India's Engineering Sector in Dire Strait

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The global economy is passing currently through severe stress due to a sharp decline in manufacturing activity following the deep slowdown in the world economy. While the world economy is yet to overcome the fallout of the Lehman Brothers' collapse in 2008, the exit of United Kingdom (popularly known as Brexit) from the European Union has multiplied uncertainty in the global economy. The world awaits its actual implication on the global economy and its spill over to the manufacturing sector. The quantum of implication, however, will be known only after the United Kingdom's ability to cope with the new lease of life and protect itself from any massive economic and political instability. The United Kingdom, meanwhile, is certain to face a crisis to maintain its geographical and business integrity not only with the rest of the countries in the European Union and world.

Interestingly, frequent change in the economic growth of the United States has sent an uncertain signal to the world economy resulting into the global manufacturing sector pushed through rock bottom.

Mining and engineering sectors have, therefore, performed the worst growth in the last eight years. Surprisingly, there is no ray for its recovery in near future as the United States' Federal Reserves (US Fed) delayed raise in the interest rates sending thereby the global manufacturing into yet another jittery.

Significance of Engineering Sector in Steel Industry

Engineering sector contributes nearly 10-12 per cent of global steel consumption in the form of heavy, medium and light machinery. India's engineering exporters found themselves battling global slowdown in 2015, marked by sharp erosion in commodity prices leaving a negative outlook for these shipments which may be confined to $60 - 62 billion for the current fiscal despite seven to eight per cent depreciation in rupee against dollar. In the fiscal 2014-15, engineering exports had aggregated over $70 billion. Engineering exports account for about 23 per cent of India's total merchandise exports. Primary iron and steel along with all non-ferrous metals and products contribute the maximum to the engineering export basket. These segments saw a real blood bath in the export market, leaving absolutely no pricing power with the producers of suppliers. The situation has been worsened by excessive protection given by the government to the domestic large scale steel firms by way of safeguard duty, anti-dumping duty and minimum import price (MIP).

Impact on India's Engineering Exports

Engineering exports from India, which remained heavily dependent with its large equipment supply upon manufacturing sector, declined by half in the financial year 2015-16 due to weak global economic sentiment. The growth rate in the top 25 countries during April-February 2015-16, taken together recorded fall in exports by 18.1 percent which is more than the fall in India's total engineering exports by 17.4 per cent.

"The global trade has been going through a major crisis like situation with demand slowdown across different segments. Still, the neighbouring markets which are also members of the SAARC trade regime, have been contributing a significant chunk to the engineering exports. While differential trade regime is in prevalence for these countries, a lot more emphasis needs to be given to Sri Lanka, Nepal and Bangladesh. In fact, these countries are a low hanging fruits for us, when the going is tough," Chairman of the EEPC India T. S Bhasin said.

The level of distress for India's engineering exporters can be gauged from the fact that the drop in several key destinations has crossed 50 per cent while in the case of Malaysia, the fall has been above even 90 per cent, almost evaporating the market , for January 2016 over the same month last year, according to an EEPC India analysis. Malaysia, for example, one of the top 25 destinations for India's engineering exports witnessed a sharp decline in engineering exports from india. For January, 2016 the shipments there plummeted to mere $78.22 million from a sizeable $830.88 million a year ago. When close to a billion dollar disappears from a single market in just one of the sectors, the depth of the problems can be gauged.

Sri Lanka, Nepal and Bangladesh have emerged as the major destinations for India's engineering exports together accounting for a sizeable chunk of $5.17 billion, necessitating increased policy priorities to the neighbouring three countries. Though the shipments to the neighbouring countries have also dropped significantly in value terms, the trend is in line with the rest of the global markets which are witnessing new lows thanks mainly to a prolonged meltdown in prices of commodities and metals. Despite the drop in values, Sri Lanka itself occupies the third most important space in Indian engineering exports. After the US and UAE, Sri Lanka gave the next best markets to the Indian shipments with $2.63 billion during April-February period of the fiscal 2015-16. The US market was at the top with $6.31 billion billing and the UAE at $3.8 billion for the period. In certain segments like iron and steel, the neighbouring nations dominate the shipments. For instance, in steel, Nepal tops the list importing 8.4 per cent of India's total export in these products during April- February 2015-16. It imported $426 million during the period, way up other major markets including the US and China. In the entire engineering pack, Nepal accounted for $1.2 billion while Bangladesh $1.3 billion for the period under review. Cumulative engineering exports from India conceded 17.33 percent fall during April 2015 –February 2016 to $53.68 billion from $64.94 billion during the same period of the previous fiscal.

Regional Preferences

Out of the top 25 countries, 19 countries recorded negative growth in the month of January 2016, while of 33 engineering products, 22 recorded contractions. The analysis shows that engineering exports to UAE, the second largest market destination after the US, dropped by more than half to $484.12 million from $991.17 milion year-on-year. To the Middle East and West Asia region, which has been witnessing its own serious problems because of a significant downturn in the crude oil prices, India's engineering consignments dropped by 43.88 per cent to $803.39 million from $ 1.43 billion Y-on-Y. China which was considered an engine of global economic growth and the major consumer of the global metals and products gave Indian engineering exporters a much lower(by 36.35 per cent) market at $124 million in January this year against $ 195 million.

When it comes to products category, the major fall has been witnessed in iron and steel dropping by almost 50 per cent to $355 million from $709 million Y-on-Y. Likewise, the fall in copper and products was over 47 per cent from $306 million to $160 million. Overall, as a pack, the engineering exports that accounted for nearly 23 per cent of merchandise export in January 2016 dropped by 28.07 percent to $4.824 billion from $6.707 billion Y-on-Y. The worst thing is that such a drop has come about on a low base created by almost a similar drop in the same month last year.

Steel Duty Protection Hit Producers

Engineering goods exporters hailed extension of safeguard duty on steel as an anti-SME (small and medium enterprises) move that will further dent the country's exports, already down in the dumps. The Steel Ministry itself has taken note of the fall in steel imports by almost one-fourth in April - February period of the fiscal 2016-17. Even with the Quality Control Order and the MIP (Minimum Import Price) regime continues, "There was no case for continuation of Safeguard duty till March 2018, when there are already indications that global prices of steel have started to increase." The continuation of the safeguard duty not only makes engineering exports uncompetitive, but also there is no specific reason for the levy on HR Coils, which is a basic raw material for engineering products, especially when MIP has already been slapped.

Cautioning the imposition of Minimum Import Price on steel products will lead to further erosion in engineering exports, exporters sought from the government a compensatory mechanism to make up for the increased raw material price which the distressed exporters, mostly in the SME segments will be made to bear, following big protection given to the large steel manufacturers.

"The introduction of the Minimum Import Price on steel products will raise the cost of raw materials for engineering products by about 6-

10 per cent depending upon the nature product. This will have a serious debilitating impact on engineering exports which have already declined by a huge 15 per cent in the first nine months of the current fiscal," said Bhasin.

Segments like auto and auto parts, industrial and electrical machinery, products of MSME sector, which in any case have low margins and are facing cut throat competition will face sudden escalation in raw material price, giving a further jolt to the exporters. Moreover, the move will have an inflationary impact on the entire manufacturing sector and leakages of money as all import invoices will be at MIP now. The government must provide steel at global competitive prices and exporters sought from the government a compensatory mechanism for higher steel prices that the MIP entail on domestic prices. A new International Price Reimbursement Scheme (IPRS) should be immediately introduced.

Conclusion

To uplift the sentiment in engineering sector, the government should help improve competitive strength of the exporters, particularly by revisiting some of the flagship schemes of the Commerce Ministry. In the wake of a sharp fall in the exports for over 15 months and re-modeling of the global supply chain where outsourcing is being replaced by domestic supply of inter-mediaries, the heady days of the double digit growth would stay only in memory, at least for some time. Thus, the Commerce Ministry's MEIS (Merchandise Exports from India) scheme should be set aside and replaced with a new dispensation wherein the benefits accrue for all tariff lines and for all countries, exporters urge to the government. This will also lower transaction costs as the need for landing certificates or any other alternatives will not be necessary, they said. Besides, the MSME investments limit in plant and machinery is yet to be enhanced by the Government which had proposed to enhance the upper limit to Rs. 30 crore from the present level of Rs. 10 crore. This has not yet been done, though the Bill for the amendment was introduced in April 2015. "We request the government to increase the limit as it is important for the success of the 'Make-in-India' initiative of the government of India. This will enable the MSME Sector to play a pivotal role in the laudable initiative of the Prime Minister Narendra Modi and the success of the 'Make-in-India initiative as well as becoming part of the global value chain, exporters said.

There are many countries which are sanctioned against by EU and USA, such as Syria, Sudan, and Lebanon etc. The RBI allows payments to be received from Open cover countries. However, Indian banks do not accept such payments even if they are from Open cover countries. It is suggested that either India should have a currency swap agreement or Rupee Trade Mechanism for this purpose. In fact India should try to have Rupee Trade Mechanism with those countries with whom it has a trade surplus.