Assessment of Neomercantilism in India's Economic Policies in Post-COVID Era

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Abstract. The COVID-19 outbreak has exposed various problems in global governance and impacted the international system and the old international order. In order to cope with the epidemic and the changing international situation and to leave from economic difficulties, the Modi government has adopted a series of neomercantilism policies to meet the uncertain challenges. This paper analyzes the implementation of Indian policy from the manufacturing, international trade, and consumption industry. Because the epidemic factors will be long-term and policies are effective only within a period, neomercantilist policies are only viewed as a phased tool. They cannot provide long-term support for economic development. Coupled with structural contradictions in the Indian economy, the effect of Indian policies is not good. The long-term development of the Indian economy still needs to be worked hard to solve the economy's fundamental problems and realize industrial transformation and upgrading.

Keywords: Indian economy; Neomercantilism; Post-COVID era.

1. Introduction

One of the most distinctive features of India’s economic growth since the liberalization reforms of the 1990s is the fastest growth of the service industry, followed by industry and relatively weak agricultural growth. As one of the largest developing countries in the world, India’s international trade and services industry has maintained strong growth momentum.

Since the early 21st century, India has gone beyond the initial crisis-driven stage, beginning with the global economy, internal structural reform, and further external integration. India’s economy has developed more profoundly into the world economy simultaneously. Its biased economic development has been troubled, including slowing growth, investment decline, high unemployment, and manufacturing recession [1].

As one of the countries hit by the pandemic, India’s economy has been hit by two waves of a pandemic. With the blockade, annual economic growth set the worst record since independence, trade shrank, unemployment soared, the gap between rich and poor widened, inflationary pressure remained high, and industrial development was severely frustrated [2].

The opportunity for profound changes in the international order is to turn the crisis into an opportunity to the maximum extent possible and act accordingly to advance our external strategy. From the official statements and specific policy practices, India believes that the epidemic has accelerated the reform of the international order, intensified the strategic competition between China and the United States, and accelerated the reshaping of the global industrial chain, which has more challenges and opportunities for India. India’s strategic community generally believes that the epidemic has weakened the leadership of China and the United States over the change in the international order and that India has the responsibility and the opportunity to become the leader of the multilateralism.
2. Literature Review

2.1 Overview of the Research on the Neomercantilism

As the starting point of the development of modern economics and the precursor of national interventionism, the mercantilist originated in the era of excellent navigation, that is, in the process of the first globalization. In the traditional framework of the history of economic thought, mercantilism is regarded as an economic theory that emphasizes the development of a commodity economy. Today, it is widely criticized for its backwardness in the vigorous development of liberalism.

Adam Smith, who initially proposed the “mercantilist”, attacked the mercantilist in the Wealth of Nations as a state intervention to limit the free development of wealth. Joseph Alois Schumpeter even regarded the mercantilist as a “fictitious system” and summarized the core of its theoretical system as export monopolism, foreign exchange control, and trade balance [3].

Typical mercantilists in the late 17th century believed that material prosperity would be inseparable from an effectively controlled economy. The critical point is to encourage the development of local industries and export business behavior and the restrictions on imports, that is, adhere to the trade balance theory, advocate the development of industry, expand the amount of excess of foreign trade, ensure the import of a large amount of money, and thus bringing about the accumulation of domestic monetary wealth.

Over more than 500 years, mercantilism has fallen under liberalism at the theoretical level. However, in terms of economic practice and foreign policy of major powers, mercantilism frequently appears as a standard means for governments to deal with economic challenges.

After the First World War in the 1920s, the neomercantilism was born in response to the post-war economic crisis. It was named for the policy it described as much like the mercantilist of the 15th century. The two have many differences on the same basis. First, the neomercantilism follows the analysis method of Keystone theory, arguing that trade surplus also has multiplier effects like investment and consumption. In addition to inheriting many core elements of classical mercantilism, It also contains many new elements and new ideas: (1) the neomercantilism no longer accumulates the money stock, and instead emphasizes the circulation of money and the accumulation of physical wealth and the prosperity of industrial economy; (2) the neomercantilism borrowed from neoclassical economics, greater emphasis on economic development and the acceptance of free economic competition to a greater extent, more economic means rather than administrative means to intervene in the national economy; (3) the neomercantilism attaches more importance to economic independence and fair competition, and adopts protectionist policies to ensure the level playing field of their commercial and industrial economies in the world economic system; (4) the neomercantilism adopts various economic policies to regulate the economy and achieve the leapfrog economic development [4].

The idea of the neomercantilism has evolved today, providing some countries with “effective” methods to protect national interests and trade security in the face of “black swan” events such as COVID-19. Nowadays, the issue of global epidemic governance has become a hot topic of academic research. Some scholars believe that the definition of neomercantilism should be linked with the “new localism” in the global background, more accurately, the embodiment of the pursuit of regional [5]. Through the appearance of various countries in the COVID governance, the failure to establish an international joint prevention and control mechanism, and the trade friction among countries, it can be found that the root cause of this situation is that realism (mercantilist) is still the dominant concept of epidemic governance in the international community.

2.2 Studies on the Indian Economy and Mercantilism

After the 1970s, many new industrial countries (NIC) were welcomed by many major countries in the national trade market due to their endowment, inexpensive export products of labor, natural resources, and other factors. Trade has maintained a long-term surplus and accumulated many foreign
exchange reserves and assets, thus gaining a particular competitive advantage in foreign trade. The gradual rise of India as an emerging market economy using the export-oriented development strategy is also an essential manifestation of the development of the neomercantilism.

Since the outbreak of COVID-19 in 2020, many scholars have conducted in-depth research on the impact on the Indian economy and have achieved rich results. The mainstream academic circle believes that COVID has “worsened” the Indian economy; that is, India, already in the economic downturn, suffered the impact of the epidemic, forcing the Indian government into constraints. In addition, the Indian government, after realizing the seriousness of the situation, has already responded and taken measures to withstand the second outbreak of the disease in India.

The Modi government, coming to power after the 2014 Indian election, has built an ambitious policy vision bound to take a larger share of the international system. However, some Indian scholars, after observing the government’s expectations and actual results, believe that the Modi government prefers a kind of “political marketing” [6]. Under the management of the Modi government, India’s GDP growth fell from more than 8% in 2016-2017 to about 4.0% in 2019-2020, but the pandemic has masked the mistakes and incompetence of the Modi government. At present, the Modi government is facing all-around pressure, such as sluggish macroeconomic growth, the difficult recovery of the real economy, continuously rising unemployment and inflation, the high fiscal deficit, and the sustained depreciation of the rupee. This reveals that the Modi government is seemingly bad at dealing with complex economic problems.

Based on the neoclassical growth model analysis of the impact of the epidemic outbreak in different sectors of India, some scholars believe that the spreading COVID pandemic has distorted the world’s booming economy in unpredictable and ambiguous terms. However, it is also accompanied by a unique opportunity for India’s economic development to develop “Made in India” with independence on a sustainable development model [7]. The Modi government’s slogan, “India is Made for the World,” highlights the current mercantilism tendencies in the current context of India’s openness [1]. Meanwhile, India has adopted high tariffs, low-price exports, and other trade policies that have reflected the characteristics of neomercantilism.

Most Indian scholars believe that Indian export growth has a positive impact on economic growth. Based on it, some scholars use the Granger causality test to find and confirm the two-way causal relationship between India’s exports and economic growth and import and economic growth [8]. That is, India’s economic development is inseparable from international trade, which explains why its economy is dying down so quickly under the closed control of the epidemic. India’s raw materials and product manufacturing are highly dependent on overseas markets. The epidemic’s impact makes the manufacturing supply chain enter a short period of “stagnation”. In the post-epidemic era, India’s economic recovery shows “K” characteristics. Large companies grow rapidly, small, medium, and micro enterprises (MSME) continue to shrink, and the differentiation is increasingly apparent. If separated from the government macro-control, it can be predicted that the monopoly of enterprises will become stronger and stronger, and the balance of the domestic market cannot be guaranteed.

The debate about liberalized trade has continued for a long time. Some Indian scholars have found that since the late 1980s, the Indian policy has shifted from “pro-market” to “pro-business” and was accompanied by the acceleration of India’s economic growth [9].

Until now, under the background that “the Indian government should pay for its own policy mistakes and the economic impact of the pandemic,” the concept was widespread [10]. Some scholars believe that the political will of the Modi government should be biased toward protecting people’s lives rather than a short-term election victory [11].

At present, the Indian government is in place by delivering grim information about the global epidemic prevention and control situation, shaping the image of India’s rising international influence during the epidemic, and easing the domestic people’s dissatisfaction with the government’s epidemic prevention and control.
2.3 Research Gap

So far, international research on the challenges and development trends facing the Indian economic epidemic has achieved many results, and some studies are still relatively thorough in some aspects. However, they lack an analysis of the Indian policy. This study prepares under the neomercantilism horizon according to the government of India, combined with the Indian historical background, analysis of the deep reasons behind the impact of the Indian economy, defines the future development of its economic development, and analyzes India’s international trade policy trend, in order to assess better the Indian economic development trend.

3. India’s Economic Dilemma

3.1 Manufacturing

India’s manufacturing sector had been in trouble for quite a long before the COVID-19 outbreak, and its share of the GDP has fallen for several years, from 17% in 2006 to 13% in early 2020 [1]. The main reason is that India’s infrastructure construction is weak, the traditional technology manufacturing industry accounts for a large proportion, the industrial chain development is slow and relatively single, and the manufacturing industries urgently need transformation and upgrading. With the outbreak of the epidemic and the policy control, the workforce demand of the traditional manufacturing industry is not met; many countries have adopted closed quarantine policies, resulting in the lack of the upstream of the Indian manufacturing industry chain and the shutdown of the supply chain.

In the Indian market, according to the World Bank’s ease-of-business index, India is not ranked high, with further reforms in “tax payment”, “emissions,” and “execution contracts” mainly needed [9]. This reflects the challenges multinational enterprises face in the Indian economic market environment and sets up obstacles for foreign investors to choose an investment. India’s infrastructure, land, and labor policies are deficient, so only a quarter of the direct investment that flows into India enters manufacturing.

As shown in Figure 1, in January 2020, the purchasing managers’ index (PMI) was 55.3, at its highest point in eight years. This was driven by a significant increase in production and higher new orders overseas. India’s manufacturing PMI was 54.5 in February, slightly down from January. The index continued to fall slightly in March to 51.8. In April, PMI was 27.4, which was already well below the baseline value of 50. The poor situation is mainly due to the increasing number of confirmed COVID-19 cases in India at the end of March. On March 25th, in response to COVID-19, a “shutdown” policy was announced, which stopped the plant, resulting in large numbers of unemployed workers and lower domestic demand. At the same time, foreign outbreaks have led to a sharp drop in new export orders. The international market also cannot support it either [12]. These combined reasons have put India’s manufacturing PMI below the baseline of 50 by August 2020.

![Fig 1. Manufacturing PMI trends in India 09, 2019-08, 2022 [13]](image-url)
3.2 International Trade

India’s main growth point in its economy has remained in services, mainly service export and outsourcing, a critical way to make up for its massive trade deficit.

India has a bidirectional causal relationship between exports and economic growth. As a result, economic growth surges by increasing exports, which positively impacts economic growth. Therefore, the growth-oriented export-oriented and export-oriented growth hypotheses are valid for India. Thus, in India, economic growth surges by increasing exports, which positively impacts economic growth [8].

Fig 2. Indian export figures 09, 2019-08, 2022 [14]

Fig 3. Indian import figures 09, 2019-08, 2022 [15]

The outbreak of the epidemic in early 2020 made India’s international trade into trouble, and the import and export data shrank considerably. As shown in Figure 2 and Figure 3, India’s total trade in goods for the 2020-2021 fiscal year was $686.244 billion, down 12.92% from $788.07 billion in the 2019-2020 fiscal year. Exports were $291.808 billion, down 6.88%, while imports were $394.435 billion, down 16.91%. The trade deficit was $102.627 billion, down 36.39% from $161.348 billion in the same period of the previous fiscal year. India’s restrictions on the national level are lifted as economic activity and liquidity recover [2].

3.3 Consumption

In India, a country whose labor force is mainly employed in intensive low-end jobs, the lockdown is devastating, and unemployment remains high for a long time despite the current pandemic development period. The epidemic has hit India’s traditional economy, especially the service economy, leaving 38 million tourism workers unemployed in India unemployed, 60 million directly or indirectly affected, and the tourism unemployment rate of more than 70% [2].
During the outbreak, the demand market of Indian industries, especially the manufacturing sector, was weak. As shown in Figure 4, the consumer confidence index fell sharply from 89.4 in September 2019 to 49.9 (July 2020). It lasted for nearly a year, significantly when the second significant rebound in India in May 2021 fell to 48.5, a historic low.

With consumer spending accounting for more than half of India’s GDP, the global pandemic’s repeated impact and the lockdown’s second wave. On the one hand, normal consumer consumption activities are restricted. On the other hand, the spread of the outbreak caused a large number of enterprises shut down, increasing unemployment rate, income reduction, and rising prices, leading to consumers’ confidence in market development prospects, expanding panic psychology, deliberately reducing the demand for non-necessities, consumer demand is generally reduced.

With the easing of the epidemic and the lifting of lockdown measures after 2021, Indian consumer confidence in the coming year will recover. However, as the epidemic has not seen signs of an end, the people’s willingness to consume is still not strong, and insufficient domestic consumption may further drag down India’s economic growth.

On the supply side, the prolonged shutdown and halves of Indian industrial companies, coupled with the impact of the pandemic on the global supply chain, have stretched the manufacturing sector with sharply reduced annual capacity, increased input costs, and lower profits. On the demand side, due to the pandemic, Indians are underemployed, their incomes fall, and their confidence in the market outlook falls, leading to lower demand for industrial products.

4. Policy

Since the Modi government took office in 2014, it has been wavering on globalization by signing RCEP in 2019, keeping the global supply chains, and trying to keep as many production links as possible at home.

At the same time, early in the COVID-19 outbreak, the Modi government established a proprietary COVID-19 workforce to assess the outbreak’s impact on various industries and design countermeasures. At the macroeconomic level, in May 2020, Modi announced a stimulus package of 2 trillion Rs (around $256 billion), focusing on infrastructure development, technology-driven systems, and supply chain optimization [2]. The government also tried to transfer the crisis caused by the COVID-19 pandemic into opportunities for India.

However, there are also some problems, with some economists in India criticizing the Modi government’s 2 trillion Rs of actual stimulus payments for less than 10 percent [2]. A large number of businesses have failed without waiting for timely aid from the Indian government. India’s inflation rate was already high before the outbreak, and it is now still rising internally because of more economic stimulus.
4.1 Manufacturing

Temporary tariffs will be imposed on some manufacturing products to ensure the development of domestic manufacturing enterprises. The pandemic has plagued the manufacturing industry, which relies on imported raw materials, prompting the Indian government to step up efforts to protect local companies. As a result, the Indian government plans to impose temporary tariffs on some manufacturing products to ensure domestic consumer demand and increase the consumer demand space for local Indian manufacturing companies. For example, the Indian government plans to impose a 15% Covid-19 tariff on all chemical and petrochemical product imports from 1 May 2020 to 31 March 2021, guaranteeing the demand side of the domestic consumer market for local manufacturing products [17]. Since the rapid growth of the epidemic in India in early March 2020, the Indian government announced that it would not export essential drugs and active substances, including hydroxychloroquine and acetaminophen, to avoid the shortage of relevant domestic materials and meet the domestic epidemic prevention needs [18].

More foreign investment is attempted to be attracted to promote the development of the local manufacturing industry. The Indian government, on 1 April 2020, announced a Production-related Incentive Plan (PLI Plan) to optimize investment links to attract investors to mobile phone manufacturing and specific electronic components in India.

India’s tariff level has risen from 13 percent to 18 percent since Modi took office in 2014 to protect local industries from the epidemic. Selective high tariffs on “naive” industries and promoting expected inter-state growth through national industrial specialization, protecting domestic industries, setting high tariffs and export restrictions, and policy intervention to promote growth in industries, especially manufacturing.

Many MSME in India are considered the “cornerstone of the Indian economy”. To protect MSME from the outbreak, the Ministry of Industry and Internal Trade Promotion has given startups up to 5 million Rs to use to enter the market and commercial scale businesses through convertible bonds. About 3,600 startups are expected to benefit from the Indian startup seed fund program, with early supported startups that have created many jobs for India, with the potential to reduce the number of unemployed people.

The Indian government continues to increase its investment and subsidies in the manufacturing industry, intervening in the natural development of the market through government behavior, and when the protection of the Indian manufacturing industry aims to raise the level of the Indian manufacturing industry and drive India’s manufacturing industry to grow into an indispensable part of the global supply chain.

From the perspective of neomercantilism, various economic policies are adopted to regulate the economy, such as increasing the level of the government’s foreign exchange holdings, thus making monetary policy and fiscal policy more effective; emphasizing fixed currency and independent monetary policy, controlling capital flows and concentrating currency decisions on the central government. To protect India’s MSME from foreign competition, the Indian government has also revised foreign direct investment rules. Through national political and economic means, the government aims to protect domestic enterprises from the foreign capital competition, to maintain the domestic market, to enhance the protection of their domestic MSME, and to prevent the emergence of “opportunistic acquisitions” and predatory acquisitions.

4.2 International Trade

In March 2021, Indian Finance Minister Ali Sitalaman submitted his budget for 2021-2022 to parliament. In the budget, the import tariff adjustment focuses on electronic and mobile products, steel, chemicals, auto parts, renewable energy, textiles, products manufactured by MSME, and agricultural products that encourage local production. Tariffs on certain car parts, mobile phone parts, and solar panels have been raised to boost domestic manufacturing.

Since early 2022, India has continued to restrict the export of commodity raw materials, such as banning wheat exports, lowering domestic commodity prices, and thus reducing inflation. In addition,
India’s recent addition of rice tariffs is bound to affect the international food price, raise the global low-end price of whole rice, and the international price of broken rice will rise to a new height. For the domestic consumption downturn, the export restrictions can protect the primary demand of Indian consumers and drive domestic consumption growth. However, it will significantly impact the international food price trade structure.

On 31 March 2020, the Ministry of Industry and Commerce urgently announced a one-year extension of the Foreign Trade Policy for 2015-2020. As the engine of the Indian economy, the export of the Indian service trade industry is the focus of the Indian government, with several specific plans, such as The Indian Commodity Export Plan and Export Commodity Tax Relief Program. Export is encouraged by offsetting the associated costs due to infrastructure inefficiency. The Plan rewards exporters in the form of tariff credit vouchers to cover the loss of the tariff. Under the Plan, the Indian government rewards all exporters with 2% to 5% of the value of the export FOB. The Indian government will compensate exports for taxes due to raw materials and consumption [2]. As India’s service sector exports have significantly been affected by the outbreak, the Ministry of Industry and Commerce has reformed the plan to expand its coverage to benefit more MSME. India’s Ministry of Industry and Commerce hopes to continue stimulating exports of its goods and services by extending the foreign trade policy deadline.

From the perspective of mercantilist, India, although still adopting trade balance in international trade theory, pays attention to the trade deficit, not only by state control but by more emphasis on economic development and a greater degree of free economic competition, more economical means rather than administrative means to intervene in the national economy, which is in line with the neomercantilist tendency.

4.3 Consumption

India’s economic growth is driven by consumption, with limited contribution to investment, including foreign investment, which has been a long-term deficit.

The coordination of fiscal and monetary policy keeps inflation within the target range. During the outbreak, India’s central and local fiscal revenues fell sharply, and welfare spending increased. In 2020, India saw the fiscal deficit ratio to GDP reach 12.8%, of which the central fiscal deficit ratio was 8.6%, and the central fiscal public debt ratio to GDP rose from 52% in 2019 to 63% in 2020. At the same time, the Reserve Bank of India has implemented a loose monetary policy, keeping interest rates low. In December 2021, the Monetary Policy Committee announced that it would keep the policy interest rate, i.e., the repo rate, at 4%. It is the lowest interest rate since independence and has been around for nearly 18 months. During the same period, the reverse repurchase rate also fell to 3.75%, and the interest rate corridor has remained stable, with no significant change compared with before the epidemic [1]. Lower interest rates can reduce the cost of government borrowing. At the same time, the Reserve Bank of India also directly increases the supply of liquidity in society through a series of open market operations, thus avoiding the possible crowding-out effect of government borrowing on private investment.

5. Conclusion

This paper studies India’s economic policy in the context of COVID-19 from the perspective of neomercantilism. The Indian government’s package of economic stimulus measures has stabilized and promoted the Indian economy, achieving a rapid economic recovery. The Indian government’s numerous economic subsidies and interest-free loans to MSME will help stabilize employment and restore the economy. Though small, many poor people and workers receive direct cash and food subsidies, significant for social stability and consumption promotion.

In the post-epidemic era, the Indian government’s tendency of neomercantilism is becoming more evident. According to the ongoing economic policies, India’s economic growth path is getting closer
to the neomercantilism model. For example, exports and manufacturing have played a prominent role in the economic recovery after the pandemic.

At present, India’s support and reform plans for various industries are also vehemently opposed by some social groups. For example, Indian farmers protest against the agricultural reform conducted by the Indian government, believing that the price of agricultural products cannot be protected after the reform, which will damage the interests of farmers. Pay-to-pay funding for manufacturing subsidies has raised doubt that the goals of “self-sufficient India” and “made in India” can be achieved after the pandemic.

It does not mean that India will move smoothly into an export-oriented economy led by manufacturing. However, overprotection as a double-edged sword may not prompt the rapid growth of the Indian industry. Instead, rising trade barriers are likely to provoke trading partners and take punitive measures.

Under the current background of globalization and liberalization, neomercantilism can be used as a “specific drug” to provide some help when the market relies on laissez-faire policies will cause chaos. However, after the market order gradually stabilizes, we should open up the government’s intervention in the market and return to a free and fair market environment.

The outbreak and global economic cyclical factors will exist for a long time, coupled with other structural contradictions within India. India’s short-term economy is based on the low base rapid rebound but is not optimistic in the long term. The Indian government should intensify reform and solve the institutional and structural contradictions to boost the Indian economy. Mercantilism is not a good cure-all receipt for India’s economy.

Here analyze the two sides of neomercantilism. India’s economic policy tendency in the post-epidemic era is mainly unique means adopted in particular periods. If the neomercantilism policy is adopted for long-term development, it will bring a particular impact on the future. New protectionist measures, including higher tariffs, procurement rules restricting competitive options, health and quarantine measures that are not based on science, and specific Indian standards inconsistent with international standards, all effectively exclude producers from global supply chains and limit the expansion of bilateral trade.

Although India’s economy has experienced an unprecedented downturn due to a lower base and driving factors, the continuing impact of the pandemic and the consumption contraction caused by inflation are likely to offset a considerable part of the upward momentum. Fiscal policy is linked to job growth, increased investment, and debt risk control. The growth of private consumption caused by employment will directly boost the Indian economy. In the future, whether the Indian government can control the balance between fiscal stimulus and debt control is a critical variable in India’s macroeconomic direction. However, any of these tasks are now difficult for the Indian government. Blindly relying solely on government support will hit the Indian economy. After overcoming the problematic period of the epidemic, the Indian economy still needs to adapt to the rules of globalization and liberalization and learn the economic model of coexistence with COVID.

References