TARIFF RATIONALIZATION - ECONOMY

NEWS: ***The Union Budget 2025-2026 has*** *rationalized the Indian Tariff* ***with respect to industrial goods and such a move has come against the backdrop of a "****tariff war****" that the United States of America has initiated against*** *Canada, Mexico and China.*

WHAT'S IN THE NEWS?

Tariff Rationalization

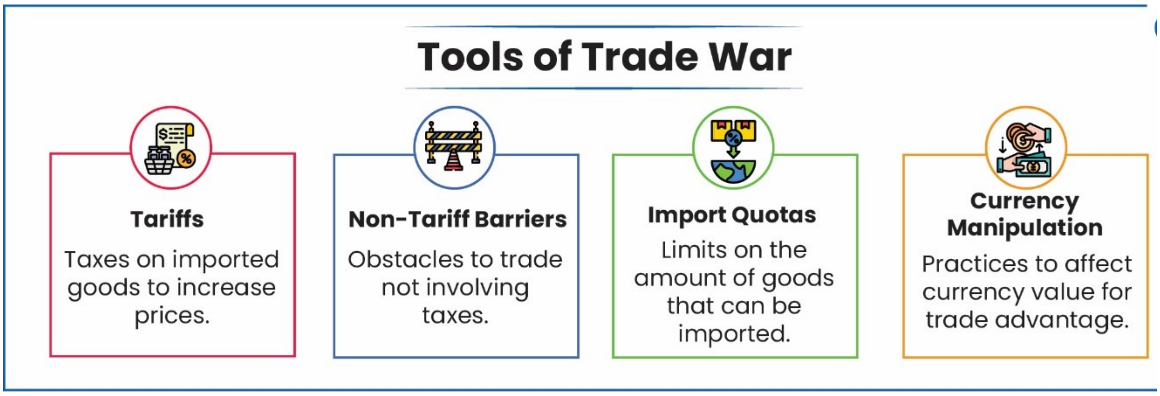
- **Definition of Tariff Rationalization**
    - Tariff rationalization refers to **modifying a country's tariff structure** to address inconsistencies and inefficiencies.
    - These inconsistencies can arise due to **frequent policy changes** or **protectionist measures** aimed at safeguarding domestic industries.
- **Objective of Tariff Rationalization**
    - **Enhancing cost-effectiveness** of raw material imports to support industrial production.
    - **Lowering production costs** to make domestic manufacturing more competitive.
    - **Promoting exports** by reducing the cost of finished goods in international markets.
    - Ensuring **a balanced customs tariff structure** that fosters industrial growth.
- **Role of a Well-Structured Customs Tariff**
    - A well-planned **customs tariff framework** ensures that raw materials remain affordable for domestic industries.
    - This availability of **low-cost inputs** can enhance domestic manufacturing.
    - Improved manufacturing efficiency **boosts exports** by making finished goods competitively priced.

Key Features of Tariff Rationalization in the 2025-2026 Budget

1. Simplified Tariff Structure

- **Reduction in tariff slabs** from 15 to 8, simplifying tariff classification and reducing legal disputes.
- **Capping of peak tariff rates** for industrial goods at **70%**, significantly reducing earlier rates of **100%, 125%, and 150%**.
- **Introduction of Additional Import Duty (AIDC1)** for selected goods:
    - AIDC is either **equal to or lower** than the import duty.
    - Aims to streamline taxation without overburdening imports.

- **Elimination of surcharges** for goods where **AIDC is applicable**, reducing complexity in the tariff system.



2. Addressing Inverted Duty Structure

- The **inverted duty structure** occurs when import duties on **raw materials are higher** than on **finished goods**, discouraging domestic manufacturing.
- The budget aims to **correct this imbalance** to encourage local production.
- **Key adjustments:**
  - **Lower customs duties on components** for industries like **LCD/LED TVs** and **Lithium-ion batteries**, promoting local assembly and production.
  - **Duty reductions on essential raw materials** such as **copper, lead, and tin scrap**, ensuring cheaper inputs for manufacturing.

3. Revising Import Duties on Motorcycles

- **Addressing U.S. concerns** over India's **high import duties** on motorcycles, particularly those with high engine capacities.
- **Duty reductions for high-capacity motorcycles:**
  - **Motorcycles up to 1600cc** – duty reduced from **50% to 40%**.
  - **Semi-knocked-down (SKD) and completely-knocked-down (CKD) units** – import duties lowered.
- Aimed at **improving India-U.S. trade relations** and making India a more attractive market for foreign motorcycle brands.

Impact on India's Economy

1. Boosting Domestic Manufacturing

- **Lower tariffs on raw materials** reduce **production costs** for manufacturers.
- Encourages **growth in domestic industries**, particularly in **electronics, automobiles, and renewable energy**.
- **Increases competitiveness** of Indian products in both domestic and global markets.

2. Fostering Export Growth

- **Lower input costs** reduce the price of finished goods, making Indian exports **more competitive globally**.
- Encourages **greater participation in global supply chains** by reducing costs for industrial production.

- Helps **expand market access** for Indian manufacturers in **Western markets** by offering competitively priced goods.

3. Strengthening Bilateral Trade Relations

- **Addresses trade concerns** of major partners like the **United States** by lowering high tariffs.
- **Encourages foreign direct investment (FDI)** by making India a more attractive investment destination.
- Eases **trade tensions** with key economic partners, fostering a **more favorable trade environment**.

Conclusion

- Tariff rationalization in **Budget 2025-2026** simplifies the tax structure, reduces costs, and improves trade competitiveness.
- The **correction of the inverted duty structure** ensures that domestic manufacturers can compete with imports.
- **Lowering tariffs on industrial inputs** supports domestic production and fosters **economic growth**.
- Strengthened **bilateral trade relations** with global partners enhance India's **trade and investment opportunities**.
- Overall, **tariff rationalization is a strategic step** toward making India a **global manufacturing hub** while improving trade efficiency.

What are Tariffs?

A **tariff** is a type of tax imposed by a government on foreign goods that are imported into a country. The primary purpose of tariffs is to make imported goods more expensive, thereby encouraging consumers to prefer domestically produced alternatives.

Global Context of Tariffs

The **United States** is currently the world's largest importer of goods. In the year **2022**, the total value of goods imported into the U.S. amounted to approximately **USD 3.2 trillion**, reflecting the country's significant reliance on foreign products.

Who Pays the Tariff?

The **importer** or an **intermediary** acting on behalf of the importer is responsible for paying the tariff at the time of bringing goods into the country. However, the **ultimate burden of the tariff cost is typically passed on to consumers** in the form of higher prices for imported products.

Impact of Tariffs

Since tariffs **increase the price** of imported goods, they make **domestic products relatively cheaper** in comparison. This helps protect local industries from foreign competition by discouraging excessive reliance on imported goods. However, it may also lead to increased costs for consumers and businesses that rely on imported materials.

Other Trade Barriers

Apart from tariffs, governments use various other **trade barriers** to regulate imports and exports. These include:

- **Quotas** – A restriction on the maximum quantity of a product that can be imported within a specific period.
- **Licenses** – Government-issued permits required to import certain goods.
- **Standardization** – The imposition of technical and quality regulations that foreign goods must meet before being allowed into the country.

Common Types of Tariffs and Trade Restrictions

1. **Specific Tariffs** – A fixed tax imposed on each unit of an imported good, such as charging **$10 per kilogram** of an imported product.
2. **Ad Valorem Tariffs** – A tariff calculated as a percentage of the product's value, such as **15% of the total cost** of an imported vehicle.
3. **Licenses** – Authorization issued by a government allowing specific goods to be imported in controlled quantities.
4. **Import Quotas** – A limit on the total volume or value of a particular product that can be imported.
5. **Voluntary Export Restraints (VERs)** – Agreements between exporting and importing countries where the exporter voluntarily limits the quantity of goods sent to the importer.
6. **Local Content Requirements** – Regulations requiring a certain percentage of a product's components to be sourced from domestic manufacturers.

Other Important Concepts Related to Tariffs

1. Inverted Customs Duty Structure

- The **inverted customs duty structure** occurs when the **taxes (customs duties) on raw materials and intermediate goods** are higher than the taxes imposed on the final manufactured products.
- This situation leads to **higher production costs** for domestic manufacturers because they pay more for raw materials than the final imported product itself.

Impact:

- Increases **cost inefficiencies**, making local manufacturing expensive.
- Can cause **imported finished goods** to be cheaper than locally produced alternatives.
- **Reduces competitiveness** of domestic industries, making Indian exports less competitive in global markets.

2. Basic Customs Duties (BCD)

- The **Basic Customs Duty (BCD)** is a standard **tax imposed on goods at the time of import** into a country.
- It is one of the primary revenue sources for a government and is applied based on the **classification of goods** under the country's tariff schedule.

Impact:

- **Higher BCD** on imported goods protects domestic industries by making foreign goods more expensive.
- **Lowering BCD** on raw materials can reduce **production costs** for domestic manufacturers, making their goods more affordable and **competitive** in both local and international markets.

Source: https://www.financialexpress.com/opinion/a-case-of-tariff-rationalization-amidst-tariff-wars/3762325/