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Govt likely to correct inverted duty structure in FY24 budget

Centre also weighs steps to expand export credit and insurance cover

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NEW DELHI: The government will likely consider correcting the inverted duty structure across sectors impacting domestic manufacturing in the upcoming Union budget, as muted external demand affects India's exports and current account balance.

The government is also considering measures to expand export credit and insurance cover, encourage services exports and provide marketing and branding support for products such as khadi and coir with geographical indication (GI) labels.

The inverted duty structure, where inputs or raw materials are taxed at higher rates than finished products, hurts the competitiveness of Indian manufacturers, especially in sectors such as textiles and apparel. This makes an Indian-made product more expensive than an imported finished product.

India has been increasing import duties since 2014-15 to correct the inverted duty structure for non-FTA countries. BLOOMBERG

"Correcting duty anomalies is key to attracting investments in manufacturing and improving India's export competitiveness. The ministries of finance and commerce have examined it and may try to correct the anomaly where deemed fit," a government official said, requesting anonymity.

India's current account deficit (CAD) widened to a nine-year high of 4.4% of GDP in the second quarter because of a higher trade deficit, reflecting the impact of slowing global demand on exports. The country recorded a CAD of 3.3% of GDP in the first half of the current fiscal.

Businesses have raised concerns about the inverted duty structure of finished products made from aluminium, copper, and copper alloys, such as tubes, sheets, and rods, which can be imported duty-free from Asean while a 5% import duty is imposed on essential raw materials like aluminium and copper scraps and copper cathodes used to manufacture them in India.

Arpita Mukherjee, a professor at policy think tank ICRIER, said high import duty is making it difficult for companies to establish global value chains. "For instance, if a company from China is shifting its value chain to India, it needs a smooth global value chain. We need to understand the reason for import dependence. If it is because we don't have the raw material and intermediate product, we don't have an option but to allow import. And it should be as cheap as possible because if we have a manufacturing base, it should be cheaper," Mukherjee said.

The budget is also expected to announce adjustments in the duty structure for the $200-billion apparel and textile sector. Textile manufacturers said they have been forced to cut production days due to high cotton prices, while cotton yarn exports, a key raw material, are projected to drop 28-30% in FY23 due to weakening global demand.

Queries emailed to the spokespeople for the ministry of commerce and industry and the finance ministry on Tuesday remained unanswered till press time.

India has been increasing import duties since 2014-15 to correct the inverted duty structure for non-free trade agreement countries, and the average tariff rose from 13.5% in 2014 to 15% in 2020 and 18.3% in 2021, according to the World Trade Organization (WTO). The past two budgets sought to correct it by removing duty exemptions and lowering the duty on raw materials.

Asean's share in India's total imports has grown from 8.2% in FY11 to 11.1% in FY21, while exports have remained stagnant at 10%.

Merchandise exports are affected by the demand slowdown in key markets, with outbound shipments at $31.99 billion in November, a mere 0.59% increase from a year earlier, according to official government data. Merchandise exports contracted 16.7% to $29.8 billion in October.

Biswajit Dhar, a professor at Jawaharlal Nehru University, said the focus on fixing inverted duty structure should be on either export-oriented sectors or having high export potential. "On the one hand, the government wants to reduce import dependence, and in trying to do that, they are putting a higher duty on components that they want to indigenize... take the example of active pharmaceutical ingredients (APIs)," Dhar said.