Implications of Increase in Import Duties

Why in news?

The government is reportedly considering a further increase in import duties on crucial components used in electronics manufacturing.

What is the proposal?

- The Union ministry of commerce is examining a possible increase in the import tariff imposed on compressors.
- Compressors are an integral part of the cooling mechanism in such white goods as air-conditioners (ACs) and refrigerators.
- A duty hike is also considered in pre-coated steel sheets and copper tubes that are also used in the manufacturing process of these items.
- This follows a previous increase in the duty on compressors last year, from 7.5% to 10%.

What is the rationale?

- The central idea is to boost domestic manufacturing.
- Also, the commerce ministry is said to be concerned about the growing current account deficit (CAD).
- [The current account measures the flow of goods, services and investments into and out of the country.
- The current account includes net income, including interest and dividends, and transfers, like foreign aid.
- A country runs a current account deficit mainly if the value of the goods and services it imports exceeds the value of those it exports.]
- CAD was dangerously close to 3% of the gross domestic product (GDP) in the quarter between July and September 2018.
- So a tariff hike that raises the price of imported goods would depress the demand for those items.
- This would, in turn, exert downward pressure on the current account deficit.

Why is it not advisable though?

- Increasing the import duties will have dangerous long-term implications.
- Merely raising import duties hardly ever improves the overall outcomes either for consumers or producers.

- Domestic consumers will likely suffer the impact of costlier imports.
- Raising the tariff on components pressurises large companies to move manufacturing offshore.
- E.g. manufacturing of flat panel LCD screens was moved out to Vietnam after an increase in duty

What can be done?

- A safe way to deal with a current account deficit that is structurally high is to increase exports in a sustainable manner.
- This can be achieved by creating a globally integrated, competitive manufacturing sector within India.
- Manufacturers need a sense of security about their costs.
- They would otherwise choose to locate their plants in places where there is more predictability about the availability and cost of components.
- So the government should not raise tariffs impulsively as is being considered now.
- Tariffs that are high only dis-incentivise the incorporation of India into the global supply chains.
- Crucially, this engagement is central to how manufacturing, especially in the electronics and appliances sector, works today.
- A robust approach would be to institute wide-ranging measures to boost exports and simultaneously reduce the import-intensity of the economy.
- Also, protectionist policy cannot be controlled for the benefit of one sector or another.
- So it is important to ensure that tariffs stay low across the board.

Source: Business Standard