India and the World

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India's evolving approach to trade agreements

Concerns that the processes of economic globalisation had come to an end might be overstated. There are signs of dips, but the total trade in goods and services has increased almost five times since 1995, and the global trade-to-GDP-ratio was 29% in 2023, compared to 20% in 1995. Data show, however, an increased fragmentation of trade and investment flows along geopolitical fault lines, making international economic cooperation sensitive to considerations of national economic security.

India stands to gain from diversification trends in the wake of such changes. How potential is transformed into real activity is, however, still too early to tell. Yet, clearly, New Delhi must find ways to leverage a transforming environment for international economic cooperation to its advantage if it is to achieve its stated goals of becoming a leading power, and 'Viksit Bharat', by 2047.

Notably, India's ambitions are both economic and political. To be 'Viksit Bharat' involves moving from the lower middle-income country category of today, out of the middle-income category completely; a "leading power" would exert influence over international norms and rules-setting. The continued growth of India's economy is foundational for this transition.

The exact path for growth is a matter of ongoing domestic discussion. There are strong currents of economic nationalism in India's intellectual history. Yet, historically, a balanced integration into global value chains (GVC) and investment flows has been critical for countries to ascend the economic ladder in the short and medium term, and to possibly access international political benefits in the long term.

India's general outlook towards FDI and value chain integration has already altered considerably over the past two decades. But the case for furthering economic integration is not always easy to make in a country with a vivid historical memory of free trade arguments that eventually served colonial expansion. The case could be even harder to make to those Indian audiences who are wary of competition with China, have a mercantilist view, or place high confidence in indigenous industrial conglomerates and their role in the expanding domestic market. Tellingly, despite a high growth rate, India's trade in both services and goods as a share of GDP has fallen in the last decade, and the country's share in global trade remains at around 2%.

In its recent development update for India, the World Bank looked closely at India's export targets for 2030 and in connection, at the country's trade stance. In the report, the World Bank argues that while the National Logistics Policy and digitalisation has enhanced trade facilitation, tariff and non-tariff barriers keep restricting openness to trade. The World Bank proposes that India could consider diversifying exports and become more integrated in GVC's, as possible steps for meeting its 2030 export targets.

Bilateral or regional agreements for trade and investments may be a vehicle for India to diversify and integrate in GVC's. India has historically preferred to work through the World Trade Organisation, rather than establishing bilateral, or joining regional, trade agreements. This posture changed somewhat during the first decade of the 2000s, when Free Trade Agreements (FTA) were finalised with neighbouring countries, and negotiations commenced with other countries or regions, including the EU and EFTA. FTAs were complemented by other bilateral trade agreement instruments, such as Comprehensive Economic Partnership Agreements, and sequenced agreements in lieu of FTAs.

However, officials complain that the Indian private sector's utilisation of some of these agreements has been low. With ASEAN, for example, imports have grown more than exports following the signing of an FTA more than a decade ago. In light of this, India has been reviewing its stance on FTAs. For the last six to seven years New Delhi is now focusing efforts on partners that have a high potential in increased Indian exports, enable resilience in supply chains, production integration, and enhance digital trade.

India is currently in advanced or early stages of negotiations on trade agreements with three partners in the Eurasian geography: The EU, the UK and the Eurasian Economic Union. Additionally, New Delhi and the EFTA bloc (Iceland, Norway, Liechtenstein and Switzerland) closed a Trade and Economic Partnership Agreement in March this year. Although relatively narrow in scope, the agreement is likely to reverse a negative trend in India-EFTA trade volumes, as it lowers or eliminates tariffs and duties in select important sectors and improves market access for both basic and processed agricultural products. The most striking aspect of the agreement, however, is a pledge from EFTA to aim to invest $100 billion in India over 15 years. This is almost a tenfold increase from the bloc's net FDI disbursement into India between the years 2000 and 2023.

Negotiations between India and the EU are surrounded with decreased enthusiasm, and a widening gap between public rhetoric and real progress. The latest round of negotiations, which ended September 28, reportedly saw exchanges over both the EU's Carbon Border Adjustment Mechanism (CBAM) and the now-delayed EU deforestation regulation (EUDR). Estimates from India show that the CBAM could amount to an additional cost of 25% on Indian exports to the EU from hard-to-abate sectors. India's Finance Minister, Nirmala Sitharaman, recently called CBAM an arbitrary trade barrier, and said that New Delhi had raised concerns with the EU but she did not expect the issue to harm the ongoing negotiations.

New Delhi is also concerned about aspects of the FTA process that will involve the participation of "civil society", which is deeply controversial within Indian politics. For their part, Indian bureaucrats across the board have gradually been showing less interest in easing market access for EU industries. The apparently arbitrary implementation of Quality Control Orders has targeted a variety of foreign manufacturers in sectors with a high presence of Chinese imports.

With discussions moving towards contentious issues, political will for a clear breakthrough on both sides is essential. The EU, which negotiates on the basis of the same mandate as it did during the last period of negotiations (2007-2013), aspires for a comprehensive deal that is WTO+. India, on the other hand, seems to look for an agreement more in line with the narrower options it has been pursuing with other partners, and there are emerging signs of institutional capacity limitations affecting the pace for progress.

One possibility that has been discussed behind closed doors in EU member-state capitals is whether a trade deal could be concluded sequentially. The risk of a sequenced deal from the EU's perspective is that a full FTA may never see the light of day, as India's appetite to move beyond early-harvest agreements may decline. This appears to be the case, for example, with the agreement between India and Australia. The benefit for the EU, on the other hand, would be to get predictability in possibly critical areas of economic cooperation, and not to lose out to external competition.

India is also in advanced stages of negotiations with the UK regarding an FTA. After 14 rounds of negotiation, consensus has been reached on most of the 26 chapters of the trade deal. However, some contentious issues remain, and it is unclear how the change of government in the UK will affect the process. While a liberalised visa regime for Indian workers might be easier to agree to for a Labour government with a history of less pointed rhetoric on migration, New Delhi is also concerned about how Indians working temporarily in the UK end up paying for national insurance without being eligible for social security benefits. The UK also wants India to lower tariffs on goods like whisky and cars. Additionally, the UK seeks greater access to India's market for its financial, legal, and other services, which is facing opposition from business interests in India.

India's policy makers must now find ways of making trade work for its young and ambitious population by utilising connections to external economies for long-term job and wealth creation at home, to upgrade its services and manufacturing industrial bases, and continue to ready its domestic economy for a digital and green future. Their European counterparts, who are aware of their industries interests in India's talent pool and market, and of the need to reduce supply and value chain concentrations, will need to acknowledge that trade agreements with India require more flexibility, given both the complexity of Indian politics and the possibilities of the Indian economy.

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