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For India, countertrade holds promise

India, for instance, can secure critical raw materials, while supporting the borrower countries in infrastructure creation

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In a world characterised by heightened uncertainties and greater volatility, countries are increasingly looking at countertrade as a tool for meeting developmental needs, securing key resources, saving scarce foreign exchange reserves and circumventing sanctions. Countertrade refers to the exchange of goods and services in whole or part, with other goods and services as payment, rather than with any acceptable currency.

The beauty of countertrade lies in the fact that it can take a variety of forms, including barter, counterpurchase, offsets, buyback/compensation, switch trading, clearing arrangements, and debt-for-goods, among others.

Countertrade could be a key instrument for sustainable growth in developing countries which are at a perilous juncture in their developmental journey. Access to affordable development finance will be critical for these countries to make a faster recovery. However, sovereign borrowing in foreign currency has historically been expensive for developing countries, and its availability is being further constrained due to rising debt sustainability concerns.

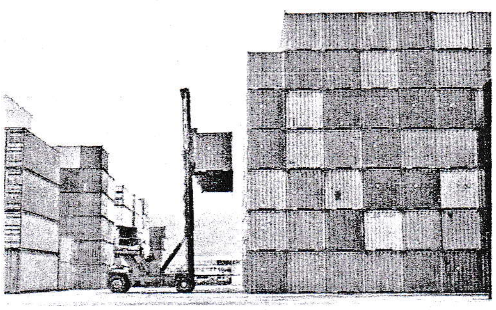
According to the IMF, nearly 60 per cent of the low-income countries are under debt distress or at the risk of debt distress. There is a pronounced need for countertrade arrangements given the soaring global debt and the depleting foreign exchange reserves of several low- and middle-income countries.

Global debt has recorded the largest single year jump since World War II, increasing from $226 trillion in 2020 to $303 trillion in 2021, and to a new record level of over $305 trillion in Q1 of 2022. The spectre of spiralling debt is looming large on the development plans of low-income economies, especially as the world enters a new phase of rising interest rates and resultant higher loan repayments. Faced with scarce forex reserves, high inflation, rise in external debt burden and uncertainty over repayment capacity, low-income countries would have fewer resources for development projects. Amid such constraints, countertrade models such as resource-for-infrastructure or debt-for-goods model would be important for addressing the unmet financing needs.

The resource-backed financing for infrastructure (RFI) model is a type of countertrade that has been used by Chinese creditors since early 2000s. Under this, the borrowing country commits future revenues to be earned from exports of natural resources to pay for loans secured for infrastructure projects. Such a model can be adopted by India, to promote mutually beneficial outcomes for both India and borrower countries. India, under its development partnership programmes, can finance infrastructure projects in developing countries, with part or full repayments for the financing through imports of mutually identified resources at mutually agreed terms.

Such a model can help India secure supplies of critical raw materials for industrial processes. Currently, primary commodities, precious stones and gold comprise nearly 50 per cent of India's merchandise imports, with fuel imports alone accounting for more than 28 per cent of merchandise imports. Over the next three decades, the import bill for fossil fuels in India is expected to triple, necessitating a strategy for achieving energy security.

Moreover, going forward, with expansion of manufacturing, and greater focus on sustainable and low carbon technology, the demand for non-fuel minerals is also expected to grow manifold. There are currently no known reserves in the country for minerals like nickel, cobalt, molybdenum, rare earth elements, neodymium and indium, that are important for the renewable energy transition.



India has implemented several countertrade transactions successfullyISTOCK

Some other minerals that are domestically available, such as copper and silver, are also not available in sufficient quantities. The RFI model can help India secure these raw materials for its production processes, while concomitantly supporting the borrower countries in infrastructure creation.

The RFI model can also help expand the horizons of Indian companies executing the infrastructure projects, as it can open opportunities in lesser explored geographies facing restrictions in outward remittances and other payment constraints.

Apart from the RFI model, other models of countertrade also have immense potential amid the rising uncertainties in the global market. Countries are increasingly entering into government to government (G2G) deals for alleviating concerns over supply of important commodities. Given the growing salience of such G2G deals, India may utilise its stockholding of wheat for countertrade with countries to secure supplies of essential commodities at mutually agreeable terms.

For example, countertrade for exports of wheat from India to meet Indonesia's foodgrain demand in exchange for uninterrupted supply of palm oil from Indonesia to address the domestic supply concerns, could be considered. The RBI's recent circular on additional arrangement for invoicing, payment and settlement of trade in Indian rupee further paves way for establishing clearing arrangements with countries such as Russia and Sri Lanka.

In the past too, India has implemented several countertrade transactions successfully. The railway project in Malaysia which was supported by the Palm Oil Board and the oil transactions with Iran are two such well-known examples.

Stumbling blocks

Notwithstanding the growing relevance of countertrade, there are several policy, diplomatic, resource-specific and institutional issues that may impede its implementation. First, there is no policy for countertrade in India, except in the case of defence imports. Navigating through the legal framework and regulations in countries involved in a countertrade transaction is complex, and an essential first step should be designing a clear umbrella policy for countertrade that delineates the role of various ministries and clarifies the payment settlement mechanism.

For this purpose, a task force for countertrade may be set up with representation from the Finance External Affairs, and Commerce and Industry Ministries, the Directorate General of Foreign Trade, the RBI, commercial banks, development financial institutions such as India Exim Bank, and public sector trading companies. A roundtable with relevant stakeholders who would be interested in sourcing such commodities from the identified overseas countries would be critical.

There may also be diplomatic issues as many overseas governments may be unwilling to accept countertrade for commodities of interest to India. Countertrade should not be perceived as an aggressive measure to recover dues, but as a mechanism to boost trade and investment in lesser explored geographies.

There may also be resource-specific issues — commodities that the overseas government may be willing to trade, which may not have sufficient domestic demand. In that case, options such as switch trading may be explored. Under switch trading, an international trading house can be engaged to serve as a switch trader, and the borrowing government could sell the negotiated value of goods to the switch trader. The payment for the goods can be credited to the lender by the switch trader, which would be utilised to service the debt of the borrowing country.

There are also institutional issues, as such a G2G mechanism would depend critically on the strength and capability of public sector enterprises in borrower countries to engage in such transactions, as also seamless coordination among institutions in India. Addressing these issues can be a win-win for both India and partner countries.

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