India can be a part of the Regional Comprehensive Economic Partnership (RCEP)only if the issues it has raised are addressed

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"Despite India's willingness to join the RCEP and its perceived benefits over the long term, members' aversion to addressing its chief concerns forced its hand. It must be emphasised that Indian industry is not afraid of a lower tariff regime"

Over the years, India has been a willing partner in expanding trade amongst its emerging economic peers, most notably in it's 'Look East Policy'. But unlike in the past, the government has stood firm in its position on the conditions for joining the RCEP. It has been consistent throughout on its stance, and when it became clear that the domestic interests could be compromised, India had no other option but to opt-out. But given the importance of such a major regional trade agreement, India quite rightly has kept the door open to joining at a later date, provided unresolved issues are duly addressed.

Government's concern is right

Amongst RCEP members, India already has an FTA (free trade agreement) with ASEAN, Japan and Korea. If we look at only merchandise trade, India's trade deficit with the bloc has doubled from $55 billion in 2010-11 to over $105 billion in the fiscal, which is almost 60 per cent of India's overall deficit. With ASEAN it has increased over four-fold. This is without other RCEP partners China, Australia and New Zealand being part of any trade deal with India. Any move to lower tariffs post-RCEP could worsen India's trade balance, at least under the current terms, where many crucial concerns of India remained unresolved.

Were India's concerns justified?

China quite obviously was the elephant in the room, as it already accounted for over half of this trade deficit with the RCEP bloc, and that too without current offers on the table. As per the deal, India had to reduce duties on 80-90 per cent of trade items for all member countries, including China.

Even if that entailed a phased reduction over 25 years from China, less than stringent rules of origin could have allowed Chinese manufactured goods to be routed via other countries to India. This could have led to a surge in imports, hurting interests of the domestic industry.

India also faced a big threat to its dairy industry from New Zealand, as over 90 per cent of dairy products from that country are exported. India, the world's largest milk producer is already quite self-sufficient in its dairy needs, and any surge in imports could have led to a supply glut, which would pull down prices, much to the detriment of around 100 million farmers engaged in the dairy business.

Despite the current growth slowdown in India, the fundamentals remain strong. International Monetary Fund estimates show global growth would increasingly come from India – its contribution would increase to 15.5 per cent in the next five years vis-à-vis falling share from others, including China and other Asia-Pacific nations. Hence, the current juncture was not conducive for joining the bloc, as there was a strong apprehension of dumping across sectors, arising from excess capacities in other countries. India's concerns are, therefore, not entirely unreasonable.

India's concerns were not duly addressed

Till the last moment, India had hoped to be part of the RCEP, provided its concerns were adequately addressed. India wanted to safeguard the interests of the domestic industry, and not jeopardise its 'Make In India' programme. Under this programme, the government had revised its customs duties for certain products, e.g., electronics, and thus rightly wanted the base year for tariff reduction to be moved to 2019. But members insisted on 2014, which essentially meant India had to move duties back to 2014 levels.

This would have jeopardised the investments already made and the desire to encourage domestic manufacturing in these industries. India also wanted an auto-trigger mechanism, which would have allowed raising tariffs against any surge in imports beyond a threshold. Another issue was exemptions from 'Ratchet obligations', which prevents signatories from going back from accepted offers if in future the situation demands so. As these issues remained unfulfilled, it forced India's hand.

Indian FTA utilisation also constrained by non-tariff barriers/ measures

Studies have shown that India had benefitted little from the FTAs, most notably with the ASEAN. According to a recent review by an inter-ministerial group, India has utilised only six per cent of its current FTA with ASEAN against 36.3 per cent utilisation by ASEAN countries. In other words, ASEAN countries have utilised the FTA six times more than India. While the decline in average tariffs by India was from over 11 per cent to only 4.3 per cent, the corresponding tariff reduction by trading partners was only 200 bps for India's exports. Such lowering of import duty by India is an important reason for the rising trade deficit. For example, only nine per cent of India's auto components' export goes to ASEAN while ASEAN corners 15 per cent of India's auto-component imports. Any further lowering of tariffs would severely impact the trade balance in the sector. Besides, lowering of import duty has resulted in an inverted duty structure, which has caused it to lose share in the domestic market.

The tariff liberalisation for ASEAN has affected agri-trade too, specifically spices, where import of poor quality pepper from Vietnam is severely affecting the Indian pepper market since pepper from Vietnam has high pesticide residues. There are many examples from other sectors too – steel, textiles, paper, tyres, pharmaceuticals etc.

Non-tariff barriers/ measures (NTMs) is a major factor constraining India's exports to the region. In fact, NTMs have become more restrictive than the existing tariffs, inflicting higher transaction costs and thus negating the effect of periodic reduction in applied tariffs. China leads the way with one in every ten NTM imposed globally and one-third coming from other RCEP members.

Non-tariff barriers/measures imposed by ASEAN countries have adversely impacted India's agri-trade, as over 83 per cent of Agri trade is covered by at least one NTM, and an average product facing seven to eight separate NTMs. No wonder more than a third of India's imports are from the RCEP bloc, while India's exports were only 20 per cent to this region. The NTMs were one of the reasons why India was unable to gain ground in exports despite the rupee depreciating by over 55 per cent during the past decade. This also explains why even after eight years of Indo-ASEAN FTA, India has not been able to significantly increase exports to this region, including CLMV countries. Any improvement in exports during this period, thereby, can be attributed to product and destination diversification rather than trade agreements.

The Way Forward

Despite India's willingness to join the RCEP and its perceived benefits over the long term, members' aversion to addressing its chief concerns forced its hand. It must be emphasised that the Indian industry is not afraid of a lower tariff regime. However, it faces an uneven playing field due to various factors, such as higher cost of capital, logistics costs, inflexibility of labour, higher time taken for land acquisition and environmental clearances, higher compliance costs etc.

While improving India's competitiveness remains a top priority, we must also engage with our trading partners to lower trade costs owing to NTMs, for which NTMs must also be part of trade agreements. It is also important for industry to improve its standards, as on an average only ten per cent of imported products follow BIS regulations, whereas the compliance is 70 per cent in Europe.

For India this needs to be increased to at least 40 per cent. In fact, international standards must be used wherever possible instead of the discretion of importing countries. Moreover, the government could also make it mandatory for importers to register, as it has done for steel imports with the Steel Import Monitoring System for some specified steel products (where there is increasing threat of import surge).

Nonetheless India remains committed to its stance on free trade and has kept its options open to join the RCEP at a later date, as soon as its legitimate concerns are duly addressed by other members.

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