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Indian duty increases on imports divide a nation grappling with a weak rupee

Government wants to prop up the currency and narrow the trade imbalance

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Employees work on the outdoor units of split system air conditioners on an assembly line at the Daikin Air Conditioning India Pvt. factory in Neemrana, Rajasthan, India. Bloomberg

India's efforts to prop up the rupee by raising duties on several “non-essential” imports, ranging from fridges to gemstones and shoes, is causing alarm among some business leaders who believe the move could do more harm than good to the economy.

“Reducing imports artificially — to what extent does that make sense?” says Parimal Shah, the vice president of MK Jokai Plantation, one of India's largest manufacturers and exporters of Assam tea. “It will make the manufacturing sector of the country lazier, less quality oriented and less competitive. Markets mature when they are fluid, deregulated and highly competitive.”

The Indian finance ministry on Wednesday evening announced it was raising import tariffs on 19 items, coming into effect that night. India imported close to $12 billion (Dh44bn) worth of these goods in the last financial year, it said. Custom duties on fridges, and air conditioners, for example, have been doubled to 20 per cent, while aviation turbine fuel customs duty, which was previously not imposed, has been added at a rate of 5 per cent. Some plastic items and suitcases are also among the affected products. There are also expectations that there could be more steps to reduce imports.

New Delhi is hiking duties to try to support the Indian rupee, which has slumped to a series of record lows against the US dollar in recent weeks. It is Asia's worst performing currency this year, down about 13 per cent.

Apart from the strength of the dollar, another factor contributing to the rupee's weakness is India's widening current account deficit. With the country importing far more products than it exports, its current account deficit widened to $15.8bn in the April to June quarter this year from $14.9bn a year earlier, official figures show. Imports are paid for in foreign currency — primarily US dollars — so the demand for foreign exchange in India has a negative impact on the value of the rupee.

Consequently, the government wants to curb imports by raising their costs through higher duties with the aim of narrowing the current account deficit. The rupee did strengthen marginally following the announcement but it quickly gave up those gains and is hovering at about 72.50 to the dollar.

Not everyone is convinced that lowering imports is the best solution, especially for the longer term.

“The durable solution for having a volatile currency can only be raising India's export competitiveness and hence, earning more foreign exchange rather than curbing imports,” says Vidya Mahambre, the professor of economics at Great Lakes Institute of Management in Chennai. “Imports provide competition to domestic industry, helping it to become more efficient.”

Moreover, she points out that these products make up a relatively small portion of India's total import bill and doubts there will be a sufficient impact on the account deficit.

There are also concerns that various companies that depend on imports could be hurt by the measures, including airlines, which are already struggling to eke out profits.

Suhas Harinarayanan, the head of institutional equities research at JM Financial, an Indian investment banking company, said that this particular step to add a duty to aviation turbine fuel was “unanticipated” and would only exacerbate their bills.

Carriers are already grappling with higher crude prices, as is the rest of the country, which depends on imports for the vast majority of its oil requirement, heavily weighing on the current account deficit.

Meanwhile, Swedish furniture company Ikea, which last month opened its first shop in India in Hyderabad and is expanding in the country in one of the most significant foreign investments for India, has said it is unhappy with the steps to curb imports.

“Trade barriers such as import duties are against ideas of a global economy and ease of doing business and will lead to higher costs in India, which is not customer friendly,” Ikea's deputy country manager Patrik Antoni told *The Economic Times* newspaper.

Other analysts doubt the government has studied its move.

“Is the government actually zeroing in on the right kinds of imports?” says Indradeep Ghosh, the associate professor and faculty dean at the Meghnad Desai Academy of Economics in Mumbai. “We don't know, unless the government explicitly tells us what its view is on this matter or time passes and we actually see whether the move has been successful in reducing imports.”

Alongside the hope of boosting the rupee, the government is also eager to reduce imports to help grow its own domestic manufacturing industry.

Prime Minister Narendra Modi's Make in India scheme aims to transform the country into a global manufacturing hub, help the economy's expansion and create much-needed jobs.

Pankaj Mohindroo, the national president of the India Cellular and Electronics Association, explains that India undoubtedly has the scope to expand its electronics manufacturing sector, but there

is a lot of work that still needs to be done to achieve this outcome.

“Many import items in electronics can be easily produced in India, such as power banks,” he says. “Strategically, however, India will have to focus on making itself a global manufacturing hub for electronics and not merely focus on import curbs or substitution.”

India is also eager to boost its exports and there is speculation that New Delhi may soon announce steps to boost them, which could further help plug the trade imbalance.

The weakness of the rupee is positive for Indian exporters because it makes their prices more competitive abroad.

However, there are those who support the efforts being made to lower import volumes.

“Imports are very negative for the Indian growth story,” says Arun Singh, the lead economist at Dun & Bradstreet India. “Non-oil and non-gold imports have surged and I would say that the actions taken by the government are for the good health of the Indian economy.”

The Make in India programme has not “picked up” as planned, partly because of the fact that imports from countries including China are so cheap, so there could be scope to increase more duties on goods that could be manufactured in India, Mr Singh says.

But he warns the risk that comes with raising import duties is that other countries may react by imposing retaliatory tariffs. This comes at a time of growing protectionism and concerns about global trade wars.

“We are a global economy and we're not decoupled,” says Mr Singh. “Any action taken by any country will have significant repercussions from other importing and exporting countries. That would impact our exports going forwards.”

Navin Khanna, the India director of BoConcept, a Danish luxury furniture brand, explains that although his company depends on imports, its products are not among the items affected by the increases and he welcomes the measures, which he describes as “a good move”.

What worries Mr Khanna is the slump in the rupee, because this makes his own imports more expensive, so he is happy to see that the government is actively trying to arrest its slide.

“If the rupee continues to fall, that's a much bigger concern,” he says.

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