INDIA'S ENGAGEMENTS IN FREE TRADE AGREEMENTS

LOOKING AHEAD

India Exim Bank

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India's Engagements in Free Trade Agreements: Looking Ahead

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EXECUTIVE SUMMARY

Introduction

The COVID-19 outbreak caused disruptions across the world including India, with the external sector being hit the hardest. India has a GDP target of US$ 5 trillion to be achieved by 2024-25. The exports of both goods and services will have a major role to play in this as they are expected to contribute to 20% (US$ 1 trillion) of this target.

India's combined exports of goods and services were registered at US$ 538 billion in 2019, growing at an AAGR of just under 3%, followed by an on-year decline of nearly (-) 11 % in 2020 amid the COVID-19 outbreak[1]. Imports, on the other hand, grew at an AAGR of 2.0% during 2011-19, followed by a steep decline of (-) 25.2% in 2020, resulting in a trade deficit of US$ 7.6 billion. India's export to GDP share has fallen from 24.5% in 2011 to 18.4% in 2019. However, India has displayed a strong on-year recovery in FY 2022, with merchandize exports breaching the US$ 400 billion mark.

With external sector being impacted, India will have to increase the competitiveness across sectors that are performing below potential. The trade agreements are a critical component of the trade ecosystem across the world. This holds true for India as well. Apart from being a co-signatory to some critical trade agreements like the ASEAN-India FTA, India is also a part of certain prominent regional blocs like Asia Pacific Trade Agreement (APTA), India ASEAN Trade in Goods Agreement (TIG), South Asia Free Trade Agreement (SAFTA), among others.

[1] During 2020, while India's merchandize exports registered an on-year decline of (-) 14.8%, the services exports declined by (-) 5.4%.

Rationale for Trade Agreements

Over the last two decades, trade has been a key determinant of the rapid expansion in the world economy. With respect to the rationales of the trade agreements, there are multiple reasons, which inter alia includes, reducing or eliminating certain barriers to trade and investment; to facilitate stronger trade and commercial ties between participating countries; ability to improve economic efficiency; better terms-of-trade to increase its national income; besides amongst others allowing governments to avoid terms-of-trade conflicts and to resist pressures from the private sector to take a departure from a liberal trade policy. At the same time, FTAs leads to better jobs, new markets, and increased investment. Free trade spreads values and beliefs as well as goods and services

Assessing the Impact of FTAs: Key Areas

Economies of Scale	Impact on FDI	Competitiveness and Long-Run Growth Effects	Value Chain and Production Linkages	Enabling Structural Policy Changes and Reforms
Usually occur due to improved technical efficiency in large-scale production, greater capability to spread the administrative costs and overheads over a bigger operation, or better logistics because of larger volumes	Bilateral and regional FTA formation attracts long-term, risk-sharing investment flows by creating a more integrated marketplace within which multinational corporations can enjoy a regional division of labour with low transaction cost	Increased exposure to competition from partner countries weeds out less productive firms and favours more productive ones which gives the firms an incentive to invest in more efficient productive process and technology	FTAs help in putting a country into the value chain, which in turn, makes the country specialized in that process, ultimately making the country a favourable destination for investment	FTAs are affecting deeper integration by addressing behind-the-border measures like quality standards, laws related to corporate and public governance, customs procedures, competition policy, including the reform of state-owned enterprises, and other sensitive sectors

Further, it may be noted that the cumulative number of regional trade agreements (RTAs) has increased from 22 in 1990 to 305 in 2020. Even though non-discrimination among trading partners is one of the core principles of the

WTO, RTAs constitute one of the exemptions and are authorized under the WTO, subject to a set of rules. Region-wise, the highest number of RTAs in force during 2020 were in Europe, followed by East Asia and South America.

Revisiting Major World Trade Agreements

ASEAN Free Trade Agreement (AFTA)

During 2010-19, ASEAN's merchandize exports registered an AAGR of 3.7% to reach US$ 1.4 trillion, contributing to 7.6% of world exports in 2019, up from 7.0% in 2010. Major exporters from ASEAN are Singapore, Vietnam, Malaysia, Thailand, and Indonesia. ASEAN's trade balance has been in surplus during the last decade and was recorded at US$ 31.0 billion in 2019.

After entering AFTA, the intra-regional trade of the member countries registered a higher growth (7.2%) than their trade with rest of the world (6.9%), during 2010-19. While the intra-regional integration expansion has led to diversification in the variety and quality of products, ASEAN's intra-regional trade share has decreased slightly from 23.7% in 1995[2] to 20.7% in 2020. Also, exports of manufacturing goods represent more than half of ASEAN exports.

For majority of the AFTA member countries, a notable increase in the exports of high-technology products, as a percentage of manufactured exports, was registered during 2010 and 2019. For instance, in terms of manufacturing upgrading, Vietnam, which used to be a predominantly agricultural economy, saw a notable pivot towards specialization in textiles, apparel, and hi-tech products.

With respect to FDI, total inward FDI in the ASEAN aggregation increased at a CAGR of 8.8% during 1990 and 2019. In the last decade, the total FDI inflows in the ASEAN countries were recorded at US$ 20.6 billion in 2019, nearly double from US$ 10.0 billion in 2010 with top recipient sectors being manufacturing, financial and insurance, and wholesale and retail trade.

[2] The earliest data available on ASEAN's intra-regional trade share on UNCTAD Stat pertains to 1995.

United States–Mexico–Canada Agreement (USMCA)

Under the terms of erstwhile NAFTA, the United States, Canada, and Mexico agreed to gradually phase out all tariffs on merchandise trade and to reduce restrictions on trade in services and foreign investment by granting MFN status to each other. In July 2020, the United States–Mexico–Canada Agreement (USMCA) succeeded the erstwhile NAFTA (USMCA, henceforth) with new policies on labour and environmental standards, intellectual property protections, and digital trade provisions.

USMCA aggregation accounted for 13.6% of global merchandize trade in 2019, amounting to US$ 2.5 trillion. During 2010-19, the exports from USMCA to world registered a modest AAGR of 3.2% with main export items being mineral fuels, capital goods, vehicles, and electrical machinery. Top three export destinations for the exports originating in USMCA are the USMCA members themselves, accounting for 49% of the total exports in 2019, followed by China (5%) and Japan (3%). It may be noted that USMCA's intra-regional trade share increased from 46.0% in 1995 to 49.2% in 2020.

Production sharing between the US and Mexico has increased as the manufacturers have started to work together. This has also led to increased merchandize trade between the two nations.

On the investment front, total FDI inflows in the USMCA were recorded at US$ 329.5 billion in 2019, marginally lower from US$ 337.9 billion in the previous year and registering an AAGR of 14.8% during 1994-2019. USMCA had a significant positive impact on Mexico's overall economic development by supporting the infrastructure and improving investors' confidence, which allowed non-USMCA members to invest in Mexico to enter the North American markets.

Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)

CPTPP is a free trade agreement among eleven countries in the Asia-Pacific region and came into effect in December 2018. The countries included in the pact are Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, Peru, New Zealand, Singapore, and Vietnam. The pact binds its signatories,

which represented about 16% of global merchandise trade in 2019, to 30 chapters providing for freer trade and investment access.

The CPTPP provides for 98% elimination of tariffs among the participants with minor exceptions in select sensitive areas like rice exports by Japan and dairy products exports by Canada. It provides a single set of rules of origin and allows content from all CPTPP countries to be cumulated.

CPTPP also includes rules on issues that have not yet been incorporated into other trade agreements, such as rules relating to provision of a level playing field to the state-owned enterprises (SOE).

The merchandize exports by the CPTPP aggregation in 2019 were recorded at US$ 3 trillion, up by US$ 38.5 billion from 2018. It is noted that the share of exports from CPTPP in the world exports has risen from 15% in 2017 to 16% in 2019. Japan is the largest exporter and importer among the CPTPP members. In 2019, highest increase in the merchandize exports from the CPTPP aggregation was recorded by Vietnam. During the year, more than 23% of Vietnam's exports were directed to the USA and 16% to China.

According to a Study by the World Bank, the highest growth of exports and output under the CPTPP are projected to occur in food and beverages, apparel, and textiles. Their collective exports will expand by 28% relative to baseline conditions in 2030, boosting production within the CPTPP by almost 5%.

As far as the FDI is concerned, the total FDI inflows in the CPTPP countries were recorded at US$ 275.8 billion in 2019, marginally higher from US$ 274.8 billion of FDI in 2018. CPTPP offers new opportunities for local businesses in the developing countries to participate in trade while widening the existing import and export markets.

Assessment of India's Major Trade Agreements

ASEAN- India Free Trade Agreement (AIFTA)

The existing free trade agreement between India and the Association of Southeast Asian Nations (ASEAN) is split across three aspects - Trade in Goods;

Trade in Services; and Investment. Even though the exclusion lists under AIFTA are subject to an annual tariff review with a view to improving market access, there are 489 tariff lines listed under the negative list, belonging to the sectors like agriculture, textile, machinery, automobile, chemicals, and plastics.

In the agreement, preferential imports form nearly 70% of the imports of India from ASEAN. With respect to ASEAN's imports from India, preferential imports cover 48% of imports.

India has remained a net importer of merchandize with the AIFTA aggregation, with a constant widening of trade deficit during the last ten years, increasing from US$ 6.7 billion in 2010 to US$ 22.8 billion in 2019. The trade balance was primarily weighed down because of high imports of coal, crude palm oil, and petroleum oils. The highest deficit was noted with Indonesia, arising mainly due to the imports of crude palm oil, followed by Singapore, Malaysia, Thailand, and Vietnam. India's exports to the ASEAN aggregation primarily comprised of medium petroleum oils, frozen meat, light floating vessels, light oils, and aluminium.

The study analyses the trade intensity index (TII) for the top ten export items by India to ASEAN region. TII determines whether the value of trade between two countries is greater or smaller than would be expected based on their importance in world trade. TII for India's overall merchandize exports to the ASEAN aggregation is greater than one, indicating that the trade flows are larger than expected. Amongst the top ten export items, the TII for items like Natural pearls and semi-precious stones and Electrical Machinery has been estimated at less than one, indicating the untapped export potential.

On the investment front, FDI inflows into India from ASEAN during 2010 and 2019 were recorded at US$ 87.2 billion, approximately 37% of total FDI flow into India. About US$ 10 billion worth of FDI was sourced from Singapore alone, due to the bilateral Comprehensive Economic Cooperation Agreement.

South Asian Free Trade Agreement (SAFTA)

The South Asian Free Trade Area (SAFTA) is the free trade arrangement of the SAARC countries. The agreement came into force in 2006, succeeding

the SAPTA. As per the agreement, the products from the "sensitive list" of each member country are considered a part of the agreement's "negative list". It may be noted that SAFTA's intra-regional trade share has increased marginally from 6.9% in 2006 to 7.1% in 2020. For India, the key items in the sensitive list for Non-Least Developed Contracting States (NLDCS) range from vegetables and man-made staple fibres to Footwear and Iron & Steel. Around 89% of India's total imports from SAARC countries are preferential imports. However, preferential tariff items form only 23% of total imports of SAARC from India. In essence, India's tariff related benefits due to SAFTA are relatively less compared to its SAARC trading partners and this is also a case of unequal exchange in terms of tariffs.

India has remained a net exporter of merchandise with respect to trade with the SAFTA aggregation. The exports increased at an impressive AAGR of 9.0% during 2010 and 2019 to reach US$ 18.5 billion in 2019, more than twice of the exports in 2010. Imports, on the other hand, were recorded at US$ 3.2 billion in 2019, growing at an AAGR of 7.4% during the same time. India's trade surplus with the SAFTA aggregation largely arose on account of high exports of medium oils, electrical energy, cotton, motorcycles, and semi-finished products of iron and steel. Bangladesh, Nepal, and Sri Lanka were top exporting destinations for India.

Further, the TII analysis for India's exports to SAARC was estimated at 2.06, in 2019, indicating higher than expected level of trade flows. However, it is observed that exports of crucial items like pharmaceutical products, organic chemicals and mineral fuels were significantly subdued during the year.

India-South Korea CEPA

The India-Korea CEPA came into effect in January 2010, after a negotiation of over twelve rounds. As per the agreement, South Korea abolished tariffs on 93% of Indian imports and India did the same on 75% of Korean imports. A wide range of goods falling under the category of vegetables, spices, edible oil, alcoholic beverages, and vehicles fall in the 'EXC' category of the agreement and are exempted from the obligation of tariff reduction or elimination.

In India-South Korea preferential trade, while in terms of share of preferential items in imports of India/South Korea there is some sort of equal exchange, in terms of preference margins the imbalance is there mainly due to relatively lower MFN Tariffs of Korea.

India has remained a net importer of merchandize from South Korea during 2010 and 2019, with trade deficit amounting to US$ 11.4 billion in 2019, nearly double of US$ 6.3 billion recorded in 2010. It is to be noted that the deficit largely arose on the account of high imports of electrical machinery, iron and steel, machinery, and plastics. It is important to note that an ambitious target of US$ 50 billion worth of bilateral trade by 2030 has been set between the two countries.

Considering India's top ten export items to South Korea in 2019, it is noted that while the TII for overall exports was less than one, the index exceeded the benchmark value for key items like aluminium, lead, ores, and cotton. The TII was low for items such as iron and steel, electrical machinery, organic chemicals, and mineral fuels.

With respect to the FDI, total FDI inflows received by India from South Korea during 2010 and 2019 were recorded at US$ 3.8 billion, growing at an AAGR of 39.2%. FDI inflows from South Korea into India have shown an upward trend each year, after the CEPA came into effect.

India-Japan CEPA

The India-Japan CEPA came into effect in August 2011, with the objective to eliminate tariffs on 90% of Japanese exports to India, like auto parts and electric appliances, and 97% of imports from India, including agricultural and fisheries products, until 2021.

India has been a net importer of merchandize from Japan during 2010 and 2019, with trade deficit amounting to US$ 7.9 billion in 2019, significantly higher than US$ 3.5 billion recorded in 2010. It is to be noted that the deficit largely arose on account of high imports of electrical machinery, machinery & mechanical appliances, and iron and steel.

In the India-Japan preferential trade, while the preference margin is high in the case of most of the items on India's import side, on the Japanese side, the preference margin is relatively less as already India enjoys low or zero MFN tariffs in Japan. But in some important items of export interest to India like leather and footwear, organic chemicals and fish & related items, India has benefitted. Thus India-Japan CEPA is relatively a fair exchange, in terms of tariffs.

The TII for overall merchandize exports as well as the top ten export items, except ores, aluminium, marine products, and mineral fuels, was recorded below the benchmark value, in 2019, indicating lower than expected exports. Sectors like iron and steel, apparel, machinery, and organic chemicals should, therefore, be made the focal points to boost India's exports to Japan.

During 2010 to 2019, Japan's cumulative FDI in India amounted to US$ 29.5 billion, making it the third largest source of the FDI in India after Mauritius and Singapore. Major recipient sectors were automotive OEM, metals, automotive components, real estate, and industrial equipment.

India-Australia Economic Cooperation and Trade Agreement

Australia and India launched negotiations for an Economic Cooperation and Trade Agreement (ECTA) in May 2011. The negotiations were formally relaunched in 2021 and concluded on a fast-track basis by March end 2022.

India was a net importer of merchandize to Australia in 2019, with a trade deficit amounting to US$ 7.6 billion, as against the trade deficit of US$ 10.4 billion in 2010. The exports from India to Australia in 2019 primarily comprised of mineral fuels (12%), precious metals (9%), pharmaceutical products (8%), railway or tramway locomotives, rolling stock and parts thereof (6%) and machinery (5%). In 2019, Australia ranked 30th amongst destination countries of India's total merchandize exports. For Australia's exports, meanwhile, India was the sixth largest destination.

On the other hand, major imports from Australia were relatively more concentrated and comprised of mineral fuels (78%); precious metals (5%); inorganic chemicals (4%); ores, slag, and ash (2%); and aluminium and articles thereof (1%).

The India-Australia ECTA is the first trade agreement of India with a developed country in over a decade. The agreement covers diverse areas such as trade in goods, rules of origin, trade in services, technical barriers to trade (TBT), sanitary and phytosanitary (SPS) measures, dispute settlement, movement of natural persons, telecom, customs procedures, textiles, and cooperation in other areas. India is also expected to enjoy greater market access for its products while easing of regulatory processes for pharmaceutical products while opening a US$ 12 billion market in Australia. India has also been conscious about its agricultural sector and has kept certain items away from the list. One significant decision for the services sector has been Australia granting a post-study visa for 4 years.

With this agreement, the trade in goods and services between India and Australia is expected to reach US$ 45-50 billion over 5 years, up from the current US$ 27 billion. This is expected to generate over 1 million jobs in India.

India and the RCEP

The Regional Comprehensive Economic Partnership (RCEP) concluded in November 2020 after eight rounds of negotiations starting from 2012. The RCEP represents the world's largest trading bloc. The agreement sought to simplify the customs procedure and rules of origin laws among countries - implying reduced potential regulatory frictions for firms and countries for regional supply chains.

It may be noted that had India signed the agreement, it would have become a part of the world's largest trading bloc and gained access to a vast market that accounts for around 25% of the world GDP (excluding India), 30% of the world trade, 26% of the FDI flows, and 45% of the world's population.

Additionally, withdrawal from the RCEP is also expected to have an impact on India's global value chain participation, especially for hi-tech goods.

India's key import items from the RCEP, in 2019, included electrical machinery, mineral fuels, machinery, organic chemicals, and plastics. It may be noted that the RCEP aggregation accounted for about 32.6% of India's total merchandize imports and 19.7% of total merchandize exports during 2019.

Further, India saw a potential threat to many domestic industries. For instance, in the dairy industry, it was felt that until the dairy sector in India reaches the stage to be able to compete with giant players like New Zealand, it was necessary to safeguard the interest of dairy farmers and not be a signatory to any pact that prescribes duty-free import of dairy products.

Also, agreeing to RCEP's e-commerce rules would have restricted India's flexibility to fine-tune its policy space. In particular, the RCEP draft is opposed to data localization, while India fears the monopoly power of digital giants.

Finally, India had been seeking an auto-trigger mechanism, which would have allowed India to raise tariffs on items in instances where imports cross a certain threshold. However, majority of RCEP member countries were against the idea of including an auto-trigger mechanism in the agreement.

It may be noted that while India's dairy sector could have been impacted, India's top export items to the RCEP also comprised of marine and meat products, which registered an AAGR of 16.1% and 20.0% respectively, during 2010-19.

Trade data during the last ten years indicates that India's deficit with China (US$ 51.1 billion) is higher than that of the other RCEP member countries put together (US$ 41.1 billion) in 2019. In this regard, India, during the RCEP negotiations, had proposed the introduction of more stringent Rules of Origin (ROO) norms in the RCEP framework, primarily to avert the threat of Chinese goods entering domestic markets routed through other RCEP member countries.

Potential Trade Agreements between India and Developed Countries

India-Canada CEPA

Canada and India launched Comprehensive Economic Partnership Agreement (CEPA) negotiations in November 2010. The CEPA is a wide-ranging economic and trade agreement covering trade in goods and services and addressing non-tariff barriers.

India's merchandize exports to Canada were recorded at US$ 2.9 billion in 2019, more than double of the exports in 2010. During this time, while India's merchandize exports to Canada registered an AAGR of 10.9%, imports grew at an average of 8.8%, reaching US$ 3.9 billion, resulting in a trade deficit of US$ 1 billion in 2019. India mostly exported articles of iron and steel, pharmaceutical products and machinery to Canada during 2010 and 2019. Canada's exports primarily comprised of mineral fuels, natural pearls and semi-precious stones and fertilizers. In services, India's exports to Canada have risen significantly in response to the growing telecommunication and financial services sector.

On the investment front, total FDI inflows received by India from Canada during April 2000 and March 2020 were recorded at US$ 1.9 billion, making up for 0.41% share in India's total FDI inflows. Both the countries have been in negotiations to finalize a Foreign Investment Promotion and Protection Agreement (FIPA), which is expected to improve the investor sentiments through a framework of legally binding rights and obligations.

Some of the top segments in which India has received investments from Canada include solar electric power; metals; financial services; among others. India's investments in Canada were mostly in the segments of chemicals; metals; and IT and software services.

Some of the segments that could be explored for negotiations in this CEPA are mobile phones and communication apparatus; pulses; and canola oil.

India-European Union Bilateral Trade and Investment Agreements (BTIA)

The negotiations on the Bilateral Trade and Investments (BTIA) between India and the EU were launched in June 2007 to liberalize the trade in goods and services. BTIA negotiations have been on a standstill since 2013, after fifteen rounds, over diverging opinions on the 'sensitive lists' of both the parties, especially concerning the opening up of Indian markets like automobile, alcoholic beverages and BFSI for the EU businesses.

India was a net exporter of merchandize to the EU 27, with a trade surplus amounting to US$ 4.5 billion, as against the trade deficit of US$ 6.9 billion in 2012. The exports from India to the EU primarily comprise of mineral fuels, organic chemicals, machinery, precious metals, and articles of apparel and clothing. On the other hand, major imports from the EU are machinery, precious metals, electrical machinery, optical and surgical instruments, and organic chemicals.

With respect to the investment, the EU's share in foreign investment inflows to India more than doubled from 8% to 18%, between 2010 and 2019. The total FDI received from the EU in India during April 2000 and March 2020 was recorded at US$ 109.55 billion, and the top countries included the Netherlands, the UK, Germany, and France. Top sectors were renewable energy, transportation and warehousing, and automotive OEM.

Some of the segments that could be explored for negotiations in this agreement are services, and renewable energy.

India-UK Free Trade Agreement

Post-Brexit, the possibilities of a free trade agreement between India and the UK, covering trade in goods and services as well as investments, have reached a critical juncture. During the last ten years, the trading patterns between the two countries show a high degree of complementarity, with India's export basket having a high match with the UK's import basket, and vice-versa.

India has been a net exporter of merchandize to the UK during 2010-19, with trade surplus reaching US$ 1.9 billion in 2019, higher from the trade surplus of US$ 1.2 billion recorded in 2010. In 2019, India's exports to the UK primarily comprised of machinery, apparel, jewellery, pharmaceuticals, and footwear. India's imports from the UK included gold and silver, machinery, petroleum coke, waste and scrap of iron and steel, and unworked non-industrial diamonds.

The total FDI received from the UK in India during April 2000 and March 2020 was recorded at US$ 28.2 billion, accounting for almost 6% of the total FDI inflows received during the same period. And the top sectors were metals, renewable energy, and electric components.

Some of the important sectors that could be explored during the negotiations are aerospace and parts, and scotch and whiskey.

India's Trade Agreements: Looking Ahead

Addressing the Unequal Exchanges in Existing FTAs

In most cases, when India is on the import side, the preferential tariffs are significantly lower than the MFN tariffs, while for India's partner country, the preferential tariffs are closer to MFN tariffs when they are importing. This indicates that the Margin of Preference given by India to its FTA partners is higher than the Margin of Preference given by them. As a result, the partner countries might not find much benefit if they decide to switch their imports to India, since the margin of preference is relatively low. These are the uneven distribution of gains that exist in India's trade agreements.

To address the problem of unequal exchange it is important to re-evaluate the existing and potential FTAs through a zero-budgeting exercise. Renegotiations of FTAs must also address the problem of prevailing inverted duty structures. Lastly, incorporation of an offset clause, as often done for procurement of defence equipment through deals or agreements, should be extended to wider trade agreements, especially for technology intensive sectors like automobile and electronics.

Further, to determine the economic usefulness of preferential tariff to countries in a trade agreement, "preference utilization rate" is examined. It indicates what percentage of given imports is using the preferential duties offered by the free trade agreements. While the global utilization of preferences is as high as 70% to 80%, for India, it stands at around 5%-25%. Going forward, it will be important to relook at India's existing FTAs and explore the possibility of renegotiating them to address the low levels of the preference utilization rates.

Incorporating WTO's Agreement on Technical Barriers to Trade in the FTAs

In the modern world, technical barriers to trade (TBT) are playing a much bigger role in restricting the trade across geographies than tariffs. The TBTs directly translate into higher indirect costs for the exporters, thereby offsetting the initial reduction in trade costs facilitated by entering into trade agreements.

WTO's TBT Agreement lays down the framework to identify those technical regulations, standards, and testing and certification procedures which do not create unnecessary obstacles to cross-border trade. It is suggested that India's trade agreements, especially with the developed countries, be comprehensive and tailor-made and built upon the foundations and provisions of the WTO's TBT agreement to provide a wider market access to domestically manufactured goods.

Provision of an Emergency Action Plan

Given the dynamic growth trend in India's GDP and the uneven growth in the constituents of GDP (like the government expenditure and exports) recorded in the last few years, the trade agreements that India enters must provide for a transitional tariff-based emergency action mechanism, which is a temporary bilateral safeguard measure used to protect the domestic industry and exporters against the events that can cause unforeseen damage in form of unprecedented surge in imports or fall in exports. Such arrangements must

be comprehensive and specify the qualifying conditions for imposition and the duration for which the action may be maintained.

Trade agreements negotiations could also propose to have a 'graduation clause' with other developing country FTA partners, extending a 'sunset clause' for periodic review of the terms of select agreements, and a 'trigger mechanism' if the FTAs lead to a sudden surge in imports.

Reducing Trade Restrictiveness in Services

India has a Services Trade Restrictiveness Index (STRI)[3] score, exceeding the world average, in all sectors and the highest in 3 of the total 22 services. Among the sectors, rail freight transport has the highest STRI value (1), which is the maximum STRI value. The other two with high STRI values are legal services (0.886), and accounting services (0.827).

To effectively overcome shortcomings like Restrictions on Foreign Entry; Restrictions to movement of natural persons; Other Discriminatory measures; Barriers to Competition; and Regulatory Transparency that prevent India in leveraging its strengths in the services sector, it is suggested that the current and potential trade agreements should seek to further suitably liberalize the trade in services with substantial sub-sectoral coverage.

Focussing on introducing Mutual Recognition Agreements (MRAs) as clauses in existing and potential trade agreements

Entering into Mutual Recognition Agreements (MRAs) could significantly expand the market access of India's exports (both goods and services) and lead to better price discovery in partner countries, especially the ones that are also the co-signatories to trade agreements. The MRAs with India's existing and potential FTA partners could be focussed on areas like regulatory standards, conformity assessment, accreditation procedures, qualifications, visas and social security.

[3] The Services Trade Restrictiveness Index (STRI) is an evidence-based tool published by the OECD, that collects information on services trade restrictions across 19 major services sectors that allows countries to benchmark their services market regulations against the global best practice, identify outlier restrictions and current bottlenecks.

Some of India's existing MRAs include:

- MRA between the Institute of Chartered Accounts of India (ICAI) and the CPA ("Certified Practising Accountant") Australia.
- MRA between the Institute of Chartered Accounts of India (ICAI) and the Malaysian Institute of Certified Public Accountants (MICPA) to enable appropriately qualified Chartered Accountants of either Institute to join the other Institute by receiving appropriate credit for their existing accountancy qualification.
- MRA between India and the USA for the recognition of Authorised Economic Operators (AEOs), for faster export clearance.

Additionally, the purview of existing MRAs could also be explored and extended to other critical areas like healthcare and para-medical services, especially with India's existing FTA partners.

More Engagement in CEPAs

India should focus on entering into comprehensive economic agreements like CECA and CEPAs for better growth prospects. It is to be noted that CEPAs are essentially FTAs plus packages, comprising of an integrated package of agreement on goods or services, investment, mutual recognition, e-commerce, intellectual property and more. This could also drive the Government's ambitious "Assemble in India for the World" scheme, which seeks to merge "Assemble in India" with the existing "Make in India".

1. INTRODUCTION

Overview

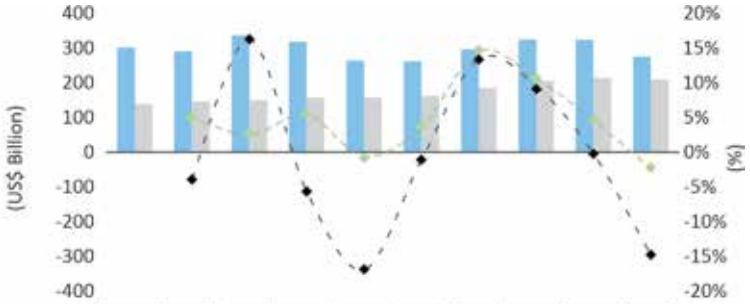
In the post-pandemic world, as India is posed with a newer challenge to reverse the steep decline in the output caused by the pandemic, it is important to identify the factors that can fuel the desired growth to hit the ambitious US$ 5 trillion GDP mark by 2024-25.

Exports of goods and services are expected to substantially complement India's goal of a US$ 5 trillion economy, with a goal of US$ 1 trillion (20% of GDP) by 2024-25. The roadmap for India to harness the potential of highly dynamic markets, both domestic and foreign, would require a multi-pronged approach, with foreign trade providing a strong momentum by spearheading growth in the international markets.

Trade projections have garnered wider significance amid the ongoing COVID-19 crisis that has deeply impacted the economies worldwide. In particular, trade through value chains has helped countries access food and essential medical supplies during the crisis. As per the IMF's January 2022 World Economic Outlook, after shrinking by (-) 8.2% in 2020, world trade volume (goods and services) is estimated to have grown by 9.3% in 2021 and is further projected to grow by 6% in 2022.

India's total exports were recorded at US$ 484.8 billion (goods and services, combined) in 2020, registering an AAGR of 2.8% during 2011-19, followed by a sharp on-year decline of (-) 9.8% in 2020. Imports, on the other hand, grew at an AAGR of 2.0% during 2011-19, followed by a steep decline of (-) 25.2% in 2020, resulting in a trade deficit of US$ 7.6 billion.

Chart 1.1: India's Exports – A Cursory Glance



	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Merchandize Exports	301.5	289.6	336.6	317.5	263.9	261.0	295.9	324.0	323.3	275.5
Services Exports	138.5	145.5	149.2	157.2	156.3	161.8	185.3	205.0	214.4	209.3
On-year change in Merchandize Exports		-4.0%	16.2%	-5.7%	-16.9%	-1.1%	13.4%	9.5%	-0.2%	-14.8%
On-year change in Services Exports		5.1%	2.5%	5.4%	-0.6%	3.5%	14.5%	10.6%	4.6%	-2.4%

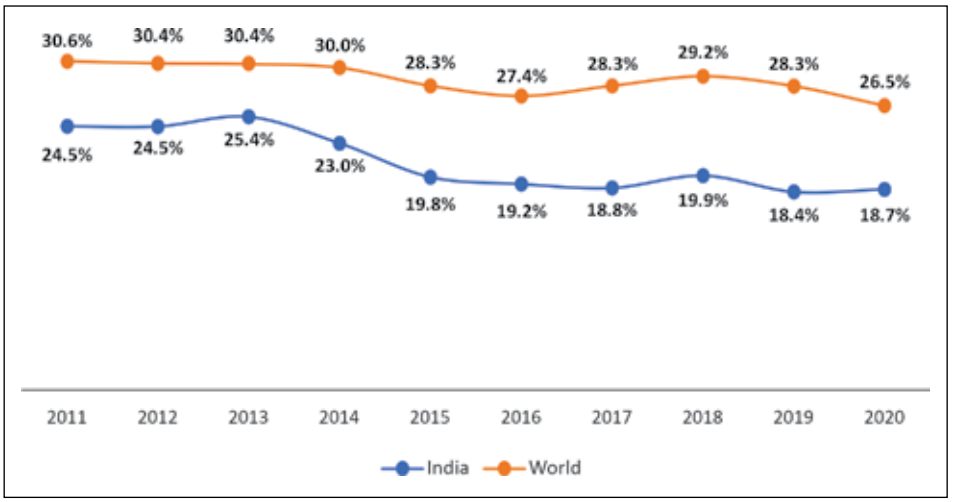
Source: Data accessed from ITC Trade Map, India Exim Bank Research

Exports have formed a crucial part of Indian economy's growth over the last few years, contributing to 18.7% to the GDP in 2020. However, a gradual decline is noted in India's exports as a per cent of GDP during 2013-19. Also, in this regard, India lagged the world average of 26.5% in 2020 as well as that achieved by other developing countries like Vietnam (105.5%)[4] and Mexico (40.2%).

While an unforeseen disruption in India's foreign trade of both, goods, and services, was caused on account of the country-wide lockdown measures enforced to curtail the spread of COVID-19, it may be noted that a strong on-year recovery has been recorded FY 2022, with merchandize exports crossing the US$ 400 billion mark.

[4] During 2010-19, while Vietnam's exports of goods and services increased at a CAGR of 12.8% to reach US$ 279.7 billion. At the same time, the total imports also increased at a CAGR of 11.3% and were valued at US$ 271.3 billion in 2019. In this regard, it is noted that if the economy imports a lot to export, only the value added to the imports for the purpose of exports is added to the calculation of the GDP. Put overall, this leads to more than proportionate growth in exports as compared to the GDP of the country.

Chart 1.2: Exports of Goods and Services as a percentage of the GDP: India vs World



Source: Data accessed from World Bank Database, India Exim Bank Research

To come back stronger from COVID-19 disruptions, India's external sector will have to work on the competitiveness of its products across the sectors. This can only come through reforms in various elements of the economy such as infrastructure and logistics as well as entering into strategic trade agreements.

Going forward, given the criticality of its external engagements, India needs to renew its commitment to reforms and better reap the benefits of global integration. However, to integrate with the global economy, there is a definite need to increase the competitiveness across sectors that are performing below potential. While this calls for reforms to improve the quality of infrastructure and logistics, greater ease of doing business, a sound financial system, and skill development, it would also require entering into strategic trade agreements with select countries across specific sectors.

It is to be noted that trade agreements do not just reduce and eliminate tariffs, but also help address behind-the-border barriers that would otherwise

impede the flow of goods and services. In effect, they result in increased foreign investment and improve the rules affecting issues such as intellectual property, e-commerce, and government procurement.

India's Engagement in Trade Agreements

Varied forms of trade agreements (Free Trade Agreements, Preferential Trade Agreements, Regional Trade Agreements, Comprehensive Economic Cooperation Agreements, Comprehensive Economic Partnership Agreements, Comprehensive Economic Cooperation and Partnership Agreements and Economic Cooperation and Technical Cooperation Agreements) have become a critical part of the foreign trade ecosystem across the world. Apart from being a co-signatory to some critical trade agreements like the ASEAN-India FTA, India is also a part of certain prominent regional blocs. In a short time, India has negotiated many trade agreements, and many are in the pipeline including expansion or graduation of existing FTAs to CECAs[5].

As of 2020, India was a part of ten Free Trade Agreements (FTAs) and six Preferential Trade Agreements (PTAs) which are already in force, along with several other on-going trade negotiations. Following are the major trade agreements and negotiations, India is currently a part of. The impact of these agreements on India's foreign trade is analyzed in detail in the subsequent chapters.

Table 1.1: India's Major Trade Agreements

Name of the Agreement	Member Countries	Classification
Asia Pacific Trade Agreement (APTA)	Bangladesh, China, India, Republic of Korea, Sri Lanka	Preferential Trade Agreement
India ASEAN Trade in Goods Agreement (TIG)	Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam and India	Free Trade Agreement
Bangladesh, India, Myanmar, Sri Lanka, Thailand Economic Cooperation (BIMSTEC)	Bangladesh, India, Myanmar, Sri Lanka, Thailand, Bhutan and Nepal	Under negotiations

[5] Relooking India's Tariff Policy Framework, India Exim Bank, March 2020

Name of the Agreement	Member Countries	Classification
Global System of Trade Preferences (GSTP)	Algeria, Argentina, Bangladesh, Benin, Bolivia, Brazil, Cameroon, Chile, Colombia, Cuba, Democratic People's Republic of Korea, Ecuador, Egypt, Ghana, Guinea, Guyana, India, Indonesia, Iran, Iraq, Libya, Malaysia, Mexico, Morocco, Mozambique, Myanmar, Nicaragua, Nigeria, Pakistan, Peru, Philippines, Republic of Korea, Romania, Singapore, Sri Lanka, Sudan, Thailand, Trinidad and Tobago, Tunisia, Tanzania, Venezuela, Viet Nam, Yugoslavia, Zimbabwe	Preferential Trade Agreement
India Brazil and South Africa (IBSA)	India, Brazil and South Africa	Under negotiations
South Asia Free Trade Agreement (SAFTA)	India, Pakistan, Nepal, Sri Lanka, Bangladesh, Bhutan and the Maldives	Free Trade Agreement
Indo Sri Lanka FTA (ISLFTA)	Sri Lanka, India	Free Trade Agreement
Indo Malaysia CECA (IMCECA)	Malaysia, India	Free Trade Agreement
India Singapore CECA (ISCECA)	Singapore, India	Free Trade Agreement
Japan India CEPA (JICEPA)	Japan, India	Free Trade Agreement
India Korea CEPA (IKCEPA)	South Korea, India	Free Trade Agreement

Source: Ministry of Commerce and Industry

This Study

This Study seeks to analyze the way trade agreements have worked in the past and going forward how could these agreements be leveraged to gain an edge in the international markets. This would however require some renegotiations.

Accordingly, an attempt is made to arrive at the impact of current trade agreements in which India is a party to, while also identifying the potential

agreements that align with sectors or sub-sectors of country's trade competitiveness.

It is also noted that in a world of increasingly fragmented production processes, it is equally important for India to integrate and move up along the global value chains. In principle, by promoting exports, trade agreements can help the country move up the value chain. That, in turn, can provide India an edge vis-à-vis non-member countries.

The Study has also touched upon some of the developed countries and regions with which India can explore suitable opportunities to sign an FTA like the EU, the UK, Canada and Australia to gain wider market access.

In essence, the idea would also be to highlight the factors that need to be considered before entering into trade agreements. Focus is laid on overcoming some of the challenges like - non-tariff barriers, high turnaround time, and key areas beyond merchandise trade (such as services trade and investments) not being a part of many agreements - that have prevented India to optimize gains from the old and existing trade agreements, by drawing a parallel with other trade agreements across the world.

2. REVISITING MAJOR GLOBAL TRADE AGREEMENTS

Economic Rationale for Trade Agreements

Over the last two decades, trade has been a key determinant of the rapid expansion in the world economy, by making it possible for economies to gain a better access to resources beyond their geographical borders. While free trade is often considered the best alternative to maximize efficiency and welfare gains, multilateral liberalization of trade globally is practically unachievable, given the political and socio-economic dissimilarities across countries. As a result, this leads to unilateral trade policies that inefficiently restrict trade flows, coexist with trade agreements that aim to reduce such unilateral measures in the world trade.

It is vital to understand the difference between the Preferential Trade Agreements (PTAs) and Free Trade Agreements (FTAs). PTAs, like the FTAs, have both positive and negative effects, and are considered the "second-best" options after free trade. In a PTA, two or more parties agree to reduce tariffs on agreed number of tariff lines. The lists of products on which the partners agree to reduce duty is called positive list. In FTAs, on the other hand, tariffs on items covering substantial bilateral trade are eliminated between the partner countries. However, each maintains individual tariff structure for non-members.

Broadly, two rationales have been used to justify the growing attention towards trade agreements. First, in the absence of a trade agreement, a country may be tempted to manipulate the terms-of-trade in order to increase its national income at the expense of its trading partners. Second, trade agreements allow governments to avoid terms-of-trade conflicts and to

resist pressures from the private sector to take a departure from a liberal trade policy[6].

Table 2.1: Types of Trade Agreements

Trade Agreement	Coverage
Preferential Trade Agreement	Two or more parties agree to reduce tariffs on agreed number of tariff lines. The list of products on which the partners agree to reduce duty is called positive list. For example: India-Mercosur PTA.
Free Trade Agreement	Tariffs on items covering substantial bilateral trade is eliminated between the partner countries. Each signatory maintains individual tariff structure for non-members. For example: India Sri Lanka FTA.
CECA and CEPA	Essentially FTA+ packages, these consist of an integrated package of Agreement on goods or services, investment, mutual recognition, e-commerce, intellectual property etc. For example: India Korea CEPA.
Custom Union	Partner countries may decide to trade at zero duty among themselves, however they maintain common tariffs against rest of the world. For example: European Union
Common Market	Customs Union with provisions to facilitate free movements of labour and capital, harmonize technical standards across members. For example: European Common Market.
Economic Union	Economic Union is a Common Market extended through further harmonization of fiscal/monetary policies and shared executive, judicial & legislative institutions. For example: European Union.

Source: WTO Regional Trade Agreements Database

Broadly, two rationales have been used to justify the growing attention towards trade agreements. First, in the absence of a trade agreement, a country may be tempted to manipulate the terms-of-trade in order to increase its national income at the expense of its trading partners. Second, trade agreements allow governments to avoid terms-of-trade conflicts and to

[6] Flexibility in Trade Agreements: WTO
(https://www.wto.org/english/res_e/booksp_e/anrep_e/wtr09-2b_e.pdf)

resist pressures from the private sector to take a departure from a liberal trade policy[7].

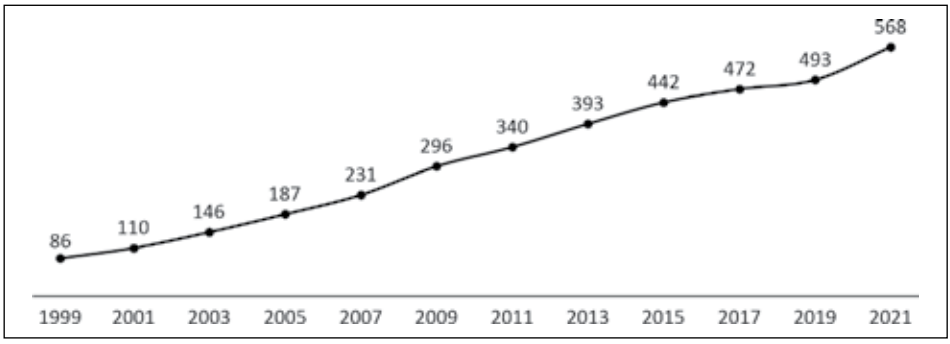
Table 2.2: Types of RTAs in Force

Type of Agreement	Enabling clause	GATS Article V	GATT Article XXIV	Total
Free Trade Agreement	22	0	290	312
Economic Integration Agreement	0	181	0	181
Partial Scope Agreement	27	0	0	27
Customs Union	7	0	11	18
Customs Union - Accession	2	0	10	12
Free Trade Agreement - Accession	1	0	8	9
Economic Integration Agreement - Accession	0	7	0	7
Partial Scope Agreement - Accession	2	0	0	2
Grand Total	**61**	**188**	**319**	**568**

Source: WTO Regional Trade Agreements Database

RTAs across the world have risen in number and reach over the years, including a notable increase in large plurilateral agreements under negotiation. Even though non-discrimination among trading partners is one of the core principles of the WTO, RTAs constitute one of the exemptions and are authorized under the WTO, subject to a set of rules.

Chart 2.1: Cumulative Number of RTAs in Force



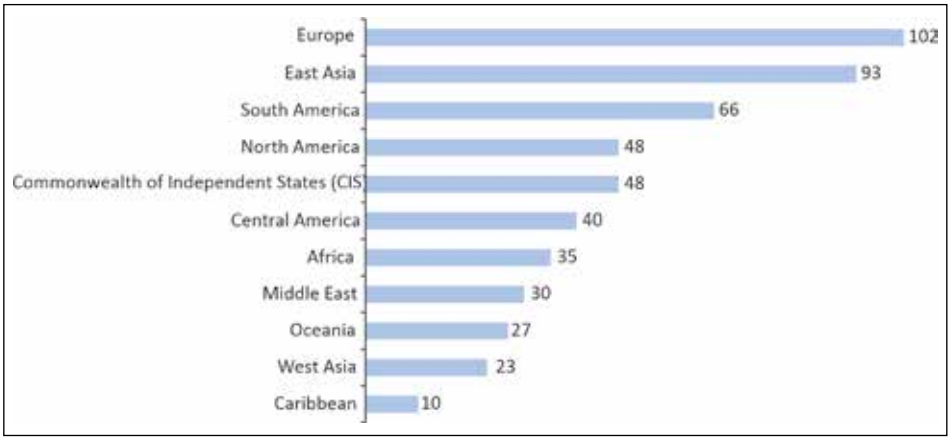
Source: WTO Regional Trade Agreements Database

[7] Flexibility in Trade Agreements: WTO
(https://www.wto.org/english/res_e/booksp_e/anrep_e/wtr09-2b_e.pdf)

It may be noted that the nature of provisions in RTAs have evolved from market access in goods and services (and related WTO rules) to provisions on issues such as investment, competition, government procurement, environment, labour, electronic commerce, small and medium sized enterprises, and gender related issues.

Region-wise, the highest number of RTAs in force during 2020 were in Europe, followed by East Asia and South America.

Chart 2.2: Region-wise Notifications of RTAs in Force



Source: WTO Regional Trade Agreements Database

With regards the number of signatories, the choice between unilateral and multilateral approaches plays a crucial role in determining the effectiveness of reducing trade barriers. Unilateral trade preferences are essentially non-reciprocal trade preference mechanisms usually adopted for developed-developing country trade relationships. Multilateral trade agreements, on the other hand, are reciprocal trade preference settings involving three or more countries without discrimination between the members.

It is noted that, broadly, multilateral agreements have a major advantage over the unilateral agreements. The economic gains from international trade are reinforced and enhanced when multiple countries or regions agree to a mutual reduction in trade barriers by integration of markets.

While the benefits largely depend on the design, industry, and country, following are the key areas through which the impact of an FTA can be analyzed.

- **Economies of Scale**

  Economies of scale usually occur due to improved technical efficiency in large-scale production, greater capability to spread the administrative costs and overheads over a bigger operation, or better logistics because of larger volumes. By creating a larger market for firms operating in partner countries, FTAs allow producers to take advantage of a larger customer base and, hence, produce at a lower average cost on all sales.

- **Impact on FDI**

  Bilateral and regional FTA formation attracts long-term, risk-sharing investment flows by creating a more integrated marketplace within which multinational corporations can enjoy a regional division of labour with low transaction costs.

  The patterns of FDI that follow the creation of an FTA may be similar to the effects of trade creation and trade diversion. Further, FTAs usually induce more FDI flows into the region by multinationals that are headquartered outside the region. An FTA may also induce intra-bloc investment by multinationals with a regional origin.

- **Competitiveness and Long-Run Growth Effects**

  The reduction in trade barriers allows members to benefit from healthy increased intra-bloc competition. Increased exposure to competition from partner countries weeds out less productive firms and favors more productive ones. This also gives firms an incentive to invest in more efficient productive process and technology.

  For each member economy and for the FTA, these competitive forces improve structural efficiency and resource allocation as different members specialize in the production of specific final and intermediate goods. Increased competition on productivity and efficiency fronts put together, result in better long-run growth prospects for FTA members.

- **Value Chain and Production Linkages:**

  While ascertaining the likely impact of trade agreements on GVCs, it may additionally be noted that aspects like tariffs, customs and anti-dumping are already subject to some form of commitment under the WTO+ provisions. However, other critical obligations outside the mandate of the WTO+ provisions like investment and competition policy play an equally important role in the impact assessment of trade agreements.

- **Enabling Structural Policy Changes and Reforms**

  Although traditionally focused on commercial policy at the border, increasingly, FTAs are affecting deeper integration by addressing behind-the-border measures like quality standards, laws related to corporate and public governance, customs procedures, competition policy, including the reform of state-owned enterprises, and other sensitive sectors with important links to the rest of the economy. The inclusion of these non-traditional areas in FTAs shows how instrumental these agreements have become in shaping and harmonizing the national economic policies of members.

Relooking at the Major World Trade Agreements

1. ASEAN Free Trade Agreement (AFTA)

The Association of Southeast Asian Nations (ASEAN) comprises ten nations. It can be divided into two groups - the ASEAN 6 - Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand – and the CLMV countries – Cambodia, Lao PDR, Myanmar and Vietnam. ASEAN took the first step in economic integration as ASEAN Free Trade Area (AFTA) in 1993.

Trade Volumes and Intra-regional Trade

During 2010-19, ASEAN's merchandize exports registered an AAGR of 3.7% to reach US$ 1.4 trillion, contributing to 7.6% of world exports in 2019, up from 7.0% in 2010. With regards member countries, the highest exports, in 2019, were recorded for Singapore (27.4%), followed by Vietnam (18.6%), Malaysia (16.7%), Thailand (17.2%) and Indonesia (11.8%). Further, the trade

balance for ASEAN aggregation has been in surplus during the last ten years, reaching US$ 31.0 billion in 2019.

In addition, it is noted that 20% of intra-ASEAN trade is preferential, with over 70% of intra-ASEAN trade at MFN zero rate, and more than 90% for some bilateral agreements. Trade liberalization within ASEAN has involved removing tariffs and reducing other administrative procedures in getting products to market. Particularly, in the ASEAN-6 group, rates have been effectively zero since 2010[8].

It is also noted that after entering AFTA, the intra-regional trade of the member countries registered a higher growth (7.2%) than their trade with rest of the world (6.9%). While the intra-regional integration expansion has led to diversification in the variety and quality of products, ASEAN's intra-regional trade share has decreased slightly from 23.7% in 1995 to 20.7% in 2020.

Table 2.3: Intra-ASEAN Trade at a Glance (US$ Billion)

Country	Exports to ASEAN			Exports to Rest of the World		
	2010	2019	AAGR	2010	2019	AAGR
Brunei Darussalam	1.1	2.5	14.2%	7.8	4.8	-2.3%
Cambodia	0.7	1.3	14.5%	4.9	13.5	12.3%
Indonesia	33.3	41.5	3.1%	124.4	126.2	1.0%
Lao	1.2	3.5	17.4%	0.8	2.3	19.4%
Malaysia	50.5	68.6	3.8%	148.3	169.6	2.0%
Myanmar	4.2	4.3	2.9%	4.7	13.8	13.6%
Philippines	11.5	10.8	0.0%	40.0	59.6	4.7%
Singapore	107.8	112.0	1.3%	245.5	278.4	1.8%
Thailand	44.3	62.6	4.3%	151.0	182.7	2.3%
Vietnam	10.4	24.9	11.0%	61.9	239.7	16.5%

Source: Data accessed from ITC Trade Map, India Exim Bank Research

[8] UNCTAD Research Paper: The Asian Economic Integration Cooperation Agreement: Lessons for economic and social development

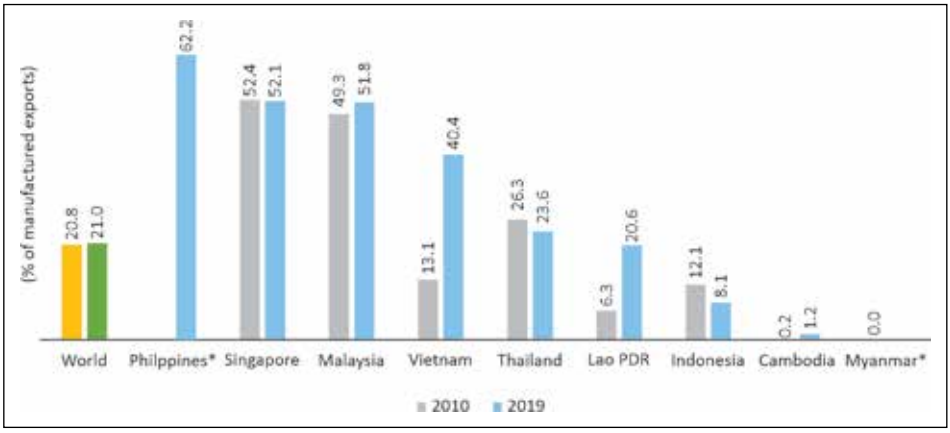
The increase in intra-regional trade is expected to contribute to further integration into supply and value chains across ASEAN. Interestingly, the expansion of vertical intra-industry trade in parts and components, other intermediate goods, and final products have been a key determinant of trade upgrading and diversification.

Intra-regional integration expansion has led to diversification in the variety and quality of products. Also, exports of manufacturing goods represent more than half of ASEAN exports.

Trade Specialization

On a macro level, the economic benefits of entering into trade agreements also enable countries to specialize in the production of goods and services in which they have a relative comparative advantage. The lowering of trade barriers among RTA partners, could lead both to trade creation whereby higher cost domestic production is replaced by imports from a lower cost RTA partner, as well as trade diversion whereby imports from a low-cost producer outside the agreement are replaced by imports from a higher cost producer inside the agreement.

Chart 2.3: ASEAN's High-technology Exports as a percentage of Manufactured Exports (2010 vs 2019)



Source: Data accessed from the World Bank Database, India Exim Bank Research

**2010 data for Philippines and 2019 data for Myanmar is not available*

Further, for majority of the AFTA member countries, a notable increase in the exports of high-technology products, as a percentage of manufactured exports, was registered during 2010 and 2019.

The increasing share of trade in intermediate goods, particularly in medium and high technology and electronics, and in services, has also been prompted by improvements in physical infrastructure, logistics, rapid developments in ICT, and reductions in trade barriers and trade costs.

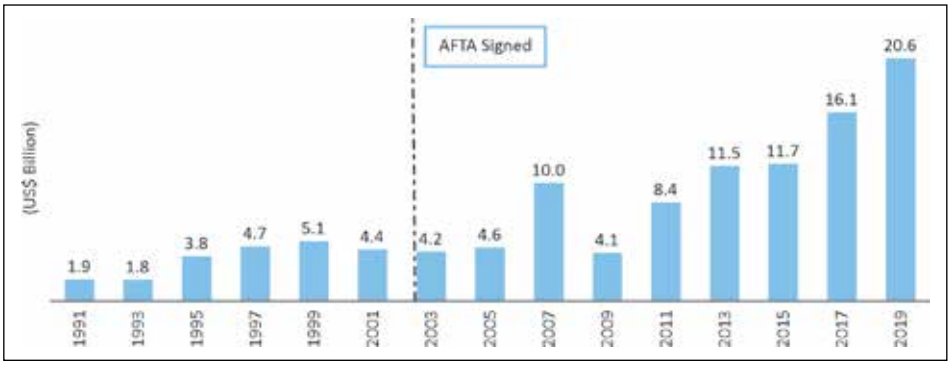
In terms of manufacturing upgrading, Vietnam, which used to be a predominantly agricultural economy, saw a notable pivot towards specialization in textiles, apparel, and hi-tech products. Similarly, Thailand emerged as a leading vehicle and automotive-parts exporter. Over the years, other ASEAN members have built export industries based on natural resources. For instance, Indonesia has become the world's largest producer and exporter of palm oil and coal, and the second-largest producer of cocoa and tin. Myanmar, an LDC which recently began its economic and political transformation, has large reserves of oil, gas, and precious minerals. Philippines initially specialized manufactures and agriculture exports but has moved into information technology and business process outsourcing, becoming a major offshoring services provider.

Increase in FDI

Over the last few years, many ASEAN countries have adopted the export-led growth strategy. In doing so, these countries also promote the export sector by liberalizing FDI to ease the direct investment from overseas. It is noted that the total inward FDI in the ASEAN aggregation increased at a CAGR of 8.8% during 1990 and 2019.

The total FDI inflows in the ASEAN countries were recorded at US$ 20.6 billion in 2019, nearly double from US$ 10.0 billion in 2010. It is further noted that the FDI inflow was largely concentrated amongst the top ten recipient sectors, representing around 94% of the total FDI inflows.

Chart 2.4: Inward FDI in ASEAN



Source: Data accessed from UNCTAD Stat, India Exim Bank Research

The FDI inflows to ASEAN classified by sector in 2019 indicate how that manufacturing, financial and insurance, wholesale and retail trade sectors were the top three recipients of FDI, collectively accounting for 78% of the total FDI inflows. This captures the foreign investment inflow on account of increased specialization which is reflected in the changed trade patterns of ASEAN countries after AFTA came into force.

2. United States–Mexico–Canada Agreement (USMCA)

Under the terms of erstwhile NAFTA (USMCA, henceforth), the United States, Canada, and Mexico agreed to gradually phase out all tariffs on merchandise trade and to reduce restrictions on trade in services and foreign investment by granting MFN status to each other. It also requires the exporters to get the Certificate of Origin to waive off tariffs. This meant that the exports had to originate in the United States, Canada, or Mexico. A product made in Peru but shipped from Mexico would still pay a duty when it entered the United States or Canada.

In July 2020, the United States–Mexico–Canada Agreement (USMCA) succeeded the erstwhile NAFTA with new policies on labour and environmental standards, intellectual property protections, and digital trade provisions. Broadly, it covers the following revisions to the erstwhile NAFTA:

- **Country of origin rules:** Automobiles are required to have 75% of their components manufactured in Mexico, the US, or Canada to qualify for zero tariffs (up from 62.5 percent under NAFTA).

- **Labour provisions:** About 40 to 45% of automobile parts must be made by workers who earn at least US$ 16 an hour by 2023.

- **Intellectual property and digital trade:** The deal extends the terms of copyright to 70 years beyond the life of the author, up from 50 years specified in USMCA. Further, it includes new provisions to deal with the digital economy, such as prohibiting duties on music and e-books, and protections for internet companies.

- **Sunset clause:** The agreement adds a 16-year sunset clause, which means the terms of the agreement expire, or "sunset," after 16 years. The deal is also subject to a review every six years, at which point the US, Mexico, and Canada can decide to extend the USMCA. In addition, it eliminates the need for companies to establish headquarters in any other USMCA country and encourages cross-border business by excluding US companies from the need to localize data, open a Canadian or Mexican headquarters.

Trade Volumes and Intra-regional Trade

The USCMA aggregation accounted for 13.6% of global merchandize exports in 2019, amounting to US$ 2.5 trillion. During 2010-19, the exports from USMCA to world registered a modest AAGR of 3.2%, increasing from US$ 1.9 trillion in 2010 to US$ 2.5 trillion in 2019. Broadly, the top export commodities comprised of mineral fuels[9] (12.7%), capital goods[10] (12.5%), vehicles[11] (12.3%), and electrical machinery[12] (10.4%).

The inter-regional trade in the bloc or intra-USMCA trade saw a substantial and sustained increase after the agreement came into effect in 1994. This is evident from the fact that the top three export destinations for the exports originating in USMCA were the USMCA members themselves, accounting for 49% of the total exports in 2019, followed by China (5%) and Japan (3%).

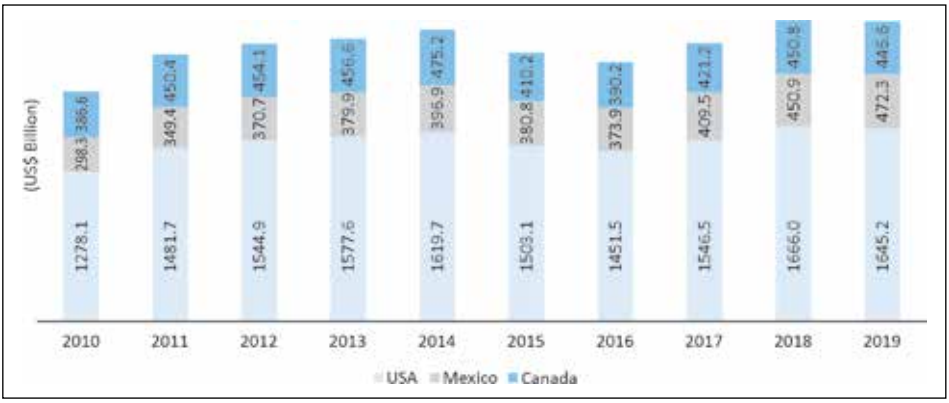
[9] HS 27: Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes

[10] HS 84: Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof

[11] HS 87: Vehicles other than railway or tramway rolling stock, and parts and accessories thereof

[12] HS 85: Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles

Chart 2.5: USMCA's Foreign Trade



Source: Data accessed from ITC Trade Map, India Exim Bank Research

Table 2.4: Intra-USMCA Trade at a Glance (US$ Billion)

Country	Exports to USMCA			Exports to Rest of the World		
	2010	2019	AAGR	2010	2019	AAGR
USA	412.9	548.7	3.4%	1,278.0	1645.1	3.0%
Canada	294.2	342.3	2.0%	386.5	446.5	1.9%
Mexico	249.5	373.0	4.7%	298.3	472.2	5.4%

Source: Data accessed from ITC Trade Map, India Exim Bank Research

Trade Specialization

A direct impact of erstwhile NAFTA was observed with shifting of manufacturing to destinations with relatively higher comparative advantage. In particular, a substantial part of the increase in US-Mexico trade is attributed to specialization as manufacturing and assembly plants reoriented to take advantage of economies of scale.

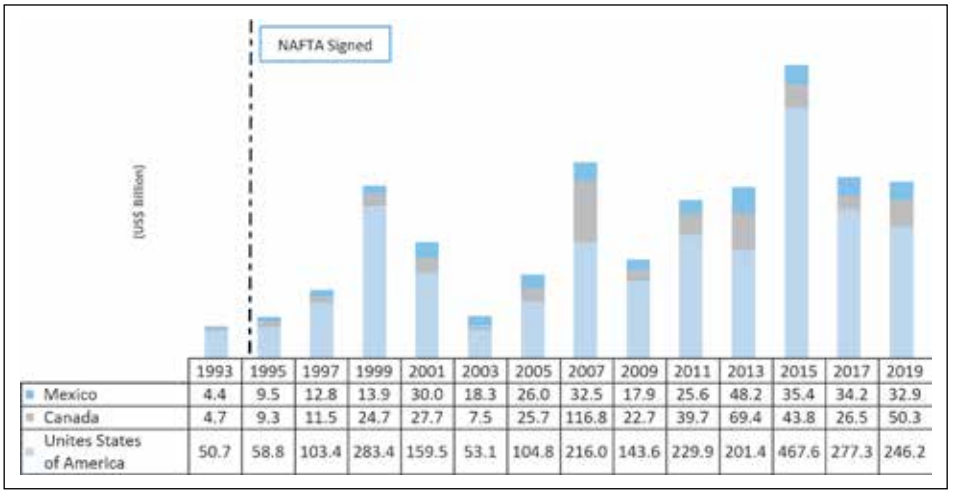
Production sharing between the US and Mexico has increased as the manufacturers have started to work together. This has also led to increased merchandize trade between the two nations. Further, the trade expansion has resulted in the creation of vertical supply relationships, especially along the US-Mexico border.

The flow of intermediate inputs produced in the United States and exported to Mexico and the return flow of finished products greatly increased the importance of the US-Mexico border region as a production site[13].

Increase in FDI

The total FDI inflows in the USMCA were recorded at US$ 329.5 billion in 2019, marginally lower from US$ 337.9 billion in the previous year and registering an AAGR of 14.8% during 1994-2019.

Chart 2.6: Inward FDI in USMCA



	1993	1995	1997	1999	2001	2003	2005	2007	2009	2011	2013	2015	2017	2019
Mexico	4.4	9.5	12.8	13.9	30.0	18.3	26.0	32.5	17.9	25.6	48.2	35.4	34.2	32.9
Canada	4.7	9.3	11.5	24.7	27.7	7.5	25.7	116.8	22.7	39.7	69.4	43.8	26.5	50.3
Unites States of America	50.7	58.8	103.4	283.4	159.5	53.1	104.8	216.0	143.6	229.9	201.4	467.6	277.3	246.2

Source: Data accessed from UNCTAD Stat, India Exim Bank Research

USMCA had a significant positive impact on Mexico's overall economic development by supporting the infrastructure and improving investors' confidence, which allowed non-USMCA members to invest in Mexico to enter the North American markets. The rules of origin system of the agreement enabled foreign firms to use Mexico as an exporting platform to the US.

[13] Federation of American Scientists: U.S.-Mexico Economic Relations: Trends, Issues, and Implications (https://fas.org/sgp/crs/row/RL32934.pdf)

3. Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)

The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) is a free trade agreement between eleven countries in the Asia-Pacific region: Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam, which came into effect in December 2018. The pact binds its signatories, which represented about 16% of global merchandise trade in 2019, to 30 chapters providing for freer trade and investment access. Coming together of these economies is expected to cause a substantial shift in global supply chains.

It is noted that even though the United States withdrew from TPP in 2017, there could be significant gains to the remaining eleven signatories. The United States, on the other hand, is likely to suffer losses from such arrangement in two ways. First, it would have to forego the benefits that would otherwise accrue from being a signatory to the relatively large TPP agreement, and second, the new Asia-Pacific agreements is likely to substantially reduce US exports to the region as countries shift their trade to other competing economies of the United States.

The CPTPP provides for 98% elimination of tariffs among the participants with minor exceptions in select sensitive areas like rice exports by Japan and dairy products exports by Canada. It provides a single set of rules of origin and allows content from all CPTPP countries to be cumulated.
For instance, if a good is required to have at least 70% CPTPP content to qualify for preferential tariffs, any combination of the CPTPP members can be put together to constitute that share.

In addition, the CPTPP also includes rules on issues that have not yet been incorporated into other trade agreements, such as rules relating to provision of a level playing field to the state-owned enterprises (SOE). The key areas taken into account by the agreement to do so are[14]:

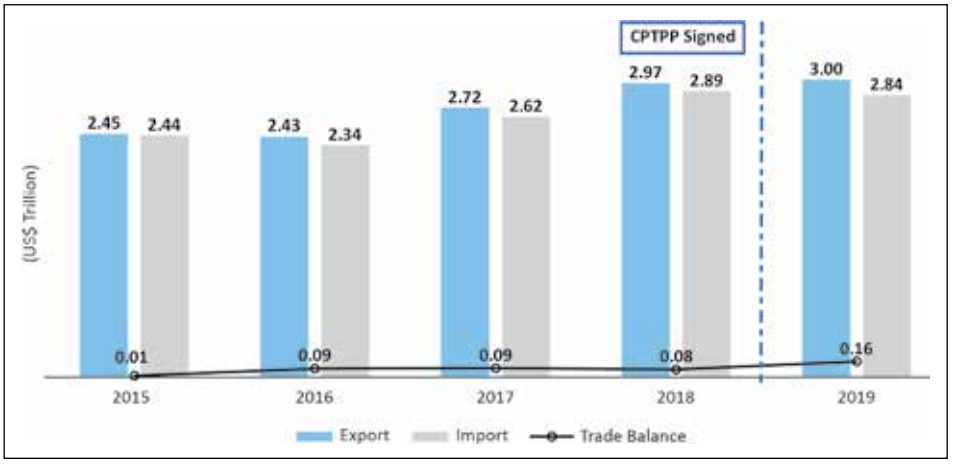
[14] Government of Canada: What does CPTPP mean for state-owned enterprises? (https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptpgp/sectors-secteurs/state_owned-appartenant.aspx?lang=eng)

- **Commercial considerations:** SOEs are to act in accordance with commercial considerations except when providing a public service; this rule would only apply when the SOE is engaged in commercial activities.
- **Non-discrimination:** SOEs are to buy and sell goods and services in a non-discriminatory manner; this rule would apply only when the SOE is engaged in commercial activities.
- **Non-commercial assistance:** No CPTPP country is to cause harm to another CPTPP country using non-commercial assistance provided to its SOEs; this rule would not apply to services supplied at home.
- **Transparency:** CPTPP countries are required to disclose certain information regarding their SOEs. These transparency rules are designed to encourage good corporate governance.

Trade Volumes and Intra-regional Trade

The merchandize exports by the CPTPP aggregation in 2019 were recorded at US$ 3 trillion, up by US$ 38.5 billion from 2018. It is noted that the share of exports from CPTPP in the world exports has risen from 15% in 2017 to 16% in 2019, after the agreement came into effect in 2018.

Chart 2.7: CPTPP's Foreign Trade



Source: Data accessed from ITC Trade Map, India Exim Bank Research

Among the members of CPTPP, Japan was both the largest exporter and the largest importer in 2019 with exports amounting to US$ 705.8 billion and imports amounting to US$ 720.9 billion. On the export front, Japan accounted for 23.5% of total exports by the CPTPP aggregation in 2019 and was followed by Mexico (15.7%), Canada (14.9%), Singapore (13%), and Vietnam (10.6%).

With regards trading partners, the USA was the largest export destination, accounting for 33% of total exports by the CPTPP aggregation in 2019, followed by China (14.8%), South Korea (4%), and Hong Kong (3.8%). CPTPP's exports to the USA saw a notable increase from US$ 957.1 billion in 2018 to US$ 991.9 billion in 2019. This increase was largely led by the export of vehicles, electrical machinery, and capital goods, which registered a y-o-y growth of 3.0 %, 4.0% and 4.0% in 2019, respectively.

Nearly a year and a half after coming into effect, the CPTPP economies have seen mixed results in the short term. While the exports of CPTPP members to the world increased in response to the agreement, the intra-CPTPP trade in 2019 showed minor downward deviations.

Table 2.5: Intra-CPTPP Trade at a Glance (US$ Billion)

Country	Exports to CPTPP			Exports to Rest of the World		
	2018	2019	Growth	2018	2019	Growth
Australia	47.8	46.9	(-) 1.9%	254.5	272.6	7.1%
Brunei Darussalam	3.9	4.9	25.8%	6.5	7.2	11.4%
Canada	22.0	20.7	(-) 5.8%	450.8	446.5	(-) 0.9%
Chile	12.3	11.3	(-) 7.5%	75.4	69.1	(-) 8.3%
Japan	97.2	89.1	(-) 8.3%	738.1	705.8	(-) 4.4%
Malaysia	73.4	69.0	(-) 6.0%	247.4	238.1	(-) 3.8%
Mexico	24.1	22.9	(-) 5.1%	450.9	472.2	4.7%
New Zealand	11.0	10.2	(-) 7.6%	38.4	38.1	(-) 0.7%
Peru	5.2	6.4	23.4%	47.2	45.1	(-) 4.4%
Singapore	95.0	89.1	(-) 6.2%	412.0	390.3	(-) 5.3%
Vietnam	44.1	48.3	9.5%	243.7	318.2	30.6%

Source: Data accessed from ITC Trade Map, India Exim Bank Research

With regards intra-CPTPP exports, highest increase in exports amongst member countries was recorded for Brunei Darussalam, primarily through its exports of liquified natural gas[15], which grew by 14.5% in 2019 on a y-o-y basis. On the other hand, Canada's exports to the CPTPP aggregation registered a y-o-y decline of (-) 5.8% in 2019. Further, exports from Japan and New Zealand to the CPTPP members witnessed a downward trend during the same time registering a negative y-o-y growth of (-) 8.3% and (-) 7.6% respectively.

In 2019, highest increase in the merchandize exports from the CPTPP aggregation was recorded by Vietnam. During the year, more than 23% of Vietnam's exports were directed to the USA and 16% to China. Vietnam's merchandize exports primarily comprised of mobile phones[16], parts of mobile phones[17] and electronic integrated circuits[18].

Trade Specialization

According to a Study by the World Bank[19], the highest growth of exports and output under the CPTPP are projected to occur in food and beverages, apparel, and textiles. Their collective exports will expand by 28% relative to baseline conditions in 2030, boosting production within the CPTPP by almost 5%. It is noted that reduction in tariffs is likely to further deepen the specialization of Vietnam and Malaysia across sectors like textiles and apparel.

Additionally, reduction of imposed trade barriers is also projected to increase imports in all sectors, with the highest changes in food processing, agriculture, wearing apparel, textiles, and all services. Import expansion in these sectors will be partly induced by a stronger demand on cheaper intermediate inputs

[15] HS 271111: Natural gas, liquefied

[16] HS 851712: Telephones for cellular networks "mobile telephones" or for other wireless networks

[17] HS 851770: Parts of telephone sets, telephones for cellular networks or for other wireless networks and of other apparatus for the transmission or reception of voice, images or other data, n.e.s.

[18] HS 854321: Electronic integrated circuits as processors and controllers, whether or not combined with memories, converters, logic circuits, amplifiers, clock and timing circuits, or other circuits

[19] Actual and Potential Trade Agreements in the Asia-Pacific: Estimated Effects (https://documents1.worldbank.org/curated/en/171731585114146413/pdf/Actual-and-Potential-Trade-Agreements-in-the-Asia-Pacific-Estimated-Effects.pdf)

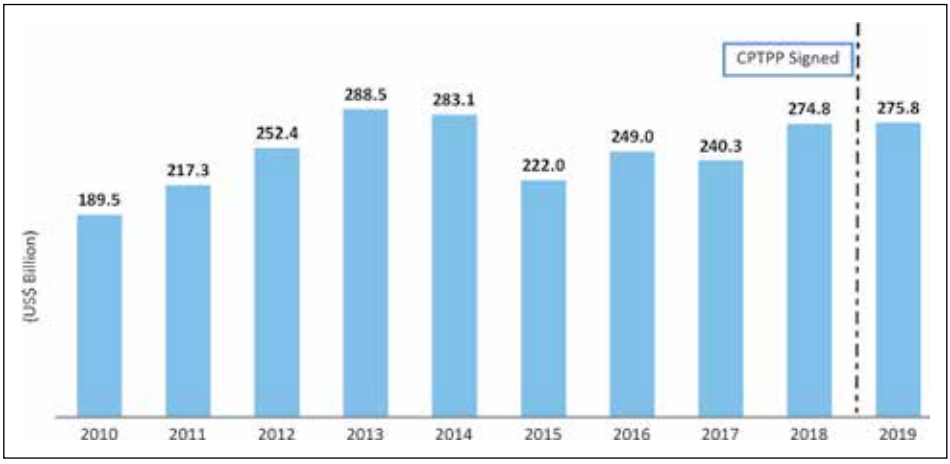
from other CPTPP members (especially in textiles and apparel having high shares of intermediate inputs in their output). For instance, textile sector in Vietnam will observe significant increases in imports of textile products to higher demand from the booming apparel sector.

The CPTPP is also expected to stimulate the growth of services sectors, especially Trade and transport services, mainly due to a higher demand on these services by all other sectors as they are used as an input in all sectors.

Increase in FDI

The total FDI inflows in the CPTPP countries were recorded at US$ 275.8 billion in 2019, marginally higher from US$ 274.8 billion in 2018.

Chart 2.8: Inward FDI in CPTPP



Source: Data accessed from UNCTAD Stat, India Exim Bank Research

While the larger impact of FDI inflows cannot be ascertained in one year of CPTPP coming into effect, it is noted that the agreement offers new opportunities for local businesses in the developing countries to participate in foreign trade or widen the existing import and export markets. Amongst the underlying incentives that is likely to encourage investment flows is elimination of 95% of customs duties in a market comprising of over 500 million consumers.

Box 2.1: African Continental Free Trade Agreement (AfCFTA)

Launched by the African Union, the African Continental Free Trade Area is expected to be the largest free trade area by number of participating countries, since the formation of the WTO. The agreement covers 54 countries with a combined GDP of about US$ 2.5 trillion and a population of 1.2 billion people.

The underlying idea of the agreement is to create a single goods and services market across Africa and establish a continental customs union to streamline trade and foreign investments. Trading under the AfCFTA Agreement was due to commence on 1 July 2020, but due to the COVID-19 outbreak, it was delayed and was finally launched on 1 January 2021. As at January 2022, 41 of the 54 signatories (76%) have deposited their instruments of AfCFTA ratification.

The merchandize exports by African region during 2020 were recorded at US$ 394.6 billion in 2020, registering a fall of 17% over 2019 due to the pandemic. The major products exported from Africa in 2020 included mineral fuels and oils (28.5%), pearls and precious stones (17.2%), ores, slag, and ash (6.4%), copper and its articles (4.6%), and vehicles (3.3%).

As per the UNCTAD, intra-African trade has remained relatively lower than that of the other continents and was recorded at 2% during the period 2015-17, while comparative figures for America, Asia, Europe and Oceania were 47%, 61%, 67% and 7%, respectively. The Economic Commission for Africa estimates that AfCFTA has the potential both to boost intra-African trade by 52.3% by eliminating import duties, and to double this trade if non-tariff barriers are also reduced.

Box 2.2: Southern Common Market (MERCOSUR)

The Southern Common Market (MERCOSUR) is a regional integration process, initially established by Argentina, Brazil, Paraguay, and Uruguay. It was subsequently joined by Venezuela which was suspended indefinitely in 2016. Bolivia is to be a part of Mercosur; however, it is still complying with the accession procedure.

The main objective of Mercosur is to promote a common space that generates business and investment opportunities through the competitive integration of national economies into the international market[20].

The member countries of Mercosur have a combined GDP of almost US$ 1.9 trillion, marginally more than the second largest trade bloc of the region called Pacific alliance. It may be noted that Bolivia, Chile, Colombia, Ecuador, Guyana, Peru, and Suriname are associate members of Mercosur and receive tariff benefits when trading with the full members. However, these nations do not have the full voting rights.

The total exports of Mercosur in 2020 were recorded at US$ 279.5 billion in 2020, a fall of 8.2% over the exports in 2019. A couple of decades ago, the exports from Mercosur were just US$ 89 billion. Brazil is the largest exporter from this bloc with a share of almost 75% in the exports from Mercosur. Further, top products exported from this region include oil seeds and oleaginous fruits (12.7%), Ores, slag, and ash (10.4%), mineral fuels and oils (10.3%), meat (7.9%), and cereals (6%). The intra-Mercosur trade stood at just 9.5% in 2020. It may be noted that the intra-Mercosur trade in the last two decades has not been impressive. The intra-Mercosur exports were at US$ 16.5 billion and reached as high as US$ 54.2 billion in 2011. However, the same has fallen in the recent years and was recorded at US$ 26.5 billion in 2020.

Mercosur and India signed a PTA in 2004. By this PTA, India and Mercosur agreed to give tariff concessions, ranging from 10% to 100% to the other side on 450 and 452 tariff lines respectively. The agreement became operational in 2009. India-Mercosur trade has grown impressively since the agreement came into effect. The trade between the two regions has increased from US$ 5.6 billion in 2009 to US$ 10.6 billion in 2020, registering an AAGR of 8.5%. EU and Mercosur also reached a political agreement for an ambitious, balanced, and comprehensive trade agreement in 2020.

[20] MERCOSUR in brief, Official website

3. ASSESSMENT OF INDIA'S MAJOR TRADE AGREEMENTS

Overview

Over the last two decades, trade has steered the expansion of global economy by enabling economies to reorient their production in accordance with their relative comparative advantages across specific sectors, items and processes. The role played by trade agreements in propelling the increase in cross-border trade flows by dismantling various tariff and non-tariff barriers has been quite notable. However, so far, India has had a mixed experience with the trade agreements and other agreements of wider economic cooperation. The impact of these agreements on the economy is largely contingent on a few critical factors that enable the benefits to flow through and disperse throughout the economy; for example, the regulatory environment, quality of institutions and ease of doing business across sectors.

With this background, this chapter seeks to analyze in detail, the impact of major trade agreements on India that it has been a signatory to.

1. ASEAN- India Free Trade Agreement (AIFTA)

The existing free trade agreement between India and the Association of Southeast Asian Nations (ASEAN) is split across three aspect - Trade in Goods; Trade in Services; and Investment. Initially, the ASEAN-India Trade in Goods Agreement was signed and entered into force in January 2010, wherein the ASEAN Member States and India mutually agreed to open their respective markets by progressively reducing and eliminating duties on 76.4% of the goods. This was followed by signing of the ASEAN-India Trade in Services Agreement and the ASEAN-India Investment Agreement in November

2014, which introduced provisions on transparency, domestic regulations, recognition, market access, national treatment and dispute settlement.

Even though the exclusion lists under AIFTA are subject to an annual tariff review with a view to improving market access, there are 489 tariff lines listed under the negative list, belonging to the sectors like agriculture, textile, machinery, automobile, chemicals, and plastics. Lastly, the Investment Agreement was brought into force with a view to safeguard investment and ensure fair and equitable treatment for investors, non-discriminatory treatment in expropriation or nationalization as well as fair compensation.

In the agreement, preferential imports form nearly 70% of the imports of India from ASEAN. India has extended zero, near-zero and low preferential tariffs in most of the products except coffee, tea, mate, etc., with 32.3% and oilseeds, etc., with 15.2% average weighted preferential tariffs. However, the MFN tariff is nearly double the preferential tariffs in both cases resulting in the high preference margins.

With respect to ASEAN's imports from India, preferential imports cover 48% of imports. The preference margin is less for many HS 2-digit codes and the value of preferential imports covered under different codes is also relatively less. The challenge for India here is that there might be some preferential margin benefit to India, such as in the case of cereals where preferential tariff is 3.8% and MFN tariff is 9.5%, the value of preferential imports is very low[21].

Trade Volumes and Intra-regional Trade

During 2010-19, AIFTA's merchandize exports to the world registered an AAGR of 4.3% to reach US$ 1.8 trillion, contributing to 9.6% of world exports in 2019, up from 8.4% in 2010. Amongst the prominent gainers were Vietnam, Lao PDR, and Cambodia, registering double-digit AAGR in their exports to both the AIFTA aggregation and the world.

[21] Relooking India's Tariff Policy Framework, India Exim Bank, March 2020

Table 3.1: Intra-AIFTA Trade at a Glance (US$ Billion)

Country	Exports to AIFTA			Exports to Rest of the World		
	2010	2019	AAGR	2010	2019	AAGR
Brunei Darussalam	8.9	7.2	0.6	8.8	7.2	0.6%
Cambodia	0.7	1.4	14.7%	5.5	14.8	12.0%
India	22.9	34.2	6.6%	220.4	323.3	5.3%
Indonesia	43.3	53.6	3.1%	157.7	167.4	1.4%
Lao PDR	1.2	3.6	17.6%	1.9	5.8	17.0%
Malaysia	57.0	76.6	3.9%	198.8	238.1	2.5%
Myanmar	5.2	4.3	(-) 1.3%	8.8	16.7	9.6%
Philippines	12.0	11.3	0.1%	51.4	70.3	3.7%
Singapore	121.2	123.4	1.0%	353.2	390.3	1.6%
Thailand	48.7	70.0	4.5%	195.3	245.3	2.8%
Vietnam	11.4	32.1	13.0%	57.0	243.7	18.2%

Source: Data accessed from ITC Trade Map, India Exim Bank Research

Composition of AIFTA's trade - both within member countries and with rest of the world, has changed significantly during 2010-19. A gradual decline in the share of mineral fuels[22] and machinery[23] in AIFTA's total exports to the world has been noted, while that of textiles[24], footwear[25], and optical instruments[26] increased, during the last ten years. However, electrical machinery and equipment[27] remained the top export item from the AIFTA aggregation, with its share in AIFTA's total exports increasing from 19.1% in 2010 to 23.7% in 2019.

It is to be noted that AIFTA's exports of electrical machinery and equipment accounted for 15.6% of the world exports of the same in 2019, up from 12.4% in 2010. Amongst member countries, Vietnam accounted for the

[22] HS 27: Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes

[23] HS 84: Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof

[24] HS 61: Articles of apparel and clothing accessories, knitted or crocheted; HS 62: Articles of apparel and clothing accessories, not knitted or crocheted

[25] HS 64: Footwear, gaiters and the like; parts of such articles

[26] HS 90: Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof

[27] HS 85: Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles

highest exports of electrical machinery and equipment in 2019, led by mobile phones[28] and integrated electronic circuits[29], exports of which increased by over 25 times 2010-19.

Impact on India's Foreign Trade

India has remained a net importer of merchandize with the AIFTA aggregation, with a constant widening of trade deficit during the last ten years, increasing from US$ 6.7 billion in 2010 to US$ 22.8 billion in 2019. The trade balance was primarily weighed down because of high imports of coal[30] (US$ 6.9 billion), crude palm oil[31] (US$ 3.5 billion), and petroleum oils[32] (US$ 2.4 billion), in 2019. As regards trading partners, the highest deficit was noted with Indonesia, arising mainly due to the imports of crude palm oil, followed by Singapore, Malaysia, Thailand, and Vietnam.

India's exports to the ASEAN aggregation primarily comprised of medium petroleum oils[33] (US$ 4.5 billion), frozen meat[34] (US$ 2 billion), light floating vessels[35] (US$ 1.8 billion), light oils[36] (US$ 1.6 billion) and aluminum[37] (US$ 1.4 billion).

The findings based on an ex-ante analysis of the AIFTA's impact in a full trade liberalization case, indicate that while the agreement may result in India's increased allocative efficiency, but the terms of trade effect is likely to remain negative and worsen continuously[38]. On the other hand, the analysis based

[28] HS 851712: Telephones for cellular networks "mobile telephones" or for other wireless networks

[29] HS 854321: Electronic integrated circuits as processors and controllers, whether or not combined with memories, converters, logic circuits, amplifiers, clock and timing circuits, or other circuits

[30] HS 270119: Coal, whether or not pulverized, non-agglomerated (excluding anthracite and bituminous coal)

[31] HS 151110: Crude palm oil

[32] HS 270900: Petroleum oils and oils obtained from bituminous minerals, crude

[33] HS 271019: Petroleum oils and oils obtained from bituminous minerals, crude

[34] HS 020230: Frozen, boneless meat of bovine animals

[35] HS 890590: Light-vessels, fire-floats, floating cranes and other vessels, the navigability of which is subsidiary to their main function (excluding dredgers, floating or submersible drilling or production platforms; fishing vessels and warships)

[36] HS 271012: Light oils and preparations, of petroleum or bituminous minerals which >= 90% by volume "incl. losses" distil at 210°C "ASTM D 86 method" (excluding containing biodiesel)

[37] HS 760110: Aluminum, not alloyed, unwrought

[38] Ahmed, 2010; and Sikdar and Nag 2011

on ex-post analysis, it has been concluded that post AIFTA, India's exports to ASEAN increased substantially, with the largest gains across Thailand, Cambodia, Vietnam, Malaysia, the Philippines and the Lao PDR.

Chart 3.1: India's Trade with the ASEAN Aggregation

Source: Data accessed from ITC Trade Map, India Exim Bank Research

The intra-ASEAN trade, however, remained largely unaffected after the agreement came into force[39]. Going forward, this highlights the need for constant evaluation of the AIFTA's impact on India's foreign trade. In 2019, India's top ten import items from ASEAN accounted for 78% of the total imports from the region. After the agreement came into effect in 2010, the cumulative imports of these items from the ASEAN member countries registered an AAGR of 13.3%, significantly higher than the AAGR of 4.1% recorded for India's imports of these items from rest of the world.

[39] Venkatesh and Bhattacharyya (2014)

Table 3.2: India's Top Ten Imports from ASEAN member countries vs Rest of the World

HS Code	Description	India's Imports (US$ Bn)				Share in India's Total Imports of the Item				AAGR in Imports (2010-19)		Likely Impact of FTA on Domestic Manufacturers
		2010		2019		2010		2019				
		From ASEAN	From ROW	From ASEAN	From ROW	From ASEAN	From ROW	From ASEAN	From ROW	From ASEAN	From ROW	
27	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	7.3	103.5	11.7	141.0	6.6%	93.4%	7.7%	92.3%	9.0%	7.3%	Moderate
85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles	3.0	22.6	9.0	41.9	11.7%	88.3%	17.7%	82.3%	14.0%	7.8%	Significant
84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	2.7	25.1	5.5	38.9	9.8%	90.2%	12.4%	87.6%	9.8%	5.6%	Significant
15	Animal or vegetable fats and oils and their cleavage products; prepared edible fats; animal or vegetable waxes	4.7	1.8	5.3	4.5	72.7%	27.3%	54.4%	45.6%	5.4%	12.8%	Insignificant
29	Organic chemicals	1.8	10.3	2.5	18.1	14.7%	85.3%	12.1%	87.9%	11.7%	7.0%	Insignificant
39	Plastics and articles thereof	1.0	6.3	2.4	12.2	14.0%	86.0%	16.4%	83.6%	15.1%	7.9%	Significant
89	Ships, boats and floating structures	0.8	2.8	2.0	2.6	21.9%	78.1%	43.4%	56.6%	34.3%	3.0%	Significant
72	Iron and steel	0.4	10.3	1.9	9.9	3.8%	96.2%	15.8%	84.2%	24.5%	1.0%	Moderate
74	Copper and articles thereof	0.2	1.5	1.6	3.6	10.8%	89.2%	30.4%	69.6%	33.8%	12.2%	Significant
90	Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof	0.4	4.9	1.3	8.2	8.2%	91.8%	14.0%	86.0%	14.5%	6.2%	Moderate
Top Ten Imports		**22.3**	**189.0**	**43.2**	**280.8**	**10.6%**	**89.4%**	**13.3%**	**86.7%**	**10.2%**	**6.1%**	**Significant**

Source: Data accessed from ITC Trade Map, India Exim Bank Research

Trade Intensity Index

The trade intensity index (TII) is used to determine whether the value of trade between two countries is greater or smaller than would be expected based on their importance in world trade. It is defined as the share of one country's exports going to a partner divided by the share of world exports going to the same partner.

Value of the index will be one for an expected bilateral trade flow. An index of more (less) than one indicates a bilateral trade flow that is larger (smaller) than expected, given the partner country's importance in world trade. It is calculated as:

$$T_{ij} = (x_{ij}/X_{it})/(x_{wj}/X_{wt})$$

Where, x_i: value of country i's exports to country j,

x_{wj}: value of world exports to country j,

X_{it}: country i's total exports and

X_{wt}: total world exports.

For an expected bilateral trade flow, share of one country's exports to its partner country or region should be at least equal to the share of world exports to the same partner country or region. In other cases, it is implied that the country fails to exploit the market in its partner country or region and there is scope for expansion of its exports trade in the partner country or region.

The TII for the top ten exports by India to the ASEAN aggregation, as well as the total exports in 2019, is considered to check if the level of trade flow between India and the ASEAN aggregation is equal to that of the expected.

Table 3.3: Trade Intensity Index – India and ASEAN (2019)

HS Code	Description	Exports (US$ Billion)	Share in India's total Exports to ASEAN	TII
27	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	6.5	19.0%	1.51
89	Ships, boats and floating structures	3.3	9.6%	26.92
84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	2.7	8.0%	1.58
02	Meat and edible meat offal	2.2	6.5%	12.87
29	Organic chemicals	2.0	5.8%	1.69
72	Iron and steel	1.9	5.6%	1.50
76	Aluminium and articles thereof	1.5	4.4%	3.55
87	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	1.5	4.3%	2.51
71	Natural or cultured pearls, precious or semi-precious stones, precious metals, metals clad with precious metal, and articles thereof; imitation jewellery; coin	1.4	4.0%	0.62
85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles	1.1	3.3%	0.63
Total Exports		**34.2**	**100%**	**1.40**

Source: Data accessed from ITC Trade Map, India Exim Bank Research

As can be seen, even though the TII for India's overall merchandize exports to the ASEAN aggregation is greater than one, indicating that the trade flows are larger than expected, amongst the top ten export items, the TII for items like Natural pearls and semi-precious stones and Electrical Machinery has been estimated at less than one, indicating the untapped export potential.

Investment

The total FDI inflows in the AIFTA aggregation was recorded at US$ 206.3 billion in 2019, significantly higher from US$ 140.4 billion in 2010, registering an AAGR of 4.9% during this time. Amongst the highest recipients of the FDI, in 2019, were Singapore (US$ 92.1 billion), India (US$ 50.5 billion), Indonesia (US$ 23.4 billion), and Vietnam (US$ 16.1 billion).

Chart 3.2: Inward FDI in AIFTA

Source: Data accessed from UNCTAD Stat, India Exim Bank Research

The FDI inflows into India from ASEAN during 2010 and 2019 were recorded at US$ 87.2 billion, approximately 37% of total FDI flow into India. About US$ 10 billion worth of FDI was sourced from Singapore alone[40]. Further, according to fDi markets, sectoral analysis shows that Singapore invested in India across the sectors such as real estate, coal, oil and gas, renewable energy, and finance. In this regard, it is important to take note of the fact that ever since the CECA between India and Singapore came into force, it has widely been used as a channel to reroute FDI inflows in India from other countries.

2. South Asian Free Trade Agreement (SAFTA)

The South Asian Free Trade Area (SAFTA) is the free trade arrangement of the SAARC countries: Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, and Sri Lanka. The agreement came into force in 2006, succeeding the SAPTA, leading to creation of a wider South Asian economic union.

[40] DPIIT

As per the agreement, the products from the "sensitive list" of each member country are considered a part of the agreement's "negative list". It is to be noted that the sensitive list is reviewed after every four years or earlier as may be decided by SAFTA Ministerial Council (SMC), with a view to reducing the number of items in the List. For India, the key items in the sensitive list for Non-Least Developed Contracting States (NLDCS) range from vegetables and man-made staple fibres to Footwear and Iron & Steel.

Around 89% of India's total imports from SAARC countries are preferential imports. India has extended zero or near zero preferential tariffs for most of the top items which also have high preference margins. These items include ships, boats, etc.; many textile items; iron & steel; salt, sulphur, etc.; electrical machinery, etc.; nuclear reactors, boilers, etc.; residues from food industry, etc.; plastics; beverages, etc.; copper & articles; inorganic chemicals; rubber & articles; and animal or vegetable fats. Mineral fuels also have zero duties but very small preference margins. Thus, on India's import side, a variety of items have zero or near zero preferential tariffs with high preference margins. However, preferential tariff items form only 23% of total imports of SAARC from India.

While India has zero or low preferential tariffs with high preference margins for imports from SAARC, other SAARC countries have applied relatively high preferential tariffs on imports from India with a low preference margin.

In essence, India's tariff related benefits due to SAFTA are relatively less compared to its SAARC trading partners and this is also a case of unequal exchange in terms of tariffs.

Trade Volumes and Intra-regional Trade

During 2010-19, SAFTA's merchandize exports registered an AAGR of 5.4% to reach US$ 407.8billion, contributing to 2.2% of world exports in 2019, up from 1.8% in 2010.

Table 3.4: Intra-SAFTA Trade at a Glance (US$ Billion)

Country	Exports to SAFTA			Exports to the World		
	2006	2010	2019	2006	2010	2019
India	6.2	11.1	22.6	121.2	220.4	323.3
Afghanistan	0.1	0.2	1.1	-	5.1	5.4
Bangladesh	0.3	0.4	1.2	11.7	19.2	46.6
Pakistan	1.7	2.8	2.4	16.9	21.4	23.8
Sri Lanka	0.6	0.6	1.0	6.8	8.3	11.3
Nepal	0.3	0.6	0.6	0.0	0.9	1.0
Bhutan	0.1	0.2	0.2	0.4	0.4	0.3
Maldives	0.0	0.0	0.0	0.1	0.1	0.3

Source: Data accessed from ITC Trade Map, India Exim Bank Research

Composition of exports by the SAFTA to the world has largely remained unchanged during the last ten years, with medium oils and preparation, diamonds, light oils and preparation, medicaments and articles of jewellery accounting for 21% of total exports in 2019, compared to 23% in 2010.

Impact on India's Foreign Trade

India has remained a net exporter of merchandise with respect to trade with the SAFTA aggregation. The exports increased at an impressive AAGR of 9.0% during 2010 and 2019 to reach US$ 18.5 billion in 2019, more than twice of the exports in 2010. Imports, on the other hand, were recorded at US$ 3.2 billion in 2019, growing at an AAGR of 7.4% during the same time.

India's trade surplus with the SAFTA aggregation largely arose on account of high exports of medium oils[41] (US$ 2.2 billion), electrical energy[42] (US$ 610.7

[41] HS 271019: Medium oils and preparations, of petroleum or bituminous minerals, not containing biodiesel

[42] HS 271600: Electrical energy

million), cotton[43] (US$ 602.3 million), motorcycles[44] (US$ 544.8 million) and semi-finished products of iron and steel[45] (US$ 408.6 million).

Chart 3.3: India's Trade with the SAFTA Aggregation

Source: Data accessed from ITC Trade Map, India Exim Bank Research

With regards trading partners, highest exports from India to the SAFTA aggregation in 2019 were recorded for Bangladesh (US$ 8.2 billion), followed by Nepal (US$ 7.1 billion) and Sri Lanka (US$ 4.2 billion). Interestingly, the composition of India's top ten imports from the SAFTA aggregation has changed drastically from 2006 to 2019. To assess the impact that entering into SAFTA has had on India's imports, the average annual growth in India's top ten import items from the SAFTA aggregation is compared with the same recorded with in imports from rest of the world.

In 2019, India's top ten import items from the SAFTA aggregation accounted for 61% of the total imports from the SAFTA. After the agreement came into effect in 2010, the cumulative imports of these items from the SAFTA member countries registered an AAGR of 13.3%, significantly higher the AAGR of 4.1% recorded for India's imports of these items from rest of the world.

In India's top import items from the SAFTA aggregation during 2019, the AAGR in India's imports from the SAFTA aggregation were higher than that of the imports from the rest of the world for nine items. Amongst the imports

[43] HS 520100: Cotton, neither carded nor combed

[44] HS 871120: Motorcycles, incl. mopeds, with reciprocating internal combustion piston engine of a cylinder capacity > 50 cm^3 but <= 250 cm^3

[45] HS 720719: Semi-finished products of iron or non-alloy steel containing, by weight, < 0,25% of carbon of circular cross-section, or of a cross-section other than square or rectangular

Table 3.5: India's Top Ten Imports from SAFTA member countries vs Rest of the World

HS Code	Description	India's Imports (US$ Bn)				Share in India's Total Imports of the Item				AAGR in Imports (2010-19)		Likely Impact of FTA on Domestic Manufacturers
		2010		2019		2010		2019				
		From SAFTA	From ROW	From SAFTA	From ROW	From SAFTA	From ROW	From SAFTA	From ROW	From SAFTA	From ROW	
15	Animal or vegetable fats and oils and their cleavage products; prepared edible fats; animal or vegetable waxes	0.0	6.4	0.4	9.5	0.1%	99.9%	3.6%	96.4%	442.7%	5.6%	Significant
08	Edible fruit and nuts; peel of citrus fruit or melons	0.2	1.1	0.3	2.7	13.9%	86.1%	11.2%	88.8%	18.9%	12.4%	Insignificant
62	Articles of apparel and clothing accessories, not knitted or crocheted	0.0	0.1	0.3	0.3	26.8%	73.2%	50.3%	49.7%	42.6%	19.0%	Significant
89	Ships, boats and floating structures	0.1	3.5	0.3	4.2	2.3%	97.7%	5.7%	94.3%	1467.6%	6.0%	Significant
09	Coffee, tea, maté and spices	0.1	0.2	0.2	0.5	36.6%	63.4%	26.0%	74.0%	15.2%	13.3%	Insignificant
53	Other vegetable textile fibres; paper yarn and woven fabrics of paper yarn	0.1	0.1	0.2	0.2	55.3%	44.7%	48.4%	51.6%	15.0%	14.3%	Insignificant
72	Iron and steel	0.2	10.5	0.2	11.6	2.2%	97.8%	1.9%	98.1%	5.1%	2.7%	Insignificant
13	Lac; gums, resins and other vegetable saps and extracts	0.0	0.1	0.1	0.1	36.8%	63.2%	47.0%	53.0%	21.9%	8.4%	Significant
23	Residues and waste from the food industries; prepared animal fodder	0.1	0.1	0.1	0.6	32.9%	67.1%	18.8%	81.2%	10.9%	18.7%	Insignificant
61	Articles of apparel and clothing accessories, knitted or crocheted	0.0	0.1	0.1	0.4	12.6%	87.4%	25.9%	74.1%	53.0%	22.5%	Insignificant
Top Ten Imports		**0.9**	**22.2**	**2.3**	**30.2**	**3.7%**	**96.3%**	**7.0%**	**93.0%**	**16.7%**	**4.1%**	**Significant**

Source: Data accessed from ITC Trade Map, India Exim Bank Research

that saw the highest increase were Ships & Boats and Edible Oils. The sharp increase in India's imports of Ships & Boats was mainly on account of surge in imports of cruise ships and excursion boats[46] from Sri Lanka, which grew at an AAGR of 21.3% during 2010-19. Imports of edible oils, on the other hand, largely comprised and were driven by the sudden surge in imports of palm oil from Nepal in 2018 and 2019.

Trade Intensity Index

The TII for the top ten exports by India to SAFTA, as well as the total exports in 2019, is considered to check if the level of trade flow between India and the SAFTA aggregation is equal to the expected level.

Table 3.6: Trade Intensity Index – India and SAFTA (2019)

HS Code	Description	Exports (US$ Million)	Share in India's total Exports to SAFTA	TII
27	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	3.7	16.9%	0.97
52	Cotton	2.0	9.3%	2.03
87	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	2.0	9.2%	16.21
84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	1.7	8.0%	3.14
72	Iron and steel	1.6	7.4%	3.18
85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles	0.8	3.7%	2.45
29	Organic chemicals	0.7	3.2%	0.67
39	Plastics and articles thereof	0.7	3.1%	2.90
30	Pharmaceutical products	0.6	2.7%	0.03
54	Man-made filaments; strip and the like of man-made textile materials	0.5	2.2%	0.82
Total Exports		**21.7**	**100%**	**2.06**

Source: Data accessed from ITC Trade Map, India Exim Bank Research

[46] HS 8901: Cruise ships, excursion boats, ferryboats, cargo ships, barges and similar vessels for the transport of persons or goods

The trade intensity index with reference to the bilateral trade between India and the SAFTA aggregation was estimated at 2.06, in 2019, indicating higher than expected level of trade flows. However, it is observed that exports of crucial items like pharmaceutical products, organic chemicals and mineral fuels were significantly subdued during the year.

Investment

India, being the largest economy in the SAFTA aggregation, had substantial outflow of capex to other member countries after the agreement came into effect. Between 2010 and 2019, a total envisaged capex of US$ 12.9 billion was done by India across SAFTA members, through 132 projects. At US$ 7.6 billion, Bangladesh was the highest recipient of the envisaged capex from India, during this time.

Table 3.7: India's Envisaged Capex in the SAFTA Member Countries (2010-19)

Country	Capex (US$ Million)	Projects
Bangladesh	7651.7	38
Sri Lanka	3096.9	65
Maldives	1364.7	7
Nepal	505.1	16
Bhutan	303.1	4
Afghanistan	15.2	1
Pakistan	8.2	1
Total	**12944.9**	**132**

Source: Data accessed from fDI Markets, India Exim Bank Research

With regard to recipient sectors for the envisaged capex outflow by India to the SAFTA aggregation during these years, the major sectors were coal, oil and gas, real estate, and financial services. Some of the major Indian companies investing in the SAFTA member countries were Reliance Power, NTPC Limited, and Tata Group.

3. India-South Korea CEPA

The India-Korea CEPA came into effect in January 2010, after a negotiation of over twelve rounds, to bolster the bilateral trade and investment. As per the agreement, South Korea abolished tariffs on 93% of Indian imports and India did the same on 75% of Korean imports.

The India-Korea CEPA classifies about 11,200 tariff lines of South Korea and 5,200 tariff lines of India broadly into six categories for the purpose of reduction or elimination of tariffs. The categories include those which eliminate tariffs completely on implementation of the agreement and those with annual tariff reduction of 20% or 12.5%, and other categories under which final tariffs will be reduced to 1-5% after 8 years, and an exclusion category which will enjoy no tariff reduction. Most of the agricultural products and textiles, being sensitive to both sides, are a part of the exclusion category[47].

The agreement classifies goods under the tariff lines in six categories and specifies the phased manner in which the duties will be reduced, eliminated or excluded for trade between India and South Korea. A wide range of goods falling under the category of vegetables, spices, edible oils[48], alcoholic beverages[49] and vehicles[50] fall in the 'EXC' category of the agreement and are exempted from the obligation of tariff reduction or elimination.

Further, in the imports of South Korea from India, 69% of imports have Preferential Tariffs. While many industries at HS 2-digit level have zero preferential duties, the preference margin is not that high compared to India's preference margin for imports from South Korea. This is because South

[47] Brief on India-Korea Economic and Commercial Relations (https://www.indembassyseoul.gov.in/page/india-rok-trade-and-economic-relations/)

[48] HS 15: Edible vegetables and certain roots and tubers

[49] HS 22: Beverages, spirits and vinegar

[50] HS 87: Vehicles other than railway or tramway rolling stock, and parts and accessories thereof

Korea's MFN tariffs are relatively lower. The major items with preferential tariffs of zero or low duties (other than mineral fuels which have zero or low tariffs in all countries) are aluminium, organic chemicals, iron & steel, nuclear reactors, etc., cotton, zinc, etc. and electrical machinery, etc.

It may be noted that the share of preferential imports to total imports of India from South Korea is around 75%. Almost all significant items at HS 2-digit level have near-zero or low preferential tariffs except Vehicles other than Railways, etc. (6.0%) and Inorganic Chemicals (2.8%). However, in both these cases, preference margin is high as India's MFN tariffs to world are high at 16% and 6.9% respectively. Major items with zero, near-zero and low duties include electrical machinery, etc.; iron & steel and other metals; nuclear reactors, etc.; optical, photographic items, etc.; plastics & articles; chemicals; rubber & articles; paper & paperboard; tanning or dyeing extracts; and some textiles items.

Overall, in India-South Korea preferential trade, while in terms of share of preferential items in imports of India/South Korea there is some sort of equal exchange, in terms of preference margins the imbalance is there mainly due to relatively lower MFN Tariffs of Korea[51].

Impact on India's Foreign Trade

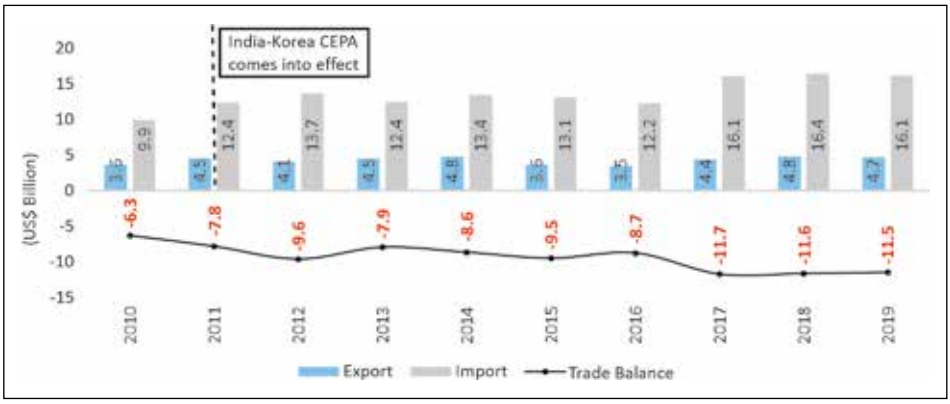
India's merchandize exports to South Korea were recorded at US$ 4.7 billion in 2019, up from US$ 3.6 billion in 2010, registering an AAGR of 4.0%. Imports, on the other hand were recorded at US$ 16.1 billion in 2019, growing at a higher AAGR of 6.3% during the same time. In 2019, while the exports primarily comprised of aluminum[52] (18%), mineral fuels (17%) and organic chemicals (10%), major import items were electrical machinery (18%), iron and steel (16%), and machinery (14%).

[51] Relooking India's Tariff Policy Framework, India Exim Bank, March 2020

[52] HS 76: Aluminum and articles thereof

Overall, India has remained a net importer of merchandize from South Korea during 2010 and 2019, with trade deficit amounting to US$ 11.4 billion in 2019, nearly double of US$ 6.3 billion recorded in 2010. It is to be noted that the deficit largely arose on the account of high imports of electrical machinery, iron and steel[53], machinery and plastics[54].

Chart 3.4: India's Trade with South Korea



Source: Data accessed from ITC Trade Map, India Exim Bank Research

It is important to note that an ambitious target of US$ 50 billion worth of bilateral trade by 2030 has been set between the two countries[55]. Going forward, it is crucial to acknowledge that even though India and South Korea pursued different growth trajectories after their independence, the two countries have come at par in terms of competence in sectors like engineering and manufacturing. Particularly with reference to foreign trade, South Korea has been an export-driven economy and the growing consumer base in India constitutes a large potential captive market for South Korea's consumer goods.

In 2019, India's top ten import items from South Korea accounted for about 84% of the total imports from South Korea. After the CEPA came into effect in 2011, the cumulative imports of these items from South Korea registered

[53] HS 72: Iron and Steel

[54] HS 39: Plastics and articles thereof

[55] Prime Minister's address at 'India-ROK Business Symposium', (https://pib.gov.in/PressReleseDetail.aspx?PRID=1565741)

Table 3.8: India's Top Ten Imports from South Korea vs Rest of the World

HS Code	Description	India's Imports (US$ Bn)				Share in India's Total Imports of the Item				AAGR in Imports (2010-19)		Likely Impact of FTA on Domestic Manufacturers
		2010		2019		2010		2019				
		From South Korea	From ROW	From South Korea	From ROW	From South Korea	From ROW	From South Korea	From ROW	From South Korea	From ROW	
85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles	1.7	23.8	2.9	47.9	6.7%	93.3%	5.8%	94.2%	10.4%	8.7%	Moderate
72	Iron and steel	1.3	1.8	2.5	2.5	42.7%	57.3%	50.0%	50.0%	9.9%	6.8%	Moderate
84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	1.6	26.2	2.3	42.2	5.8%	94.2%	5.2%	94.8%	11.9%	6.0%	Insignificant
39	Plastics and articles thereof	0.8	6.5	1.7	13	11.2%	88.8%	11.4%	88.6%	12.5%	8.3%	Moderate
29	Organic chemicals	0.7	11.4	1.2	19.3	5.8%	94.2%	5.9%	94.1%	17.8%	6.8%	Moderate
87	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	0.8	3.2	0.9	4.5	19.9%	80.1%	16.6%	83.4%	4.2%	4.9%	Insignificant
27	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	0.7	110.1	0.8	151.8	0.6%	99.4%	0.5%	99.5%	1.0%	7.3%	Insignificant
90	Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof	0.3	5.0	0.5	9.1	5.0%	95.0%	4.8%	95.2%	9.8%	7.0%	Insignificant
73	Articles of iron or steel	0.2	1.4	0.4	4.8	12.9%	87.1%	6.8%	93.2%	8.7%	16.2%	Insignificant
40	Rubber and articles thereof	0.3	10.4	0.3	11.5	3.1%	96.9%	2.4%	97.6%	8.9%	2.8%	Insignificant
Top Ten Imports		**8.4**	**199.8**	**13.4**	**306.6**	**4.1%**	**95.9%**	**4.2%**	**95.8%**	**8.3%**	**6.5%**	**Moderate**

Source: Data accessed from ITC Trade Map, India Exim Bank Research

an AAGR of 4.4%, as against the AAGR of 6.3% recorded for India's imports of these items from rest of the world.

In India's top import items from South Korea during 2019, the AAGR in India's imports from South Korea was higher than that of the imports from the rest of the world for seven items. The highest increase in India's imports from South Korea, during 2010-19, was noted for Organic Chemicals, which grew at an AAGR of 17.8%, as against the AAGR of 6.8% recorded for India's imports of the same from rest of the world.

Trade Intensity Index

The TII for the top ten exports by India to South Korea, as well as the total exports in 2019, is considered to check if the level of trade flow between India and South Korea is equal to the expected level.

Table 3.9: Trade Intensity Index – India and South Korea (2019)

HS Code	Description	Exports (US$ Million)	Share in India's total Exports to South Korea	TII
76	Aluminum and articles thereof	834.0	17.9%	8.19
27	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	793.1	17.0%	0.02
29	Organic chemicals	447.2	9.6%	0.02
72	Iron and steel	313.8	6.7%	0.52
84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	198.2	4.3%	0.01
52	Cotton	188.2	4.0%	4.35
85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles	175.1	3.8%	0.21
23	Residues and waste from the food industries; prepared animal fodder	156.4	3.4%	40.34
26	Ores, slag and ash	128.9	2.8%	27.83
78	Lead and articles thereof	123.0	2.6%	2.91
Total Exports		**46.5**	**100%**	**0.50**

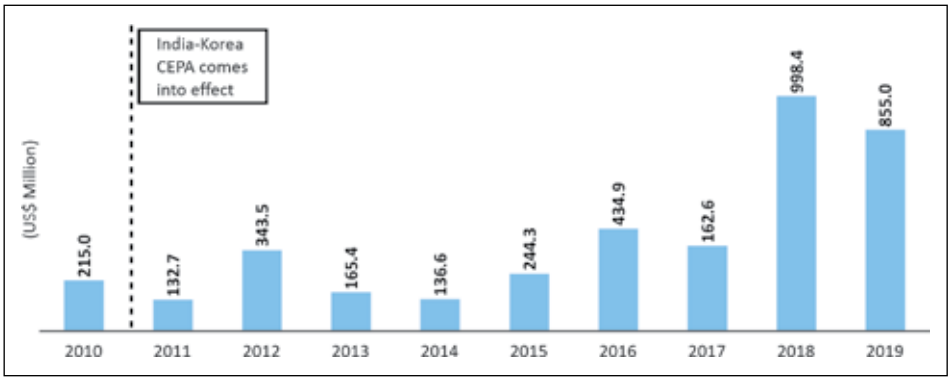
Source: Data accessed from ITC Trade Map, India Exim Bank Research

Considering India's top ten export items to South Korea in 2019, it is noted that while the TII for overall exports was less than one, the index exceeded the benchmark value for key items like aluminum, lead, ores, and cotton. Going forward, the CEPA, in this regard, should be used to unleash the underperforming exports of Iron and Steel, Electrical Machinery, Organic Chemicals and Mineral Fuels to South Korea.

Investment

The total FDI inflows received by India from South Korea during 2010 and 2019 were recorded at US$ 3.8 billion, growing at an AAGR of 39.2%. As can be seen, the FDI inflows from South Korea into India have shown an upward trend each year, after the CEPA came into effect.

Chart 3.5: FDI Inflows by South Korea in India



Source: Data accessed from DPIIT, India Exim Bank Research

Further, as per the fDi markets database, some of the key recipient sectors of the FDI inflows from South Korea in India were metals, automotive OEM, coal, oil & gas, automotive components, and chemicals. With regard to business activities, more than 75% of this FDI was received for manufacturing, followed by electricity (13%) and business services (3%).

4. India-Japan CEPA

The India-Japan CEPA came into effect in August 2011, with the objective to eliminate tariffs on 90% of Japanese exports to India, like auto parts and

electric appliances, and 97% of imports from India, including agricultural and fisheries products, until 2021. It is noted that Japan and India are the second and third largest economies in Asia, respectively, and the CEPA between the two was founded on the complementarities in trade between the two economies.

The agreement classifies goods under the tariff lines in seven categories and specifies the phased manner in which the duties will be reduced, eliminated or excluded for trade between India and Japan. It is to be noted that a wide range of fish and crustaceans has been categorized under the 'X' category, thereby excluding these goods from any commitment of reduction or elimination of customs duties.

Given that Japan is a leading importer of marine products, rearrangement of goods across the seven categories could be done to enable India's exports of marine products to meet Japan's import demand. A similar observation is made for goods falling under the broad heads of dairy and poultry products[56], vegetables[57], tea and coffee[58], a sizeable range of organic chemicals[59] and plastics[60], too.

Impact on India's Foreign Trade

India's total merchandise exports to Japan reached US$ 4.8 billion in 2019, registering an AAGR of 1.3% during 2010 and 2019. Imports, on the other hand were recorded at US$ 12.7 billion in 2019, growing at a higher AAGR of 5.8% during the same time. In 2019, while the exports primarily comprised of mineral fuels (12%) organic chemicals (12%), and marine products[61] (9%), major import items were machinery (26%), electrical machinery (11%) and iron and steel (9%).

[56] HS 04: Dairy produce; birds' eggs; natural honey; edible products of animal origin, not elsewhere specified or included

[57] HS 07: Edible vegetables and certain roots and tubers

[58] HS 09: Coffee, tea, maté and spices

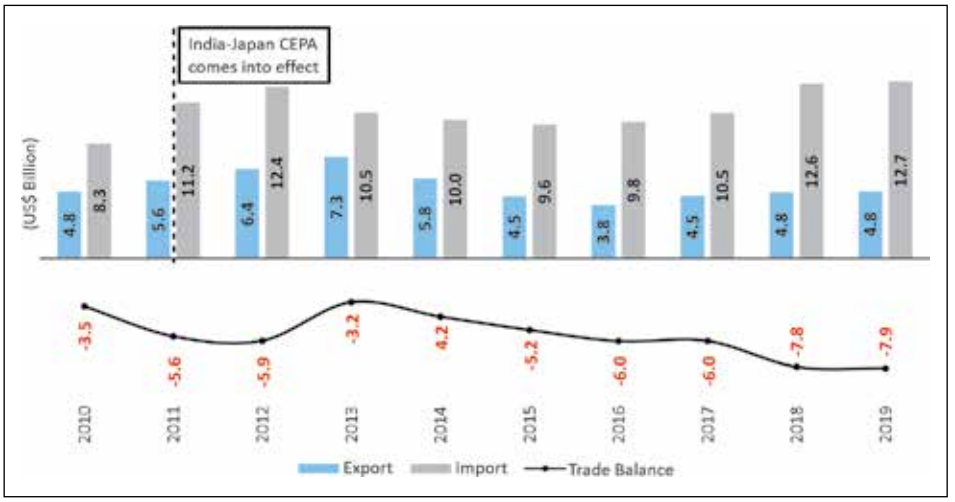
[59] HS 29: Organic chemicals

[60] HS 39: Plastics and articles thereof

[61] HS 03: Fish and crustaceans, mollusks and other aquatic invertebrates

Overall, India has been a net importer of merchandize from Japan during 2010 and 2019, with trade deficit amounting to US$ 7.9 billion in 2019, significantly higher than US$ 3.5 billion recorded in 2010. It is to be noted that the deficit largely arose on the account of high imports of electrical machinery, machinery & mechanical appliances, and iron and steel.

Chart 3.6: India's Trade with Japan



Source: Data accessed from ITC Trade Map, India Exim Bank Research

After the India-Japan CEPA came into effect, while India's imports of plastics, iron & steel and copper[62] grew substantially, the imports of vehicles[63] declined from US$ 513.8 million in 2010 to US$ 453.9 million in 2019. It is to be noted that in order to meet the growing demand for automobile in India, the highest FDI inflows by Japan during 2010 and 2019 were done in the auto sector only. Amongst the leading investing companies in the sector were Suzuki Maruti India, Toyota Kirloskar Motor, Renault-Nissan Motor and Honda Motorcycle and Scooter India Pvt Ltd. Overall, during these years, India's total merchandize import from Japan grew at an AAGR of 5.8% against the 1.3% average increase in merchandize export.

[62] HS 74: Copper and articles thereof

[63] HS 87: Vehicles other than railway or tramway rolling stock, and parts and accessories thereof

In the India-Japan preferential trade, while the preference margin is high in the case of most of the items on India's import side, on the Japanese side, the preference margin is relatively less as already India enjoys low or zero MFN tariffs in Japan. But in some important items of export interest to India like leather and footwear, organic chemicals and fish & related items, India has benefitted. Thus India-Japan CEPA is relatively a fair exchange, in terms of tariffs[64].

In 2019, India's top ten import items from Japan accounted for around 80% of the total imports from Japan. During 2010-19, the cumulative imports of these items from Japan registered an AAGR of 7.4%, as against the AAGR of 6.5% recorded for India's imports of these items from rest of the world.

In India's top import items from Japan during 2019, the AAGR in India's imports from Japan was higher than that of the imports from the rest of the world (ROW) for eight items. The sharpest increase in India's imports from Japan, during 2010-19, was noted for copper, which grew at an AAGR of 58.4%, as against the AAGR of 13.3% recorded for India's imports of the same from rest of the world. India's imports of copper from Japan during this time primarily comprised of refined copper in the form of cathodes[65] and wires of refined copper[66].

Trade Intensity Index

In order to identify the sectors underperforming on the export front, the TII for the top ten exports by India to Japan, as well as the total exports in 2019, is taken into account to check if the level of trade flow between India and Japan is equal to the expected.

[64] Relooking India's Tariff Policy Framework, India Exim Bank, March 2020

[65] HS 740311: Copper, refined, in the form of cathodes and sections of cathodes

[66] HS 740811: Wire of refined copper, with a maximum cross-sectional dimension of > 6 mm

Table 3.10: India's Top Ten Imports from Japan vs Rest of the World

HS Code	Description	India's Imports (US$ Bn)				Share in India's Total Imports of the Item				AAGR in Imports (2010-19)		Likely Impact on Domestic Manufacturers
		2010		2019		2010		2019				
		From Japan	From ROW	From Japan	From ROW	From Japan	From ROW	From Japan	From ROW	From Japan	From ROW	
84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	2.5	25.2	3.3	41.2	9.1%	90.9%	7.4%	92.6%	8.8%	6.2%	Insignificant
85	Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles	1.0	24.5	1.4	49.4	4.1%	95.9%	2.8%	97.2%	3.0%	8.7%	Insignificant
72	Iron and steel	1.0	9.7	1.2	10.6	9.2%	90.8%	9.8%	90.2%	8.0%	2.7%	Insignificant
39	Plastics and articles thereof	0.3	7.1	0.9	13.7	3.6%	96.4%	6.5%	93.5%	16.9%	8.0%	Moderate
74	Copper and articles thereof	0.0	1.6	0.8	4.4	1.7%	98.3%	15.0%	85.0%	58.4%	13.3%	Significant
29	Organic chemicals	0.4	11.7	0.7	19.8	3.4%	96.6%	3.6%	96.4%	13.7%	6.8%	Moderate
90	Optical, photographic, cinematographic, measuring, checking, precision, medical or surgical instruments and apparatus; parts and accessories thereof	0.4	4.8	0.7	8.8	8.4%	91.6%	7.6%	92.4%	9.0%	7.1%	Insignificant
87	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	0.5	3.4	0.5	4.9	13.0%	87.0%	8.4%	91.6%	-2.2%	4.9%	Insignificant
73	Articles of iron or steel	0.3	2.8	0.4	4.6	9.3%	90.7%	7.4%	92.6%	7.9%	7.4%	Insignificant
27	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	0.1	110.7	0.3	152.4	0.1%	99.9%	0.2%	99.8%	24.1%	7.2%	Insignificant
Top Ten Imports		**6.6**	**201.6**	**10.2**	**309.9**	**3.2%**	**96.8%**	**3.2%**	**96.8%**	**7.4%**	**6.5%**	**Insignificant**

Source: Data accessed from ITC Trade Map, India Exim Bank Research

Table 3.11: Trade Intensity Index – India and Japan (2019)

HS Code	Description	Exports (US$ Million)	Share in India's total Exports to Japan	TII
27	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	579.1	12.0%	1.92
29	Organic Chemicals	572.0	11.9%	0.73
03	Fish and crustaceans, molluscs and other aquatic invertebrates	419.0	8.7%	5.37
71	Natural or cultured pearls, precious or semi-precious stones, precious metals, metals clad with precious metal, and articles thereof; imitation jewelry; coin	415.6	8.6%	0.62
84	Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof	303.0	6.3%	0.23
87	Vehicles other than railway or tramway rolling stock, and parts and accessories thereof	235.6	4.9%	0.14
26	Ores, slag and ash	209.5	4.3%	92.19
72	Iron and steel	209.5	4.3%	0.30
62	Articles of apparel and clothing accessories, not knitted or crocheted	190.9	4.0%	0.02
76	Aluminum and articles thereof	150.7	3.1%	2.37
Total Exports		**4,815.6**	**100%**	**0.40**

Source: Data accessed from ITC Trade Map, India Exim Bank Research

It is noted that the TII for overall merchandize exports as well as the top ten export items, except ores, aluminium, marine products, and mineral fuels, was recorded below the benchmark value, in 2019, indicating lower than expected exports. Sectors like iron and steel, apparel, machinery and organic chemicals should, therefore, be made the focal points to boost India's exports to Japan.

Further, as has been previously noted, the CEPA between India and Japan has primarily been founded on the grounds of complementarity of the two economies. In this regard, it is important to assess the level of trade

complementarity, particularly with reference to organic chemicals and pharmaceutical products. In order to do so, the Trade Complementarity Index (TCI) is used to check how well the structures of India and Japan's foreign trade match, with reference to the aforementioned sectors.

The TCI between countries 'k' and 'j' is defined as:

$$TCIij = 100\ (1 - sum\ (|m_{ik} - x_{ij}| / 2))$$

Where x_{ij} is the share of good 'i' in global exports of country j and m_{ik} is the share of good 'i' in all imports of country 'k'. The index is zero when no goods are exported by one country or imported by the other and 100 when the export and import shares exactly match.

With reference to bilateral trade between India and Japan, the TCI is estimated for organic chemicals and pharmaceutical products. To draw insights on the impact of CEPA on the trade complementarity between the two economies for the select items, the TCI observed for 2019 is compared with that observed in 2010.

Table 3.12: Trade Complementarity Index – India and Japan (2010 vs 2019)

Pharmaceutical Products (HS 30)			
	Share of HS 30 in India's total exports	**Share of HS 30 in Japan's Total Imports**	**TCI**
2010	2.7%	2.3%	99.8
2019	5.0%	3.8%	99.4
Organic Chemicals (HS 29)			
	Share of HS 29 in Japan's total exports	**Share of HS 29 in India's Total Imports**	**TCI**
2010	2.8%	3.5%	99.7
2019	2.5%	4.3%	99.1

Source: Data accessed from ITC Trade Map, India Exim Bank Research

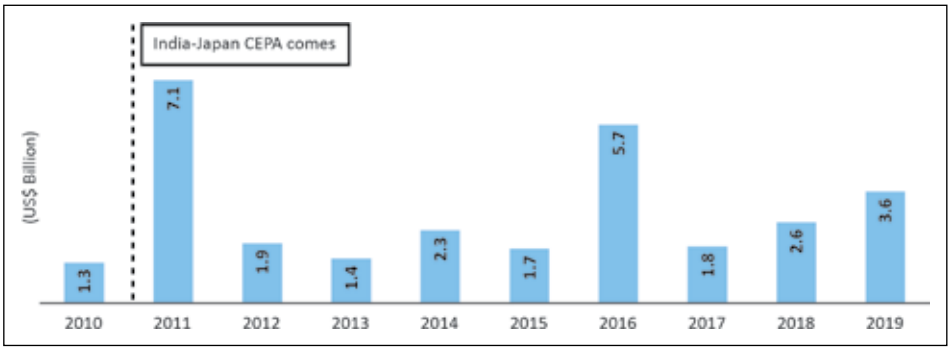
It is noted that even though the TCI for both the items remained high and close to the highest possible value of the index, a marginal decline in the same is noted when compared to the index value observed in 2010. The

value of the TCI for trade in organic chemicals and pharmaceutical products, however, indicates that both India and Japan would stand to gain from increased trade in the future as well.

Investment

According to the Department for Promotion of Industry and Internal Trade, between 2010 and 2019, Japan's cumulative FDI in India amounted to US$ 29.5 billion, making it the third largest source of the FDI in India after Mauritius and Singapore. Further, as per the fDi markets database, some of the major sectors for envisaged capex from Japan, in India, were automotive OEM, metals, automotive components, real estate, and industrial equipment.

Chart 3.7: FDI Inflows from Japan in India



Source: Data accessed from DPIIT, India Exim Bank Research

It is important to note that a sizeable fraction of the total FDI inflows from Japan were made to support the key sectors like automobile and Infrastructure. Amongst the leading Japanese companies to invest in India during this time were Suzuki Maruti India, Sumitomo Group, and Honda Motorcycle & Scooter India Pvt Ltd.

Further, over US$ 25 billion worth of capex was envisaged from Japan in India's manufacturing sector through 275 projects during 2010 and 2019, followed by construction (US$ 3.3 billion) and research & development (US$ 1.9 billion).

India-Australia ECTA

Australia and India launched negotiations for a Comprehensive Economic Cooperation Agreement (CECA) in May 2011. Further, as part of the Comprehensive Strategic Partnership (CSP) held in June 2020 between India and Australia, both the countries decided to re-engage on a bilateral Economic Cooperation and Trade Agreement (ECTA) while suitably considering earlier bilateral discussions, where a mutually agreed way forward can be found. The CSP is based on mutual understanding, trust, common interests and the shared values of democracy and rule of law. It reflects India and Australia's commitment to practical global cooperation to address major challenges like COVID-19. It is in line with India's increasing engagement in the Indo-Pacific region through her Indo-Pacific vision and Australia's Indo-Pacific approach and its Pacific Step-Up for the South Pacific. Under the CSP, both countries decided to work together in the areas of mutual cooperation across twelve[67] broad domains.

Finally, in April 2022, the Government of India and Australia signed the India-Australia ECTA. It is to be noted that the recent years have seen remarkable growth in the trading relationship between India and Australia, fuelled by the many complementarities between the two economies. Bilateral trade in goods and services has grown in value from US$ 13.6 billion in 2007 to US$ 30.4 billion in 2018[68]. During November 2018, the Australian Government formally endorsed the independent India Economic Strategy[69] and its ambitious vision for bilateral trade and investment.

[67] Enhancing Science, Technology and Research Collaboration; Maritime Cooperation for an Open and Inclusive Indo-Pacific; Defense Cooperation; Regional and Multilateral Cooperation; Terrorism; Economic cooperation: A More Prosperous Shared Future; Innovation & Entrepreneurship; Agriculture Cooperation and Water Resources Management; Education, Culture, Tourism and People-to-People ties; Support in UN and international bodies; Public Administration and Governance

[68] Department of Foreign Affairs and Trade, Australian Government

[69] The India Economic Strategy is an ambitious plan to transform Australia's economic partnership with India out to 2035.

Australia's India Economic Strategy aims to make India the third largest destination in Asia for Australian outward investment, and to bring India into the inner circle of Australia's strategic partnerships, and with people to people ties as close as any in Asia, by 2035.

Trade Scenario

India was a net importer of merchandize to Australia in 2019, with a trade deficit amounting to US$ 7.6 billion, as against the trade deficit of US$ 10.4 billion in 2010. The exports from India to Australia in 2019 primarily comprised of mineral fuels (12%), precious metals (9%), pharmaceutical products (8%), railway or tramway locomotives, rolling stock and parts thereof (6%) and machinery (5%). In 2019, Australia ranked 30th amongst destination countries of India's total merchandize exports. For Australia's exports, meanwhile, India was the sixth largest destination.

On the other hand, major imports from Australia were relatively more concentrated and comprised of mineral fuels (78%), precious metals (5%), inorganic chemicals (4%); ores, slag and ash (2%); and aluminium and articles thereof (1%). It may be noted that while the composition of India's top merchandize exports to Australia has largely remained the same during 2010 and 2019, India's exports of vehicles to Australia has reduced significantly from U$ 195.0 million in 2010 to US$ 73.1 million in 2019.

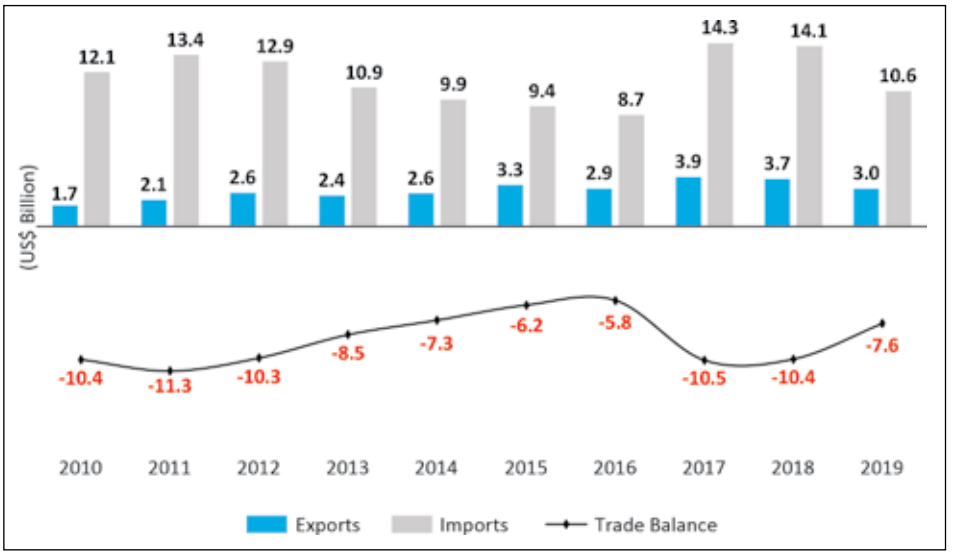
Further, it is to be noted that during 2010 and 2019, the AAGR in India's exports to Australia stood at 8.4%, significantly higher than the 0.9% AAGR in imports. At the HS 6-digit level, the merchandize imports primarily comprised of coal[70] (US$ 7.5 billion); liquified natural gas[71] (US$ 458.7 million); and gold[72] (US$ 417.8 million).

[70] HS 270119: Coal, whether pulverized, non-agglomerated (excluding anthracite and bituminous coal)

[71] HS 271111: Natural gas, liquefied

[72] HS 710812: Gold, incl. gold plated with platinum, unwrought, for non-monetary purposes (excluding gold in powder form)

Figure 3.8: India's Foreign Trade with Australia



Source: Data accessed from ITC Trade Map, India Exim Bank Research

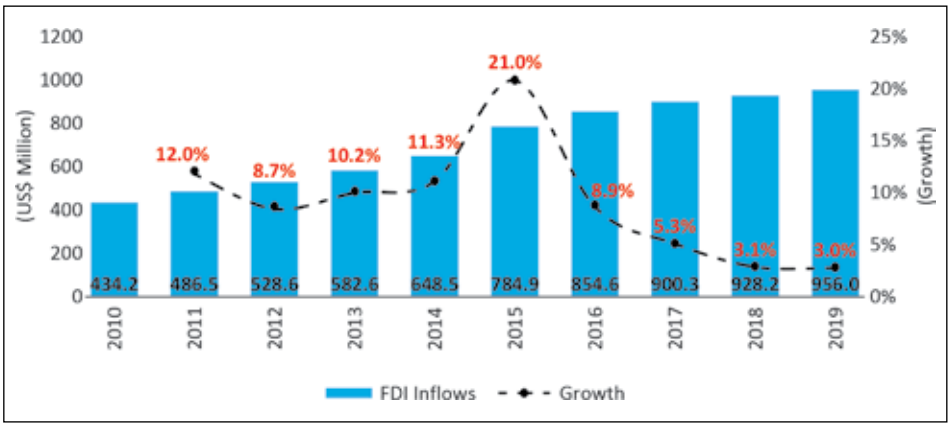
Amongst the items contributing the most to the trade deficit in 2019 were mineral fuels (US$ 7.8 billion), inorganic chemicals[73] (US$ 379.6 million) and precious metals (US$ 260.9 million). During 2010 and 2019, while the trade deficit arising from trade in mineral fuels has widened from US$ 5.1 billion to US$ 7.8 billion, the same for precious metals has come down from US$ 3.8 billion to US$ 260.9 million. Amongst the key items wherein India had a trade surplus with Australia during 2019 were pharmaceutical products (US$ 239.8 million); railway or tramway locomotives (US$ 164.4 million); and articles of iron and steel (US$ 131.0 million).

Investment Scenario

The cumulative FDI received from Australia in India during April 2000 and March 2020 was recorded at US$ 959.7 million, accounting for just 0.2% of the total FDI inflows in the same period.

[73] HS 28: Inorganic chemicals; organic or inorganic compounds of precious metals, of rare-earth metals, of radioactive elements or of isotopes

Figure 3.9: FDI Inflows in India from Australia



Source: Data accessed from DPIIT; India Exim Bank Research

Further, as per fDi markets, across sectors, the highest recipient of foreign capex inflows from Australia in India were real estate (34.3%); financial services (15.6%); and coal, oil and gas (9.3%). Amongst Australia's leading investing companies in India during these years were LOGOS India Logistics Venture[74] (US$ 1.3 billion); Oilex[75] (US$ 324 million); and Heliostat SA[76] (US$ 289 million).

On the other hand, during the same years, India's foreign envisaged capex in Australia was recorded at US$ 7.6 billion through 82 projects, resulting in an average capex of US$ 92.9 million per project. Sector-wise, the key recipients of this capex in Australia were Renewable Energy (US$ 5.9 billion); Software and IT Services (US$ 586 million); and Coal, oil and gas (US$ 468 million). Amongst the leading investing companies were Suzlon Energy (US$ 3 billion); Senvion REPower Systems (US$ 1.5 billion); and Adani Green Energy

[74] LOGOS India Logistics Venture is a joint venture between Singapore-based Assetz Property Group and Australia-based Macquarie Group. The company is focused on developing and owning high-quality, modern logistics facilities in cities across India

[75] Oilex is engaged in the exploration, appraisal, development, production, and sale of oil and gas. The company holds interests in eight licenses/permits covering an area of approximately 26,243 sq km in Australia, India, and Indonesia. Its flagship property includes the Cambay project covering 161 sq km located in Gujarat

[76] Heliostat SA is a provider of heliostat mirror systems. It uses concentrated solar power, concentrated solar photovoltaic and Heliostat Sun Tracking technology developed in partnership with the Commonwealth Scientific and Industrial Research Organization

(US$ 929 million). Interestingly, around 80% of India's envisaged capex during in Australia during these years was done in the renewable energy sector.

Select Features of India-Australia ECTA

The India-Australia ECTA is the first trade agreement of India with a developed country in over a decade. The agreement covers diverse areas such as trade in goods, rules of origin, trade in services, technical barriers to trade (TBT), sanitary and phytosanitary (SPS) measures, dispute settlement, movement of natural persons, telecom, customs procedures, pharmaceutical products, and cooperation in other areas. Various subject specific side letters covering various aspects of bilateral economic cooperation such as wine, organic goods, post-study work visas, taxation, work, and holiday visas etc. were also concluded as part of the Agreement.

It is important to mention here that the concern of Indian IT firms has also been addressed in this agreement with respect to the double taxation. Australia, as a part of this agreement, has agreed to amend local taxation laws to stop the taxation of offshore income of Indian firms providing technical services to Australia.

The agreement is going to provide zero-duty access to 96% of India's exports to Australia which include key sectors such as engineering goods, textiles, gems and jewellery, apparels, and leather. India is also expected to enjoy greater market access for its products while easing of regulatory processes for pharmaceutical products while opening a US$ 12 billion market in Australia. India has also been conscious about its agricultural sector and has kept certain items away from the list. One significant for the services sector has been Australia granting a post-study visa for 4 years.

With respect to Australia's shipments to India, the agreement is expected to provide zero-duty access to about 85% of Australia's exports. This includes industries such as coal, sheep meat and wool, and lower duty access on Australian wines, almonds, lentils etc. The zero-duty access for Indian goods will expand to 100% over five years under the agreement.

With this agreement, the trade in goods and services between India and Australia is expected to reach US$ 45-50 billion over 5 years, up from the current US$ 27 billion. This is expected to generate over 1 million jobs in India. It may also be noted that India has excluded some Australian products from the agreement which include products such as wheat, dairy products, rice, chickpeas, beef, sugar, iron ore, among others. However, Australia will hugely benefit in the coal industry which accounts for 74% of Australia's exports to India and attracts a duty of 2.5% but will now get zero-duty access to Indian market. India and Australia are also looking at the possibility of providing select access to each other's Government procurement market, on similar lines of India-UAE CEPA.

Conclusion

Overall, with reference to the major trade agreements India has been a part of, it is noted that while there has been a positive impact arising from entering into agreements like the SAFTA (though with unequal exchange in terms of tariff benefits), the gains have not been uniform across other trade agreements. It is observed that the CEPA with both South Korea and Japan, so far, has not resulted in significant increase in trade of focus sectors like iron and steel, aluminum and marine products. Going forward, it will be crucial to closely monitor the impact of trade agreements on the associated key sectors and items.

4. INDIA AND THE RCEP

After eight rounds of negotiations that started in 2012, the Regional Comprehensive Economic Partnership (RCEP) concluded in November 2020, with member countries representing about one-third of the global economy and forming the world's largest trading bloc. The negotiations concerning RCEP included trade in goods, services, and investment; intellectual property rights; and special and differential treatment to less developed ASEAN member states, among others.

At a macro-level, the agreement sought to simplify the customs procedure and rules of origin[67] laws among countries — implying reduced potential regulatory frictions for firms and countries for regional supply chains.

For instance, previously, a product made in Vietnam that contained Chinese parts might have faced higher tariffs elsewhere in the ASEAN free trade zone. Inclusion of commonly accepted set of rules of origin among the RCEP member countries will facilitate the easier movement of goods across the region and encourage these countries to look within the region for suppliers.

While India had been a part of negotiations for almost nine years, it withdrew in November 2019, stating that inadequate safeguards and lowering of customs duties will adversely impact its manufacturing, agriculture, and dairy sectors.

[67] Rules of Origin are the criteria needed to determine the national source of a product. They are used to implement measures and instruments of commercial policy such as anti-dumping duties and safeguard measures.

It may, however, be noted that had India signed the agreement, it would have become a part of the world's largest trading bloc and gained access to a vast market that accounts for around 25% of the world GDP, 30% of the world trade, 26% of the FDI flows, and 45% of the world's population.

Additionally, withdrawal from the RCEP is also expected to have an impact on India's global value chain participation, especially for hi-tech goods. Overall, with India out of the agreement, China is likely to be the trade leader, among member nations. This Chapter seeks to identify the key reasons for India's withdrawal from the RCEP and its impact in medium term.

Trade and Investment Flows in the RCEP

Merchandize Trade

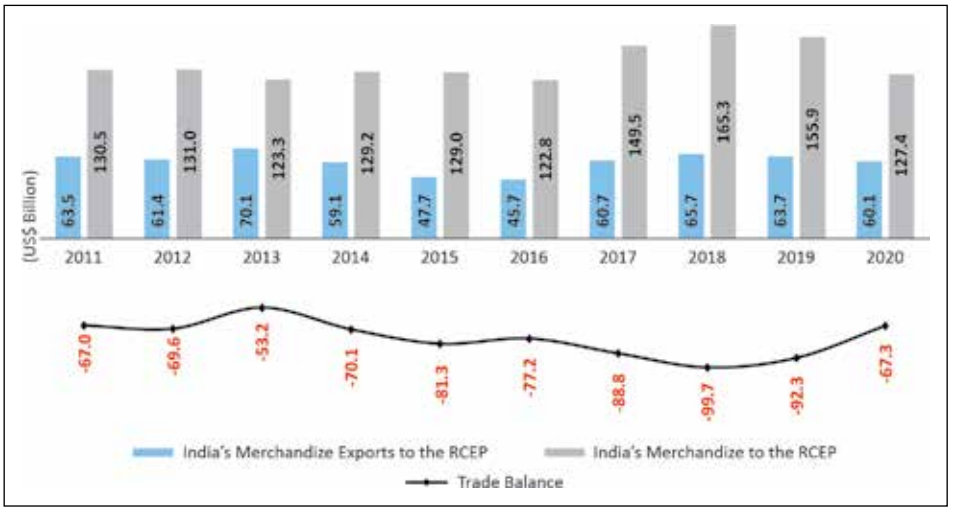
India has been a net importer of merchandize from the RCEP aggregation during 2011-20, with merchandize imports growing at an AAGR of 0.3%, against the AAGR of 0.5% in merchandize exports. India's key import items from the RCEP, in 2019, included electrical machinery[68] (20%), mineral fuels[69] (15%), machinery[70] (15%), organic chemicals[71] (7%) and plastics[72] (4%).

Item-wise, during 2019, India had the highest trade surplus in fish and crustaceans[73] (US$ 2.4 billion), meat and edible meat offal[74] (US$ 2.2 billion), ores, slag and ash[75] (US$ 1.5 billion), pharmaceutical products[76] (US$ 1.4 billion) and cotton[77] (US$ 1.4 billion). It may be noted that the RCEP

[68] HS 85: Electrical machinery and equipment and parts thereof; sound recorders and reproducers, television image and sound recorders and reproducers, and parts and accessories of such articles
[69] HS 27: Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes
[70] HS 84: Machinery, mechanical appliances, nuclear reactors, boilers; parts thereof
[71] HS 29: Organic chemicals
[72] HS 39: Plastics and articles thereof
[73] HS 03: Fish and crustaceans, molluscs and other aquatic invertebrates
[74] HS 02: Meat and edible meat offal
[75] HS 26: Ores, slag and ash
[76] HS 30: Pharmaceutical products
[77] HS 52: Cotton

aggregation accounted for about 32.6% of India's total merchandize imports and 19.7% of total merchandize exports during 2019.

Chart 4.1: India's Merchandize Trade with the RCEP



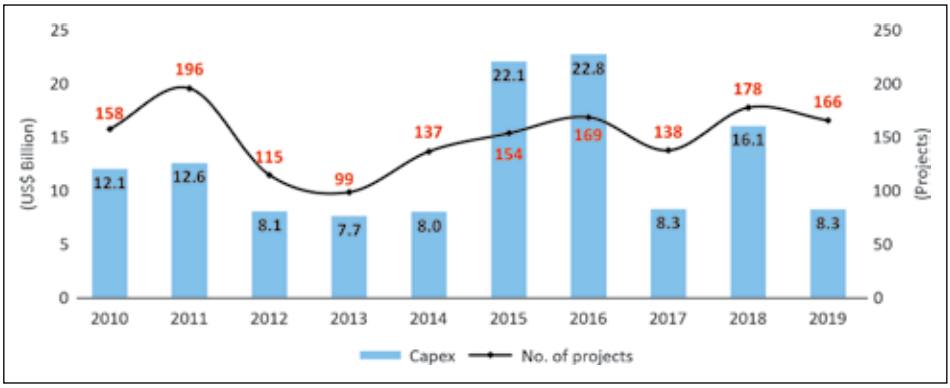
Source: Data accessed from ITC Trade Map, India Exim Bank Research

With regards trading partners from the RCEP aggregation, during 2019, India's largest merchandize import source was China (46%), followed by Singapore (10%), Indonesia (9%), Japan (8%), and Malaysia (6%). The top export destinations, on the other hand were China (32%), followed by Singapore (14%), Malaysia (10%), Vietnam (7%), and Indonesia (7%).

Investment

According to fDi markets database of Financial Times, during 2010-19, the total envisaged foreign capex inflow in India from the RCEP aggregation was recorded at US$ 126 billion, through 1510 projects, resulting in an average capex of US$ 83.5 million per project. Amongst the key recipients of the envisaged foreign capex during this time were infrastructure (US$ 20 billion), metals (US$ 15.7 billion) and automotive OEM (US$ 14.4 billion). The top investing companies were POSCO (US$ 8.2 billion), China Fortune Land Development (US$ 4.9 billion), and Ascendas-Singbridge (US$ 4.4 billion).

Chart 4.2: RCEP's Envisaged Foreign Capex in India



Source: Data accessed from fDi Markets Database, India Exim Bank Research

India's Possible Concerns in Joining the RCEP

Diverging views on Rules of Origin and Unfavorable Balance of Trade

It may be noted that India is a co-signatory to trade agreements with all the RCEP member countries, except China. Further, trade data during the last ten years indicates that India's deficit with China is higher than that of the other RCEP member countries put together. Signing the RCEP, therefore, could have opened a new window for China to flood the Indian markets with its manufactured products, thereby posing a threat to India's domestic manufacturing industry.

In this regard, India had proposed the introduction of more stringent Rules of Origin (ROO) norms in the RCEP framework, primarily to avert the threat of Chinese goods entering domestic markets routed through other RCEP member countries.

Box 4.1: Customs Rules, 2020

India in the recent years has been facing some challenges with respect to the 'rules of origin' clause, with its FTA partners. For instance, in 2017, India had put gold imports from South Korea in restricted category with the reasoning that South Korea does not produce gold, and that the country is having FTA with India, which is being used towards circumventing the

import duty. Further, India also had issues with respect to the pepper imports from Sri Lanka with which India has PTA, which is also being used by other economies for exports into India. As a result, the Government of India in 2020 notified the Customs (Administration of Rules of Origin under Trade Agreements) Rules, 2020 (CAROTAR, 2020). The aim of these rules is to supplement the existing operational certification procedures. Under the new rules, a basic level of due diligence will have to be done on the part of the importer. For this purpose, the importer is required to possess sufficient origin related information, including the regional value content. The first point of query into origin of goods, in case of doubt, will now be the importer. Earlier, merely a country of origin certificate, issued by a notified agency in the country of export was sufficient to avail the benefits of FTAs, which is not the case anymore.

According to the new rules, to claim preferential rate of duty under a trade agreement, the importer or his agent, at the time of filing bill of entry, will have to make a declaration in the bill that the imported products qualify as originating goods for preferential rate of duty under that agreement; and produce certificate of origin.

The new rules are expected to correctly ascertain the country of origin for a particular product and can assist the custom officers in clearing the product smoothly.

As a case in point, the recently signed FTA between India and the United Arab Emirates (UAE) has mandated stringent rules of origin conditions, with 40% value addition required on exporting items to avoid routing of products manufactured in third countries to India via UAE.

Potential Threat to Domestic Industry

Dairy Sector

The dairy farming in the country has grown significantly over the last few decades and there are measures in place to increase the output from 180 million tons at present to 330 million tons by 2033. Until the dairy sector in India reaches the stage to be able to compete with giant players like

New Zealand, it was felt necessary to safeguard the interest of dairy farmers and not be a signatory to any pact that prescribes duty-free import of dairy products. Currently, there is an import duty of 15% up to 10,000 tons of dairy produce and 60% for any import above that. This protection, however, would have ceased, had India signed the RCEP.

It may be noted that India's past experiences of entering into FTAs have had a substantial impact on the agriculture sector.

For instance, the edible oil sector was the most adversely impacted sector by the ASEAN-India FTA. After the FTA came into force, India transitioned from being self-sufficient in edible oils to importing around 55% of the demand. In Kerala - the largest coconut producing state, coconut production halved to 300 crore nuts in 2016-17 from 600 crore nut in 1999-2000[78]. Further, Indian markets were also flooded with black pepper imports from Vietnam, resulting in significant decline in prices.

Data localization, e-commerce and MSMEs

Agreeing to RCEP's e-commerce rules would have restricted India's flexibility to fine-tune its policy space. In particular, the RCEP draft is opposed to data localization[79], while India fears the monopoly power of digital giants. This would have been particularly worrisome in a setup with a huge presence of unorganized small and micro manufacturing and trading sector not ready for binding with e-commerce rules.

Additionally, withdrawal from RCEP was expected to give Indian manufacturers the time to revive growth amidst the ongoing decline of manufacturing output without the fear of foreign competition. The growth and expansion of global

[78] Commission for Agricultural Costs and Prices (CACP), Ministry of Agriculture and Farmers Welfare, Government of India

[79] Data localization refers to various policy measures that restrict data flows by limiting the physical storage and processing of data within a given jurisdiction's boundaries. The RBI, in 2018, had issued a circular mandating that payments-related data collected by payments providers must be stored only in India.

value chains is likely to draw momentum as corporations across the world look at relocating their manufacturing and assembly lines outside China in the post-pandemic scenario.

Auto-trigger Mechanism

To deal with the imminent rise in imports, India had been seeking an *auto-trigger mechanism*, which would have allowed India to raise tariffs on items in instances where imports cross a certain threshold. Once invoked, the concessional duty under RCEP would have been scrapped for a particular item and the normal (MFN) duty would apply. It may be noted that such a mechanism would have been an addition to the existing tools available to the Government — such as anti-dumping, countervailing and traditional safeguard duties — to act against any irrational spike in imports. This was demanded particularly to protect the domestic industries from import surge in certain sensitive products. However, majority of RCEP member countries were against the idea of including an auto-trigger mechanism in the agreement.

Secession from RCEP

Trade in Agriculture

As has been noted previously, with the New Zealand's entry in the RCEP, India's participation in the agreement could've been detrimental to the domestic dairy sector. However, it is noted that India's top export items to the RCEP also comprised of marine[80] and meat products[81], which registered an AAGR of 16.1% and 20.0% respectively, during 2010-19.

India's withdrawal from the RCEP is likely to reduce the growing opportunity for exports under the categories of marine and meat products, especially that of frozen meat of bovine animals[82], frozen shrimp[83] and frozen fish[84].

[80] HS 03: Fish and crustaceans, molluscs and other aquatic invertebrates

[81] HS 02: Meat and edible meat offal

[82] HS 020230: Frozen, boneless meat of bovine animals

[83] HS 030617: Frozen shrimps and prawns, even smoked, whether in shell or not, incl. shrimps and prawns in shell, cooked by steaming or by boiling in water (excluding cold-water shrimps and prawns)

[84] HS 030389: Frozen fish, n.e.s.

Trade in Services

Given India's competence and comparative advantage in services exports, opting out of the RCEP may reduce the services trade prospects, especially that of ICT services and other champion services like logistics. It may also be noted that while the tariff elimination under the ASEAN-India Free Trade Agreement is in force, India's exports to the ASEAN aggregation are likely to be impacted as the ASEAN member states sign the RCEP to form a trading bloc with nations like China, Japan and South Korea, apart from Australia and New Zealand, which are highly export oriented.

Conclusion

Foreign trade is expected to be an important catalyst in global economic recovery in the post-pandemic world. As per the IMF estimates, global trade volumes (goods and services, combined) registered a negative year-on-year growth of (-) 8.3% in 2020. As per the projections made in the IMF's World Economic Outlook July 2021, the global trade volumes are likely to accelerate to 9.7% in 2021, followed by a slight moderation to 7.0% in 2022.

It may be noted that the growth in trade volumes is expected to be driven by merchandize trade until the pandemic is brought fully under control, since services exports like tourism may not reach the pre-pandemic levels, given the travel restrictions across countries. However, considering the trade prospects in a longer term, services trade is one of the prominent areas for cooperation. It may be noted that the RCEP's imports of services grew at an AAGR of 6.9% during 2010-19, reaching US$ 1.2 trillion. Within the RCEP aggregation, the growth in services imports has been the highest in countries like Myanmar (19.2%), China (11.7%), Philippines (10.1%), and Thailand (4.2%).

5. POTENTIAL TRADE AGREEMENTS BETWEEN INDIA AND SELECT DEVELOPED COUNTRIES

1. India-Canada CEPA

Canada and India launched Comprehensive Economic Partnership Agreement (CEPA) negotiations in November 2010. The CEPA is a wide-ranging economic and trade agreement covering trade in goods and services and addressing non-tariff barriers. In this regard, it is to be noted that the bilateral trade between India and Canada has expanded considerably after the CEPA negotiations began. While India mostly exported articles of iron and steel, pharmaceutical products and machinery to Canada during 2010 and 2019, Canada's exports primarily comprised of mineral fuels, natural pearls and semi-precious stones and fertilizers.

Trade Scenario

India's merchandize exports to Canada were recorded at US$ 2.9 billion in 2019, more than double of the exports in 2010. During this time, while India's merchandize exports to Canada registered an AAGR of 10.9%, imports grew at an average of 8.8%, reaching US$ 3.9 billion, resulting in a trade deficit of US$ 1 billion in 2019. The trade statistics further indicate Canada's relative importance as a trading partner for India has remained low in the last ten years. In 2019, Canada's share in India's merchandize exports and imports were recorded at just 0.9% and 0.8%, respectively.

On the other hand, with regards services trade, exports to Canada have risen significantly in response to the growing telecommunication and financial services sector, making it a net importer of services from India, especially in commercial services. The bilateral trade in services between India and

Canada, in 2019, was recorded at US$ 3.1 billion and is likely to double in the next three years, driven by the growing demand for consumer goods.

Investment Scenario

While the cross-border investment flows between Canada and India have grown substantially during the last ten years, it remains modest when compared to the level of investment received by both the countries from rest of the world. The total FDI inflows received by India from Canada during April 2000 and March 2020 were recorded at US$ 1.9 billion, making up for 0.41% share in India's total FDI inflows.

In this regard, it is important to note that both the countries have been in negotiations to finalize a Foreign Investment Promotion and Protection Agreement (FIPA), which is expected to improve the investor sentiments through a framework of legally binding rights and obligations. The negotiations on the CEPA have been held back slightly after the India introduced the "hybrid" model for bilateral trade in services in return for the market access forgone in the services sector, especially with regards financial services.

Further, as per fDi markets database[85], across sectors, the highest envisaged capex received by India from Canada during 2010-11 and 2019-20 was in solar electric power (19%); metals (17%); financial services (12%); software and IT services (8%); and leisure & entertainment (5%). The largest investing companies from Canada in India during this time were SkyPower (18%); AIM (9%); Aerospace Processing India (8%); IMAX (5%); and Bombardier Transportation (5%).

On the other hand, envisaged capex by India in Canada, during the same years, amounted to US$ 4.1 billion and was the highest across sectors like Chemicals (30.6%), Metals (26.8%) and Software & IT services (20.2%). Amongst the leading investing companies were IFFCO (29.9%), Essar Steel (24.3%) and Tech Mahindra (13.7%).

[85] fDi Markets tracks cross-border investment in a new physical project or expansion of an existing investment which creates new jobs and capital investment. This data differs from official data on FDI flows as company can raise capital locally, phase their investment over a period of time, and can channel their investment through different countries for tax efficiency

Chart 5.1: FDI Inflows in India by Canada

Source: Data accessed from DPIIT, India Exim Bank Research

Suggested Sectors for Negotiations

The composition of merchandize trade between India and Canada has changed significantly before and after the CEPA negotiations between the two started in 2010. India's leading sectors of merchandize exports to Canada in 2010 back were apparels, organic chemicals, pearls & precious stones, and articles of iron or steel. While India has remained a net importer with respect to merchandize trade with Canada in the last ten years, following are the sectors which have undergone notable change.

- **Mobile Phones and Communication Apparatus**

Canada's imports of mobile phones[86] and communication apparatus[87] registered an AAGR of 7.7% during 2010-19 to reach US$ 9.9 billion in 2019. However, Canada's imports of the same from China grew at a higher AAGR of 16.6% during the same time. It is noted that in 2019, nearly 63% of Canada's import demand for mobile phones and communication apparatus was met by China alone, as against 37% in 2010.

During the same time, India's share in Canada's imports of mobile phones and communication has remained negligible in the range of 0.1% - 0.3%. As businesses realign their global supply chains in the post-pandemic world,

[86] HS 851712: Telephones for cellular networks "mobile telephones" or for other wireless networks

[87] HS 851762: Machines for the reception, conversion and transmission or regeneration of voice, images or other data, incl. switching and routing apparatus (excluding telephone sets, telephones for cellular networks or for other wireless networks)

backed by strong policy support, there exist opportunities for India to increase its exports of mobile phones and communication to Canada in the near term. It is important to note that India's exports of mobile phones during 2010-19 recorded an AAGR of 94.2% with the exports almost doubling during this period. For communication apparatus too, India's exports registered an AAGR over 40%, during the same period. The proposed CEPA, in this regard, could play a critical role in channelizing investments inflows in India for manufacturing and export of mobile phones and communication.

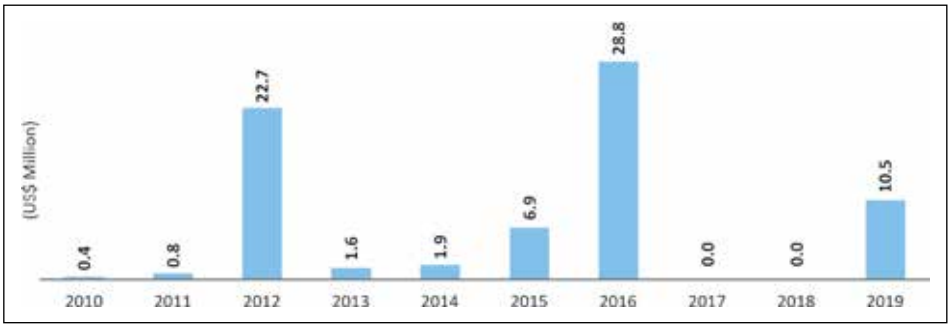
- **Foods and Beverages**

- Canola Oil

  - It is to be noted that Canada exports more than 90% of its canola as seed, oil or meal to 50 markets around the world[88]. While the import of Canola seeds is not allowed in India as they are genetically modified, small quantities of Canola Oil are being imported for blending with other oils. Amongst the leading Canola Oil producers include Cargill, Louis Dreyfus Company and Bunge.

It is important to note that even though the imports of Canola Seeds are banned in India, the import of GM Canola Oil is not. As a result, Canola seeds imported from Canada are usually crushed in Dubai and the extracted oil is then exported to India.

Chart 5.2: India's Imports of Canola Oil from Canada



Source: Data accessed from ITC Trade Map, India Exim Bank Research

[88] Canola Council of Canada

India's imports of Canola or the Rapeseed Oil[89] were recorded at US$ 31.2 million in 2019, thrice of what was imported in 2010. It is to be noted that Canada's share in India's total imports of Canola Oil has risen significantly from 3.7% in 2010 to 33.7% in 2019, while that of the UAE had declined from 94.7% to 50.8%, during the same time.

Even though India's imports of Canola Oil have shown a downward trend during 2016 and 2019, the demand is likely to increase in the next few years on account of growing population and increasing cases of cardiovascular diseases and diabetes. In addition, Canola Oil could replace the prevalent use of the Mustard Oil in India, owing to its zero pungency and zero bitterness.

Going forward, it is important to acknowledge that the India-Canada CEPA is likely to provide a growth opportunity to Canadian exporters of Canola Oil to gain a wider market share in India. While Canada accounted for around 40% of the imports of Canola Oil in 2019, the CEPA could also give Canadian exporters a significant edge over the exports from other countries like Germany and Russia. Currently, the tariffs on import of vegetable oils from Canada exceed 30% and to expand trade, the CEPA must eliminate the differential tariff structure that exists among oilseed products, which distorts the market and discriminates against certain imports. In addition, it is noted that the presence of non-tariff barriers in Canada's agri-food exports to India acts as a major obstacle, resulting in shipments being help in up in-transit and proportionate increase in the costs associated with shipping.

Accordingly, the 'negative' and 'sensitive' lists from the Indian side might need to be framed carefully, keeping in mind the likely impact of the CEPA on India's food security and increased import dependence on Canada for vegetable oils.

- Pulses:

Canada was India's largest import source for pulses[90], in 2019, accounting for

[89] HS 1514: Rape, colza or mustard oil and fractions thereof, whether or not refined, but not chemically modified

[90] HS 0713: Dried leguminous vegetables, shelled, whether or not skinned or split

28.3% of the total imports. During 2010 and 2019, India's import of pulses from Canada registered an AAGR of 30.6%, against the AAGR of 6.2% in total import of pulses during the same time.

India had a trade deficit of US$ 430.6 million with Canada for pulses in 2019, up from US$ 107.8 million in the previous year. In this regard, entering into a trade agreement with Canada could effectively arrest the widening of India's trade deficit arising on high imports of pulses.

2. India-European Union Bilateral Trade and Investment Agreement (BTIA)

The negotiations on the Bilateral Trade and Investment Agreement (BTIA) between India and the EU were launched in June 2007 to liberalize the trade in goods and services in a WTO compliant manner.

Broadly, the negotiations covered trade in goods, trade in services, investments, sanitary and phytosanitary measures, technical barriers to trade, trade remedies, rules of origin, customs and trade facilitation, competition, trade defense, government procurement, dispute settlement, intellectual property rights & geographical indications, sustainable development[91].

It is to be noted that the BTIA negotiations have been on a standstill since 2013, after fifteen rounds, over diverging opinions on the 'sensitive lists' of both the parties, especially concerning the opening up of Indian markets like automobile, alcoholic beverages and BFSI for the EU businesses.

While both the sides have agreed to eliminate tariffs on 90% of all tradable goods, India wants EU to up their offer to 95%, and EU wants India to include 98% of the tradable goods for tariff reduction[92].

The delay in conclusion of the BTIA has significantly been affected by the recent probability of Brexit because of the UK's substantive participation in

[91] Department of Commerce, Ministry of Commerce and Industry: India-EU Broad Based Trade and Investment Agreement (BTIA) negotiations (https://commerce.gov.in/international_nextDetail_WTO.aspx?LinkID=32&idwto=34)

[92] CII: India-EU BTIA Negotiations: A Status Update (http://newsletters.cii.in/newsletters/mailer/trade_talk/pdf/India-EU%20BITA%20Status.pdf)

services as well as the wine and spirits sector, both of which lay at the core of the BTIA. However, the latest statements from the Indian Government indicate that India is ready to explore the idea of PTA before proceeding for the FTA.

Trade Scenario

India was a net exporter of merchandize to the EU 27 (UK excluded, EU hereafter) in 2019, with a trade surplus amounting to US$ 4.5 billion, as against the trade deficit of US$ 6.9 billion in 2012. The exports from India to the EU in 2019 primarily comprised of mineral fuels (14%), organic chemicals (8%), machinery (8%), precious metals (6%) and articles of apparel and clothing (5%). On the other hand, major imports from the EU were machinery (22%), precious metals (14%), electrical machinery (9%), optical and surgical instruments (6%) and organic chemicals (5%).

Chart 5.3: India's Trade with the EU

Source: Data accessed from ITC Trade Map, India Exim Bank Research

It is noted that India transitioned from a net importer to a net exporter of merchandize to the EU in 2016, after fourteen years, except for once in 2013. Amongst the items contributing the most to the trade surplus in 2019 were mineral fuels[93] (US$ 6.2 billion), unworked diamonds[94] (US$ 1.4 billion) and non-antibiotic medicaments[95] (US$ 827.1 million).

[93] HS 271019: Medium oils and preparations, of petroleum or bituminous minerals, not containing biodiesel, n.e.s

[94] HS 710239: Diamonds, worked, but not mounted or set (excluding industrial diamonds)

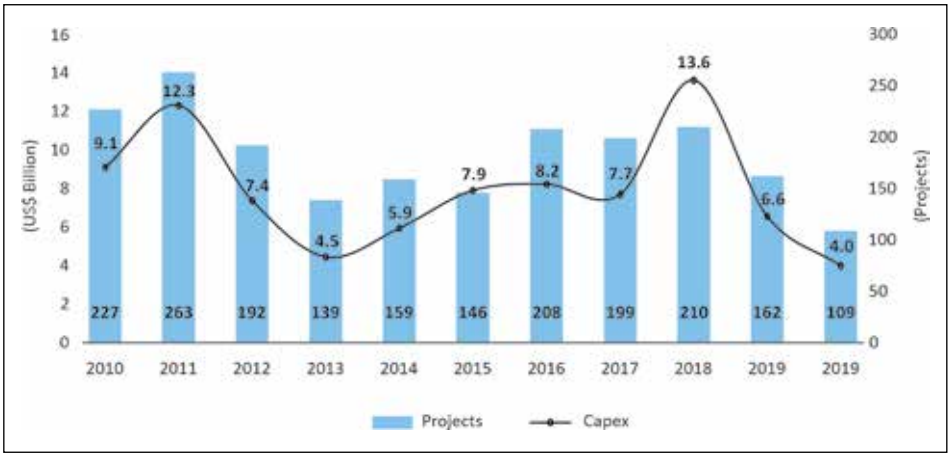
[95] HS 300490: Medicaments consisting of mixed or unmixed products for therapeutic or prophylactic purposes, put up in measured doses "incl. those in the form of transdermal administration" or in forms or packings for retail sale

Investment Scenario

The EU's share in foreign investment inflows to India more than doubled from 8% to 18%, during 2010 and 2019[96]. The total FDI received from the EU in India during April 2000 and March 2020 was recorded at US$ 109.55 billion. With regards FDI sources from the EU in India during April 2000 and March 2020, the highest inflows were from the Netherlands (US$ 33.8 billion), the UK (US$ 28.2 billion); Germany (US$ 12.2 billion) and France (US$ 8.5 billion).

Further, as per fDi markets, envisaged foreign capex worth US$ 87.1 billion was received in India from the EU through 2,014 projects, resulting in an average capex of US$ 43.3 million per project. Across sectors, the highest recipient of envisaged foreign capex from the EU in India were renewable energy (13.1%), transportation and warehousing (12.0%) and Automotive OEM (US$ 6.6 billion), during 2010 and 2020.

Chart 5.4: Envisaged Foreign Capex Inflow in India from the EU



Source: Data accessed from fDiMarkets, India Exim Bank Research

Amongst the leading investing companies from the EU during 2020 to 2019, were Peters Surgical (US$ 3.4 billion), Solarpack (US$ 1.8 billion), DHL Express (US$ 1.5 billion), SKF India (US$ 1.5 billion) and Siemens Gamesa Renewable Energy (US$ 1.3 billion).

[96] European Commission (https://ec.europa.eu/trade/policy/countries-and-regions/countries/india/)

Suggested Sectors for Negotiations

- **Services**

Bilateral trade in services between the EU and India could significantly expand the scope of BTIA once it comes into effect. Going forward, to make the most out of BTIA, it will be crucial to analyze the trade in services at a more granular level.

- Mode 1 and Mode 4

  The BTIA is likely to emerge as a medium for India to gain wider market access in the EU, especially for the services in the Mode 1 category like KPOs and BPOs. To complement the cross-border trade in services enabled by Mode 1, negotiations around Mode 4 have also gained momentum, which allows services delivered through the movement of workers as service providers. The latter could bolster the participation of India's skilled professionals across domains like engineering, architecture, and information technology, in the EU's labour market and facilitate higher remittances to India.

- Mode 3

  Thorough scrutiny of the plausible impact of agreeing to Mode 3 of services needs to be done before the BTIA comes into effect. It is to be noted that the EU has a substantial edge over Indian players in the Mode 3 related businesses like insurance, banking, legal services, and retail. It should also be noted that if BTIA takes shape of a TRIPS plus agreement, measures should be taken to protect the intellectual property rights of Indian service providers.

- **Renewable Energy**

The India-EU BTIA will play a critical role in redirecting and significantly augmenting the trade and investment flows across the Renewable Energy sector, especially in the wind and solar. This primarily rests on two premises:

- ***One***, India could lead the discussions on Renewable Energy or the Environment Goods, under the umbrella of the International Solar Alliance (ISA). Being the anchor of ISA, India could work with like-minded countries to establish an agreement which could be on the lines of the

EGA, but with a greater thrust on investment promotion and technology transfer, albeit only for solar related items. It may be noted that the solar energy sector is undergoing a rapid metamorphosis. The solar installations in the last 10 years have increased at a substantial pace. In 2007, the share of solar energy in the global portfolio of energy was just 0.8%, which has increased to more than 14% in 2017.

This exponential growth provides significant opportunities for the ISA countries to augment their production capabilities from solar energy.

- ***Two,*** the European Green Deal[97] aims to transform the EU into a modern, resource-efficient, and competitive economy, ensuring: No net emissions of greenhouse gases by 2050 and economic growth decoupled from resource use. Nearly one-third of the € 1.8 trillion investments from the NextGeneration EU Recovery Plan, and the EU's seven-year budget will finance the European Green Deal.

The India-EU BTIA could combine the likely increase in uptake of renewable energy in the EU region with India's ability to manufacture the required machinery at competitive prices to achieve the goals of European Green Deal.

The agreement may help the flow of technology and investments from the EU to India, and thereby optimize the cross-border trade of environment goods like equipment needed for tidal and geothermal energy, wind turbine blades and solar panels.

3. India-UK Free Trade Agreement

Post-Brexit, the possibilities of a free trade agreement between India and the UK, covering trade in goods and services as well as investments, have reached a critical juncture. Even more so, after the EU-UK Trade and Cooperation Agreement (TCA), the UK-Japan Comprehensive Economic Partnership Agreement (CEPA) and the UK-Vietnam Free Trade Agreement (FTA) came into effect in 2020.

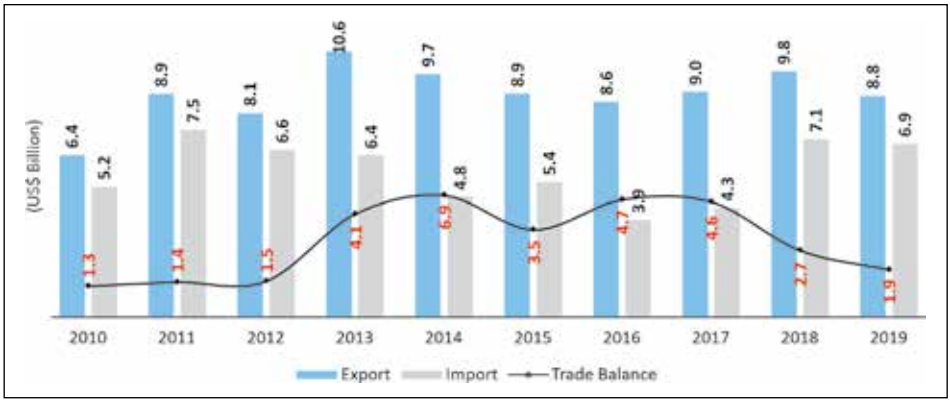
[97] European Green (https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en)

During the last ten years, the trading patterns between the two countries show a high degree of complementarity, with India's export basket having a high match with the UK's import basket, and vice-versa. With the identification of bilateral deliverables that could bolster the Enhanced Trade Partnership (ETP), in addition to the several rounds of talks held between the two countries, which are at the cusp of transition, the proposed FTA may bring pivotal shift in trade and investment flows across India and the UK. However, expanding the purview of the proposed FTA to that of a CEPA may help optimize trade and investment flows by matching the UK's manufacturing expertise across select sectors with that of relatively cheaper availability of labour in India. It may also be noted that the CEPA framework, by incentivizing investment inflows from the UK in India's manufacturing sector, may be an efficient arrangement to tackle the longstanding issue of unequal exchanges in India's FTAs.

Trade Scenario

India has been a net exporter of merchandize to the UK during 2010-19, with trade surplus reaching US$ 1.9 billion in 2019, higher from the trade surplus of US$ 1.2 billion recorded in 2010. During this time, at 6.8%, the AAGR in India's imports from the UK has been higher than the AAGR of 4.8% in exports.

Chart 5.5: India's Trade with the UK



Source: Data accessed from ITC Trade Map; India Exim Bank Research

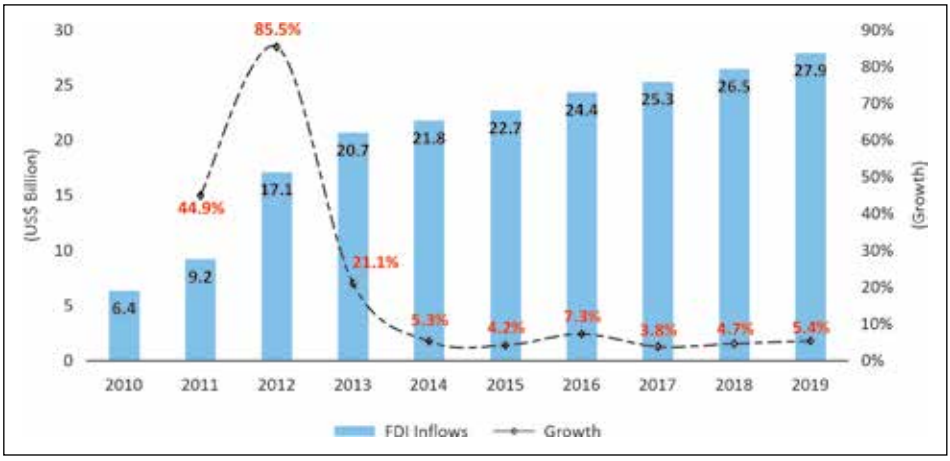
In 2019, India's exports to the UK primarily comprised of machinery (12%), apparel (9%), jewellery (9%), pharmaceuticals (6%), and footwear (5%). India's imports from the UK, on the other hand, included gold and silver (21%), machinery (6%), petroleum coke (4%), waste and scrap of iron and steel (4%), and unworked non-industrial diamonds (3%).

It is noted that the India's trade surplus arising from the merchandize trade with the UK increased from US$ 1.2 billion in 2010 to US$ 1.9 billion in 2019. Amongst the items contributing the most to the trade surplus in 2019 were articles of apparel and clothing (US$ 1.5 billion), pharmaceutical products (US$ 375.4 million), footwear (US$ 363.5 million) and other made-up textiles (US$ 264.8 million).

Investment Scenario

The total FDI received from the UK in India during April 2000 and March 2020 was recorded at US$ 28.2 billion, accounting for almost 6% of the total FDI inflows received during the same period. Further, as per fDi markets, across sectors, the highest recipient of foreign capex inflows from the UK in India were metals (15.1%), renewable energy (11.6%) and electric components (11.0%).

Chart 5.6: FDI Inflows in India from the UK



Source: Data accessed from DPIIT; India Exim Bank Research

During this time, amongst the leading investing companies were Solargise India, Vedanta Resources and Lightsource BP, with an envisaged capex of US$ 4.1 billion, US$ 3.1 billion and US$ 3.0 billion. It may be noted that with the revival of the UK-India CEO Forum in 2021, the bilateral investments across sectors are likely to witness a significant boost.

Suggested Sectors for Negotiations

- **Aerospace and Parts**

The UK has been amongst the top import sources for India's imports of aerospace and parts[98] in the last ten years. India's trade deficit for aerospace and parts was recorded at US$ 1.8 billion in 2019. Given that demand for aircraft in India is largely driven by defense projects, it is amongst the most strategically important areas for trade the India-UK FTA is likely to narrow the deficit. The agreement could also be a starting point for assembly in India as it strives to achieve self-reliance in the aerospace sector.

- **Scotch Whiskey**

The UK has been the world's leading exporter of whiskies[99], accounting for over 50% of the world exports. It may be noted that even though the basic customs duty imposed by India on the Scotch Whiskey from the UK was as high as 150% in 2019, its imports were recorded at US$ 115.5 million, registering an AAGR of 5.9% during 2010-19.

The proposed agreement, by reducing tariffs, is likely to significantly impact the UK's exports of whisky to India. In this regard, it is suggested that as the tariffs on whisky are reduced and the UK gains a wider market access, the terms of the agreement should be designed to incentivize the UK's distilleries to invest in India for final stages of production like blending and bottling.

[98] HS 88: Aircraft, spacecraft, and parts thereof
[99] HS 220830: Whiskies

Box 5.1: India-UAE Comprehensive Economic Partnership Agreement (CEPA)

Recently, in February 2022, India and UAE signed a CEPA which came after a three-month fast-tracked negotiation. It is first trade agreement that India has signed in the last one decade with the last one being an FTA with Japan in 2011. India is also expected to conclude a trade agreement with the Gulf Cooperation Council (GCC) in the near future.

It is expected that the agreement could benefit 90% of India's exports to UAE by value. The Indian sectors that are expected to benefit out of this agreement include gems and jewellery, textiles, leather, footwear, sports goods, engineering goods, automobiles and pharmaceuticals. As a result, India's trade with UAE could reach US$ 100 billion over a five-year period.

India has also excluded some products from the agreement and kept them under the 'sensitive list'. These include goods such as dairy, fruits, vegetables, cereals, tea, coffee, sugar, food preparations, tobacco, toys, plastics, scrap of aluminium, and copper.

The Government of India has also focused on anti-dumping measures in this pact, in order to prevent dumping by any other country in Indian markets using the route of UAE. A strong rules of origin clause is a part of this pact wherein 40-45% value addition would be required to quality as being originated from India or UAE. It may also be noted that this is the first time that India has included a chapter on digital trade in any FTA.

6. INDIA'S TRADE AGREEMENTS: LOOKING AHEAD

Economic impacts of FTAs in India have varied, both across partner countries and industries. The benefits arising from entering into trade agreements could be wide-ranging. However, based on the shortcomings in India's existing FTAs and key features of trade agreements around the world, this Study highlights some key areas that need to be taken into account in India's trade negotiations, in order to optimize the gains arising therefrom.

According to the Economic Survey of India 2018-19, out of the fourteen trade agreements entered into, during 1993 and 2018, India's exports of manufactured products benefitted significantly across eight[100] agreements. With respect to four[101] out of the fourteen agreements, India's manufactured exports were largely unaffected and a significant negative impact on the same was noted in case of two[102] agreements.

Further, the bilateral agreements with South Korea, Japan, and Sri Lanka, are the only ones where the percentage increase in imports are higher than that of exports[103]. Going forward, while it is crucial to engage in constant and extensive impact assessment of these agreements, it is equally important to ensure that such agreements result in creation of trade complementarities between India and its trade partners that arise from allocative efficiency of

[100] MERCOSUR-India PTA, ASEAN-India FTA, India-Nepal FTA, India-Singapore FTA, Chile-India PTA, India-Bhutan FTA, India-Afghanistan PTA, and India-Japan FTA

[101] SAFTA, BIMSTEC, India-Thailand PTA and India-Sri Lanka

[102] India-Japan CEPA and India- Republic of Korea CEPA

[103] Economic Survey of India 2018-19: Are Free Trade Agreements Beneficial? (https://www.indiabudget.gov.in/economicsurvey/doc/vol1chapter/echap05_vol1.pdf)

resources and in turn, develop economies of scale. Additionally, for the trade agreements under negotiations or in the pipeline, it would be paramount to expand the scope and prescribe to a CEPA or a CECA format in order to boost cross-border investment flows.

Key Recommendations

Possible Changes in Existing and Potential FTAs

- Addressing the Unequal Exchanges in Existing FTAs
- Incorporating WTO's Agreement on Technical Barriers to Trade in the FTAs
- Provision of an Emergency Action Plan
- Reducing Trade Restrictiveness in Services
- Examining the Utilization Rate of Tariffs

Other Areas of Economic Cooperation

- Focus on Sustainabile Trade and Investments
- Focussing on introducing MRAs as clauses in existing and potential trade agreements
- More Engagements in CEPAs

Possible Changes in Existing and Potential FTAs

- **Addressing the Unequal Exchanges in Existing FTAs**

It is vital to note that when India is on the import side, the preferential (weighted) tariffs are significantly lower than the MFN tariffs while when India's partner country is on the import side, preferential tariffs are closer to the MFN tariffs in most cases. This signifies that while India might have a benefit in importing from the trade agreement partner, the partner might not get the same financial benefit while importing from India. This is indicative of uneven distribution of gains from trade arising on account of tariff concessions agreed upon as a part of an FTA. In this regard, reduction of tariffs by India and its trade partners as per the trade agreements should capture the difference in the trade values and volumes that might be impacted on either side.

Therefore, while evaluating the potential gains from trade before entering into an FTA, it must be made sure that the domestic industry is not made to compete on unequal terms with the partner countries. In this regard, India should leverage its strengths of a relatively cheaper labour market and huge consumer base that the partner country, especially the developed countries, could get an access to by reduction of tariffs.

For instance, with regards electronics, tariff reduction while entering into a trade agreement with South Korea may be beneficial to India in terms of technology transfer and relatively cheaper imports. However, the potential gains to South Korea might exceed the gains accruing to India, with easier access to the latter's wide and growing consumer base. In cases like these, equal reduction in tariffs must happen only when India's potential gains match with what it has to offer, if the agreement comes into effect.

To address the problem of unequal exchange in totality, it is important to reevaluate the existing and potential FTAs through a zero-budgeting exercise[104] and analyze the impact of FTAs on tariff revenue as well.

Renegotiations of FTAs must also address the problem of prevailing inverted duty structures[105] that not only prevent India's domestic industry to optimize the exports of finished goods but also deter its participation in the GVCs of critical sectors like pharmaceuticals and electronics. This has been noticed with reference to the India's FTAs signed with Japan, South Korea, and the ASEAN aggregation.

[104] Zero-based budgeting involves starting with a new budget for every new period

[105] An inverted duty structure emerges when import duties on finished products are lower than those on parts/ raw materials, effectively incentivising imports of goods rather than imports of parts and inputs for local manufacturing

Lastly, incorporation of an offset clause[106], as often done for procurement of defense equipment through deals or agreements, should be extended to wider trade agreements, especially for technology intensive sectors like automobile and electronics, wherein the other participants to the agreement are obligated to engage in reverse purchase, execute export orders or invest in India's domestic industry. Most importantly, the offset clause with respect to India's trade agreements with the developed countries must be looked at as an equal exchange, given the huge market access granted to such trade partners as per the agreement.

- **Incorporating WTO's Agreement on Technical Barriers to Trade in the FTAs**

Since the formation of the WTO in 1995, the tariffs around the world have gradually reduced in the last two and a half decades. However, in the modern world, technical barriers to trade (TBT) are playing a much bigger role in restricting the trade across geographies than tariffs. With reference to most FTAs as well, TBTs are a much bigger hinderance than tariffs by restricting the access to goods manufactured by another country on the grounds of product regulations, particularly in the case of bilateral trade agreements between a developing and a developed country. While some TBTs are designed to comply with a country's food and national security interests and act as safeguards against health and safety, many TBTs could be highly trade restrictive.

The TBTs directly translate into higher indirect costs for the exporters, thereby offsetting the initial reduction in trade costs facilitated by entering into trade agreements. Such indirect costs typically arise on compliance grounds, due to dissimilar quality control standards within participants to the trade agreement and other procedural delays such as pre-shipment and post-shipment customs inspections.

[106] Offset Clause is a provision in agreements that permits each party to net amounts due against those payable before making payment. This is especially important in the event of insolvency of one party that ceases to remit amounts due to the other

In this regard, the WTO's TBT Agreement lays down the framework to identify those technical regulations, standards, and testing and certification procedures which do not create unnecessary obstacles to cross-border trade. The TBT Agreement, by establishing a common understanding of good regulatory practices, provides the framework for identification of unreasonable barriers. Some of the fundamental principles could include non-discrimination, promoting predictability of access to markets, encouraging the use of international standards, and the need to avoid unnecessary barriers to trade[107].

Going forward, it is suggested that while India's trade agreements, especially with the developed countries, be comprehensive and tailor-made to address the abovementioned issues, they should also build upon the foundations and provisions of the WTO's TBT agreement to provide a wider market access to domestically manufactured goods. In addition, the agreements could also involve the creation of a bilateral mechanism to address specific TBT issues, apart from dispute settlements. Such mechanism could go beyond the standard design of the trade agreements and identify the opportunities for mutual recognition in the area of technical regulations, standards, and conformity assessment procedures.

- **Engagement of the Public Sector Enterprises in the Trade Agreements**

Given the large presence of the public sector enterprises (PSEs) in India and their participation in foreign trade, incorporating PSE-related disciplines in the trade agreements becomes critical in order to prevent unfair competition and potential trade distortions.

It is noted that PSE practices that are not in adherence to the principles of non-discriminatory treatment in international trade (including norms on fair procurement by the PSEs), tend to restrict the potential gains from trade arising from entering into trade agreements. In order to eliminate the prospects of unfair competition and potential trade distortions, incorporating PSE-related disciplines in the trade agreements become crucial, given the

[107] Technical Barriers to Trade (TBT) (https://www.mbie.govt.nz/dmsdocument/5772-technical-barriers-to-trade-strategy)

sizeable participation of such enterprises in India's foreign trade, especially in the sectors like metals, heavy engineering, and oil & gas.

Drawing insights from the chapter on State-owned Enterprises in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), the underlying idea is to make the PSEs compete based on quality and price, and not based on discriminatory regulations, subsidies, or favoritism.

Even though the PSEs, globally, are subject to the WTO's trading functions guidelines like the GATT Article XVII and GATS Article VIII, it is noted that these rules have not kept pace with the rapidly evolving business environments across countries. For instance, the GATS Article VIII, which governs Monopolies and Exclusive Service Suppliers, was drafted when services like telecommunication and infrastructure were largely provided by the government or state-owned enterprises with minimal or no participation of private players. Hence, considering the drastically evolved dynamics between the state-owned and private enterprises, incorporating the disciplines for the former in the trade agreements becomes necessary.

However, in doing so, the policymakers must acknowledge the fact that the government's exclusive rights to operate in critical sectors like defense equipment and the energy sector should not be eliminated entirely. For instance, India's ambitious plan of all-electric vehicle by 2030 would require securing minerals like lithium and cobalt in huge quantities. In this regard, partnering with countries such as in the 'Lithium Triangle' (Argentina, Bolivia, and Chile) becomes extremely important not only to achieve the said objective but also to make new-age electric vehicles affordable for the current and potential buyers in the country.

While a consortium of three PSUs[108] has started exploring the possibility of acquiring lithium and other rare earth elements (REEs) from the resource rich countries to ensure mineral security for India, a CEPA between India and Australia or countries in South America could effectively complement India's need for strategic minerals to its competence in manufacturing and possible exports of EVs.

A comprehensive economic agreement to secure strategic minerals, apart from reducing import dependence, could also be extended to support sectors like aviation, defense, and space. Overall, a significant weightage should be given to the criticality of each sector and the related PSEs involved in those sectors, while negotiating the terms of trade agreements.

- **Provision of an Emergency Action Plan**

Based on its GDP, India's status of an emerging or developing economy has been contested in the WTO, multiple times in the last few years. This poses considerable hinderances to trade and investment flows facilitated by India's trade agreements. For instance, in February 2020, India's status of a developing economy was contested by the United States Trade Representative (USTR), making India ineligible to claim benefits for preferential treatment with respect to countervailing duties investigations under the Generalized System of Preferences (GSP) Scheme, of which India has been the largest beneficiary[109]. Such trade shocks not only have an immediate impact on the exports but also create significant economic certainty around the future foreign trade prospects.

[108] Khanij Bidesh India (KABIL) is a joint venture of three central Public Sector Enterprises — National Aluminum Company (NALCO), Hindustan Copper (HCL) and Mineral Exploration Company (MECL) formed to ensure a consistent supply of critical and strategic minerals for the Indian domestic market

[109] Over one-tenth of India's merchandize exports to the USA could enter duty-free, as per the GSP, making India the largest beneficiary of the program

Therefore, given the dynamic growth trend in India's GDP and the uneven growth in the constituents of GDP (like the government expenditure and exports) recorded in the last few years, the trade agreements that India enters into must provide for a transitional tariff-based emergency action mechanism, which is a temporary bilateral safeguard measure used to protect the domestic industry and exporters against the events that can cause unforeseen damage in form of unprecedented surge in imports or fall in exports. Such arrangements must be comprehensive and specify the qualifying conditions for imposition and the duration for which the action may be maintained[110].

To complement this, trade agreements negotiations from the Indian side should also propose to have a 'graduation clause' with other developing country FTA partners, extending a 'sunset clause' for periodic review of the terms of select agreements, and a 'trigger mechanism' if the FTAs lead to a sudden surge in imports from a particular trading partner for a given product.

On the other hand, in a long-term perspective, the aforementioned US-India trade conflict, is also a case-in-point wherein the impact of GSP withdrawal was seen in many sectors like automobile, machinery, iron & steel, and organic chemicals. However, in order to counter the negative impact of GSP withdrawal by the USA, India could enter into strategically designed FTAs or broader areas of economic cooperation without affecting the sensitive domestic sectors and put forth its demand for duty concessions for all items out of GSP.

[110] Canada-India Joint Study Group Report Exploring the Feasibility of a Comprehensive Economic Partnership Agreement

Box 6.1: Generalized System of Preferences (GSP)

In 1971, the United Nations Conference on Trade and Development asked the developed countries to help the developing countries integrate into the world economy. The Generalized Scheme of Preferences (GSP) was born and currently, about a dozen countries have GSP mechanisms in place.
United States of America:

GSP is the largest and oldest U.S. trade preference program that provides nonreciprocal, duty-free treatment enabling many of the world's developing countries to spur diversity and economic growth through trade. Economic development is promoted by eliminating duties on thousands of products when imported from designated beneficiary countries and territories[111].

The GSP provides Most Favoured Nation (MFN) clause which is considered to be non-discriminatory in nature, a permanent exception and provides a special tariff treatment to select countries. In 2018, the USTR initiated a review of India's eligibility of GSP and subsequently, revoked India's GSP status in 2019. As per the Government of India, this would not impact India significantly as the benefits under GSP amounted to only US$ 190 million per year. However, this could negatively impact the MSME sector of India and ultimately, the employment to some extent.

European Union:

While the USA implemented its own GSP in 1976, the EU GSP is older of the two and was established in 1971. The EU GSP is tailored as per the needs of the beneficiary countries. As a result of this, a three-tier structure works under the EU GSP, namely, Standard GSP, GSP+, and Everything But Arms (EBA). India falls in the category of Standard GSP which is for low and lower-middle income countries. Under this, there is a partial or full removal of customs duties on two-third of tariff lines.

It may be noted that in 2021, the European Commission has adopted legislative proposal for the new EU's Generalized Scheme of Preferences (GSP) for the period 2024-2034. The Commission is proposing to improve some of the key features of the scheme to better respond to the evolving

[111] U.S. Customs and Border Protection

needs and challenges of GSP countries as well as reinforce the scheme's social, labour environmental and climate dimension[112].

Total EU imports from India amounted to €32 billion in 2020, a 15% decline compared to the previous year. About 88% of eligible EU imports from India currently make use of the preferential duties under the GSP. These preferential imports summed up to €11.5 billion in 2020, which makes India the largest beneficiary of the Standard GSP. About 41% of India's exports to the EU market are eligible for reduced tariffs granted by the Standard GSP[113].

- **Reducing Trade Restrictiveness in Services**

According to OECD, services represent more than 50% of the value added in gross exports, and over 30% of the value added in exports of manufacturing goods. India has been a net exporter of services in the last few years with the services exports reaching US$ 209.3 billion in 2020, up from US$ 138.5 billion in 2011, registering an AAGR of 4.8%, during this period.

However, it is noted that India's trade in services is quite restricted. The relative restrictiveness of Indian services can be observed using the Services Trade Restrictiveness Index (STRI) of OECD, indicating the presence of restrictions that impede services trade. The STRI can provide information on regulations affecting trade in services in total 22 sectors across all OECD member countries plus Brazil, China, Costa Rica, India, Indonesia, Malaysia, Russian, South Africa, and Thailand. These countries comprise over 80% of global trade in services.

Despite India's high competence and strength in the export of services, it is noted that India has an STRI score, exceeding the world average, in all sectors and the highest in 3 of the total 22 services. Among the sectors, rail freight transport has the highest STRI value (1), which is the maximum STRI value. The other two with high STRI values are legal services (0.886), and accounting services (0.827). This could be attributed to the fact that accounting and auditing are reserved for licensed accountants and auditors and a license

[112] European Commission

[113] GSP Hub, European Commission

is required to own and manage an accounting or an auditing firm and only Indian nationals are eligible to obtain the license. Further, legal services, both national and international law, are reserved for licensed Indian lawyers; and railway operations are in the list of prohibited sectors and reserved for Indian Railways, a state-owned enterprise.

The STRI values for India indicate that there is a large variation in trade restrictiveness across sectors, as far as the relative importance of the policy areas[114] is concerned. India has relatively high scores on the STRI largely because of the strong ownership of the Government services areas such as banking and insurance. Further, FDI in select services areas such as financial services and retail, has an upper limit with respect to the foreign equity. In areas such as legal services, the foreign participation is not allowed at all.

Factors like in-country testing requirements and data-and-server localization requirements in the case of information and communications technology sector also restrict the services sector. While the data localization requirements cannot be compromised on account of national security concerns, there exists significant room for expansion of trade in services across sectors like BFSI. It is also important to note that entering trade agreements with the developing economies to cater to the growing demand for insurance, microfinancing, and SME loans could propel India's BFSI sector's participation in the overseas markets.

Out of India's twelve RTAs currently in force, including accessions, only five agreements[115] cover trade in services. In order to effectively overcome the aforementioned shortcomings preventing India to leverage its strengths in the services sector, it is suggested that the current and potential trade

[114] Restrictions on Foreign Entry; Restrictions to movement of natural persons; Other Discriminatory measures; Barriers to Competition; and Regulatory Transparency

[115] Five agreements covering trade in services: India-Japan FTA; India-Malaysia FTA; ASEAN-India FTA; Korea-India FTA and India-Singapore FTA

agreements should seek to further liberalize the trade in services with substantial sub-sectoral coverage.

- **Examining the Utilization Rate of Tariffs**

To determine the economic usefulness of preferential tariff to countries in a trade agreement, "*preference utilization rate*" is examined. It indicates what percentage of given imports is using the preferential duties offered by the free trade agreements. Among the key factors that determine preference utilization rate for a country include:

- ***Tariff Differential between the preferential duty rate and MFN rate***: It is noted that products with high tariff differentials have very restrictive rules of origin, intended to prevent trans-shipments from third countries misusing the preferential tariff rates. Empirical evidence indicates that even though preference utilization rate mostly has a positive correlation with tariff differentials, if the rules of origin for products with high tariff are very restrictive, the correlation may be negative[116].

- ***Savings Potential***: Typically, products for which FTA utilization leads to large tariff savings have a much higher utilization rate. FTA utilization is estimated by taking the difference between MFN and FTA duties for products at the HS 8-digit level and then multiplying the same by trade volume. Accordingly, preference utilization rates are higher for products which offer a higher savings potential when using the preferential duties instead of the standard MFN duty rates.

As per studies, a preference margin threshold, below which the cost of utilizing preferences exceeds its benefits was estimated at 5%[117]. While the global utilization of preferences is as high as 70% to 80%, for India, it stands at around 5%-25%[118]. Going forward, it will be important to relook at India's existing FTAs and explore the possibility of renegotiating them to address the low levels of the preference utilization rates.

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[116] Which Factors Determine the Utilization of Preferential Tariff Rates? (www.econstor.eu/bitstream/10419/203639/1/VfS-2019-pid-28203.pdf)

[117] New evidence on preference utilization (https://www.wto.org/english/res_e/reser_e/ersd201212_e.pdf)

[118] Export-Import Bank of India: Global Value Chain integration: Enhancing India's Exports (https://www.eximbankindia.in/Assets/Dynamic/PDF/Publication-Resources/ResearchPapers/121file.pdf)

Box 6.2: India Exim Bank's Commencement Day Annual Lecture by Dr. Arvind Panagariya

At India Exim Bank's 36th Commencement Day Annual Lecture in 2021, Dr. Arvind Panagariya gave a speech on the topic 'India's Trade Policy: The Past, Present and Future'.

The Lost Decades: 1950-80

Dr. Panagariya explained the set-up of trade regime in the post-World War II era, and how the infant-industry argument was introduced in the developing countries of the world by conceptualizing industry as a monolith and not as an amalgamation of different products.

Dr. Panagariya further explained that the industry scenario in the subsequent decades of the post-independence era for India which he termed as 'The Lost Decades: 1950-80'. It was felt necessary by the government of the day to produce heavy industry items such as railways, airplanes, and guns at home to reduce dependency on foreign players. At that time, the ultimate objective became to reorient the production basket to the consumption basket with trade filling the gap until the two baskets were fully aligned. It is interesting to note that in the initial years of independence, the Government of India did not raise trade barriers.

In the 1950s, both the level of income and the saving rates were low. With ample labour supply available, the key to fast growth was the conversion of these savings into the most productive investment possible, which countries such as South Korea and Taiwan did, Dr Panagariya added.

The Indian policymakers devoted the scarce resources to capital-intensive products and let the cottage industry produce by relying on its internal, household sources of savings. The compulsion to spread the scarce savings over as many products as possible even within the capital-intensive category meant that each of these products was allocated just enough capital to operate on the minimum technologically feasible scale. Therefore, their survival required prohibition of imports. Strict import licensing followed. Further, with denied access to any savings as well as high-quality imported inputs, labour intensive products fared no better.

Finally, in 1967, the Government of India came up with Small Scale Industries (SSI) reservation policy under which the GOI drew up a list of labour intensive products that were formally reserved for exclusive manufacture by small enterprises. This gave rise to problems such as concentration of capital, small production size, low competition, low quality, and price controls. The GDP growth during the period 1951-65 was recorded at 4.3%, while the same being recorded at 3.2% during the period 1965-81.

Hesitant Liberalisation: The Transition Decade of the 1980s

According to Dr. Panagariya, the second half of 1970s saw tiny bits of liberalization in India. It began with the revival of Open General Licensing (OGL) in 1976. An OGL list of products, for which an import license would no longer be required, was introduced. During 1980s, import liberalization took place through various channels. Canalized imports, which were a government monopoly, fell from a hefty 67% of total imports in 1980–81 to 27% in 1986–87. The government also steadily expanded the OGL list during 1980s. Further, several export incentives were also introduced during this period. Finally, the RBI allowed the Rupee to depreciate significantly in the second half of the 1980s. The result was seen in the economic growth which was recorded at 6.2% between 1981- 82 and 1987-88 and then jumped to 8.1% between 1988-89 and 1990-91. However, given rising import needs due to ongoing economic expansion at the same time, the situation could not be sustained, and a balance of payments crisis hit India in 1991.

Systematic Opening and Take-off: The 1990s and Beyond

The government formed in 1991 fundamentally altered the policy framework. With some exceptions, the GOI ended both import and investment licensing in one fell swoop. The government also adopted a policy of opening the economy to foreign direct investment. By 1996-97, the top industrial tariff was down to 50%, from 355% in 1991. It fell to 10% in 2007-08.

With the reforms in the 1990s, the economy sustained a growth rate of 5.8% between 1992-93 and 2002-03. By 2002-03, the combination of low tariffs and undervalued rupee had set the stage for the take-off of India's

exports. By 2003-04, the exports-to-GDP ratio had crossed 15% mark and by 2013-14, 25% mark. By 2019-20, this ratio had fallen to 18.6%.

Trade Policy Today: Creeping Protectionism

Dr. Panagariya referring to the WTO Trade Policy Review reports, published in 2011, 2015, and 2020 observed that the protection has seen a steady rise. In the year 2010-11, simple average of tariffs was the lowest on record, 8.9%. Since then, the simple average of tariffs has risen to 9.5% in 2014-15, 10.8% in 2019-20 and 11.1% in 2020-21. Tariffs have been raised on precisely those products in which substantial imports exist and domestic industry is failing to compete.

Additionally, Anti-Dumping (AD) duties by India have complemented these tariff increases. With just 2.53% share in the world merchandise imports in 2019, India accounted for 12.6% of all AD measures. However, it may also be noted that unlike the situation prevailed in the pre-1991 India, the policy regime today is free of its most restrictive instrument, import licensing. Equally important, India has steadily opened sector after sector to FDI.

However, Dr. Panagariya went on to narrate the negative effects of protectionism. By its nature, protection attracts firms that principally want to make quick profits by selling the product in the protected domestic market. Lacking global ambition, they also choose to operate on a scale much smaller than their counterparts in the global economy.

Looking Ahead: Trade Policy for Tomorrow

Dr. Panagariya stated that there is no country in the world that has achieved rapid transformation without conquering the world markets. As in 2020, 42.5% of India's workforce was employed in agriculture. For rapid transformation, approximately half of this workforce must move to industry and services in the next 10 to 15 years.

The only way this can be accomplished is by creating an environment in which successful export-oriented firms can emerge and flourish in labour-intensive sectors. Success in export markets requires first and foremost an open trade regime.

According to Dr. Panagariya, there are two possible avenues for liberalising trade. First, we may lower tariffs against all trading partners. India successfully deployed this approach from 1991-92 to 2007-08. Second, India can enter into free trade agreements with its major trading partners. A good starting point for this would be the UK and EU.

Box 6.3: Japan-UK Trade Deal

After its exit from the European Union, the UK entered into a major trade deal with Japan. The trade deal is estimated to be bring about a trade benefit of over £ 15 billion between UK and Japan. This trade deal could be one of the stepping-stones for the UK in being a part of CPTPP that could further help the UK businesses expand in the APAC region.

The deal, other than to the free trade of goods and taking into the GIs aspect for iconic items, also laid emphasis on the growing digital businesses and cross-border services trade.

- **Digital & data provisions** – The provision has the aim of free flow of data along with its protection. For instance, under this deal, the UK will be operating on the net neutrality principles and has also introduced a ban on data localization. This is expected to save the extra cost for UK business with respect to setting up servers in Japan.
- **New protections for creative industries** – The deal is expected to protect the brands and innovations by the businesses. It may be noted that this goes beyond the provisions of EU that cater to the online infringement of IP rights, like film and music piracy.
- **Mobility for business professionals** – The deal is expected improve the talent movement between the two nations as it is more flexible. For instance, the formalities for visas are aimed to be clear, transparent, and same will be processed in 90 days.

*Source: The Government of the UK (*https://www.gov.uk/government/news/uk-and-japan-agree-historic-free-trade-agreement*); and Market Screener (*https://www.marketscreener.com/news/latest/UK-and-Japan-agree-historic-free-trade-agreement--31272366/)

Other Areas of Economic Cooperation

- **Focus on Sustainable Development in the Trade Agreements**

Amid growing concerns on sustainable investments across the world, pioneered by the EU, sustainability clause in trade agreements around the world has come to the forefront. It may be noted that a key roadblock in the conclusion of India-EU FTA is also the EU's demand to have a chapter on Trade and Sustainable Development (or TSD), which requires both parties to adhere to international labour and environmental norms in the economy.

In particular, a chapter on TSD would require India to ensure fundamental labour rights, address climate change, and comply with certain international conventions related to ecological protection. It may be noted that nearly all recent EU FTAs contain chapters dedicated to sustainable development, which comprise a number of environmental and labour standards.

India's hesitation to include TSD chapter in the India-EU FTA stems primarily due to two reasons. One, it will become a sovereign commitment to amend the existing local labour and environmental laws to come at par with the international standards prescribed by the ILO or the Paris Agreement. And second, a mechanism will have to be put in place to ensure that the domestic exporters abide by the revised laws. With regards India-EU FTA, it may also be noted that two upcoming EU-wide initiatives, human rights due diligence and the carbon border adjustment tax, will penalize the EU companies for labour and environmental violations in their supply chains outside the EU, including in India. Indian exporters, therefore, are likely to suffer additional costs and reputational damage, in case they fail to adhere to the international labour and environmental norms. With the EU being India's largest market for key labour-intensive industries such as textile and leather, such non-adherence to laws will hinder the expansion of these industries.

However, given the fact that fundamental labour rights are already guaranteed under Indian law and ambitious environmental commitments under the Paris Agreement have already been announced, inclusion of TSD chapters in India's FTAs may not be as difficult. Interestingly, India has already acceded to and ratified almost all international conventions that are generally covered by TSD chapters such as the Convention on Biological Diversity (CBD)[119] and the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES)[120].

Lately, outside the EU also, dedicated chapters on sustainable development have found their way in critical trade agreements globally. For instance, the United States-Canada-Mexico Agreement (USMCA) has specific commitments on protecting labour rights, not found in any previous FTA negotiated by the parties. Similarly, the upcoming EU-Mercosur FTA will require all parties to make several commitments on environmental protection aligned to their targets under the Paris Agreement.

Going forward, including TSD commitments in FTAs would require the government to incentivize Indian exporters to adopt better labour and environmental protections in their operations, differentiating them from competitors and enhancing India's attractiveness as a sourcing base for foreign importers. In fact, if India becomes an integral part of the global trading rules-based order, accepting TSD clauses in FTAs, it will have even better labour and environmental standards in place and as a result, could cater to a wider market base.

- **Focussing on introducing MRAs as clauses in existing and potential trade agreements**

Mutual Recognition Agreements (MRAs) are bilateral agreements focussed on benefitting industries by providing easier access to conformity assessment,

[119] The Convention on Biological Diversity, known informally as the Biodiversity Convention or CBD, is a multilateral treaty for "the conservation of biological diversity, the sustainable use of its components and the fair and equitable sharing of the benefits arising out of the utilization of genetic resources" that has been ratified by 196 nations.

[120] The Convention on International Trade in Endangered Species of Wild Fauna and Flora or CITES is an international agreement between governments. Its aim is to ensure that international trade in specimens of wild animals and plants does not threaten the survival of the species.

thereby facilitating wider market access and promoting trade. Mutual recognition agreements lay down the conditions under which one Party (non-member country) will accept conformity assessment results (e.g. testing or certification) performed by the other's Party (the EU) designated conformity assessment bodies (CABs) to show compliance with the first Party's (non-member country) requirements and vice versa. Broadly, MRAs include relevant lists of designated laboratories, inspection bodies and conformity assessment bodies in both India and its trading partners.

Entering into MRAs could significantly expand the market access of India's exports (both goods and services) and lead to better price discovery in partner countries, especially the ones that are also the co-signatories to trade agreements. The MRAs with India's existing and potential FTA partners could be focussed on areas like regulatory standards, conformity assessment, accreditation procedures, qualifications, visas and social security.

Some of India's existing MRAs include:

- MRA between the Institute of Chartered Accounts of India (ICAI) and the CPA ("Certified Practising Accountant") Australia.
- MRA between the Institute of Chartered Accounts of India (ICAI) and the Malaysian Institute of Certified Public Accountants (MICPA) to enable appropriately qualified Chartered Accountants of either Institute to join the other Institute by receiving appropriate credit for their existing accountancy qualification.
- MRA between India and the USA for the recognition of Authorised Economic Operators (AEOs), for faster export clearance.

Additionally, the purview of existing MRAs could also be explored and extended to other critical areas like healthcare and para-medical services, especially with India's existing FTA partners. Focus should also be laid on adoption of MRAs covering merchandize export items in which India has a relative comparative advantage, like automobile and auto parts; medical equipment; electrical equipment and pharmaceuticals, among others.

- **More Engagements in CEPAs**

A more holistic and sustainable approach for India to integrate with the world economy causing minimal distortions should go beyond trade and cover the trade services and investment as well. In other words, going forward, India should focus on entering into comprehensive economic agreements like CECA and CEPAs for better growth prospects. It is to be noted that CEPAs are essentially FTAs plus packages, comprising of an integrated package of agreement on goods or services, investment, mutual recognition, e-commerce, intellectual property and more.

Provision for investment flows in the comprehensive economic agreements becomes crucial because of its potential to entail greater trade flows. This could also drive the Government's ambitious "Assemble in India for the World" scheme, which seeks to merge "Assemble in India" with the existing "Make in India". For instance, as has previously been mentioned, the CEPA between India and South Korea spanned over investments, competition, IPRs, and trade in services, apart from trade in goods. While this has significantly bolstered the merchandize trade between the two countries, it has also resulted in sizeable technology transfers and foreign investment inflows in India from South Korea.

It may be noted that while India has time and again affirmed its commitment to multilateral structure of WTO, in the recent times, it has also started to adopt a new approach with respect to the Preferential Trade Agreements (PTAs).

For instance, on the bilateral front, India is in the process of negotiating trade agreement with various nations. This is because of various reasons such as export-oriented growth strategy, RCEP withdrawal by India, among others.

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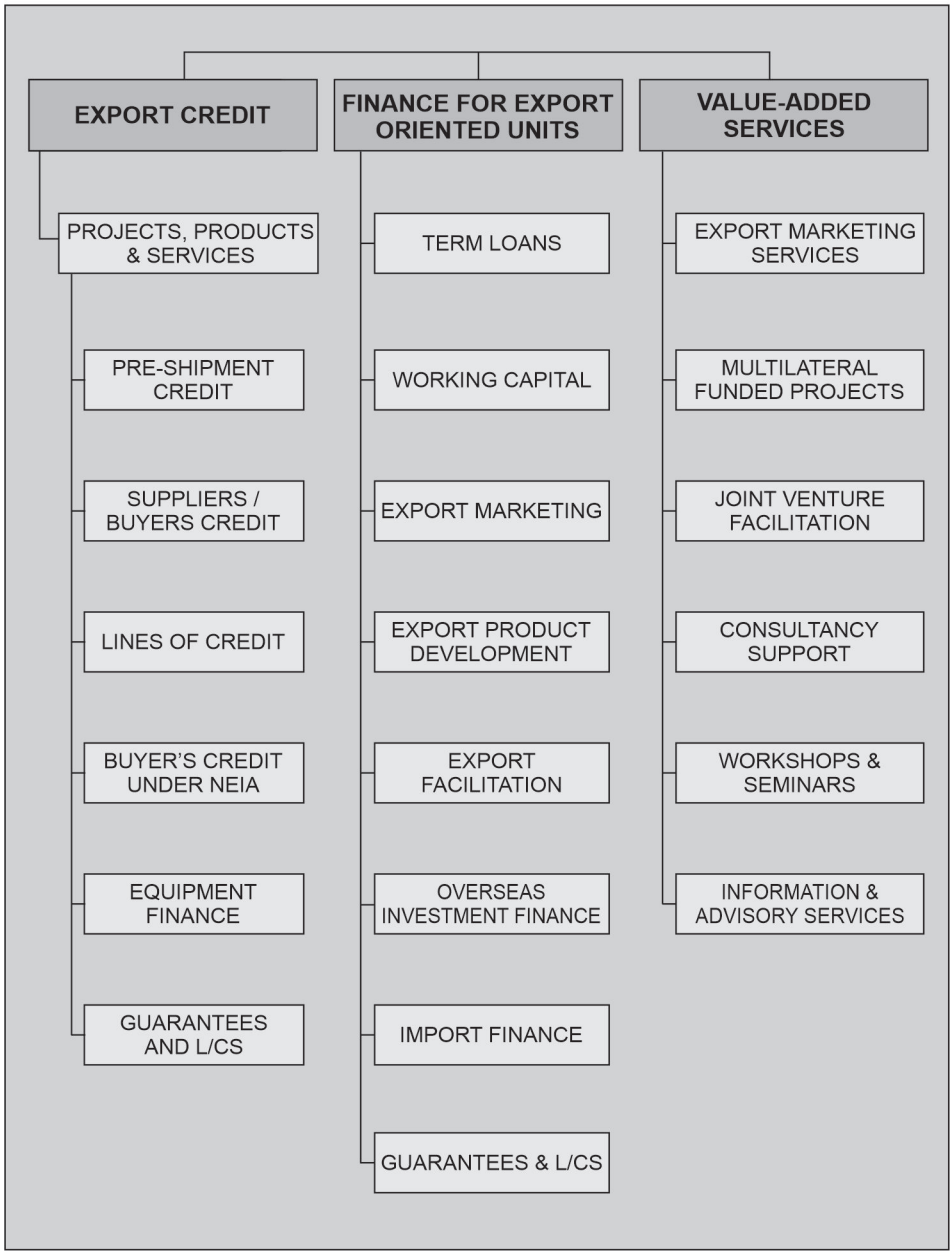

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