

## Report of the Interactive Meeting

# *Challenges and Opportunities from a Possible India–EU FTA*

*New Delhi, November 08, 2006*

### Introduction

CUTS Centre for International Trade, Economics & Environment (CUTS CITEE) in collaboration with The Centre for the Analysis of Regional Integration at Sussex (CARIS), UK, organised an interactive meeting **Challenges and Opportunities from a Possible India-EU FTA**, at India International Centre, New Delhi on November 08, 2006. The meeting is part of a EU commissioned project, “*A Qualitative Analysis of a Potential Free Trade Agreement between the European Union and India*”. Details of the project are available at <http://www.cuts-citee.org/EUIndia-RTA.htm>

As apart of the project work, researchers from India and EU tried to assess the qualitative and sectoral aspects of a free trade agreement (FTA) between India and EU, and in particular investigated more in depth the non-tariff and regulatory issues regarding trade in goods, services and investment. The meeting focused on, *inter alia*, the following issues:

- Sanitary and Phyto-sanitary (SPS) Measures;
- Technical Barriers to Trade (TBT);
- Government Procurement (GP);
- Investment; and
- Services.

### Objectives

To provide a better understanding of the key constraints to trade and investment between EU and India;

To shed light on area which will be particularly important to address in the context of future possible agreement; and

To enable the participants to provide suggestions and broad recommendations in areas that would help negotiators to better understand India and EU’s relevant concerns.

### Participations

The interactive meeting was attended by 40 participants comprising of the project partners, policy makers, researchers, business representatives and other professional experts.

### Inaugural

In the inaugural session, extending a warm welcome to the participants, Mr. Pradeep S Mehta, Secretary General of CUTS started off the meeting by introducing the special guests –



From Left: Pradeep S Mehta, Secretary General, CUTS International; Francisco da Camara Gomes, Head of Delegation of the EC in India; Rahul Khullar, Additional Secretary, Department of Commerce, MOC&I, India; Jim Rollo, Programme Director, Sussex European Institute, University of Sussex, UK.

His Excellency Mr Francisco da Camara Gomes, Head of Delegation of the European Commission to India, Bhutan and Nepal; Shri Rahul Khullar, Additional Secretary, Department of Commerce, Ministry of Commerce and Industry; and Dr Jim Rollo,

Programme Director, Sussex European Institute, University of Sussex, UK.

Initiating the discussion on the possible India-EU FTA, Mr. Mehta said that high-level trade group of India and EU nations has decided at Helsinki meeting in October 2006 that an FTA should be in place between India and EU. He informed that the proposed FTA is expected to be comprehensive in nature with mandate of deeper integration in form and would cover broader issues in trade and investment. He cited that one of the plausible reasons for initiation of India-EU FTA discussion might be the impasse in Doha Round of negotiation under World Trade Organisation (WTO).

While presenting his view further, Mehta said that if we look at the recent history we will find that though multilateral trade agreement is in place, almost 200 FTAs/RTAs have been adopted across the world since WTO came into being in 1995. However, both India and EU is outlier in the sense that FTA would be mostly formed for economic necessity than for political necessity, that has been generally the cause for FTAs between geographically contiguous countries. While highlighting the state of India-EU trade, he said that current trend in trade and investment is good, and EU has been the biggest trade partner of India representing almost 80 percent of India's foreign trade. Besides, EU has also been the largest provider of foreign direct investment (FDI) to India, he added. However, EU's share of trade with India is only two percent of its total trade.

Mr Francisco da Camara Gomes, while commenting on the fact, said that India's trade with EU is 80 percent of its total trade and EU is the largest provider of FDI to India, but EU's trade with India is only two percent of its total global trade and also India's share in inward FDI of EU is extremely small. However, there is tremendous potential of EU to increase its trade and investment to India. Much needs to be done to increase trade and investment between India and EU. He further informed that in the last summit in Helsinki both India and EU got a mandate stated by heads of government from both sides to start negotiation at the earliest. He said that there would be a timetable of activities and both sides need to report what progress has

been made for the negotiation in next summit to be held 2007 in New Delhi. Meanwhile this gives a political and moral obligation for negotiators to make progress in the negotiation.

Addressing the stakeholders, Mr Gomes said that inputs and intellectual reflection of different trade related persons are very important well before the negotiation starts. But after the negotiation were started, any further suggestions will come as post mortem, which though will be intellectually very gratifying, but probably might not be useful in terms of making progress of the FTA negotiation. So, he lauded the importance of the interactive meeting, as it cordons participants to bring in some reflections on the table so that negotiation could progress.

Mr Gomes further stated that both India and EU are deeply committed to the WTO framework negotiations, as multilateral framework is still a priority for both India and EU. The FTA is not substituting but complementing to the multilateral negotiation, he added. Both parties cannot wait for WTO to create better conditions to business but have to do business in the mean time, albeit both India and EU must do it in a way that common objective of creating satisfactory framework is not undermined. Another issue highlighted by him is that FTAs should cover areas and sectors of mutual interest of India and EU, including a global coverage of all the things to be traded, and which should respect the spirit of WTO rules.

Taking issues highlighted by Mr Gomes forward, Mr Khullar made it clear that it should be understood that India-EU FTA and the events and development of Doha Round are entirely different. It is not that one is preemptive to the other. The engagement of India-EU on FTAs is an issue of strategic partnership, which is two years old: the establishment of the high-level group comprising of government heads of both India and EU and other members is itself one year old, well before when there was any sign that Doha Round of talk will breakdown. Amongst the countries in the world, India and EU are the ones, which have stuck to the rule based multilateral system while others have gone around for bilateral deals.

He emphasised that India-EU FTA needs to be looked from the geopolitical context, and not as trade relation issues. It has to be looked at as an engagement between the EU continent and South Asian continent. He cited that without taking any such initiative for the last 10 years EU has been the largest trading partner of India, and this is not because of any consensus effort or any strategy, but it has just happened and the other traditional trading partners of India has sunk in position. India-EU FTA is to be seen not only as an FTA but also as broad based trade and investment agreement, covering General Agreement on Trade in Services (GATS), General Agreement on Tariff and Trade (GATT), Sanitary and Phytosanitary (SPS) issues, Technical Barrier to Trade (TBT) issues, Trade Facilitation (TF) and other issues, he added.

He concluded his remarks saying that the negotiation is expected to be a win-win situation for both India and EU and both needs to provide something on market access to the other to gain something out of it.

Dr Jim Rollo, in his inaugural comments, highlighted the structure and issues of the research work for India and EU. He further addressed issues like SPS Measures, TBT, Government Procurement (GP), Investment, and Services that were discussed in the subsequent sessions of the meeting.

### Session 1: SPS and TBT

Dr Jim Rollo chaired the session on SPS and TBT. In this session, brief presentations were made by J George, Professor and Head, Faculty of Economics and Development Planning, Haryana Institute of Public Administration (HIPA), Gurgaon and Atul Kaushik, Deputy Secretary, Directorate of Public Grievances, Cabinet Secretariat, Government of India.

In his presentation, Prof George highlighted that adherence to the SPS and TBT standards could provide greater market access to the developing countries in the developed countries market. He said that it would also create opportunity for developing countries to integrate into the global

supply chain for primary raw materials. He further addressed the interacted issues of SPS and TBT standards and highlighted how they impact trade.

Atul Kaushik, in his presentation, said that quality and safety are of paramount concerns for any country, particularly for the developed countries. He said that as tariffs are reduced in the last eight rounds of trade negotiations, the focus of protection has shift to non-tariff barriers (NBTs) in particular to trade remedies and standards/regulatory barriers. The legitimate



From Left: J George making a presentation  
Others: Jim Rollo and Atul Kaushik

objectives in TBT and appropriate levels of protection of health and life in SPS are largely determined at the national level, he added.

As a way forward he mentioned that collaborative efforts have already been initiated by government/bodies like the Indo-EC joint commission, Agricultural and Processed Food Products Export Development Authority (APEDA), Marine Products Export Development Authority (MPEDA), Export Inspection Council (EIC) etc. However, he expressed that these efforts need to be strengthened. He explained that developing countries have a comparative disadvantage in accessing the WTO Dispute Settlement mechanism to exercise their access rights under TBT/SPS and EU also has a comparative disadvantage in using the appropriate standards doctrine in setting up TBT/SPS Measures, or in defending them in disputes. In this case collaborative effort between India and EU may bear more fruit, he added.

Answering to the question asked by Sanchita Chatterjee on whether there is any special procedure used by government of India when a country brings SPS and TBT concerns to them, Dr. George replied that under the transparency agreement of SPS, there is a national authority, and three-enquiry points in the country which provide information on different SPS and TBT related issues in the country. He cited the example of the Agriculture Ministry and the Health Ministry, which have an enquiry point each. These enquiry points have very well laid out procedures, which is part of the transparency agreement. Over the last 10 years, India has made the procedures in terms of the international standards.

Mr Kaushik echoed the similar line that due to the provisions in WTO, we can have information through different ministry websites. However, whether the queries are satisfactorily responded or addressed, is a question, which needs to be pondered. He said that it cannot be answered how much involvement of our exporters/importers or exporting and importing community with the standard setting process is there. He further informed that there are also standard bilateral systems of getting information like the joint India-EC commission etc, as with almost every country India has bilateral arrangement to provide information on the SPS and TBT issues.

Captain Gill commented that often the state laws in India go beyond the central law, and in EU also, there is a provision that individual country can further go beyond the standards laid by EC. Individual member countries can put some standards above or below the standards laid by EC. He opined that there is need to have some commonalities in the standards, which apply to India-EU trade and other trade agreements. On addressing a question on the difference between the central and state level standards, both Mr Kaushik and Dr George say that the centre and states in India need to make sure that the state levels standard also conform to the standards set out by the centre. They further commented that Centre-State issue in India is a constitutional issue; the differences in the standards laid out by centre and states in India need to be handled domestically by the respective governments.

Captain Gill raised the issue that apart from dispute resolution at WTO what the mechanism of dispute resolution will be for any dispute arising between India and EU from the FTA. Captain Gill continued that in such case it seems feasible to have a separate dispute settlement body within the FTA for the disputes arising from the agreement. Captain Gill also raised the question whether any private sector standard if set by the industrial organisation will be technically part of the contractual agreement or outside the purview of the FTA.

While responding to the issue that there is multilateralism at one hand and bilateral agreement on the other, Dr George made it clear that we could not have separate arrangements on SPS/TBT issues under multilateralism and bilateralism. He further said that so far we have mutual recognition agreements (MRAs), with five countries that are inadequate for India: we have increased our market for SPS related products like processed foods and other such products abroad; and there should be efforts by the exporters to force government to sign more MRAs with different countries. He suggested that for the FTA between India and EU to be successful both the parties needs to make signing of MRAs a prerequisite in areas of concern before progressing further. Finally, he commented that we need to accept the standards outside, and we need to meet them, including assistance from the developed countries to meet them.

Anil Jowri, from Quality Council of India stated that the area of concern is not really standard as long as EU is following international standards; and India really cannot disagree on that international standard under SPS and TBT. He said that it is only when EU puts some higher standards it becomes a concerns for India. He said that if EU puts high standard for India it needs to justify, and whether India has the capacity to analyse the justification or counter the justification is another issue. India needs to have mutual recognition agreements (MRAs) on the sectors of country's export interest to EU and EU also needs to recognise India's standards, certificates, testing as equivalent and compliant to their standards, he added.

## Session 2: Investment

Dr Rajeev Kumar, Indian Council for Research on International Economic Relations (ICRIER), chaired the session on Investment. Dr Aradhna Aggarwal from the Department of Business Economics, Delhi University, made a brief presentation on Investment issues.

Dr Aggarwal, while presenting her views on Investment, said that EU has emerged as the largest investor in India in 1990s and retained its position in the 2000s. The share of EU in total FDI inflows of India has increased from 17.4 percent during 1991-99 to 22.7 percent during 2000-03. She informed that the share of the four countries – UK, Netherlands, Germany and France – which accounted for 79 percent of total EU FDI to India during 1991-99, has increased to 81 percent in 2000-03. She elaborated that among the four countries UK has registered the largest increase in FDI to India, the percentage share increasing from 22 percent to 30 percent, while at the same time the share of Germany on the other hand has declined. While analysing the EU FDI stock, she said that financial intermediaries, business services, petroleum, chemical rubber, plastic products, trade and repair, and transport and communication etc., accounts for over 70 percent FDI flow in India. Dr Aggarwal said that FDI flows have been increasing intensively in financial intermediaries, R&D, business services, transport, equipment, and sector-wise concentration in India is comparatively less skewed than overall EU investment pattern.

Pointing on India's outward investment, Dr Aggarwal told that manufacturing and non-financial services accounts for 54 percent and 36 percent of investment. Information Technology and Pharma are seen as the major sectors attracting FDI in EU from India. India has a huge potential in investing in EU in the areas of textile and clothing (T&C), metal and mechanical sectors financial intermediaries, metal and mechanical sector, she added.

While analysing the investment climate in India, she informed that India has already substantially improved foreign investment regulatory regime by augmenting the automatic approval route, lowering sectoral caps and simplifying exchange

controls. However, she hastened to add that the Indian government is cautious and maintains policy space.

Dr Aggarwal expressed her deep concern over investment climate (like restriction on market entry, ownership and control restrictions, operational restrictions) in India, saying that improper governance, improper infrastructure, legal issues are still acting as major bottlenecks for inflow of investment in India.

She further said that though EU offers a business-friendly environment, market entry barriers like state monopolies (non discriminatory), discriminatory treatment between EU and non-EU nationals and reciprocity requirements are acting as the major hurdles for entry of foreign firms in EU. Factors like high labour costs, labour market rigidities are also acting as prohibitive potential bottlenecks in attracting FDI to the EU.

In reply to a question whether some states may have legislations different from the central government, as there is interstate difference in the inflow of investment in India, Dr Aggarwal said that the variation is due to the difference in the investment climate and FDI rules are not different across the states though procedure and investment climate make the differences. She viewed that industrial infrastructure makes a lot of difference and the attitude of the state government and the prevailing labour laws and land laws in the states make a lot of differences.

Replying to the question of differences between automatic and Foreign Investment Promotion Board (FIPB) approval she said that these are two different channels through which approval is given for FDI and the Reserve Bank of India (RBI) gives automatic approval for investment for certain sectors. If the investment is for these sectors, then the investor gets automatic approval. In this case, the investor just needs to submit application and do not need to wait for the approval. For FIPB route, it takes some time to get approval for investment, she added.

### Session 3: Service Trade

Dr Jim Rollo chaired the session on Service Trade. Dr Reshmi Banga of UNCTAD and Mr Manab Majumdar of FICCI made brief presentations on trade in Service.

Dr Reshmi Banga started her presentation stating that UK, Germany and France have been the important trading partner of India in services, and with respect to software services, UK has been the most important trading partner of India with 15 percent of its total export going to that country. She elaborated that off shoring has become the dominant mode of delivery, accounting for about 58 percent of total exports. She said that UK and Germany with large imports of services could be identified as the India's target markets in EU for Services. Dr Banga highlighted that India's service exports has witnessed the highest growth in the world with 105.7 percent in 2004-05 and India at present is the 10<sup>th</sup> largest importer and exporter of commercial services in the world.

While commenting on meaningful market access in service, Dr Banga said that India needs mutual recognition agreements for Indian service providers in EU, acceptance of Indian qualifications like law and accountancy degrees, review of the visa rules for Indians etc. She viewed that reductions of the NTBs like the minimum capital requirements, reciprocity treatments, data protection requirements, economic need tests, local staffing requirements could help increase exports of Indian financial services in EU.

Dr Banga informed that it needs to be looked whether the domestic regulations in India are in place, especially in financial services and also whether India is competitive in Mode 3 of GATS, specifically in services like banking, legal and distribution services. She said that given India's political situation to what extent India would be able to deliver in Mode 3 and to what extent this FTA would lead to trade creation or trade diversion is a question that needs to be pondered.

Mr Manab Majumdar stated that India is much behind the other countries in terms of trade in

services. He cited the example that India's share in EU's total trade in services is just barely over one percent, while China's share will be close to three percent, and if Hong Kong's share is taken separately it stands at two percent. He added that India's export of service is less than four billion Euros (US\$5.2bn) in 2004, even though there is immense potential for India to export services to other countries.

However, Mr Majumdar said that it is very uncomfortable for the negotiators to proceed further with service trade liberalisation given the lack of progress in Doha Round, which has not been well in terms of service. He apprehended that if India and EU try to wrap up the negotiations, what will be the benchmark of negotiation is a big question. He said that financial services, architectural service, dental service, informational technology service are the areas where India has offensive interest under Mode 4 of the GATS. He made it clear that along with negotiating on Mode 4 and Mode 1 of service trade, given the change in the business perspective, India also needs to negotiate on Mode 3, which has equally become important for India.

Mr Majumdar also emphasised that though India will lock in with EU for the FTA agreement, it needs to negotiate separately with each of the EU members so that the social security and market access issues are addressed. He said that countries like UK, Finland and Sweden have already provisions for payment of pension benefits to all overseas nationals when they return to home country, and so it needs to be looked how the system can be replicated in other EU countries so that Indian professionals might get benefit.

He added that the case of horizontal issues delinking the category of independent professional from commercial presence is a major issue and is an area of India's interest. He stated EU must remove restrictions on movement of natural persons on at least some of the sectors and inter firm mobility to professional must be allowed and also all discriminations in terms of taxes, levies, regulations (sector specific, professional specific) must be eliminated. Looking at the EU's interest in India, he said that EU also wants

India to liberalise many of the service sectors like legal service, auditing, market research architecture, environmental services etc., and so he emphasised the need to make commitments in these areas as reciprocity to their demands.

He further said that though the request offer process is ambitious, there are sensitive sectors, and hence India needs to take balanced view related to ambition and sensitive list. He also highlighted that another shortcoming from Indian side is that it tends to gloss over the reality in the supply constraint. In India, many sectors face constraints by either current shortage or future shortage of skilled professionals. So he stressed that while negotiating it should be in mind that allowing market access would not lead automatically to effective market access for India unless these barriers are addressed.

Following the discussion on services, M C Verma of International Trade & Law Institute commented that the insurance sector should be opened up, as in insurance sector in India there are a lot of regulations, and therefore, not many foreign companies are coming in the country. Aditya Matto of World Bank, taking the discussion forward, said that restrictions are in place both in India and EU, but what needs to be understood is the political economies of these restrictions, and it is then only India could answer whether there could be any reciprocal deal. Moreover, India needs to decide whether it is feasible to liberalise the political economic reason more in the EU context, or might do in the WTO context, as most of our liberalisation is happening unilaterally, he added.

Dr Matto emphasised the need to conceive the political constraints in the India-EU context, which will play off. He asked for the need to discuss the feasibility of preferential liberalisation in services and desirability of the service sector liberalisation. He highlighted that before India commits to its tunnel vision of India-EU FTA, the question needs to be asked why FTA is with EU and not with other country, even US.

He finally commented that it needs to be pondered what India expects to get from EU bilaterally that the country would not get from

WTO. He felt that it needs to be decided whether it will be realistic for India to go for significant liberalisation in the EU context when EU has not been able to accomplish it internally.

Dr Matto said that India should also observe the Bologna Process, which was initiated a few years ago and is underway. By becoming an observer in the Bologna Process, India could learn how the EU nations are harmonising the standard within EU, so that India can follow it to perform some of the domestic reform in the country. It is then that some of the MRAs problem can be solved.

Pranav Kumar from CUTS said that EU is not going to stop at New Delhi only; it will go ahead in signing agreements with other countries as well. In that case, India's advantage in service trade can get neutralised very soon. In lieu of that, the benefits given to EU will be exploited for their benefits in India. It needs to be seriously looked at what India gets in return from EU. Finally, Mr Gill commented that service reciprocity has not really paid off in the WTO context. So both India and EU need to be creative in finding out the areas where formation of agreement will really move in both India's and EU's interest.

#### **Session 4: Government Procurement**

Mr M P Gupta, former Additional Secretary, Department of Expenditure, Ministry of Finance, Government of India chaired this session. Mr A K Goel, Executive Director, Railway Stores and Kailash Karthikeyan, Trade Officer (Legal) made brief presentations on Government Procurement (GP) in India.

Highlighting the case of Indian Railway's GP policy, Mr Goel stated that the largest railway network under single management have formulated well established common procurement policy which have evolved over central theme of ensuring trade transparency, fair play, quality procurement, competition and equal opportunity to eligible vendors. He informed that procurements are done through process of competitive bidding and advertised tender document are uploaded on website for free access, viewing and downloading. He



highlighted that that foreign bidders are treated at par with domestic bidders, even purchase preferences are also allowed to public sector over private sector for purchase above Rs five crore (US\$1.12mn) and up to Rs 100 crore (US\$22.5mn).

Mr Kailash Karthikeyan informed that EU procurement market is around 16 percent of gross domestic product (GDP), while estimates for India ranges between 3.4 percent and 5.7 percent. He said that India is not a member of the agreement on GP or bilateral procurement agreement and only some markets and countries may be of interest to India for GP. More efficient GP in India would lead to saving of 0.36 percent of GDP.

He elaborated that there is difficulty in accessing EU GPM, as it is lengthy and costly process, and moreover, there are regulatory barriers, differences in the contractual procedures across EU countries, lack of harmonisation and mutual recognition of standards across countries etc. He also highlighted the main problem of GP in India, which includes lack of transparency, deviation from rules, absence of formal appeal/challenges procedures etc.

Mr Karthikeyan said that by entering into agreements on GP, India could improve efficiency of GP system in the country and could also access to the large market in EU. He said that however it entails some initial administrative cost and can also have some economic and social cost in the economy. He added further that reciprocal market access provided to EU might also adversely affect the domestic industry. He highlighted that sectors in which India is likely to gain by GPA are software and communication services, financial services, professional services, and others like architectural and engineering services.

Mr Nitya Nanda of CUTS commented that government of India has made the GP policy for the country by looking at the World Bank procurement policy, WTO transparency agreement etc., and government of India is

committed to make changes in the procurement policy. He said that if market access needs to be ensured, then there must be transparency and if there is any discrepancy in government procurement, it is mostly in the post government policy. After bidding are done and evaluation of the contract is over, a bidder is selected, but it is not published why a particular bidder is selected and not the others, he elaborated. Mr Nanda said that in this case there is transparency problem in India though the situation is changing in India, as now we have the right to information. As of today as per as the transparency requirement we have the public procurement followed by many other countries as required under WTO or followed in any bilateral trade agreements, he added. However, one problem, he mentioned, lies with India is that it is a huge country and procurement is done at different levels and getting all information together is going to be extremely costly. For transparency, we do not have any problem now, information is now published voluntarily, he concluded.

Anirudh Senegal commented that the rules for GP vary across states, as each state has its own GP policy and the financial rules are also different across the states. He said that government of India is now updating it, so every government is doing the same, for example, Bihar government is also updating it. He elaborated that every state will fall in the line and it is just a matter of persuading. M P Gupta said that though state rules vary from one state to other, they are broadly in conformity with the rules of the central government. There is no major deviation of the rules of the state government from the rules of the central government, he added. He informed that basically what Indian government has done is that it has put all the bidding documents of World Bank and Asian Development Bank (ADB) on the website and made transparency issue a strong point. He concluded by saying that India has also put the manual of worst procurement and manual of selecting consultants also on the Internet and all government offices are made to follow this.