Commentary: Why India walked away from Asia’s mega free trade deal

Fears of predatory trade practices and the lack of competitive export-oriented industries have driven India to opt out of the RCEP, says Sreeram Chaulia.

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NEW DELHI: India’s decision to drop out of Asia’s mega free trade agreement, the Regional Comprehensive Economic Partnership (RCEP), is the outcome of a hard-nosed calculation.

By stepping aside at the last minute, even as the remaining 15 members of the trade pact (10 ASEAN countries, China, Japan, South Korea, Australia and New Zealand) committed to its signing on Nov 4, India conveyed that it continues to have huge reservations over whether the trade deal can advance its national economic interests.

DUMPING AND OTHER PREDATORY TRADE PRACTICES

Indian Prime Minister Narendra Modi cited his own “conscience” and the interests of “our farmers, traders, professionals and industries” in turning down the RCEP agreement.

His foremost but unspoken fear is that the RCEP will open the doors for China’s manufactured goods to flood India’s market.

For some time now, India’s domestic producers have opposed freer trade with China. Indian politicians and observers have accused China of dumping state-subsidised, under-priced commodities.

An Indian Parliamentary Standing Committee on Commerce had expressed concerns in 2018 about India’s widening trade deficit with China and urged the Modi government to do more to tackle it.

India’s bilateral trade deficit with China stands at a whopping US$53 billion. The apprehension in New Delhi is that this unsustainable gap will widen if it signs the RCEP.

India sat out of China’s Belt and Road Initiative (BRI) too owing to related concerns

Although China insists that it does not deliberately pursue trade surplus against India, New Delhi was not sufficiently assured that the RCEP will not become a conduit for Chinese-made goods and components to be routed through other member countries such as Vietnam or Cambodia.

Indian leaders have been uncomfortable with China’s push to urgently seal the RCEP in the wake of the US-China trade war. Their reading of the situation is that Beijing will redirect its excess unsold goods blocked by the US, particularly steel, to deluge India.

Many in India fear that Modi’s ambitious “Make in India” initiative to attract foreign direct investment (FDI) for building an indigenous manufacturing base could suffer a premature death without sufficient protection of its nascent industries from an avalanche of Chinese exports.

Membership of the RCEP would compel India to cut import duties on goods like mobile phones and electronics components, products being encouraged to be manufactured at home under the “Make in India” banner.

China’s Xiaomi is already the top exporter of mobile handsets to India, displacing South Korea’s Samsung. Import dependence rather than self-reliance could deepen if India accepted the RCEP in its present form.

China’s reluctance to import Indian generic drugs and information technology (IT) services, and the strategic competition for geopolitical influence between the two Asian giants, have heightened Indian sensitivities about the RCEP, even though the deal involves 14 other countries.

RURAL STAKEHOLDERS

Indian political leaders also faced opposition to the RCEP from other constituencies, in particular, agriculturists and dairy producers, the vast majority of whom are small and medium operators.

They fear that joining the RCEP would expose them to large-scale agribusinesses competition from Australia and New Zealand.

Agriculture is the most sensitive area for India whenever it engages in trade talks, be it at the RCEP or at the broader World Trade Organisation (WTO), as it employs more than 50 per cent of India’s workforce who mostly eke out a living at a subsistence level.

Allegations that Modi might sacrifice the interests of farmers at the altar of global trade platforms have been politically damaging to the ruling Bharatiya Janata Party (BJP).

Farmers wait for the auction of onions at Lasalgaon market in Nashik district in the western state of Maharashtra, India on Dec 19, 2018. (Photo: Reuters/Rajendra Jadhav)

For these reasons, the BJP has faced intense pressure and criticism from within its own ranks, opposition parties and hundreds of millions of poor voters.

Despite nearly seven years of negotiations with RCEP partners, India is not sufficiently reassured that the deal will protect the interests of its farmers.

LIMITED BENEFITS

The fundamental problem India has is the smallness of scale in its goods production and the lack of a competitive export-oriented economy.

Unlike some of the highly industrialised RCEP members, India cannot boast of a competitive manufacturing sector that can go out and capture foreign markets via pacts like the RCEP. This lacuna causes persistent trade deficits and is the key reason why India is defensive and inward-looking in its approach to multilateral trade talks.

India signed a free trade agreement with ASEAN in 2009, but is still running a deficit of US$13 billion with the group. It has forced Modi to seek a review of the India-ASEAN FTA to make it more “balanced”.

Employees of Motherson Sumi Systems Ltd, work on a car wiring assembly line inside a factory in Noida on the outskirts of New Delhi, India April 28, 2016. (Photo: REUTERS/Anindito Mukherjee)

With South Korea and Japan, the other pivotal RCEP members, India has a trade deficit of US$12 billion and US$7.9 billion respectively.

The hurdle India faces in trade negotiations like RCEP is that they focus more on opening up trade in goods rather than liberalising trade in services, where India has a comparative advantage.

The RCEP members are wary of India’s skilled software, telecommunications and educational professionals immigrating and displacing their domestic labour.

After spurning the RCEP, the Indian government has announced that it is exploring trade agreements with the US and the European Union, where India’s service sector is competitive and enjoys trade surpluses.

But given US President Donald Trump’s tough anti-immigration politics, little headway is expected.

For the foreseeable future, exports are unlikely to be drivers of India’s economic growth.

Modi’s model of attracting FDI by rapidly improving its Ease of Doing Business rankings, and manufacturing for domestic consumption within India, is a more realistic pathway.

India’s infant industry is not yet ready for global competition. It may take a decade or longer before exports become motors of India’s growth.

REGIONAL ASPIRATIONS

There is a disjuncture between the unanimous domestic applause Modi received after he rejected RCEP and the foreign policy challenge of how India can lead Asia if it isolates itself from the primary institutional architecture for regional economic integration.

By steering the RCEP, China will be able to shape its rules, standards and supply chains. Japan and other RCEP members had hoped to have India in the tent to balance out China’s powerful hand.

But domestic economic considerations have weighed heavier than regional and international aspirations in India’s approach to the RCEP.

Still, the door to the RCEP is not completely shut to India.

Since the remaining RCEP members are already highly integrated in terms of trade and financial flows, the absence of India with its 1.2 billion consumers, might eventually persuade the other countries to accept India’s terms.

If and when India enters the RCEP, Asia would be better off as a whole. Meanwhile, Modi has much work to do to speed up his goal of industrialising India and making it a manufacturing hub that can capitalise on agreements like the RCEP.

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