Sangeeta Khorana

The FTA: A strategic call for the EU and India?

14

A fresh impetus from both sides is urgently required to reinvigorate EU–India trade talks, which have been languishing for over seven years and have gone through 15 rounds. In September, the Indian commerce minister announced the government's intention to revive talks.[1] However, this followed a blow to momentum in August, when the Indian government postponed a meeting between negotiators due to "disappointment following the EU's legally binding ban on the sale of around 700 pharmaceutical products clinically tested in India".[2] The Indian government questioned the European Union's unilateral ban on Indian drugs, and expressed in no ambiguous terms that it was waiting for a response from the EU.

Fresh talks are expected to focus on industrial goods; agricultural tariffs and services; access to each other's markets for goods and services, and to public procurement contracts; the framework for investment; rules on intellectual property and competition; and commitments on sustainable development issues such as environmental, social, and labour rights.

The proposed agreement is politically and economically crucial for both sides. In political terms, from the EU's perspective the free trade agreement (FTA) with India will be its first with an emerging economy, will support the EU's aim of employing FTAs to foster partner countries' integration into the world economy, and will strengthen its role in global trade governance.[3] From India's perspective, it will boost Prime Minister Narendra Modi's "Make in India" campaign and his ambition to establish India as a regional leader and global

1 "India is interested in reviving FTA talks with EU: Nirmala Sitharaman", the *Economic Times*, 9 September 2015, available at http://economictimes.indiatimes.com/news/economy/foreign-trade/india-is-interested-in-reviving-fta-talks-with-eu-nirmala-sitharaman/articleshow/48890728.cms.

2 Asit Ranjan Mishra, "India cancels EU trade talks over pharma ban", *Live Mint*, 6 August 2015, available at http://www.livemint.com/Politics/JtJwcwhXDZz4c01D9DGk5I/Govt-cancels-trade-negotiatorlevel-meet-with-EU.html (hereafter, Mishra, "India cancels EU trade talks over pharma ban").

3 Sangeeta Khorana and Maria Garcia, "Procurement Liberalisation Diffusion in EU Agreements: Signalling Stewardship?", *Journal of World Trade*, Volume 48, Issue 3, 2014, pp. 481–500, available at https://www.kluwerlawonline.com/abstract.php?area=Journals&id=TRAD2014016.

manufacturing centre. Furthermore, the FTA will strengthen India's attempts to harness its growing domestic economy and middle class to support its rise as a global economic power.

In economic terms, a well-negotiated agreement will boost trade and investment flows between the two regions. The EU is India's largest trading partner and investor as well as its main source of technology transfer. The value of EU–India trade stood at €72.5 billion in 2014, up from €28.6 billion in 2003. Similarly, the EU's investment stock in India increased from €0.78 billion in 2003 to €34.7 billion in 2013. Furthermore, trade in commercial services has increased since the FTA talks were launched – up fourfold from €5.2 billion in 2002 to €23.7 in 2013. For Europe, the economic rationale for the FTA is access for EU firms to a market of over a billion people, which could be a means to escape long-term economic malaise.

There are a host of studies analysing the economic effects of the proposed FTA.[4] The analysis by the Indian government suggests that India will be a net loser from the FTA in terms of the trade in goods, primarily as a result of the loss of revenues from lower or zero tariffs, although gains are expected from liberalisation of the services sector.[5] A report by Sussex University and an Indian NGO – CUTS International – also indicates that liberalisation of trade in goods would yield only ambiguous welfare effects.[6] There are also questions on the

4 See, for example, Agence Europe, C*ouncil's Green Light to Launch of Negotiations for Bilateral Free Trade Agreements with ASEAN, South Korea and India*, 2007; Yvan Decreux and Cristina Mitaritonna, "Economic Impact of a Potential Free Trade Agreement (FTA) between the European Union and India", report by CEPII/CEMIN to the DG Trade of the European Commission, Trade Specific Contract No: SI2.434.087, 2007, available at http://trade.ec.europa.eu/doclib/html/134682.htm; Thom Achterbosch, Marijke Kuiper, and Pim Roza, "EU–India Free Trade Agreement: A Quantitative Assessment", October 2008, Report No: 2008-059, Project code 20824, LEI Wageningen, The Hague, available at http://www.researchgate.net/publication/40095078_EU-India_free_trade_agreement__a_quantitative_assessment; Sangeeta Khorana and Maria Garcia, "European Union–India Trade Negotiations: One Step Forward, One Back?", *Journal of Common Market Studies*, Volume 51, Issue 4, July 2013, pp. 684–700 (hereafter, Khorana and Garcia, "One Step Forward, One Back?"); Sangeeta Khorana and A.N. Asthana, "EU's FTA Negotiations with India: The Question of Liberalisation of Public Procurement", *Asia Europe Journal*, Volume 12, Issue 3, 2014, pp. 251–263, DOI 10.1007/s10308-014-0369-7; Sangeeta Khorana and Nicholas Perdikis, "EU–India Free Trade Agreement: Deal or No Deal", *South Asia Economic Journal*, Volume 11, Number 2, September 2010, pp. 182–206 (hereafter, Khorana and Perdikis, "Deal or No Deal"); Sangeeta Khorana, Nicholas Perdikis, William A. Kerr, and M. Yueng, *The Era of Bilateral Agreements: The EU and India in Search of a Partnership* (Cheltenham: Edward Elgar Publishing, 2010) (hereafter, Khorana et al., *The Era of Bilateral Agreements*); Sangeeta Khorana, William A. Kerr, and Nicholas Perdikis, "Global economies of scale in the EU–India trade agreement: are they the key to a return to economic growth?", *Asia Europe Journal*, 13:41–55 (hereafter, Khorana et al., "Global economies of scale"); Sophie Powell, "The EU–FTA: initial observations from a development perspective", Traidcraft, September 2008, pp. 1–21, available at http://www.indianet.nl/pdf/EU-IndiaFTAInitialObservations.pdf.

5 Trade Agreements, Government of India , Ministry of Commerce and Industry, Department of Commerce, 2012, available at http://commerce.nic.in/trade/international_ta.asp?id=2&trade=i.

6 Michael Gasiorek et al., "Qualitative analysis of a potential Free Trade Agreement between the European Union and India", Executive Summary Report to DG Trade of the European Commission, Sussex, University of Sussex, Centre for the Analysis of Regional Integration at Sussex and CUTS International, Jaipur, available at http://www.cuts-citee.org/pdf/EU-IndiaStudyAnnex1May01.pdf (hereafter, Gasiorek et al., "Qualitative analysis of a potential Free Trade Agreement").

“deep” versus “shallow” effects of the proposed FTA[7] – i.e. whether it will cover only trade in goods, or cover deeper forms of integration such as investment and competition policy – while other analysts focus on the bargaining process and highlight how the different negotiating approaches of India and the EU could impede the progress of talks.[8]

Areas of disagreement

European and Indian expectations diverge on issues such as tariffs on cars, wines, and dairy products imported from the EU, and on the liberalisation of the visa regime for Indian professionals entering the EU.[9] The EU and India have even had trade disputes at the World Trade Organization (WTO) on wine and spirits and on pharmaceuticals. When FTA negotiations began, India had high tariffs in areas of interest to the EU and restrictions on foreign direct investment (FDI) in several sectors, including insurance and trade. Rules on FDI in insurance and wholesale trade and on single-brand retail have since been changed, but tariffs on goods such as wines and cars remain at between 60 and 100 percent.

Both the EU and India have voiced concerns about restrictive measures that function as a barrier to their exporters. Recently, for instance, the EU expressed anxiety over the Indian government’s requirement that 15 categories of IT and consumer electronic products must be registered in the country. A similar issue is mandatory in-country testing and certification of telecom network elements.[10] India has also been affected by EU regulations and standards, especially on agricultural exports. For example, imports of Indian Alphonso mangoes were banned in May 2014 after “non-European fruit flies” were found in some consignments, though this was lifted in early 2015.[11]

7 See Gasiorek et al., “Qualitative analysis of a potential Free Trade Agreement”; Ecorys et al., “Trade Sustainability Impact Assessment for the FTA between the EU and the Republic of India”, report for DG Trade in the European Commission, Reference no: TRADE07/C1/C01 – Lot 1, Rotterdam, available at http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc_143372.pdf.
8 Khorana and Garcia, “One Step Forward, One Back?”; Khorana and Perdikis, “Deal or No Deal”.
9 Khorana and Perdikis, “Deal or No Deal”; Khorana and Garcia, “One Step Forward, One Back?”; Khorana et al., *The Era of Bilateral Agreements*; Khorana et al., “Global economies of scale”; Mishra, “India cancels EU trade talks over pharma ban”; Jan Wouters, Idesbald Goddeeris, Bregt Natens, and Filip Ciortuz, “Some Critical Issues in the EU–India Free Trade Agreement Negotiations”, *European Law Journal*, 20 (6): 848–69, 2013, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2249788.
10 *Trade and Investment Barriers Report 2015*, Report from the Commission to the European Council, Brussels, 17 March 2015, available at http://trade.ec.europa.eu/doclib/docs/2015/march/tradoc_153259.pdf.
11 Antonia Molloy, “Alphonso mangoes: EU lifts ban on Indian mango imports”, the *Independent*, 20 January 2015, available at http://www.independent.co.uk/news/business/news/alphonso-mangoes-eu-lifts-ban-on-indian-mango-imports-9990412.html.

One of India’s key objectives is to be recognised as a data-secure country. At present, India is not considered data-secure under EU legislation, despite India amending its Information Technology Act in 2000 and issuing new Information Technology Rules in 2011, in line with the “safe harbour” principles adopted by the United States. This hampers the flow of sensitive data such as information on patients, and means that Indian firms are unable to gain market access in the EU, increasing operating costs.

Another key Indian objective is reform to allow skilled Indian professionals to temporarily reside and work in EU member states. If rules on movement of professionals were liberalised, Indian businesses would benefit significantly from increased access to the EU services market. However, the EU says it is unable to intervene on this issue because work permits and visas are under the remit of individual member states. A related issue is the differentiated qualifications and professional standards between EU partners, which restrict Indian professionals’ access to the EU markets.

For its part, the EU wants India to first liberalise its professional services sector, specifically accountancy and legal services. However, the Institute of Chartered Accountants of India and the Bar Council of India are vehemently opposed to such liberalisation as they fear competition from overseas accounting and law firms. Secondly, the EU has sought massive cuts in India’s tariffs on automobiles and auto components. Fully assembled cars attract a 60 percent import duty, rising to 75 percent for cars with free on-board value over $40,000 and engine capacity of 3,000 cc for petrol cars and 2,500 cc for diesel cars. The EU sees this as protectionism: by contrast, the tariff on Indian cars imported into the EU is 6.5 percent. However, Indian industry fears that tariff cuts would flood the domestic market with European cars, which could have an adverse impact on investment and on the “Make in India” campaign. There are also fears about auto components being imported into India at concessional rates.

Finally, the EU has sought deep tariff cuts for wines and spirits. India currently levies import duty of 60–100 percent, plus state taxes. Given that alcohol is a major source of revenue, it is not likely that Indian states will agree to cut taxes. The EU also seeks to strengthen intellectual property rights in India. Existing Indian laws do not allow evergreening of patents (extending patents when they are about to expire by making small changes to the product) or data exclusivity, preventing various drugs and chemicals from being sold in India. India argues that if it were to accede to the EU’s demand, the Indian pharmaceutical industry would not be able to sell cheap generic drugs.

The way forward

These problems notwithstanding, the proposed agreement is critical for both the EU and India. Three "mega-initiatives" will eventually dominate the global trade landscape: the Transatlantic Trade and Investment Partnership (TTIP), the Trans-Pacific Partnership (TPP), and the Regional Comprehensive Economic Partnership (RCEP).[12] The parallel negotiations on these mega-agreements have added pressure to raise the pace of the EU–India FTA talks. Should either TTIP or TPP be finalised in the absence of an EU–India FTA, Indian goods may face difficulties in accessing European markets. The mega-regional initiatives encourage the creation of global value chains in which production is split across countries to exploit each nation's comparative advantage, driving down costs while raising standards. At present, India is hardly integrated into the value chains of European companies, and the mega-agreements could divert investment away from non-members, with potentially devastating effects for India.

The FTA is also important for India from the perspective of investment flows and technical cooperation. The EU's assistance would enable European companies to help India in its plan to develop 100 "smart cities" in the near future, as well as helping other Indian initiatives.

To agree on the FTA despite the differences between the EU's and India's negotiating agendas in a tough economic climate, both partners will need to show the same determination as others have shown in negotiating mega-regional agreements. The challenges and constraints are not insurmountable. Given both sides' reluctance to agree to the other's demands, they should begin by negotiating less difficult sectors. This will demonstrate willingness to get back to the negotiating table and send a clear signal that both sides want to talk further. It is important for India to overcome its siege mentality, commit to institutional reform, and confront domestic vested interests. Reaching an agreement that will bring mutual benefit to both the EU and India will be a long journey, but, despite several missed deadlines, it is not out of reach.

12 The Regional Comprehensive Economic Partnership is a mega-regional trade and investment agreement between ASEAN and its regional partners – Australia, New Zealand, China, South Korea, Japan, and India. It proposes to create a 16-country integrated market in the Asia-Pacific region of around 3.35 billion people, with a combined GDP of $21.4 trillion or 27 percent of global GDP. Negotiations are expected to be concluded by the end of 2015.