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The Political Economy of EU-India FTA

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The proposed free trade agreement being negotiated between India and the European Union is due to be the first of its kind and may start a new generation of trade liberalisation as India is new to sign such an agreement between a developing country of South Asia, on one hand, and a group of developed countries of Europe, on the other. The contentious issues of negotiations include labour mobility, financial sector liberalisation, production of generic medicines, patent issues etc. This Briefing Paper focuses on these issues and argues that signing of a free trade agreement is not only an economic issue but also has political aspects.

Introduction

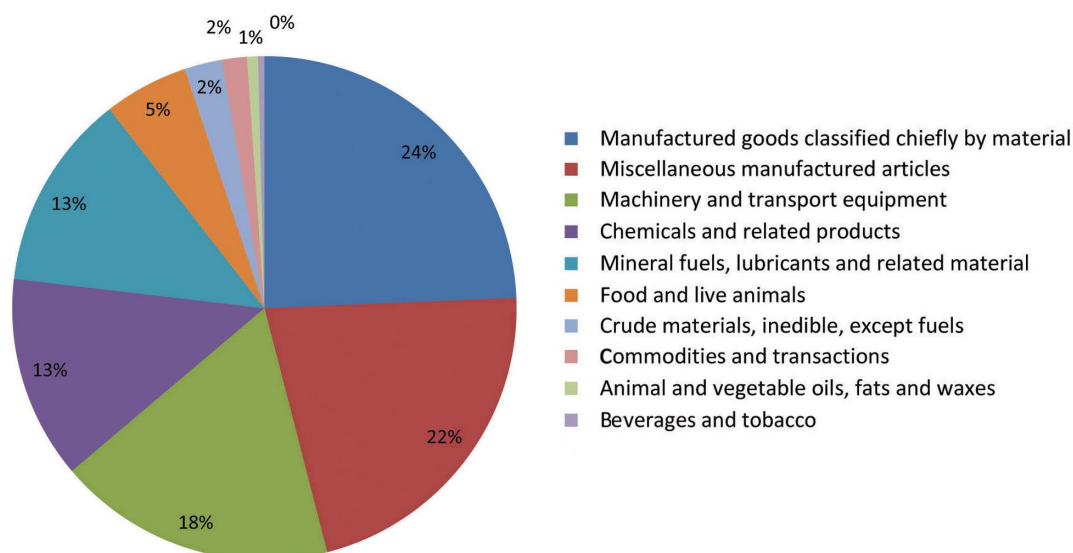
The European Union (EU) is India's one of the largest trading partner with a total trade value of around •80bn in 2011 and with an investment source of around •3bn in 2010, that is why India has sufficient reasons to be concerned about the delay of the proposed free trade agreement (FTA).¹

The EU is not only a source of investment for India or a centre of trade but has also become a major destination of overseas acquisition for many Indian companies in the past few years such as Jaguar & Land Rover, Corus (now owned by TATA), and

Schoneweiss & Co. Gmbh (now part of Mahindra and Mahindra). This has further strengthened the need for cooperation between the two partners. From the political point of view India is also a major assistance provider to Afghanistan where both EU and India wants to sustain democratic government. Both India and EU fights with Somali pirates in the Indian Ocean for smooth flow of trade through sea.

Figures 1 and 2 show that EU and India is partner in a number of products ranging from manufactured goods to crude material. With the help of FTA, India is not only looking to strengthen its economic potentials but

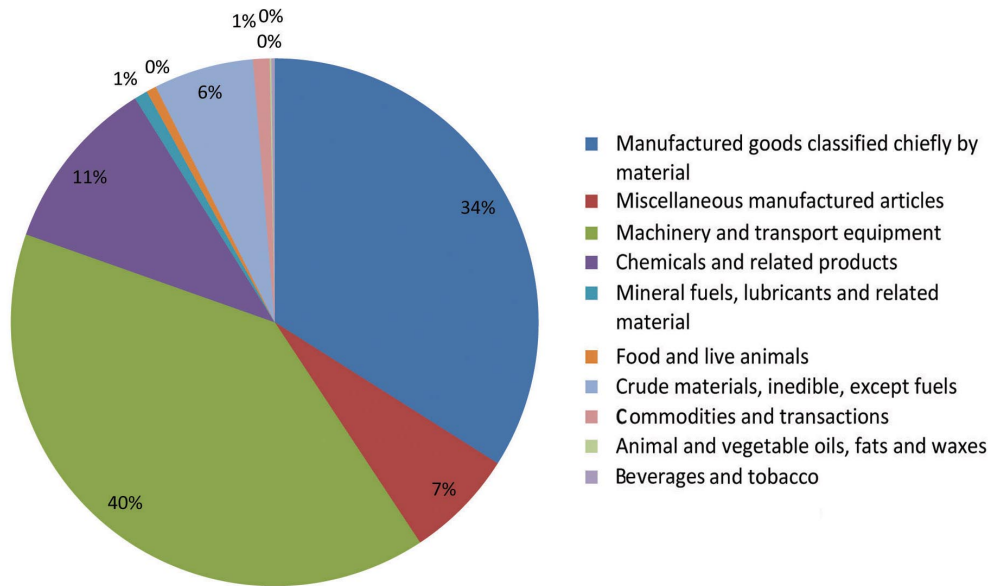
Figure 1: EU Imports from India (share of total %)



Source: Eurostat 2013

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Figure 2: EU Exports to India (share of total %)



Source: Eurostat (2013), "India-EU Bilateral Trade and Trade with the World", URL: http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113390.pdf.

also wants to get a strong political and military ally on its side. For long, India is claiming for a permanent seat in the United Nations Security Council (UNSC) and for that it needs European backing. It also wants a strong support from a potential China threat and a long term seller of arms to modernise its army.

If signed, FTA can benefit Indian industries, such as pharmaceuticals, textiles, gems and jewellery. It is hoped to increase foreign investment by the EU in India particularly in financial and defence sectors. On the other hand, EU is keen on the FTA because of India's fast economic growth which is coupled with an increase in the purchasing capacity of middle-class population, harmonised trade portfolio and untapped market opportunities especially in Financial and Automobile sectors.

In 2000, Indian Prime Minister Atal Bihari Vajpayee attended the 1st India-EU Summit in Lisbon to start new chapter on India-EU trade relations. The main purpose of the Summit was to give political and diplomatic shape to the changing nature of economic relations between the two partners. The European Commission (EC) issued a policy document entitled, *Global Europe: Competing in the World* in 2006 that identified India as a key FTA partner.² In 2006 at the 7th Summit at Helsinki, proposals of the "High Level Trade Group" to work on a broad-based Bilateral Trade and Investment Agreement (BTIA) popularly called FTA was principally accepted. Following that, negotiations for EU-India FTA were launched in June 2007 in Brussels, expected to be over in two years.

This FTA was earlier decided to be signed in December 2012 but as there is a deadlock on various issues in negotiation from both sides it has missed deadlines and a very little progress has been made after that. Following are some of the issues that have posed deadlock in the negotiation:

Negotiating Issues

Firstly, with the help of FTA, the EU seeks to achieve liberalisation of the Indian banking and financial sector, well beyond what has been achieved under General Agreement on Trade in Services (GATS) framework. The EU, particularly the UK, Germany and France are seeking market access and export gains for their large banks and financial institutions through cross border credit supply, national treatment commitments and direct investments. They have sought removal of regulations pertaining to bank branches, numerical quotas, foreign ownership, equity ceilings, voting rights and investments by state-owned companies in foreign banks in India. The EU is also demanding removal of priority sector lending requirements, borrowing limits and other regulatory measures. The EC's *Trade and Investment Barriers Reports 2012 and 2013* identify that only a limited positive movement has been seen in the area of financial sector in India particularly in equity caps.³

Secondly, disagreement between India and the EU also goes further on core issue of Indian custom duties on European products, such as automobiles and alcohol. Duties on manufactured goods have been reduced on

the Indian side except for automobiles and alcohols. There is a stalemate on reducing duties on passenger cars to 10 percent from the comfortable, protectionist 100 and 150 percent on new and used cars respectively. Indian automobile industry fears a further loss in competitiveness if important duties are slashed, given the already high costs of inputs due to inflation and the rupee's depreciation against the dollar. India's auto parts industry also suffers from the cascading effects of various taxes. This industry employs thousands of small scale units and risks being thrown out of the market if duties are reduced. The scale of auto parts manufacturing is much bigger in Europe, which makes the sector more competitive because of economies of scale.

Another contentious area is the liberalisation of the EU visa for mode 4 services. India is demanding flexible regulations and easy visa requirements for its professionals such as IT, which are in high demand in Europe. But Europe is facing unemployment problem due to fiscal crisis and opposing easy movement of persons. The contradiction is also on identifying the education and other parameters for skilled and semi-skilled workers category. India seeks to get a data secure status for its IT sector to increase IT/BPO/KPO capacity in Europe. Because of its lack of data-secure status, India currently has no access to intellectual property or other sensitive information, such as patient records required for telemedicine from EU countries. As per the EU law, outsourcing business with countries that are not data secure has to fulfil strict requirements which restricts EU companies to carry out business with India.

India is apprehensive about the implications of Registration, Evaluation, Authorisation and Restriction of Chemicals Substances (REACH) framework on their market access for chemicals, dyes, etc. in the EU. Under these regulations, each and every chemical to be imported to EU has to be registered in advance and the cost of this registration is very high. This cost is prohibitive for small and medium exporters of India and would make products of large producers also uncompetitive in EU market.

Provisions in the intellectual property (IP) and investment are of concern from a social perspective as they would limit the capacity of a country to use the public health safeguards in the WTO Trade Related Aspects of Intellectual Property Rights (TRIPs) agreement. The TRIPs-plus IP protections, including data exclusivity and TRIPs-plus IP enforcement measures would compromise India's capacity to supply generic versions of medicines. These provisions threaten access to affordable

medicines for poor people not only in India but also in other developing countries as India is a major supplier of generic medicines.

Strict Sanitary and Phytosanitary (SPS) standards of EU do not allow import of Indian dairy products. These NTBs imposed by the EU are protecting their dairy sector. Apart from that the farm size is very large in Europe with more than 500 cows per shed whereas in India normal farmers have 2-3 animals per shed. Getting farm certification which is normally demanded by EU under SPS measures is not possible in India as most of the farmers are marginal and small.

The EU is demanding for the inclusion of geographical indication (GI) in the FTA negotiation. The EU has already identified more than 700 GIs from Europe for food and agricultural products. For EU, GIs are a means to secure market access over agricultural products.

The EU has also demanded detailed articles on expropriation in the investment negotiations. This would allow it to seek redress for damages for any alleged breach of investor protection rights by the India. The provisions for investor protection in the proposed FTA may obliterate the judicial sovereignty in India which would otherwise have jurisdiction in these matters. There have been cases when investor state disputes, leading to states being dragged to international arbitration councils and sued.

Negotiations are also struck on the issue of Indian policy on government procurement. Although, the EU has narrowed its demands to Central Government purchases, but India is unwilling to give up as it considers government procurement a sensitive issue from the development perspective. But given the large corruption in India's procurement system it might be beneficial to negotiate with more open mind on this issue.

Recommendations

Though there is a deadlock over a number of issues and little progress has been made yet, there are possible ways and sufficient reasons to signing this FTA. These include: India has signed a number of FTAs with other Asian countries, such as Japan, South Korea, and South Asian Free Trade Area (SAFTA) in South Asia and with ASEAN which is yet to provide long-term sustainable benefits to the country.⁴

However, whether a FTA outside of Asian boundaries will benefit India has not been studied widely as these

have not been concluded before. Most of previous FTAs were signed between the developing countries but this time it is between a group of developed countries, on one side, and a developing country, on the other. India is new to signing bilateral FTAs outside Asia that is why it may expect to get substantial benefits in some of its core sectors.

Apart from that, this FTA is not only comprehensive in nature but also can even boost India's international image as an emerging economic powerhouse particularly in the Western world. The recent visits of French President, Francois Hollande and British Prime Minister, David Cameron to India should be seen in the context. These diplomatic moves present the reality of the shifting global balance of power.

The EU is also recognising India's potential role in Afghanistan post 2014, when the North Atlantic Treaty Organisation (NATO) forces plan to leave South Asia. This would be an implicit acknowledgement of the change in India's image.

Studies conducted by CUTS International shows that for the EU, the social impacts of this FTA would be minimum, with no impact on wages, and only minor labour displacement, while for India there would be an increase in wages of skilled and unskilled workers of 1.7 percent in the short run and 1.6 percent in the long run, as well as some labour displacement in the direction of better paying jobs.⁵

India has a social responsibility to make generic drugs and protect its citizens from high cost patented drugs of European companies. India needs to assert that it cannot go beyond the parameters of the TRIPs agreement governing patent system in the negotiations.

From Indian point of view, the investment provisions should be relaxed and not include investor to state arbitration mechanism. Indirect expropriation and fair and equitable treatment should be precisely and narrowly defined to protect legitimate government regulations in support of public health, access to medicines and other public interests from challenge by foreign investors. Public interests at large must be safeguarded in negotiating FTAs by both the partners.

To include transparency in negotiations all existing negotiation documents and government commissioned studies must be made public. Current proposals from both sides must be debated and discussed in the parliament, with state governments and with civil society organisations (CSOs). It is also necessary to undertake new studies that expressly take into account the impact of the FTA, in particular on labour standards, consumer protection, informal economy, agriculture, and generic medicines.

In Lieu of a Conclusion

In this context, India and the EU should start careful but speedy dialogue that must go beyond norms setting and leads to concrete action. It will require balanced economic bargaining and broad political alignment. In this context, the India-EU security dialogue which is happening since 2006 can be taken as an example.

An FTA is favourable for both partners but it has to be finalised soon despite the economic and political challenges. Continuous deadlock on negotiations poses a challenge for political class from both the sides in their efforts to justify the status of India-EU strategic partnership.

Endnotes

- 1 European Commission (2013), "India-Trade", <http://ec.europa.eu/trade/policy/countries-and-regions/countries/india/>.
- 2 Two key economic criteria for new FTA partners were identified in that document: market potential and the level of protection against the EU export interests. India, Russia, ASEAN, Korea, Gulf Cooperation Council and Mercosur made entry in the direct interest to the EU based on these two criteria (see the report on: http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130370.pdf).
- 3 European Commission (2013), "EU Reports on Fight against Protectionism", <http://trade.ec.europa.eu/doclib/press/index.cfm?id=878>.
- 4 Chatterjee, Bipul and Purna Chandra Jena, (2013), "India Needs a Better Deal from Trade Pacts", Business Standard, 06 March 2013; and also see Purna Chandra Jena (2013), "India Gets the Wrong End of Trade Deals", Business Standard, January 08, 2013.
- 5 ECORYS, CUTS and CENTAD (2009), "Trade Sustainability Impact Assessment for the FTA between the EU and Republic of India", http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc_143372.pdf; and also see CARIS and CUTS (2007), "Qualitative Analysis of Potential Free Trade Agreement between the European Union and India", http://trade.ec.europa.eu/doclib/docs/2007/june/tradoc_135112.pdf.

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