How India’s decision to not join major trade pacts can help its aim of being a $5-trillion economy

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Synopsis

The government has decided that it would be best not to be a part of multilateral trade agreements with major economies in the region. Instead, it is on a FTA-signing spree with a host of countries. Is this approach the right way for a nation that has ambitious economic goals?

The government is keen on making the country a global manufacturing hub and a key player in the global supply chain. While it has announced several initiatives towards this goal, its decision to not be part of multilateral trade agreements has raised eyebrows.

On November 15, 2020, 15 member countries from the Asia-Pacific — accounting for nearly 30% of global GDP — signed the Regional Comprehensive Economic Partnership (RCEP) and became the world's largest trade bloc. It was positioned as a pact that would foster trade ties between the Asian nations. RCEP was meant to broaden and deepen member countries' economic linkages and connectivity with the region, open opportunities and offer preferential access into growing markets in the region.

On March 8, 2018, 12 economies in the Asia-Pacific signed the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). It created a trade bloc that accounted for 15% of the world's GDP. The agreement gave signatory countries easier access to each other's markets and reduced tariffs on trade on a vast majority of items.

India took a decision to not join either trade pacts. In fact, the government had walked away from the RCEP talks in November 2019, saying it had to protect its domestic economy from an influx of cheap Chinese products that the agreement would facilitate. Similarly, India decided not to join the CPTPP when it came into force in 2018, citing issues related to data localisation and environmental standards.

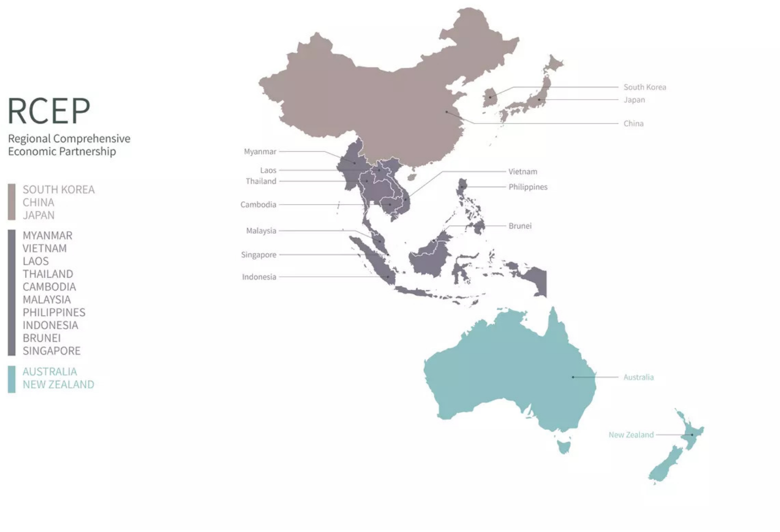
By not being part of major trade pacts, which carry a lot of clout, will India's ambition of becoming a $5-trillion economy lose steam? After all, it is the flow of raw materials and goods to and from various geographies that leads to manufacturing of various products, more trade and faster growth.

Experts, however, contend that while India may not have joined the trade pacts, it has its strategy on point to become a bigger player on the global stage. By increasing its engagement through foreign trade agreements (FTAs), instead of these trade pacts, the country is looking at expanding its trade and investment potential.

"India's reluctance to join these pacts comes from an informed space of finding stronger grounds via bilateral trade ties where it may find more muscle and, at the same time, flexibility to negotiate crucial deals," says Adarsh Sharma, Managing Director, Primus Partners, a management consultancy.

Supply chains

Other experts agree with the argument that for India, bilateral FTAs are a better bet than multilateral trade pacts for now. They point out that being a part of global supply chains is the winning card when it comes to economic growth. Large and small companies use these channels to supply raw materials to big manufacturers and to take finished goods to customer markets. Some experts say CPTPP and RCEP do not help India become a part of global supply chains.



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15 member countries from the Asia-Pacific — accounting for nearly 30% of global GDP — make up the Regional Comprehensive Economic Partnership (RCEP).

Senior economist and NITI Aayog member Arvind Virmani says FTAs are more critical for India to be an intrinsic part of global supply chains. “For instance, Japanese supply chains have already been established in Southeast Asia so it becomes very difficult (for India to have a dominant role here). Even if India joins these pacts, it will be a small player. That has been the experience. They (Southeast Asian nations) are already integrated while we are way behind,” he says.

The senior economist suggests that we take efforts to get into supply chains as opportunities still exist with the European Union and the United Kingdom, unlike in Southeast Asia. “Policies like PLIs (production linked incentives) and FTAs are the right steps in this direction. Many of these supply chains, at least in developing countries such as Vietnam, have an FTA with the EU. This gives them access to markets for goods like electronics, which are at zero duty. So, they immediately get a 12.5% advantage over India. So, if we have an FTA with the EU, this differential will go away and we can compete on equal terms,” he says.

Another reason India did not join the RCEP is that it would have given China access to the domestic market. It would have allowed Chinese companies to flood the Indian market with cheap goods, making it tough for domestic manufacturing to be innovative or grow.

Virmani links this to giving the Chinese a backdoor entry. “I do not think there is any value to India joining the RCEP. It would just be a way of having an FTA with China, which we have consciously decided not to as we do not want to be dependent.”

It is important for India to reduce its dependence on China for trade and strategic reasons. Many other countries have also expressed similar views.

Virmani says: “China has a monopoly. For example, in both automatic data processing (ADP) and in the telecom sector, it has 40% of the global market which is huge in itself. What India and the world really needs is the diversification of sources for many manufactured goods.”

Alluding to such concerns, Prime Minister Narendra Modi had at the RCEP Summit in Thailand in 2019 stated that the pact did not cater to the interests of India. “Today, when we look around, we see during seven years of RCEP negotiations, many things, including the global economic and trade scenarios, have changed. We cannot overlook these changes. The present form of the RCEP agreement does not fully reflect the basic spirit and the agreed guiding principles of the RCEP,” he had said.

In the case of the CPTPP, issues relating to intellectual property regulations and labour standards cropped up, and India decided against joining the pact.

Virmani says India can consider joining CPTPP as it does not have China. Other experts have also expressed similar views.

Arvind Panagariya, professor at Columbia University, & Former Vice-Chairman, NITI Aayog, had said that there was good reason for the country to consider joining the CPTPP. He tweeted that while India has numerous advantages over competitors in the China+1 race, the disadvantage was an insufficient engagement with Asia. “It must seriously study the pros and cons of entry into the CPTPP.”

Panagariya had told The Times of India that India was unlikely to consider RCEP since China was a part of it. “This leaves only two main avenues to deepening the engagement with Asia: strengthening the existing FTA with the Association of South East Asian Nations (ASEAN) and seeking the membership of CPTPP,” he had stated.

The FTA strategy

Experts say trade pacts need to be viewed differently now than earlier, given the evolving economic prowess of India. Strengthening the FTA game plan, some say, would lead to more gains for India in the long term.

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Discussions are now underway for FTAs with the UK, EU, and Canada.

“India can negotiate and implement an FTA with preferred nations rather than a bloc of nations. An independently negotiated FTA would be a boon for domestic manufacturers (shielding them from cheap imports) and would keep the end customer in mind and priority,” says Ramendra Verma, Partner and Government Sector Leader at Grant Thornton Bharat.

India, incidentally, has been on an FTA-signing spree. According to a PIB release, the country has signed 13 Regional Trade Agreements (RTAs) or FTAs with various countries over the past few years. Last year, the Comprehensive Economic Partnership Agreement (CEPA) with the UAE came into being. The bilateral trade between India and the UAE touched “historic highs” during FY 2022-23, according to the PIB. “During the CEPA implementation period (from May 22 to Mar 23), bilateral trade increased from $67.5 billion (May 21-Mar 2022) to $76.9 billion (May 22-Mar 2023) – an annual increase of 14%,” it noted.

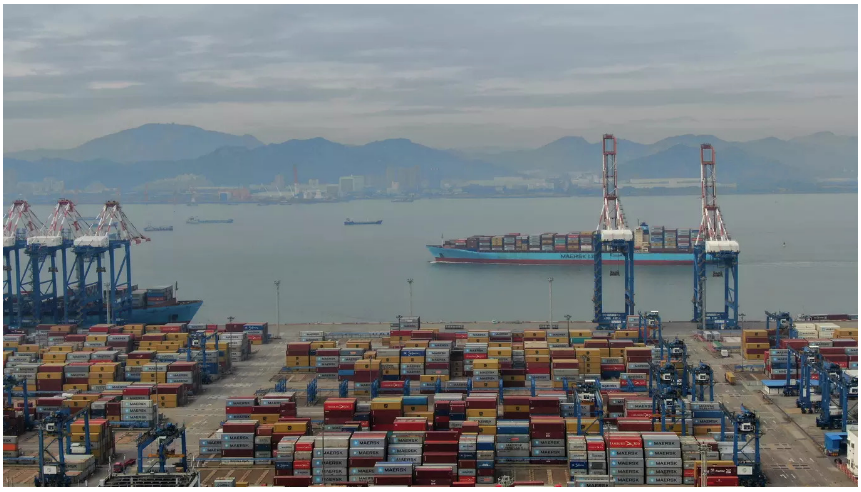
Besides this, the Australia-India Economic Cooperation and Trade Agreement (ECTA) came into effect on December 29, 2022, making over 85% of Australian goods exports to India and 96% of imports from India by value tariff free. Discussions are now underway for FTAs with the UK, EU and Canada.

Through FTAs, India plans to boost exports to large markets and move closer to its goal of $1-trillion exports by 2030.

While discussing these FTAs, India should ensure that there are no slippery grounds.

Development economist Santosh Mehrotra says, “At this juncture, let’s negotiate our three FTAs which are currently under negotiations, but properly. We need to make sure that our future interests of both exports as well as domestic manufacturing are safeguarded.”

Explaining his point further, he states that India’s experience with FTAs has not been too great in the past. This, he adds, has primarily been because we have been importing a lot from such countries while not exporting as much to them. “This approach has not allowed our own manufacturers to grow, rather it has fostered the manufacturing sectors of partner countries instead. We never prepared ourselves in the way that we should have,” he adds, without mincing any words.



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India has decided to focus on bilateral trade ties where it may find more muscle and, at the same time, flexibility to negotiate crucial deals.

The FTAs which India signed in the past decade, such as with ASEAN, Republic of Korea, Japan and Malaysia, have not played out in India’s favour. In fact, Commerce and Industry Minister Piyush Goyal recently said India’s free trade pact with the Asean was the “most ill-conceived”. He had also observed that even though India had opened its markets for Japan and Korea, exports to Japan had not grown “at all” but imports from that country had jumped 200%.

The way from here

So, what really is the way forward for India to up its game and achieve its economic aspirations?

Virmani says that joining trade pacts will not really help unless domestic reforms are also simultaneously introduced. “You cannot benefit unless the tax system and bureaucracy is simplified. It is not magic – it has to be complementary. While reforms such as GST have come in, a lot more remains to be done. If small companies are trying to match quality and time schedules to compete with their counterparts which have been in business for 30 years, they don’t have time to waste on such aspects. We can’t forget the ease of doing business. A lot remains to be corrected,” he says.

The senior economist also suggests that care be given to a key area that can emerge as a dominant advantage for India: skill development. “In 20 years, we can be the top country in value chains, if we skill our people. This is what we have to do if we want to dominate value chains, eventually. It is about labour-intensive parts of the production chain where we can find a stronghold and generate more jobs," he adds.

Experts say infrastructure development, Intellectual Property Rights (IPR) protection, policy consistency and predictability can help India enhance its competitiveness. And addressing issues here will clear a way for more investments.

With "de-risking" being the buzz word for supply chains in a post-pandemic world, such a strategy may help India carve a more advantageous niche for itself in the long run.

BY

Neha Dewan
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"Yes, pharma companies in India follow what is called 'dual track manufacturing'," says Dinesh S Thakur, a public health activist who has co-authored a book detailing the manufacturing, dispensing, selling and regulation of drugs in India. "They run one facility that complies with the standards required to sell drugs in the US and Europe, while operating a different facility that manufactures the same drugs for India and for poorer, less regulated countries like the Gambia. In most cases, the facility making drugs for India will be of a much lower standard compared to the one that makes drugs for the US."

Too big to ignore
India exports almost half of the drugs it makes. According to the data, roughly 54% of the exports go to developed countries, 35% to developing countries and 11% to least-developed countries.