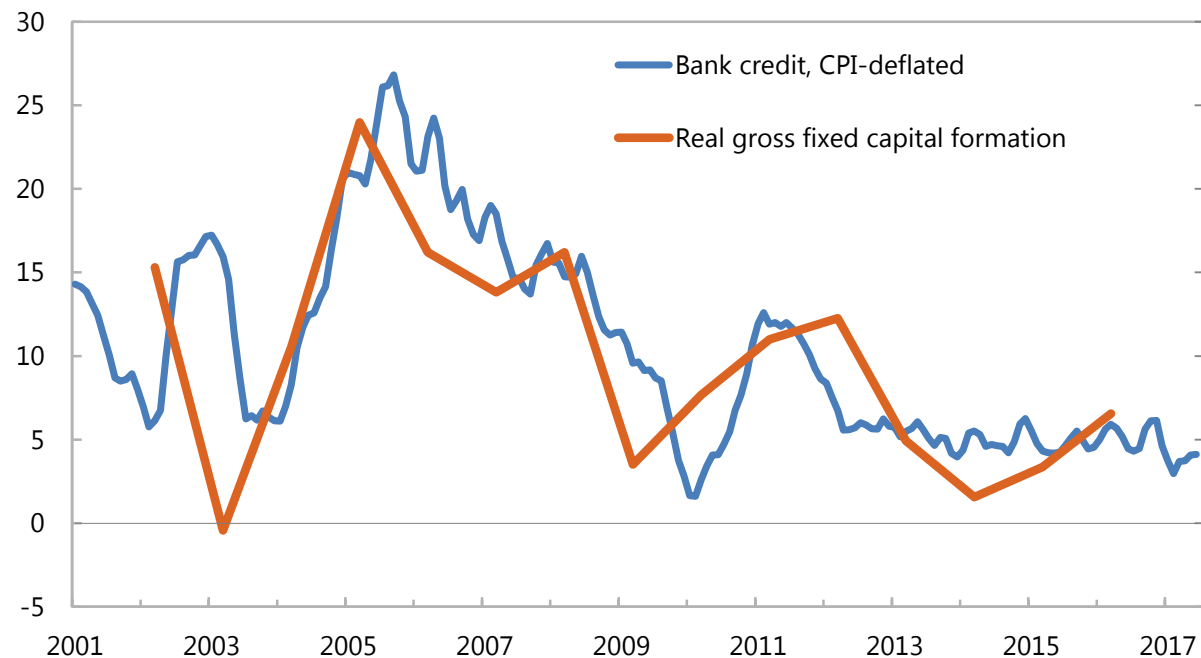


4. Address Banking Strains and Resource Allocation

- Corporate and banking sector strains hinder resource reallocation to higher productivity sectors and firm growth.
 - See Hsieh and Klenow (2009); Das et al, IMF Working Paper (forthcoming).

India: Bank Credit Growth and Fixed Investment

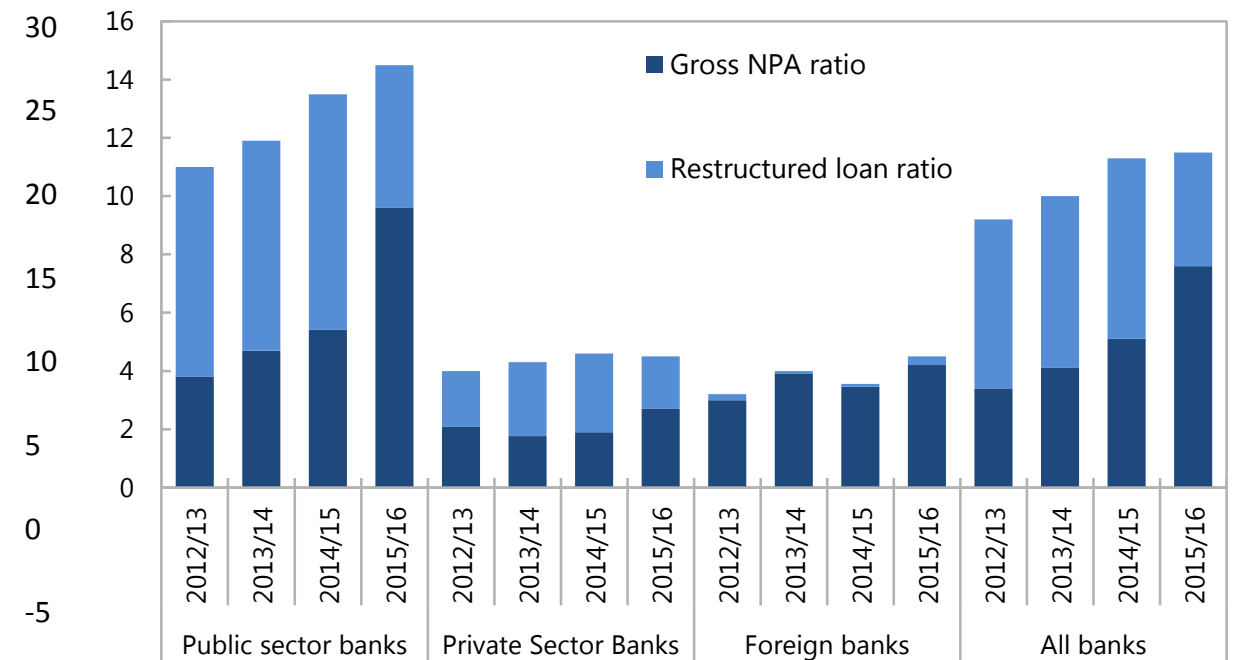
(In annual percent change)



Sources: Haver Analytics; and IMF staff estimates.

Banks' Nonperforming and Restructured Assets

(In percent of outstanding advances)



Sources: Reserve Bank of India; and IMF staff estimates.

New “Normal” for Exports: Lessons from India

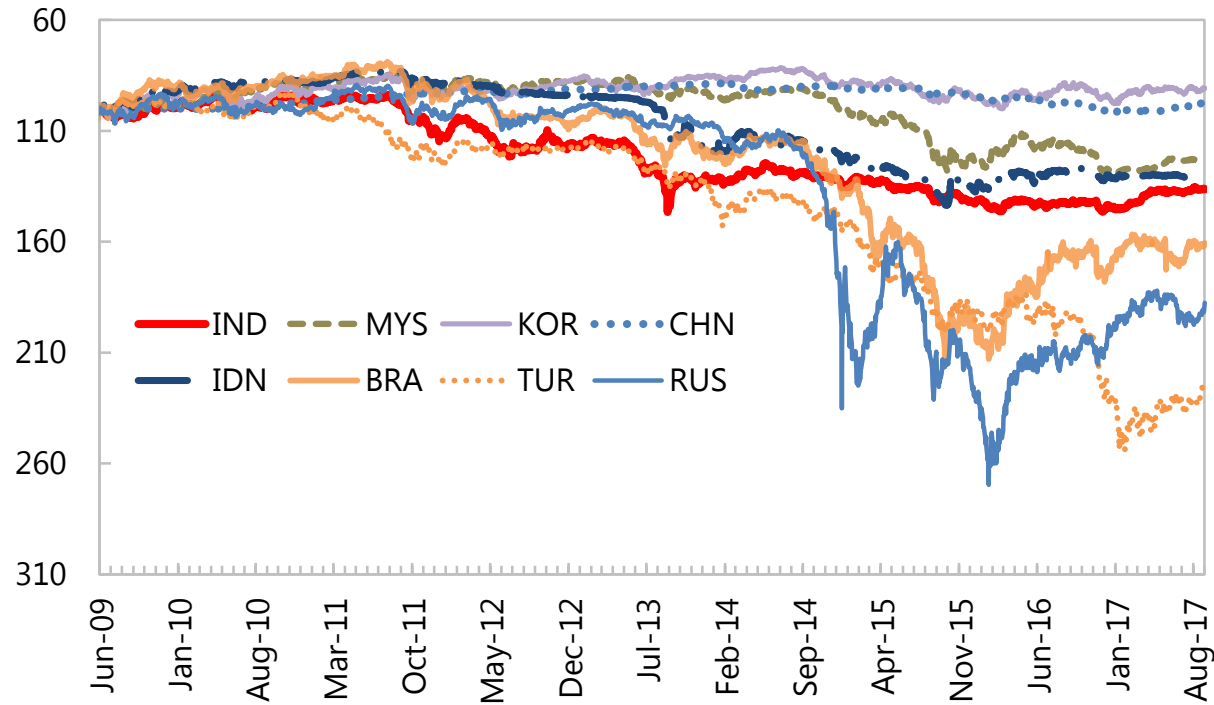
- Expand India’s export potential
 - Further trade and investment liberalization.
 - Deepen global and “national” value chains given economic size.
 - Create space to spend and expand infrastructure.
- Strengthen relative price signals and resource allocation
 - Address banking / corporate balance sheet weaknesses.
 - Labor and product market reforms to enhance flexibility and competition.

References

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Exchange Rate

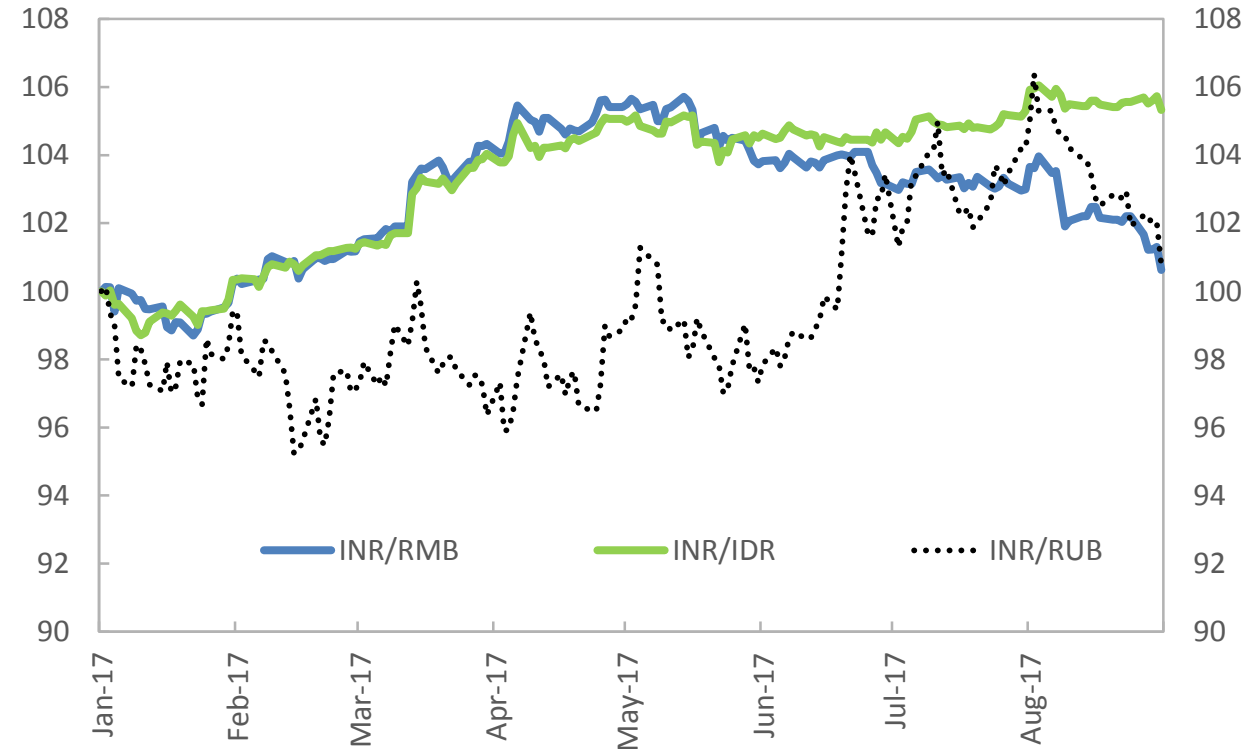
(Index, June 1, 2009=100, NC/US\$)



Sources: Bloomberg; and IMF staff calculations.

India vs. BRICS Exchange Rates

(Index, Jan 2, 2017 = 100)



Sources: Bloomberg Financial L.P., IMF staff calculations.