The considerations leading to the imposition of the regulatory duty on imports have been set out in the Finance Minister's statement in Parliament on 17 February 1965, which has been circulated as GATT document L/2447. Information on subsequent economic trends and the policy measures adopted is contained in the various documents circulated for the meeting.

At the time the regulatory duty was imposed, the foreign exchange reserves of India, excluding gold, had fallen to a level of around Rs.1,000 million; over 1964-65 as a whole, the decline in reserves was as much as Rs.720 million and there had been a fall of Rs.170 million despite drawal of Rs.476 million from the International Monetary Fund even during the October 1964-March 1965 half year when there is normally some improvement. The decline in reserves has continued since. During April-September 1965, there was a decline of Rs.50 million, and in addition there was a drawal of Rs.360 million ($75 million) against a standby which was negotiated last March, from the International Monetary Fund. The level of reserves on 29 October 1965 at Rs.1,343 million excluding gold, was equivalent to less than six weeks' imports. This is inadequate, particularly in view of the fact that India has an outstanding commitment to repurchase $125 million from the International Monetary Fund.

The serious pressure on reserves has been the result of a rising debt service burden, larger imports of food and requirements for development, and expansion of exports at an inadequate rate. While the utilization of external assistance and the proportion available in non-project form have shown improvement, this has not sufficed to prevent the fall in reserves.

During 1964-65, imports amounted to Rs.13,630 million as compared to Rs.12,030 million in the previous year. The increased payments for food purchased outside Public Law No. 480 alone rose by Rs.290 million between the two years, in spite of an increase in foodgrains output of over 10 per cent. This was because stocks had been depleted as a result of the stagnation in agricultural output in the previous years. Increased imports of other commodities were the result of a faster tempo of development and some liberalization of import licensing during that year. A high level of imports has continued during the current fiscal year.

The level of exports during 1964-65 at Rs.8,030 million showed a rise of only Rs.10 million in comparison with the previous year. During 1964-65, there was some lag between export shipment and receipts, partly on account of an interest
rate differential between the United Kingdom and India until February. This gap has narrowed in recent months. Currently, however, exports are running at levels slightly below those of last year. For April-August 1965, customs data indicate exports of Rs.3,140 million as against $3,260 million in the corresponding period last year. In part, the fall in exports is the result of lower world prices for items such as iron ore and sugar. The availability of vegetable oils for export has been negligible owing to a poor crop.

The debt service burden is mounting in spite of gradual improvement in the terms and conditions of fresh assistance. The payments of interest and amortization of loans amounted to Rs.1,210 million in 1964-65 as compared with Rs.1,110 million in the previous year; in the first half of the current fiscal year such payments have amounted to Rs.700 million—nearly 40 per cent more than in the comparable period of last year.

While the payments on invisibles account are governed by the exchange control, there has been a steady decline in receipts in recent years.

The balance-of-payments position during last year and during the current year would have been even worse but for the substantial improvement in the utilization of external assistance, which in turn has been possible, in part, because of the larger share of non-project assistance. Aid utilization in 1964-65 was Rs.5,026 million of which non-project assistance amounted to Rs.1,910 million. Utilization of project assistance in the previous year was Rs.2,564 million and of non-project assistance Rs.1,500 million.

The regulatory duty is one of the series of measures designed to deal with the balance-of-payments situation. It seeks to effect a measure of economy in imports. No doubt imports are restricted through quantitative controls. There are, however, commodities such as petroleum products for which the use of quantitative restrictions is administratively inconvenient. It has been the practice to inhibit the consumption by duties, providing exchange allocations adequate to satisfy the demand. Further, in the case of imports for which the foreign exchange necessary has to be determined on an ad hoc basis, such as imports of machinery and spare parts, detailed physical screening of the list of goods proposed to be imported cannot be fully effective and a price deterrent for imports was judged to be necessary. Over the years considerable capacity has been built up within the country for the manufacture of numerous items of industry, transport, power, mining and other equipment. A higher level of import duty on the finished goods encourages industry to actively seek local substitutes, thereby resulting both in some reduction in aggregate foreign exchange outlay and more efficient use of the foreign exchange that is, in fact, spent on imports. While the regulatory duty is thus conceived as an instrument to relieve the heavy pressure on India's balance of payments, it is not likely to result, as it has not, in an absolute decline in imports. India’s needs for imports will grow with development; the problem is only to put a restraint on the growth consistent with the ways and means position. It may be added that the regulatory duty has, consistently with the objective behind it, been applied in a wholly non-discriminatory manner as between commodities; only a few exceptions have been made.
The Finance Minister observed, while introducing the regulatory duty along with other measures: "The strictest fiscal and monetary discipline has to be observed in the interest both of stability of prices and of improvement in the payments position." The measures taken included the increase in the bank rate by a full percentage point from 5 to 6 per cent, a further stiffening in the terms of lending by the Reserve Bank to the commercial banks in the interest of credit control, a decision to review all demands for imports against free foreign exchange and an appeal to the Aid India Consortium for maximum possible assistance in non-project form. Just about that time, India approached the International Monetary Fund for a standby credit of $200 million.

Further measures have since been taken to strengthen the balance of payments. The budget for 1965-66 visualized a nominal surplus for the first time in many years. In order to stimulate private savings and investment, personal income taxation was reduced at all levels; and in order to stimulate industrial growth, concessions were given to priority industries in corporate taxation. The budget contained special provisions for stimulating exports. A number of concessions in taxation were given to an important export industry, namely, tea, following the recommendations of a committee. A new scheme of tax credit certificates was introduced under which exporters are granted tax credit certificates up to 15 per cent of the value of the exports. The tax credits so far announced cover around half of India's exports. It may be added that adoption of more liberal commercial policies by India's trading partners can make a very useful contribution to these efforts.

As the pressure on reserves continued to recur in the earlier part of the current fiscal year, it became necessary to suspend the issue of fresh import licences other than against assistance and private capital inflow from about the middle of May, licensing being resumed from 1 July 1965. The import policy for the current year was announced on 30 June in so far as established importers are concerned and the procedure with regard to actual user licensing was announced on 2 July. The full import trade control policy for the year was subsequently published on 15 July 1965.

In order to phase the utilization of licences already issued, a scheme of advance deposit against imports was introduced under which importers were required to make a deposit of 25 per cent of the value of imports. The deposits were refundable after a period of two months. This was essentially a transitional measure. In the supplementary budget for 1965-66, which was presented in August 1965, the import tariff was rationalized and at the same time it was announced that the advance deposits would no longer be called for. As a result of the supplementary budget, the tariff structure has been readjusted to suit the present stage of Indian development. Unnecessary discrimination as between tariff items has been removed, the broad structure of rates adopted being 35 per cent for machinery (with lower rates for certain items, such as those important for agriculture), 40 per cent for basic industrial raw materials, 60 per cent for other intermediate goods and 100 per cent or the previously existing rates for consumer goods.
It may be noted that the surcharges on duties levied earlier have been withdrawn, with a view to simplification. Duties bound under the GATT were not raised above the bound levels, but it was stated that in due course renegotiation might be sought on some of these items. Certain excise duties were also raised. A supplementary budget was necessary because it was found that expenditures were running at levels higher than anticipated and it was thought desirable to take timely action in the interest of stability. The rationalization of the import duty structure would also, it was stated, help import substitution.

The balance-of-payments situation has become even more acute as a result of recent developments on India's borders. The policy of the Government of India continues to be to pursue development vigorously while making adequate provision for the country's defence. It is now considered essential to strengthen the balance of payments even more rapidly than was visualized earlier. Certain measures have been recently announced to further this objective. Reference was made earlier to the reduction in inward remittances on account of invisibles. Under the National Defence Remittance Scheme certain import facilities are granted against inward remittances to Indian nationals by way of gifts, family remittances and transfer of capital. A new Gold Bond Scheme has been announced providing for the return after fifteen years of gold subscribed in the form of bullion or ornaments, with an interest rate of slightly below 4 per cent. New series of Government bonds have also been issued to mobilize internal resources.

While all these measures will be of help, the difficulties of balance of payments are likely to continue in view of the expected decline in production in certain crops this year. Failure of rains has affected the groundnut crop and also the cotton crop in several parts of the country. No firm estimates of crop are yet available, but it is feared that the decline in oilseeds' production will be substantial and that the cotton crop may be about 5 per cent lower. The position regarding food grains is also difficult. Production of rice will at best be the same as last year; as regards wheat, sowings have been reasonably satisfactory, but the position will be known only after a few months, since the main crop is harvested in March-April. Government is determined to intensify procurement operations and also improve the machinery for distribution, introducing rationing in towns with the population of more than a million. With the best effort, however, some imports of food grains will be necessary and this will put a pressure on the balance of payments.

A decline in output of commercial crops such as cotton and oilseeds will tend to reduce export earnings and in spite of the concerted effort being made to step up exports, a substantial improvement will be difficult to achieve in the short run. Import requirements, both for food and articles needed for development are growing. The Indian balance of payments will thus continue to be under considerable pressure during the coming year. While capital inflows will be of considerable assistance, it will continue to be imperative to take all measures necessary for restraining imports and making the best use of the foreign exchange available. It is against this background that the levy of the regulatory duty on imports must be viewed.