Book Reviews

Foreign Trade Regimes and Economic Development: India. By Jagdish N. Bhagwati and T.N. Sirinivasan. New York Columbia University Press (Published by the National Bureau of Economic Research 1975) 261 pages.

This volume on India is one of a series of research projects on exchange control, liberalization, and economic development, undertaken for many less developed countries. The study deals with three major topics: exchange control, liberalization, and growth. First, under 'The Anatomy of Exchange Control', the methods of allocation and intervention in the foreign trade and payments practised by the government during the restrictive period 1956-66 and their economic impact are discussed. Then, a detailed analysis of the 'Liberalization Episode' which covers the policies in the period 1966-68, including the June 1966 devaluation, and the episode's effect on price level, economic acitivity, and exports is given. Finally, the overall growth effects of the foreign trade regime (broadly defined as exchange rate policy plus the frame-work of rlevant domestic policies such as industrial licensing), and their possible contribution to India's rather unsatisfactory economic performance are examined.

The book is divided into five parts. Part I, provides a brief summary of the central economic and political characteristics of the Indian economy under successive five-year plans and a general view of principal developments in economic indices such as GNP price level foreign trade, and agricultural production. In order to facilitate the analysis, the authors divide the period of study, 1950-70, into five phases and identify the chronological development of the country's payments regime through these phases.

'The Anatomy of Exchange Control' is discussed in Part II. The analysis concentrates very generally on the static efficiency effects of the various foreign trade policies. This part consists of three chapters: Import Control Policy: Criteria for Allocation and Effects; Export Policy and Performance 1951-66; and Liberalization Efforts prior to 1966.

The import and exchange policy regime throughout the period 1956-66 aimed at comprehensive direct control over foreign exchange utilization. The system led to the usual disadvantages of: corruption; frustration of priorities; delays in decision making; absence of competition; bias in favour of industries using imports; protection to industries regardless of cost, efficiency or comparative advantage; and adverse distributional impact and discrimination against exports due to an imbalance between the effective export exchange rate and the effective import exchange rate.

During 1956-61, India's export performance deteriorated; but it improved during 1962-66 in consequence of subsidies granted and as a result of an expansion of trade with the socialist bloc. However, the authors maintain that the export promotion policies were inefficiently drawn and implemented. These policies became more efficient with the devaluation in June 1966, though.

Part III, the 'Liberalization Episode', contains detailed analysis of attempts to liberalize the payment regime. In the analytical framework devaluation and liberalization are carefully distinguished. This part consists of seven chapters.

Export subsidization policies were essentially of two forms: (a) fiscal measures and (b) import entitlement schemes. While the export promotion measures deployed by the Indian government involved numerous aspects (including outright subsidies and tax concessions) the principal instrument of export promotion soon became the import entitlements schemes under which eligible exporters received import licenses fetching huge import premiums pro rate to the value of exports. The import entitlement schemes set in the framework of an overvalued exchange rate were undoubtedly a useful improvement to the existing situation in which exports were seriously discriminated against; but the entitlement scheme led to unpredictably difficult and bizarre incentives for resources allocation.

On June 6, 1966, the Indian Rupee was devalued by 57.5 percent, with an increase from Rs. 4.76 to Rs. 7.50 in its official rate relative to the dollar. The objectives of the devaluation were to replace the prevailing inefficient *de facto* devaluation by a *de jure* devaluation and to reduce through the net additional devaluation plus liberalization, the adverse impact on export proformance. The devaluation was accompanied by various other measures including, in particular, a removal of the major export subsidy device—the import entitlement scheme—and a significant reduction in import duties. But the intended reform of the trade and payments regime was not fully achieved as the complex of multisided and selective export subsidization was revived. The overvaluation of the exchange rate still continued after the June 1966 devaluation; therefore, the logic in favour of export subsidization was indeed strong.

Overall, the total policy package (inclusive of export subsidization) as of and since June 1966 did improve export performance. The improvement in export performance and inflow of promised aid after June 1966, helped ease the restrictiveness on imports but it was short-lived. An industrial recession and a cancellation of promised aid after 1966-67 caused the revival of import restrictions.

Other changes noticed in the economy were a rise in prices in 1966-67 and a severe draught. The authors think that given the external constraint of the demand for a devaluation by the aid donors as a precondition for the resumption of large-scale aid and in view of the events that followed the government was probably wise in having acted in a reasonable cautions fashion by keeping the net devaluation within reasonable bounds.

In the fourth part on 'Growth Effects' the relationship of the exchange control regime to growth via static efficiency and other factors are investigated. In this regard the possible effects on savings, investment allocation, research and development and entrepreneureship are highlighted. The argument that protection for indigenously produced items was necessary to induce industrial investment is refuted by the authors. That the public sector has been an important investor in industry weakens the argument for automatic and indiscriminate protection in order to induce investment. In point of fact protection only served to influence and in conjunction with the industrial licensing machinery to determine a pattern of import substitution that certainly appears to have been relatively chaotic and unmindful of economic costs.

The implication of an improved export performance on long-term growth is explored by undertaking a simulation exercise using the Eckaus-Parikh planning model for the Indian economy. The conclusions drawn is that additional exports in the earlier years even if they were made by pushing domestic consumption down, would have more than paid for themselves by increasing investment and growth in later years.

Finally, in the 'Concluding Remarks', the authors note that the analysis in this volume points to the conclusion that India's foreign trade regime in conjunction with domestic licensing policies in the industrial sector led to economic inefficiencies which impaired economic performance.

The book is useful for those interested in a chronological account of the performance of India's foreign trade regime. While the treatment of the subject is exhaustive, intensive, and to the point, the book lacks specific policy recommendations which would be expected after such a detailed analysis. Still, the authors have taken pains in collecting data from many diverse sources and have presented a purposeful and illuminating study.

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