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India and the EU: Approaching a Free Trade Agreement

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The eleventh European Union-India Summit took place in Brussels on 10 December 2010. Leaders of the two parties (José Manuel Barroso, president of the European Commission, and Manmohan Singh, prime minister of the Republic of India) discussed several important topics and issued two declarations (the Joint Declaration on International Terrorism, and the Joint Declaration on Culture). Perhaps the most important contribution to bilateral issues, however, were "*the significant progress recorded during recent negotiations*" and the agreement "*on the contours of a final package*" of the Broad Based Trade and Investment Agreement (herein also referred to as "the Free Trade Agreement"). They also agreed that the finalization of the Agreement will take place in spring 2011. Although numerous points in the proposed agreement require clarification, strong political will seems to be overcoming the differences. The intention to integrate the markets of one and a half billion people is not new: talks intended to create a free trade zone between the EU and India began in 2007. This highly ambitious project would be a huge step forward in the strengthening of ties between India and the EU.

Though bilateral trade relations between the EU and India are quite limited, they exhibit dynamic characteristics. In the past seven years trade has almost doubled and new, very promising areas have emerged. India is the 9th most important trading partner of the EU with overall trade of nearly 53 billion euros. Exports accounted for nearly 28 billion, while imports amounted to more than 25 billion. Europe's 2.2 billion euro trade surplus is in great part due to 12 billion euros in machinery and transportation equipment exports, while the most prominent import sectors are manufactured goods, machinery, chemicals and related products. These latter sectors represent a combined share of nearly 80 percent. Though the level and intensity of bilateral trade between the EU and India may not be exceptionally important for the EU, it is for India: even ahead of China, the EU represents its most important trading partner. The principal European trade partners are the UK, Germany and the Netherlands. According to official Indian statistics, India imports goods worth 190 million USD and exports goods worth 440 million USD to Hungary (Hungarian statistical data show fewer Indian exports).

Capital flows are also increasing between the EU and India and reached a record outflow from Europe of 4.6 billion euros in 2007. The worldwide financial crisis had an adverse effect on capital movements and outflows in 2008 and 2009 decreased somewhat to 3.3 and 3.1 billion euros, respectively. In the last few years, India has also emerged as a capital exporter and has invested more and more worldwide. The combined Indian FDI stock in the EU is more than 5 billion euros (though this is much less than the European stock in India of more than 27 billion euros).

Although from the European perspective bilateral trade and investment relations with India are not exceptionally strong, their potential is enormous. India's economic progress since the beginning of the reform process in 1991 has been breathtaking. Its growth rate has climbed above 6 percent and, between 2005 and 2008, it was more than 9 percent. This performance has placed India alongside China, as the country has become one of the fastest growing regions in the world. Another very important feature of the Indian economy is its rapidly growing middle class, amounting already to more than 200 million people. These households are already capable of and also have a willingness to spend their income like American or European consumers and make up the base of the Indian domestic market. Taking into account these prospects, penetration in the Indian marketplace is of the highest interest for Europe. From this perspective, signing the new bilateral Trade and Investment Agreement could be vital.

In his speech following the talks in Brussels José Manuel Barroso stated that the new Free Trade Agreement: "*will be a key contribution to the global recovery and a signal for global openness and also a signal against protectionism. Most importantly, it will be crucial for sustainable growth, jobs and innovation both in India and in Europe. This is indeed a win-win package for both of us!*" President Barroso also added that: "*This Trade and Investment Agreement will bring new opportunities for our manufacturing companies, our traders, our businesses, big or small, and for consumers.*" Besides the positive prospects and optimism about the agreement, there are also concerns as well as disputed areas which have to be solved in the following weeks or months.

The main motivations behind the Free Trade Agreement have been the prospect of greater market access (especially for some agricultural products and the government procurement market) for European companies, while India has been working on reducing restrictions on the temporary movement of Indians working in Europe. There are other disputed areas, however, which could be major obstacles to the completion of the agreement. The EU, for example, is insisting on including the strict regulation of human rights (particularly labor rights) and environmental standards, while Indian manufacturers dispute intellectual property rights relating to generic off-patent drugs, claiming that the EU should not apply stricter regulations than those approved by the WTO.

Apart from the disputes mentioned above, other voices raise objections to the agreement as well. Some Indian sources say the totally free flow of investments (including all types of financial flows), for instance, may undermine development priorities and restrict the space of policy actions. They are also afraid of opening up industrial sectors where foreign investment is currently prohibited (including multi-brand retail, legal services and railways), or where there are currently equity limits (banking, insurance, telecommunications, media, and aviation). These objections are not totally groundless. Even in Europe some governments make use of any available measures to reduce foreign ownership in some strategic industries. In the case of a developing country like India, it may be crucial for the government to retain some room for industrial policy. Indians would also like to preserve some types of performance requirements imposed upon foreign firms in the form of export obligations and maintaining the domestic content of value added. Finally, the removal of restrictions on capital transfers could undermine financial stability in India and could exacerbate sudden speculative capital outflows.

Despite differences in the overall level of development and in the approach to some strategic questions, both the European Union and India have a substantial interest in signing the new Trade and Investment Agreement. Reconciling these differences, however, is no easy matter. In December, President Barroso was overly optimistic in stating that: "*our aim is to conclude negotiations next spring or in any case as early as possible during 2011*". A month later, Daniele Smadja, the EU ambassador to India, said that only an agreement on the main elements of the deal would be finalized by April and the draft version would not be ready until later. Given the strong commitment exhibited by both sides, finalization of the project is not impossible. But it will be necessary to stick to the strict time schedule.

From January 2011, Hungary has taken on the presidency of the EU. This mandate has created valuable opportunities for the country to present itself in the international arena and influence the policy making process of Europe. Though bilateral relations between Hungary and India are not strong, traditional ties established during the 1960s and 1970s have not been completely broken. Cooperation in power generation, water treatment and public transportation serve as examples. We all know, however, that these links, after the millennium, are not particularly important. But reviving some of them would help to accelerate the completion of the Free Trade Agreement. We hope that Hungary will be able to capitalize on its current position as President of the Council of the European Union and become a major force behind the finalization of the broad based EU-India Trade and Investment Agreement.

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