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„The India-EU Broad Based Trade and Investment
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for the EU and India in Negotiating a Free Trade
Agreement“

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1. Introduction

„None of these FTAs, CEPAs, Treaties, or Trade Agreements as they may be called is as ambitious in scope and coverage as the proposed FTA (also named BTIA: Broad based Trade and Investment Agreement) with EU, for reasons of the “deep” integrative nature.“ (Modwel, Singh 2012: 3).

1.1 Problem

In February 2012, the 12th India-EU Summit was held in New Delhi with India and the European Union (EU) being represented by their major political leaders. They were aware that completing this agreement would be a milestone in the history of free trade in general and the economic prospects of both partners. At the end of this summit, both sides agreed to continue the negotiations on a free trade agreement (FTA), which had been in progress since 2007: *the India-EU Broad based Trade and Investment Agreement (BTIA)*.

Despite some noteworthy scepticism, free trade agreements have gained significant popularity among international actors in recent years. Member states of the World Trade Organization (WTO) as well as non-member states have been actively engaged in creating bilateral as well as regional trade agreements (RTAs) (WTO Regional trade agreements 2013). The motives behind this aim are multifold. The EU has been exploring free trade zones recently in order to further deepen trade with their partners going beyond questions of traditional trade barriers. Such agreements are considered a means to examine trade restrictions other than tariffs more closely and – where applicable – abolish them. The underlying idea remains the promotion of free trade for the improvement and prosperity of the involved economies. Albeit latecomers, Asian countries have become very active in the field of FTAs. So far their FTAs have focused on regional cooperation between Asian states, and emerging markets (China, India, Indonesia) play a key role in their development. Despite systemic problems accompanying the high number of agreements, which bear the risk of overlapping each other and creating the so-called the “noodle bowl” problem, Asian countries have discovered regional trade as a potential key to enhanced sustainable trade in order to deepen their market-driven economic integration (Kawai, Wignaraja 2011).

Therefore, although FTAs are by no means unusual, the specific kind and scope of the envisioned treaty between India and the EU is unprecedented. It is the first treaty to be negotiated between two very large economies and secondly, the areas to be integrated go beyond mere tariff reductions. What is more, it would be India's first agreement with a large trading partner and the EU's first agreement with an emerging market (Mukherjee 2011: 3). Therefore, the question of the treaty's future success or failure will be a vital lesson for future international trade negotiations. As either outcome seems possible and both partners are aware of the risks, an expert group - the High Level Trade Group - was set up to examine the possibilities for an agreement. It evaluated the potential of "trade in goods, trade in services, investment, trade facilitation, public procurement, intellectual property rights, competition and dispute settlement," (Report of the EU-India High Level Trade Group to the EU-India Summit 2006: 1) and in its reports it came to the conclusion that a bilateral agreement is deemed beneficial for both economies.

Since the beginning of the negotiations in 2007, several negotiation rounds have taken place in both Europe and India. Among other developments, the willingness to pursue a significant increase in bilateral economic cooperation and deepened investment relationships proved both parties' dedicated commitment to reaching an agreement (Report of the EU-India High Level Trade Group to the EU-India Summit 2006: 1). The summit in February 2012 concluded with the prospect of a completed FTA by fall 2012. However, substantial disagreements have been paralyzing the finalization of an FTA. Access to the European labour market for Indian citizens, the limitation or even abolition of generic drug manufacturing in India, and India's foreign policy (e.g., towards Iran and its nuclear programme) are some of the striking issues that remain unsolved.

1.2 Relevance of the Topic

With a population of 1.21 billion, India has astonished the world with its decades-long high economic growth. In the early 1990s, restrictive politics and significant kerbs on foreign investment gave way to a more liberal approach. "The effects of this (partial) liberalization were clearly reflected in the GDP growth rates" (Luif 2007: 39) that showed consistent improvement.

In terms of economic power, India constitutes roughly 2 per cent of world trade. The figures for world trade in services show a different picture since here India's share is higher than in trade in goods: services contributed to 66% of India's growth from 2000 to 2010. In the medium term, service sector development is believed to play a critical role in the country's growth (ADB 2012). One major advantage of India's huge population is the tremendously high supply of labour. The 2012 estimation of the active labour force was 498.4 million, making India a harbour of cheap labour. In addition to that, India has gained "considerable influence on the developed countries through its quickly increasing production capacities combined with services in the area of high-technology" (Luif 2007: 40).

However, more recently the economy has been facing serious problems and India's economic prospects have been corrected downward in recent months. In 2012, the country missed the 6.5% forecast, instead slumping to 5.6% (ADB 2012). The reasons for this were declining investment and export demand, and the resulting effects on the financial situation: the rapid depreciation of the Indian Rupee and inflation pose a major threat to price stability and hence consumption in the domestic market. In addition to the high inflation of 8.9% in 2011, the large fiscal deficit has limited the effectiveness of fiscal and monetary policy to stimulate the Indian economy. India is falling well below its potential economic growth rate and, in addition, the Indian economy has been confronted with a paralysed government, years of underinvestment in infrastructure, a large bureaucracy, corruption, and an investment-unfriendly environment. Serious political as well as economic reforms have been absent for many months, in spite of the strained economic situation (ADB 2009: 201). A highly fragmented parliament making reforms difficult and facilitating a drop in investment (particularly in real estate and infrastructure) and domestic consumption add to the above (ADB 2012). These dominant internal factors and the fear of decreasing external demand drive India to look for potential, long-term trading partners. The demand for knowledge and technology transfer, market access, and capital flows drives the country towards seeking an FTA with the EU, which could support India's development.

The EU, meanwhile, is facing its own economic troubles and as it copes with the consequences of the global financial crisis, which left it with decelerated growth. Several countries within the monetary union have faced financial problems and severe debt; the currency is under pressure, as are the viability and reliability of the Eurozone (Economist

Intelligence Unit Country Report EU 2012). The unemployment rates has increased due to the financial crisis and stands at about 7.5% in the Eurozone, with youth unemployment becoming a bigger threat to the social environment.

Despite the financial crisis and a projected growth rate of 1.1 per cent, the EU's overall economic situation remains positive and secures its strength on the international scale (European Commission Press Release 2013c). In terms of economic power, the EU is still one of the big players: it accounts for 19% of total world trade (exports and imports) and is the world's biggest exporter and second-biggest importer. Closely followed by the US and China, the EU meets the attribute of being an "economic giant". At the same time, the EU feels the pressure of emerging economies and is attempting to secure its place as one of the big players in international trade. These developments are potential explanations for both partners' motivations for working towards a FTA. It would boost their economies or, at the least, prevent further deterioration.

In the past decade, trade integration in emerging markets has increased tremendously. Particularly China and the ASEAN group countries have increased their international competitiveness in commodity trading. India joined free trade agreement negotiations relatively late but it has caught up quickly (Modwel, Singh 2012). Such regional agreements constitute serious competition to the traditionally strong trading countries in Europe and the United States. As the near future of large Asian regional agreements such as the Regional Comprehensive Economic Partnership (RCEP), which consists of the 10 ASEAN member states plus Australia, China, India, Japan, South Korea and New Zealand or the Trans-Pacific Partnership Agreement (TPP) with twelve currently negotiating nations United States, Japan, Australia, Peru, Malaysia, Vietnam, New Zealand, Chile, Singapore, Canada, Mexico, and Brunei Darussalam is uncertain, the analysis of the BTIA becomes all the more important (Petri, Plummer, Zhai 2011, 5). The EU could also avail itself of a major spur in its trade relations as they were negotiating for the Transatlantic Trade and Investment Partnership (TTIP). However, negotiations were cancelled on October 4th 2013 due to the US administration shutdown (European Commission Trade Agreements 2013).

1.3 Research Question and Interest

The following research question arises from this issue:

What are the fundamental and peripheral obstacles in the free trade agreement negotiations between India and the European Union?

The following sub-questions will be answered in the course of the thesis:

What are the potential gains and losses from free trade agreements?

In what respect do the two economies and their interests in the BTIA differ from each other?

What will be the impact of the integration of intellectual property rights and government procurement on both parties?

First and foremost, it is important to consider which issue areas will be included in the FTA and which trade-offs and subsequently obstacles both parties will face. Both economies have been confronted with the consequences of slow business cycles, which shifted priorities towards domestic consolidation. The question at hand is whether India and the EU will both recognize the BTIA as a contribution to their path out of slow growth and therefore whether the BTIA can gain momentum again.

1.4 Current State of Research

The scientific literature on trade, free trade, and agreements is extensive. Numerous countries have committed to such agreements and a similarly high number are in negotiation status. Although the issue is formally embedded in trade theory within the discipline of economics, political, developmental, social, environmental, and legal aspects weigh in equally. This may be one of the reasons why there is little literature on the BTIA between India and the EU. Despite the long negotiation period, the potential outcomes of enhanced trade have not been researched much. Naturally, the parties involved release little information on the progress of the negotiations as well as on the issues that are under serious discussion. It was difficult to find enough reliable and detailed information, which is why this topic became all the more interesting to research. There are a number of press releases by the European Commission, the EU's chief negotiator, as well as notifications from the European Parliament. The Indian side

has kept much of the information under tight wraps and there are hardly any detailed documents.

Furthermore, it came as a surprise that India's usually very active civil society has not dealt with this issue extensively – yet. There are few articles and studies published on the implications of the FTA, one of which is “Trade Invaders” (2010) by the Corporate Europe Observatory and India FDI Watch (Eberhardt, Kumar 2010). It examines the impact of large businesses, especially retailers, on the FTA-negotiations and provides a highly critical point of view.

The Asian Development Bank provides a useful and well-structured overview of the main information on the negotiations and the agreement. A listing of the latest news, opinions, and studies and research on the topic can be found on their website. The WTO also provides basic and useful information. The single most detailed study is “Qualitative analysis of a potential Free Trade Agreement between the European Union and India - Main Report” (Gasiorek et al 2007). The study conducted by Ecorys Research and Consulting, CUTS International and Centad Centre for Trade and Development (2009) “Trade sustainability impact assessment for the FTA between the EU and the Republic of India” looks into the quantitative side of the agreement based on computable general equilibrium modelling (CGE) and gravity modelling (Ecorys 2009).

1.5 Relevance in the Context of International Development

The WTO has been regulating trade between nation states for several years and the developments of a highly globalized world have yielded new challenges in trade. Industrialized, emerging, and developing countries are affected by these changes and they require new answers to old questions such as: how do we create sustainable economies, which grow in a way that their citizens can pursue decent lives? This is a question where free trade agreements play a vital role. Therefore, the relevance for the discipline International Development stems from the following perspective.

The institutional framework of the WTO provides numerous rules and regulations under which its FTAs work and it puts clear restrictions on WTO members who sign such agreements. Under the WTO, countries are bound to the Most-favoured-nation (MFN)

treatment, which constrains them to treat every member state equally in terms of lower tariffs fewer barriers, and market access, as well as the flow of investments (WTO Principles of the trading system 2013). FTAs, however, are like an exception to this rule and underlie different restrictions. To avoid potential discrimination against WTO members, parties are obliged to keep tariffs against outside parties constant and ensure compliance with WTO standards. As of now, the EU-28 and India are members of the WTO and are therefore obliged to favor fellow WTO members in terms of trade barriers. The FTA would put tariffs and potential export and import ratios to a new discussion as they could potentially fade away within the scope of a FTA (WTO Principles of the trading system 2013). Considering India's growing economy along with a high poverty rate (among other domestic challenges), the extent of exposure to the WTO and FTA regulations - and the subsequent benefits - becomes a central factor of analysis. Market protection mechanisms have always played a major role in India's political and economic development. Scholarly opinion differs as to what extent the country's growth can be ascribed to excessive protection or not. The consequences of an FTA on a rather protective economy like India is hence considered part of the developmental relevancy of the subject.

Since India's economy has started to slow down and growth rates have decreased, India's poor have been suffering the most. As Sen (2013) claims, „Living conditions in the poorer half of India are not much better, if at all, than in the poorer half of Africa,” (Sen, Drèze 2013 and New York Times 2013). Malnutrition rates in India are higher than in sub-Saharan Africa and this situation will continue to exacerbate if India does not find a way to address its wealth creation and – more importantly – the redistribution (Sen, Drèze 2013 and New York Times 2013). In the EU, on the other hand, the debt crisis has affected a couple of member states and it requires smart economic reforms. Furthermore, it raises questions about the EU's cohesion as a political project. A trade agreement like the BTIA of the size and relevance may prove beneficial to its recovery.

Nevertheless, it is central to deal with the question of beneficiaries of a FTA between India and the EU as intensive trade between an emerging country and a highly industrialized economic zone such as the EU carries implications for different economic starting bases as well as negotiation positions. I believe this question is highly relevant in the context of international development, as it will illustrate the potential of mutually beneficial cooperation even in the face of vastly different starting points.

1.6 Structure of Thesis

The approach to the topic at question is interdisciplinary: the political, economic and developmental perspectives complement each other and blend together in order to provide a holistic analysis.

In order to understand both partners' ambitions for a bilateral agreement thoroughly, I start with a detailed introduction to both partners. Information on the respective political structure, history, economic status, and fiscal and monetary policy is provided. With respect to India, its developmental indicators and prospects will also be illustrated. Following that, chapter 3 will deal with the trade relations of the two economies and outline the current trade patterns, the investment situation and recent trends.

In the course of the thesis, I will introduce basics of trade theory relevant to the understanding of this thesis. Hereby the focus is on free trade and foreign trade policy. After that the institutional framework, which was the General Agreement on Tariffs and Trade (GATT) at first and later became the World Trade Organization (WTO) will be described.

In the subsequent section the characteristics of the BTIA will be described based on the material that is available. It is important to note that there is no publicly available proposal on the table, so the key issue areas of the negotiation are based on literature review. Nevertheless there are some facets that can be summarized and presented to ease the understanding of the process.

In chapter 6 I then extract two cases – intellectual property rights and government procurement – and conduct an analysis of their impacts on both negotiation parties' economies, social and environmental spheres. The findings yielded in the analysis will then be summarized and potential solutions will be put forward. In the end a general conclusion will attempt to bring the different facets of the thesis together and put the results into a developmental perspective.

This thesis builds on a purely theoretical approach. I work solely with primary and secondary literature. As mentioned earlier, although the available literature on the broader topic of free trade is abundant, information on the BTIA itself as well as the negotiations is limited to a small number of studies. Unfortunately, attempts to conduct interviews with stakeholders relevant to the impact analysis of this thesis were unsuccessful.

2. Profiles of the Two Partners

Although the partners' cases we are looking at are very different from each other, they also have many things in common. On the following pages, I provide detailed profiles of India and the EU. The profile contains information on the respective political situations, policy trends, fiscal and monetary policies as well as a forecast on future developments.

2.1 Profile of India

The Republic of India is commonly referred to as the largest democracy worldwide. Its population has exceeded the one-billion benchmark in the 1990s and currently it stands at 1.21bn (March 2011; provisional estimate from 2011 census; Economist Intelligence Unit Country Report India 2013: 15). This makes India the second most populous country in the world (BBC India Country Profile 2013). Forecasts predict India's population to overtake China's by 2025 (United States Census Bureau 2009). By 2035, about 65 per cent of the population will be of working age making India not only the country with the largest population, but also the world's largest labour market¹ (Kazmin 2010). With a higher level of industrialization, the Indian population is increasingly concentrated in urban areas. The main towns include (pop. in million in parenthesis): New Delhi (capital, 21.8 million), Mumbai (Bombay, 20.8 million), Kolkata (Calcutta; 14.6 million), Chennai (Madras; 8.9 million), Bangalore (8.7 million), and Hyderabad (7.7 million) (Economist Intelligence Unit Country Report India 2013: 16). Culturally and linguistically, India is highly diverse. The country is home to multiple different tribes and religions. The major religions are Hinduism (80.5 per cent of the population) and Islam (13.5 per cent) with Christianity (2.3 per cent), Sikhism (1.9 per cent), Buddhism (0.8 per cent), and Jainism (0.4 per cent) also being notably present (Census India Government 2011). Countrywide, around 400 languages are spoken, whilst Hindi and English are the official languages (Rajbhasha 2013). The former is the primary language of 30 per cent of the population and the latter primarily serves official, administrative and business purposes (Economist Intelligence Unit, Country Report 2013: 16). The federal organizational structure equips individual states to legislate their own official language if they wish to do so.

India's variety is also reflected in its topography and climate. The Himalayan mountain chain

¹ In 2011, the total labour force was at 476,663,507 (World Bank data Labour force total 2013).

and tundra stretch over the far north, Rajasthan in the East is characterized by the desert and corresponding weather conditions, the Ganges basin is humid subtropical; the North-West (Punjab, Haryana) with strong largely semi-arid agriculture. Most parts of the Indian peninsula are tropical humid with monsoon rains in June-September.

The Indians use the metric system with numbers often written in lakhs (100,000) and crores (10 million). The currency is Rupee (Rs.) with Rs.1 = 100 paisa. The fiscal year starts April 1st and ends March 31st. Major public holidays include Republic Day (January 26th), Independence Day (August 15th) and Mahatma Gandhi's birthday (October 2nd). There are several religious holidays celebrated in parts or even the whole country (India Government calendar 2013).

Table 1. India Demographics, 2008 & 2030 (mill). Get numbers from EIU

India	2001	2011	Difference
Urban population	28.6	37.7	9.1
Rural population	74.3	83.3	9.0
Total population	102.9	121	18.1
Urbanization rate	27.81%	31.16%	

Source: Census India Government 2011.

The numbers in Table 1 show the distribution of urban and rural population and their changes between the 2001 and 2011 census. The absolute population increase was larger in urban areas than in rural areas – for the first time since India's independence. According to the 2011 census, the trend towards urbanization has led to an altered distribution of 68.84 per cent versus 31.16 per cent of rural versus urban population (Ministry of Home Affairs New Delhi, 2011).

2.1.1 Political Affairs

India is a “sovereign, socialist, secular, democratic republic” with a federal form of government consisting of 28 states and seven union territories (The Constitution of India). The president, currently Pranab Mukherjee (since 2012), is the head of state and elected every five years by the members of both the Houses of Parliament “(...) and the elected members of the Legislative Assemblies of States and the Union Territories of Delhi and Pondicherry.”

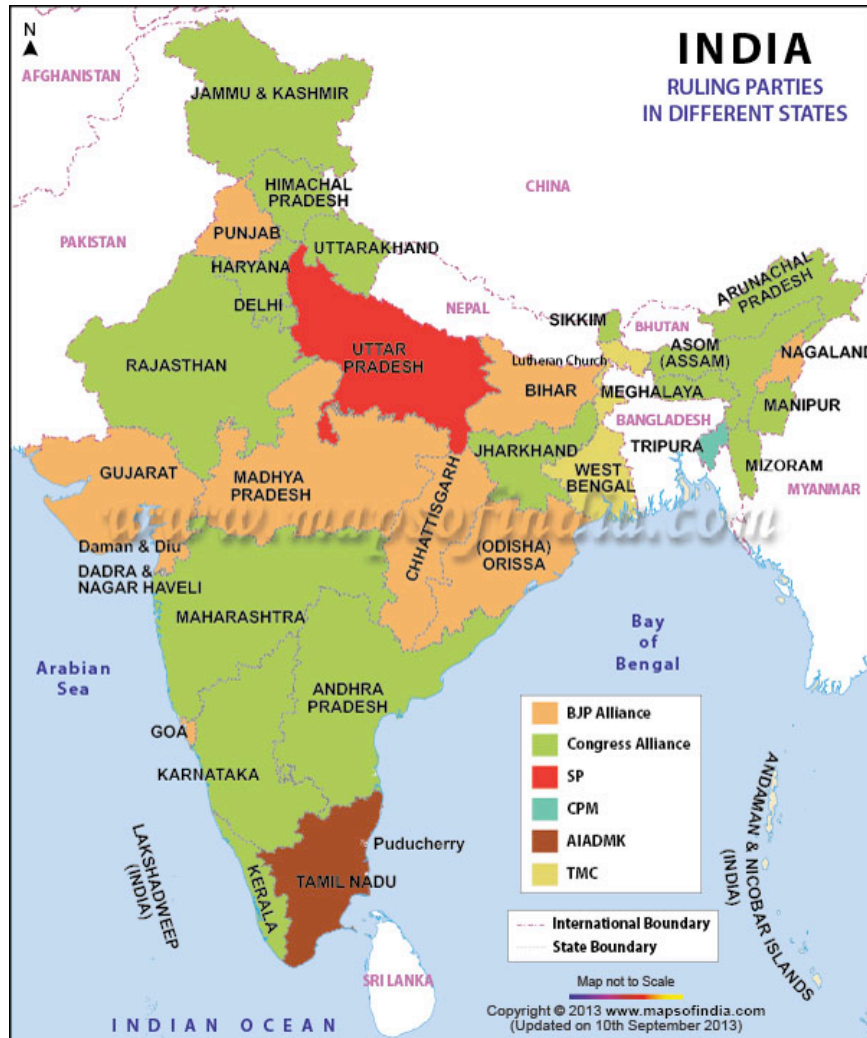
(Election Commission of India 2013).

The prime minister and the council of ministers lead the executive branch with elections taking place every four years. India's legal system is based on the 1950 constitution and English common law. The bicameral national legislature consists of the lower and upper house. The former, called the "Lok Sabha", has 545 members of which 543 are elected from single-member constituencies. 84 of the seats are reserved for "scheduled castes" and 47 for "scheduled tribes", whereas the reservation is made based on census data on the allocation of scheduled castes and tribes relative to the total population in each state (Election Commission of India, 2013 II). Two additional representatives are Anglo-Indians and appointed by the head of state. The upper house, "Rajya Sabha", consists of a maximum of 250 members, although presently there are 245 members. 233 of those are elected by weighted votes of the members of parliament, the legislative assemblies of states and union territories. The president appoints the remaining 12 members (Rajya Sabha, 2013).

The current Indian government is formed by the United Progressive Alliance (UPA) and has been in power since the elections in April/May 2009. The Indian National Congress Party dominates the coalition government and thus their nominated candidate, Manmohan Singh, was appointed Prime Minister by the president. Similarly, the Congress Party heads other key ministries (Government of India Union Government 2013).

As of July 10, 2013, India has six nationally recognized parties. The Indian National Congress is commonly categorized as centre-left wing and it is one of the two largest parties by voters in India. Sonia Gandhi, the chairwoman of the India National Congress and widow of former Prime Minister Rajiv Gandhi (son of Prime Minister Indira Gandhi) has been leading the party since 1998. The centre right religious nationalist Bharatiya Janata Party (BJP) is chaired by Rajnath Singh and constitutes the country's second largest party. The remaining four parties are Bahujan Samj Party, Communist Party of India, Communist Party of India (Marxist) and Nationalist Congress Party (Election Commission of India 2013, Political Parties). Apart from the six national parties, there are around 50 state parties.

Graph 1: Ruling parties in India



Source: Maps of India 2013.

2.1.2 History

India's economic rise took off in the early 1991, when the country was under pressure of a balance of payments crisis and the government under Prime Minister Narasimha Rao and Finance Minister Manmohan Singh came into office. The Congress administration transitioned the country from a closed, protective to an open economy by introducing several reforms (Panagariya 2007: 231). Foreign direct investment (FDI) was allowed into the economy and the new capital spurred economic growth in the subsequent years. After

independence from the British colonial Raj on August 15th 1947, India's first (and the following) administrations followed a socialist, protective approach. Due to its colonial past, the country has been dominated by a strong desire to stay as independent as possible from the "outside", the "West", which could not be trusted. Jawarlal Nehru, India's first Prime Minister and the head of the Gandhi-Nehru dynasty, introduced five-year-plans with a strong emphasis on government and state control and a highly sophisticated license regime, the license raj. This red tape system of excessive regulation and conformity to rules still exists, however, with a lower degree of severity (Business Monitor International 2013: 39). On matters of foreign policy, India follows a strong non-alignment policy.

2.1.3 Economic Growth

For the longer of the first decade in the new millennium, India's economic growth was only outstripped by China. Growth rates of 7.25 per cent a year between 2001-2010 looked promising / were promising for India to further alleviate poverty, create a trusted haven for FDI and a sound environment for trade (Planning Commission Macroeconomic Summary). Growth, however, slowed down as the global financial crisis hit India and went from 9.7 per cent in 2008 to 6.1 per cent in 2009 (first quarter data, Trading Economics 2013). After catching up for a while in 2010 with a peak growth rate of 9.4 per cent in the second quarter, the economy did not fully recover and did not reach its proclaimed growth potential. Apart from the global crisis, the country's lack of reforms and economic stimuli undoubtedly contributed to a rather slow recovery. Not only did this result in slower growth, but also in a growing fiscal deficit and higher inflation rates.

The factors that decelerate growth are versatile and include "drought in parts of southern and western India, weaker business and consumer sentiment and capacity constraints" (Economist Intelligence Unit Country Commerce India 2013: 6). The droughts in 2012 affected agricultural output heavily and output growth fell to 1.8 per cent. Furthermore, capacity constraints are often cited as a common held back for emerging economies like India. Even after a relative ease of external risk (like experienced by the economic crisis), internal supply bottlenecks remain unsolved. These constraints are accompanied by a shortage of skilled labour, a lack of infrastructure investments and "(...) difficulties involved in moving from

low-productivity agriculture to high-productivity manufacturing (...)”² (Economist Intelligence Unit Country Commerce India 2013: 6).

It was not until September 2012 that the government undertook first reforms aimed at the growing fiscal deficit (Economist Intelligence Unit Country Commerce India 2013, 5). For 2012/13, real GDP growth is forecasted at 3.3 per cent. Hopes are high that the government will undertake further reforms and catch up to an average expansion of 6.9 per cent per year in 2013/14-2017/18. Growth is forecasted to be mainly driven by private consumption and investments (Economist Intelligence Unit Country Report India 2013: 6).

2.1.4 Fiscal Policy and Policy Trends

Not only do government reforms attempt to boost the economy, but they also aim to consolidate the growing fiscal deficit. The government’s deficit widened radically between 2007/08 (2.5 per cent of GDP) and 2011/12 (5.7 per cent) (fiscal year: April-March, Economist Intelligence Unit Country Commerce India 2013: 5). The government’s budgetary plans were impeded by several developments since 2007. The global financial crisis unexpectedly slowed down economic growth and thus increased the fiscal deficit. In addition to the economic slowdown, the government’s lavish way of dealing with its budget contributed further to the negative balance. India is well-known for its inefficient and generous subsidy system. One example is electricity tariffs for farmers, which for political reasons state authorities tend to keep at an artificially low level. Free or very cheap water and fertilizers are granted, as farmers constitute the single most important voter clientele. However, these subsidies are often inefficient and wealthy farmers benefit disproportionately from them. As a result, states incur high operating deficits, which ultimately must be covered by the centre government (Economist Intelligence Unit Country Commerce India 2013: 6). Food and fuel subsidies are similarly cited as a burden on the budget.

Until September 2012, the fragmented Indian parliament hampered the timely implementation of consolidation measures. Finally, when the government undertook reforms, it primarily addressed the revenue side of its balance sheet. Rail fares were raised for the first time in a decade (Economist Intelligence Unit Country Report India 2013: 5). Furthermore, reducing

² The transition from the agricultural to the industrial and services sector is discussed in subchapter 2.1.6 in more detail.

fuel subsidies consolidated the inflated subsidy system. In total, subsidies were reduced from 5.6 trillion in 2009 to three trillion in 2011 (World Bank Data 2013b). This corresponds to a percentage of GDP deceleration from 52.0 per cent in 2009 to 21.7 per cent in 2011. In addition, as percentage of GDP, total government expenses dropped from 16.5 per cent in 2009 to 15.3 per cent in 2011 (World Bank Data 2013b).

By putting these and further measures into place, India's budgetary strategy for 2013/14 foresees a reduction of the fiscal deficit to 4.8 per cent of GDP. The EIU forecasts a reduction to 4.9 per cent of GDP, mainly led by reduced expenditure rather than an increase in revenues. However, the forecast is impaired by political developments in India, namely the general elections in May 2014.

2.1.5 Monetary Policy

By controlling its monetary policy, a country's central bank regulates money supply, credit and interest rates in the economy. By doing so, the cost of money is controlled and kept at acceptable level. Central banks use the mechanism of liquidity regulation and the implementation as well as the monitoring of directives on bank lending and deposit rates (Krugman, Obstfeld, Melitz 2012: 362 ff.). The main objectives to do so are the maintenance of price stability (inflation) and economic growth. India's central bank, the Reserve Bank of India (RBI) is legally bound by the Reserve Bank of India Act of 1934 and the Banking Regulation Act of 1949 (amendment passed December 2012). Under this legal framework, the RBI monitors the development of inflation and steps in if necessary (RBI 2013).

2.1.5.1 Financial Regulation in India: Reserve Bank of India

The RBI also supervises the activities of all domestic and foreign banks as well as non-banking finance companies (Economist Intelligence Unit Industrial Report 2013: 15). The central bank's approach towards the financial sector requires all banks to comply with its tightened prudential norms, i.e. submit annual consolidated financial statements and implement strict regulations in areas of concern. A number of guidelines have been implemented on setting up asset liability management systems, which allows the RBI to perform risk management better.

The RBI has also been implementing regulations laid down by Basel II, i.e. frameworks to

measure risk factors when exposed to sensitive sectors. These frameworks were standardised by the RBI in order to provide banks with operational risk control as well as internal models to assess market risk. In 2008, the RBI set a capital adequacy ratio of 9 per cent for all banks (1 percentage point higher than required in Basel II). This norm is applicable to foreign banks in India as well as Indian banks operating outside India equally. Another measure to limit risk exposure of banks operating in India are lending limits. They are set at 15 per cent respectively 40 per cent of capital funds to a company or industrial group. However, banks are equipped with the autonomy to raise these limits by an additional 5 per cent in “exceptional circumstances” (Economist Intelligence Unit Industrial Report 2013: 16; RBI 2013). In the last few years, the RBI has undertaken a number of steps in order to decrease risk exposure of all banks and increase compliance with international standards. The government complemented these efforts by targeting bad loans. In 2002, it passed the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act. The law is aimed at reducing default and allowing creditors to enforce their interests without having to consult a court (Economist Intelligence Unit Industrial Report 2013: 16).

In the past decade, the RBI has shown a strong tendency towards deregulation of interest rates and other controls. This, together with the previously mentioned actions, underlines the RBI and the government’s efforts for a strong and secure financial sector. This emphasis is supported by the compliance with international standards, such as the Basel II pillars (pillar 2: supervisory review process and pillar 3: market discipline guidelines) and signalizes trust and stable expectations to international investors (Economist Intelligence Unit Industrial Report 2013: 17).

2.1.5.2 Monetary operations

In order to keep prices stable, the RBI performs a number of monetary operations. Open market operations (buying and selling of government assets) are the most commonly used mechanism to influence money supply in the economy (Krugman, Obstfeld, Melitz 2012: 467 ff.).

Due to the Indian economy’s slowdown and concurrent low real GDP growth, the RBI cut the

repurchase rate³ several times. Since October 2013, it stands at 7.75 per cent (Reuters 2013, Economist Intelligence Unit Country Report India 2013: 5). The central bank repurchases government securities from commercial banks at the repo rate and modifies the rate according to the level of money supply it desires to maintain in the country. Thus a decreased repo rate will subsequently increase the money in the economy as banks can cheaply swap their assets for cash. Additional money supply ought to increase investments and henceforth spur the economy.

The RBI recently pointed to the relatively limited scope for further quantitative easing⁴ and thus an increase of the repo rate in the near future. Accordingly, the government is asked to step in and fulfil its responsibility of boosting investments and subsequently GDP growth. The RBI also recommends strict compliance with laid-out goals such as fiscal consolidation, “easing supply bottlenecks and improving governance” (EIU Industrial Report 2013, 18).

2.1.5.3 Current Account

In 2012, the Indian currency stood at an average of Rs. 53.44 = US\$ 1⁵ (Economist Intelligence Unit Country Report India 2013: 9). Compared to 2011, the rupee depreciated by 12.7 per cent and it stands at a record high in 2013 of Rs. 62.39 to US\$ 1 (Yahoo Finance 2013). The advantage of the weak rupee has been a reason for an increase in Indian exports since it made Indian exports cheaper to foreign buyers.

³ “Repo rate is the rate at which the central bank of a country (RBI in case of India) lends money to commercial banks in the event of any shortfall of funds.” (The Economic Times 2013).

⁴ Quantitative easing refers to an increase in the money supply and subsequent decrease of interest rates through the central bank by purchasing securities from the market (Investopedia Quantitative Easing 2013)

⁵ Average in 2011: Rs. 46.67 = US\$ 1 in 2011 (Economist Intelligence Unit Country Report India 2013, 9)

Graph 2: USD/INR exchange rate 2013



Source: Yahoo Finance 2013.

In the long term, the rupee's value is ought to rise and offset current unfavourable effects such as expensive imports and a negative perception of the Indian economy⁶. The factors currently putting pressure on the currency, such as the current account deficit, are forecasted to narrow and discontinue putting pressure on the rupee. On the other hand, strong foreign capital inflows are ought to aid the rupee to appreciate in the short-term. However, risks to the currency remain and are to be taken seriously. They include the risks of a fiscal crisis in case the government cannot cope with the deficit; a strong rise in prices as well as volatile capital inflows due to political and economic uncertainty (Economist Intelligence Unit Industrial Report India 2013: 18).

The RBI reports India's current account, which is "the sum of net exports of goods and services, net primary income, and net secondary income" (World Bank Data 2013b, Current Account Balance). India's balance in 2011 was minus 60 bn. dollars. The account featured a deficit of US\$ 18.10 bn. in the first quarter of 2013 (3.6 per cent of GDP, Trading Economics India Current Account 2013). The deficit decreased from a historically high level of 84.3 per cent of the country's Gross Domestic Product in 2003 to 67.57 per cent in 2012 (Trading Economics India Government Debt to GDP).

⁶ Investors associate a weak currency with a weak economy and are consequently hesitant to invest in the economy.

Weak imports of for instance crude oil and gold imports have been distorting India's trade balance for years. Further, this widening trade deficit has been accompanied by a slowdown of inward remittances from overseas Indians, which, however, are forecasted to start growing again over the period of 2014 to 2017 (Economist Intelligence Unit Country Report India 2013: 7).

Despite the recent positive development of the current account, the RBI recommends to remain careful, to eschew from optimism, as markets seem rather unpredictable. The RBI is constrained in performing further monetary easing and suggests a close look at market developments while formulating policies.

2.1.5.4 Inflation

India has been confronted with rising consumer prices over the past decade, which often hit the poorest strongly. The main measure of inflation in India is the wholesale price index (WPI), which itself is divided into three groups: primary articles (20.1 per cent of total weight), fuel and power (14.9 per cent) and manufactured goods (65 per cent). A wholesale goods basket using these categories is put together and used to determine a representative consumer basket. In 2012, the inflation rate⁷ stood at 8.2 per cent (World Bank Data Inflation 2013).

2.1.6 Labour

India's ranks as the world's second most populous country results in a large labour force. The labour force participation rate was at 36.4 per cent in 2011, with males dominating the labour force. Official unemployment numbers are at 8.7 per cent, however, they do not reflect the high number of unregistered people (Economist Intelligence Unit Country Report India 2013: 7). The distribution of employment between the primary, secondary and tertiary sector has changed significantly, as the following table shows:

⁷ "Inflation as measured by the annual growth rate of the GDP implicit deflator shows the rate of price change in the economy as a whole. The GDP implicit deflator is the ratio of GDP in current local currency to GDP in constant local currency." (World Bank data Inflation 2013).

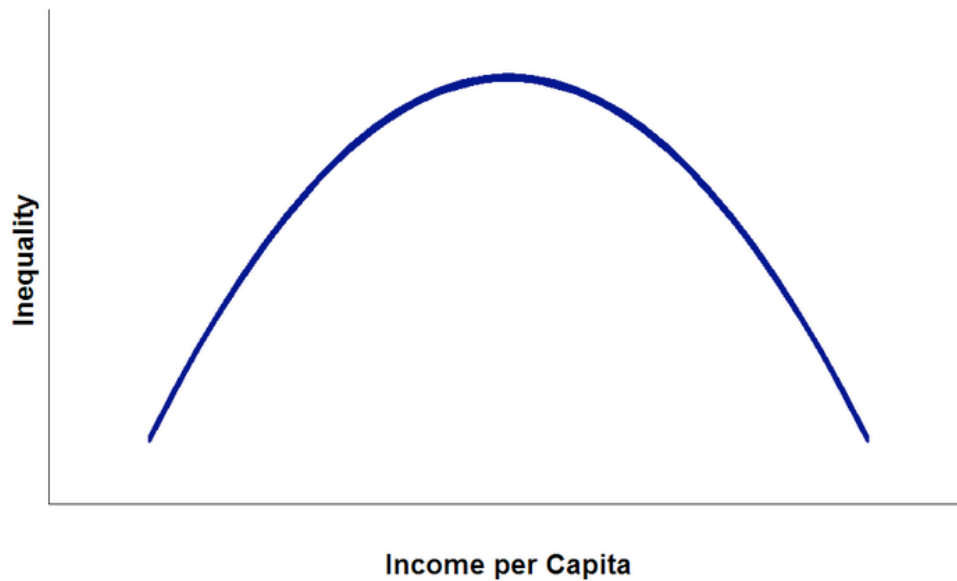
Table 2. Indian Employment in 2005 and 2011 (in millions).

Employment	2005	2011	Difference
Agriculture	207.1	212.5	5.4
Industry	69.4	105.4	36
Services	92.4	116.6	24.2
Total labour force	380.8	447.0	66.2
Total employed	368.9	434.6	65.7

Source: Census India Government 2011.

The data underline the perception of India's disproportionally growing services sector, which shows a difference of 24.2 million between 2005 and 2011. In comparison, the secondary sector increased to 105.4 and the agricultural sector shows little growth. These figures become all the more interesting if they are put into context of the Kuznets process (Kuznets 1955). According to Simon Kuznets, a Ukrainian-Russian-American economist, countries grow according to an inverted-U-shaped graph (see graph 2). The horizontal axis reflects economic development (which is measured by per capita income) and the vertical axis measures income equality. When economies start growing, they are highly agricultural and show a low level of income inequality but also a low level of per capital income. As economies develop further, they enter the industrialization stage. Here, income inequality increases over time. At a critical point, inequality starts dropping and per capita income increases further. In this last stage, countries' growth stems largely from the services sector (Tam 2008: 368).

Graph 3: Kuznets curve



Source: Private notes.

As with any economic model, to many economic models, this hypothesis has to be treated with caution. A number of counter-examples suggest the Kuznets model to be inaccurate or even completely non-applicable. The East-Asian tiger states, for instance, can be cited as counter examples: Taiwan, Hong Kong, South Korea and Singapore grew rapidly in the 1990s with a secondary sector based development plan and decreasing income inequality (Asian Development Bank 2009: 232 ff.).

With regards to India, the curve can be applied to its labour distribution in the three sectors: the data suggests that India has a strong agricultural and services sector, whereas the industrial sector is only growing marginally. Relating this thought back to India's large labour force, economists suggest that India has skipped the industrial phase, which, however, will cause problems. Since the services sector requires relatively fewer and more educated labour, India's large unskilled and large labour supply is at risk of remaining unemployed or seeking employment in the low-income agricultural sector. This development bears the risk of India being manoeuvred back in its economic development (Asian Development Outlook 2007, 270 f).

2.1.7 Development Indicators

The next Lok Sabha elections are due in May 2014 and promise to be a close run up between the BJP and the Congress Party and their leading candidates. Narendra Modi, the BJP's candidate for next Prime Minister and Chief Minister of the state of Gujarat since 2001, is highly controversial and well known for his not fully investigated involvements in the 2002 Gujarat riots⁸ (BBC Profile Narendra Modi 2009). On the other side of the spectrum, the Congress party fielded chairwoman Sonia Gandhi's son, Rahul Gandhi. Both parties' campaigns are dominated by India's current account deficit⁹ and the falling rupee, both of which point out India's economic problems and its worst consequence: growing poverty. Onion prices, which are a popular indicator for inflation, have been exploding and moved the spotlight on one pressing question: Why has the Indian government - despite a decade of substantial economic growth - failed to pull its poor out of desperate poverty?

Especially in light of the upcoming general elections, this issue is discussed widely. Some scholars point at the lack of infrastructure investment, others at the wasteful government subsidies. Two scholars, however, have been dominating the debate: Amartya Sen and Jagdish Bhagwati.

Sen, who is often falsely associated with the Congress party, published his book "An Uncertain Glory" in the summer of 2013, in which he argues that India has failed to invest in healthcare and welfare. This lack of investment, in turn, has caused the economy to suffer as a country's economic state is highly depended on its people's well-being (New York Times 2013). Even though India had managed to alleviate poverty to a large extent and create a new middle class, there are still hundreds of millions of poor people – which seems contradictory to India's high economic growth rates of the previous decade, as is illustrated in Table 3. Sen, for example, compares India's growth to Bangladesh, which grew at a lower rate but nevertheless has outperformed India in key development indicators.

⁸ The 2002 Gujarat violence erupted after Hindu pilgrims were killed in a train fire in the town of Godhra, Gujarat. In an subsequent violence, more than 1000 people, mostly Muslims, died. „Mr Modi was accused of failing to halt the religious violence“ (BBC Profile Narendra Modi 2009).

⁹ The current account is discussed in further detail in the next subchapter.

Table 3. India Key Development Indicators

India	2005	2010
Poverty rate ¹⁰	37.2%	29.8%
Life expectancy ¹¹	64.1 years	65.7 years
Literacy Rate	-	61.6% ¹²
Mean years of schooling	4.0 years	4.4
Fertility Rate	2.8	2.6
Gender Equality Index	0.637	0.619
CO2 emissions ¹³	1.3	1.7
HDI ¹⁴	0.547	0.507
GINI coefficient	-	33.9

Source: World Bank, Asian Development Bank, Census India, UNDP 2013.

Jagdish Bhagwati, a professor at Columbia University, makes a case for economic growth and its importance in a country's path out of poverty. In his latest book "Why growth matters" (Bhagwati and Panagariya 2013) he emphasizes the importance of a good investment environment for businesses. Such investments will subsequently create jobs and equip people with a higher disposable income, which they can use to provide themselves with healthcare and education.

Despite these considerations, the Indian government's spending priorities can be deducted from table 4, which compares health and education expenditure with military expenditure and paying off debts. The table illustrates the relative low increase in health and social security expenditures compared to, for instance, defence.

¹⁰ "National poverty rate is the percentage of the population living below the national poverty line. National estimates are based on population-weighted subgroup estimates from household surveys." (World Bank Data, 2013)

¹¹ "Life expectancy at birth indicates the number of years a newborn infant would live if prevailing patterns of mortality at the time of its birth were to stay the same throughout its life."

¹² This number is for 2011 (Census India), no numbers available for 2010.

¹³ Metric tons per capita

¹⁴ Human Development Index; World average in 2010: 0.69.

Table 4: Expenditure by function

India	2000	2008	Difference
General public services ¹⁵	596.9	1670.4	1073.5
Defence	565.1	1300.1	735
Education	703.2	1581.4	878.2
Health	156.0	382.6	226.6
Social Security and Welfare	168.7	538.9	370.2
Total	4016.9	9586.6	5569.7

Source: Asian Development Bank Country Profile India, 2013.

The Congress Party and the BJP have framed their campaigns around these two positions: one advocating equality, the other calling for more growth: the Congress considers itself to be an advocate of equity whereas the BJP makes strong cases for growth. It remains to be seen which position will more popular in the 2014 elections.

¹⁵ “Includes public order and safety” (Asian Development Bank Country Profile India, 2013)

2.2 Profile of the European Union

Since July 2013, the European Union is richer by one additional member: Croatia. The accession of a new member state signalizes political unity within what started off as European peace project and is now an unprecedented union of democratic states facing several challenges. The EU passed through a number of crises, going from a deep recession into moderate recovery and back into contraction in the last few years. Unemployment stands at a record high of 12.2 per cent (Euro area) and 11 per cent¹⁶ (EU28) in May 2013 (Eurostat Unemployment data 2013). Youth unemployment is twice as high at 23.3 per cent in the fourth quarter of 2012 (European Commission Youth employment 2013). Several countries implement strict fiscal austerity in order to reduce indebtedness and deficits and the ECB is challenged with an economy, which does not seem to be reacting to the stimulus of low interest rates.

Over the last decades the EU has been able to defend its prime position in trade. Its current account shows a moderate surplus, which strengthens investor confidence and sentiment. The EU27 account for 19 per cent of total world trade (exports and imports); it is the world's largest exporter of manufactured goods and services, the biggest export market for around 80 countries, and second-biggest importer (European Commission EU position in world trade 2013). Closely followed by the US and China, the EU meets the attribution/attribute of being an “economic giant”, although it is facing several challenges). The following pages provide an overview over the EU27 (EU28 respectively) and the euro zone, similarly to the overview provided for India's economy.

2.2.1 Political Affairs

With 28 democratic member states, the European Union consists of seven institutions – the European Parliament, the European Council, the Council of the European Union, the European Commission, the European Court of Justice, the European Central Bank and the European Court of Auditors (Europe – EU Institutions and other bodies). The European Union – but even more the European Monetary Union - is often referred to as a sui generis entity – an entity without historical precedent.

¹⁶ It stands at the highest level since 1995.

Over the past decades, member states have conferred substantial power to the EU (Eichengreen 2008: 2 ff). During this step-by-step process of pooling sovereignty several treaties evolved, which represent the EU's legal system. They include the following important treaties:

Table 5: The EU treaties

Treaty	Signed	Entered into force	Purpose
Treaties of Rome ¹⁷	25.03.1957	01.01.1958	“to set up the European Economic Community (EEC) and the European Atomic Energy Community (Euratom).”
Brussels Treaty	08.04.1965	01.07.1967	“to streamline the European institutions.”
Single European Act	07.02.1986 ¹⁸	01.07.1987	to reform the institutions in preparation for Portugal and Spain's membership and speed up decision-making in preparation for the single market.
Treaty on European Union	07.02.1992	01.11.1993	to prepare for European Monetary Union and introduce elements of a political union (citizenship, common foreign and internal affairs policy).
Treaty of Amsterdam	02.10.1997	01.05.1999	To reform the EU institutions in preparation for the arrival of future member countries.
Treaty of Nice	26.02.2001	01.02.2003	to reform the institutions so that the EU could function efficiently after reaching 25 member countries.
Treaty of Lisbon	13.12.2007	01.12.2009	to make the EU more democratic, more efficient and better able to address global problems, such as climate change, with one voice.”

Source: Europa EU Treaties 2013.

¹⁷ EEC and EURATOM treaties

¹⁸ In Luxembourg; 28 February 1986 in The Hague

The courts of the member states are responsible for the application and implementation of EU law, whereas the European Court of Justice hears special cases. The executive consists of the European Commission, the European Council and the Council of the European Union. The latter combines legislative and executive functions and consists of ministers of each member state. In its executive function, the Council of the EU meets in different councils, namely the general affairs council (foreign ministers), Ecofin (economy and finance ministers) and others (Europa ECOFIN Council 2013). The EU Commission consists of 27 commissioners and the Commission president, José Manuel Durao Barroso. It proposes new legislation to the European Parliament and the Council of the European Union and ensures the correct implementation of EU legislation. It is also the EU Commission who negotiates trade agreements (European Commission at work 2013). The third part of the executive, the European Council, is in charge of strategic policy. Its head, Herman van Rompuy, is the first full-time President of the European Council and was appointed by the European Council on March 1st 2012 for his second two and a half years term. He works together with the member states' heads of state or government (European Council President's Role 2013). The Council of the European Union and the European Parliament form the legislative power. The former consists of ministers of each member state and is coordinated by an alternating presidency and rotates among the member states every six months. The current presidency is held by Lithuania (July 2013- December 2013).

The European Parliament is the only directly elected EU institution and has 766 members representing 500 million citizens. It is the second largest democratically elected institution after the Indian parliament and elections take place every five years with the next elections planned for 2014. In those elections, every member state is represented by a fixed number of Members of the European Parliament (MEPs), which are allocated on the basis of degressive proportionality, i.e. the larger the population of a country, the more seats in the EU parliament but the smaller states "have more seats than strict proportionality would imply." (European Elections 2013). Once elected, MEPs organize themselves in political groups. Currently, there are seven of those, namely the European People's Party (Christian Democrats and similar centre-right parties; 274), Progressive Alliance of Socialists and Democrats in the European Parliament (195), Alliance of Liberals and Democrats for Europe (85), Greens/European Free Alliance (58), European Conservatives and Reformist Groups (56), Confederal Group of the European United Left – Nordic Left (35) and Europe of Freedom and Democracy Group (33). The 30 remaining MEPs are not in recognised groups at present.

The parliament's president, Mr Martin Schulz, was elected for a two and a half year term in January 2012 and "represents the European Parliament vis-à-vis the outside world and in its relations with the other EU institutions." (European Parliament's President 2013).

2.2.1.1 Political Stability and Outlook

The European Union, and in particular, the Euro area, was hit heavily by the 2008 and subsequent crises. The reasons were multifaceted and ranged from a fragile banking system with chronic capitalizing problems, high public and private debt levels to a deep gap between the different EU economies. The first country to feel the vigorous power of the decades of high debt and the like was non-EU-member Iceland, with Greece following soon after. Despite the EU stepping in and bailing its fellow member states out the following years were characterized by severe instability and a crisis of confidence in the Euro zone. It was only after the approval of Greece's second bail-out and the subsequent unprecedented injection of liquidity into the banking system by the European Central Bank (ECB) that confidence in the Euro zone was partly re-established. The signs for a stable future are rather positive, as political commitment for the EU remains strong in countries having to deal with severe austerity measures (Economist Intelligence Unit Country Report EU 2012). However, in creditor countries such as the Netherlands and Finland, Eurosceptic parties have changed the political landscape and enjoyed substantial gains in votes. It remains to be seen if the EU is capable of maintaining the presently high level of European solidarity and overcome its difficulties (Economist Intelligence Unit Country Report EU 2012).

2.2.2 Economic Growth

The euro zone and the EU-28 experienced a moderate recovery from early 2010 to early 2011 after the deep recession of 2008-2009. Real GDP picked up by 2 per cent and 1.9 per cent in the EU27 and euro area respectively. 2011, however, showed a downward trend of 1.5 per cent and 1.4 per cent respectively. Several developments caused only a mild recession in 2012 of 0.4 per cent and 0.6 per cent contraction in the EU-27 and euro area respectively (EU Real GDP growth rate volume 2013). Especially the ECB's monetary policy and the unprecedented capital injection allowed for a stabilization of the financial markets, whereas fiscal tightening was a strong factor pushing the EU deeper into recession. This development clearly shows the strong drag of austerity measures on GDP growth. It ought to be noted that growth within the

EU-27 and the euro zone bears major imbalances. The already deep divergence between stronger economies or so called core countries (Germany, the Netherlands, Austria etc.) and the periphery persists and will continue to do so unless measures to ease imbalances are undertaken (EU Real GDP growth rate volume 2013).

2.2.3 Fiscal policy and Policy Trends

Following bleak economic years, many European countries suffer from high levels of indebtedness. Several countries have violated the limit of a maximum 3 per cent deficit to GDP. This threshold, together with a maximum 60 per cent of public debt to GDP, is laid down in the corrective arm of the Stability and Growth Pact (SGP) “in order to ensure sound public finances necessary for the functioning of the Economic and Monetary Union (EMU)” (European Commission Economic and Financial Affairs 2013). Since then, a number of countries have undertaken strict austerity measures leading to tax rise and expenditure cuts (e.g. Greece, Spain, and Portugal). However, such measures do not stimulate a better economic performance but in turn worsen living standards and purchasing power. Thus, even though the SGP’s underlying objective of sound public finances is laudable, it bears the risk of a depressed economy demanding for even more fiscal austerity. Be that as it may, the SGP limits have not been strictly enforced in the context of the present crisis because of these very worries.

A brief look at the numbers reveals an average deficit for the euro area of 4.1 per cent in 2011, showing an improvement compared to 6.2 per cent of GDP in 2010 (peak in 2009 with 6.4 per cent of GDP). The EU-27 decreased its deficit from 6.9 per cent of GDP in 2009 to 4.5 per cent in 2011. Government debt (debt to GDP ratio) rose in both zones; for the euro zone from 79.9 per cent in 2009 to 85.3 per cent in 2010 and 87.2 per cent in 2011 and 74.8 per cent (2009) to 80 per cent (2010) and 82.5 per cent in 2011. The largest deficits were recorded in Ireland (13.1 per cent), Greece (9.1 per cent), Spain (8.5 per cent), the UK (8.3 per cent) and Slovenia (6.4 per cent) (EU Real GDP growth rate volume 2013). The countries with the lowest deficits are Finland (0.5 per cent), Luxembourg (0.6 per cent) and Germany (1 per cent) and Hungary, Estonia and Sweden experienced surpluses. In both zones, government revenues increased in 2011 compared to the previous years. The numbers signalize a slight ease for the EU and the euro zone and its deficit and indebtedness, even though the number are well above the SGP limits of 3 per cent deficit and 60 per cent public debt respectively (EU Real GDP growth rate volume 2013).

An alternative instrument to the SGP was created in January 2012, when 25 member states (the United Kingdom and the Czech Republic opted out) committed to the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, popularly known as the "fiscal compact" (Europa Press Release 2012). It came into force on January 1st 2013, but is not incorporated in existing EU treaties yet. It "aims to strengthen fiscal discipline in the euro area through the "balanced budget rule" (Europa Press Release 2012) and the automatic correction mechanism." (Europa Press Release 2012). The treaty requires its signatories to comply with even stricter deficit limits and to maintain a balanced budget, whereas temporary deviation from is allowed in exceptional circumstances. In case of violation, the "budgetary and economic partnership programme" applies, requiring the country to undertake structural reforms (Europa Press Release 2012). Despite good intentions, the fiscal compact will presumably have a minor role in influencing the EU member's fiscal performance, as there is little difference to the SGP and particularly the SGP's flaws. It can be forecasted, that countries with deficits over 3 per cent will need more time to bring their deficits down (Ireland, Greece, Spain, UK, France). Even though government revenues in the EU area rose on average between 2010 and 2011, they are expected to decrease when strict austerity measures weaken the overall economy (EU Real GDP growth rate volume 2013). This fear is particularly well-marked in Spain and France, where adjustment and reforms are planned to be financed by government revenues stemming from rather unrealistic GDP growth in the next years. A miscalculation in growth and subsequent non-occurrence of government revenue bears the risk of loss of investor confidence and a downgrading by rating agencies. This cycle could harm the euro zone as a whole, as higher interest rates (which could occur as result of a downgrading) make it all the more difficult to service debt.

Another exacerbating element is the lack of cohesion and governance within the euro zone, which dominate the epilogue in Greece and Portugal's drama. The macroeconomic imbalances are marginally taken into account when policy responses to the misery of the economic periphery in the EU are formulated. While such countries struggle with competitiveness and solvency, the advice mainly given by Germany emphasizes fiscal austerity and structural reforms. Although these are feasible measures in the long-run that guarantee the survival of the euro, in the short term they are rather harmful. By decreasing government spending, living standards are at risk, which in turn hinder the stimulation of domestic demand. If the latter fails to be revitalized, satisfactory GDP growth is at risk and so is the overall economic recovery.

In the near future, there is a realistic risk of Greece's default despite the bail-out and structural adjustment. In that case, contagion to similarly affected countries (Italy, Spain, Portugal) might come into play and destabilize the whole EU, if not the global financial economy.

2.2.4 Monetary Policy

In the EU, the European Central Bank (ECB) coordinates and oversees monetary policy for the 17 members Euro zone. With its main offices in Frankfurt, Germany, Euro zone members cede most the domestic central banks' powers to the ECB. The main activities of the ECB include price stability with inflation "close to but below 2 per cent; the management of interest rates and money supply as well as the coordination and deployment of liquidity to European banks and financial institutions (European Central Bank Information 2013). The ECB's economic philosophy of money neutrality is reflected in the use of short-term interest rates in order to ensure price stability¹⁹ and provide a sound economic framework for the real economy (Euro Area Interest Rate data 2013). Hence the figures of real income and employment, shall be stabilized.

The euro area's main refinancing rates (interest rate) stands at a low of 0.5 per cent (May 2013) as compared to May 2012 when it was at 1 per cent. Mario Draghi, the ECB president, announced to keep this accommodative monetary policy for a longer period of time if necessary. This announcement of the EU interest rate tendency is unprecedented and serves as a reaction to weak growth rates in the EU. By providing guidance for future rates in the EU, the ECB accommodates the rather bleak outlook for economic growth in the EU and thus aims to reduce market uncertainties. The ECB's hope is to keep interest rates (and hence the cost of borrowing money) low, and stimulate investments and as a consequence economic growth in the EU (European Central Bank Information 2013).

Pressure on the ECB to undertake boosting measures is strong and the ECB has shown unconventional support for the European banking system since mid-2011. The unprecedented liquidity injection under the long-term refinancing operations (LTRO), offered cheap and unlimited three-year loans with loose collateral requirements to a number of banks. The versatile effects of this step did not only restore investor confidence in the euro area but mitigated bank's funding concerns and prevented a credit crunch.

¹⁹ Defined as "price stability as "a year-on-year increase in the Harmonised Index of Consumer Prices (HICP)" (Euro Area Interest Rate data 2013).

Despite the unprecedented steps undertaken the last two years, the ECB remains unpopular in the media and limited in its scope of action. While sometimes not fully realized, the ECB acts as a central bank for a monetary union and is hence only able to react to aggregate levels of inflation and unemployment rather than individual state levels. In case of an economic shock in one country, the ECB is thus unable to provide the country an individual adaptation of the monetary policy. This leaves EU member states only with the fiscal policy instrument as the only effective means to influence their economies (European Central Bank Information 2013).

All things considered, it is important to keep both sides in mind. The establishment of an international regime as a credible recognized common central bank benefitted countries which were lacking such trust in their previous central banks. For smaller economies, the ECB also meant lower exchange rate fluctuations, which especially affected smaller countries with more volatile trade patterns. So reducing these fluctuations increases transparency and improves trade and investment as well as lowers transaction costs.

2.2.4.1 Inflation

At a level of 2.7 per cent in 2011, inflation declined to 1.6 per cent in June 2013 in the euro area (1.7 per cent in the EU) (Eurostat Press Release 2013). The rather high level of inflation in 2011 is said to be due to higher energy costs as well as tax increases and commodity price rises. The downward trend between 2011 and 2013 was mainly fuelled by “subdued domestic demand, ongoing fiscal austerity and weakening labour markets on wage rates” (Economist Intelligence Unit Country Report EU 2012). Compared to April 2013, when the rate was around 1.2 per cent, concerns about deflation aroused but were eased by July 2013 as commodity prices rose slightly.

2.2.4.2 Exchange rate

The Euro has been depreciating and volatile in response to the euro area’s crises. In 2010, the Euro stood at US\$1.33 on average, going up to US\$1.39 in 2011 and losing value since then. The 2011 average was at US\$ 1.39 for €1 and US\$ 1.28 in 2012 (Economist Intelligence Unit Country Report EU 2012). In 2013, the rate moved between US\$1.29 and US\$1.33 and US\$1.28 and US\$1.31 in the first and second quarter respectively. They are forecasted to be between US\$1.26 and US\$1.29 and US\$1.25 and US\$1.28 in the third and fourth quarter of 2013 respectively (MTFX Analytics 2013). The European Central Bank is determined to keep the exchange rate and investor’s trust in it stable and also keep inflation low (ECB

2013).

Graph 4: EUR/USD exchange rate 2012/2013



Source: Yahoo Finance 2013.

2.2.4.3 Current Account

The current account of the EU-27 is reported to be in balance, recording a surplus of 31.4 bn. euro (0.9 per cent of GDP) in the fourth quarter of 2012. The surplus grew by 0.2 per cent compared to the same time period in 2011 (Eurostat Current Account EU 2013). In the first quarter of 2013, the surplus was at 21.8 bn. euro (0.7 per cent of GDP) compared with a deficit of 7.7 bn. (-0.2 per cent of GDP) in the first quarter of 2012 (Eurostat Current Account EU 2013). This development is critical for the EU and particularly for those countries that are still coping with high debts. The strong export performance lead to the EU's current account surplus and gives positive growth signals (EU business 2013).

2.2.4.4 Unemployment

In 2000, around 20 million people (9 per cent) in the EU-27 were unemployed. The rate gradually decreased until the end of 2004, when 21.3 million people were without employment, corresponding to a 9.2 per cent rate. From 2005 until the first quarter of 2008, the rate again followed a downward trend, hitting a low of 6.8 per cent (Eurostat Unemployment statistics 2013). An upward trend has continued since the beginning of the economic crisis with a record high since 2000 in mid 2010 of 9.7 per cent unemployment rate. Until the end of 2012, 26 million people (10.7 per cent) were unemployed. The euro are roughly followed this trend, with lower unemployment between 2000 and 2004 and higher

rates between mid-2010 and late-2012. At the end of 2012, the euro area experienced its highest rate since 1995 of 11.8 per cent (Eurostat Unemployment statistics 2013). The most recent numbers mark euro area unemployment at 12.2 per cent and EU27 at 11 per cent (May 2013, Eurostat Press Release 2013b). In both zones, youth unemployment remains a strong challenge.

2.2.5 Policy Trends: “Deep Integration”

The EU certainly knows well about its economic strength and this fact is reflected in its “Deep Integration” approach. The eradication of trade barriers is accompanied by far-reaching liberalisation measures in further sectors. Those could involve investments, services and government procurement. Focus is also put on IPR as well as certain standards for labour and environment protection (European Policy Center 2009: 16 f.). Such “WTO plus” FTAs may also include cooperation in and the harmonization of rules and regulations. This approach, if applied to countries meeting the combined framework of interesting market potential as well as the willingness to eradicate tariff barriers and similar obstacles for the EU, offers a good point for defining selected FTA partners like India (European Policy Center 2009: 16 f.).

The profiles of India and the EU suggest that both economies are experiencing challenging economic times. India is confronted with growth rate that are below the potential of the economy and the EU is growing slowly after years of coping with a debt crisis. Politically, India is expecting turbulent elections in May 2014, which will determine the country’s future economic and developmental strategies. The next chapters are approached against these similarities and differences.

3. The EU and India's Trade Relations

The previous chapters gave a first overview of the two partners' economic and monetary states and indicated some challenges they are currently facing. In this chapter I provide an overview of the trade and investment relations between the European Union and India. It is against this background that the negotiations are taking place. It should be noted that "India was one of the first countries that initiated diplomatic relations with the European Economic Community in the 1960s" (Luif 2007: 45). Since then, both sides have shown their interest in intensifying economic relations and they have been doing so in various fields such as politics, trade, developmental assistance and investment.

Diplomatic relations between the independent India and the then European Economic Community date back to 1962. Since then, both sides have shown their interest in intensifying their relations and they have been doing so in various fields such as politics, trade, developmental assistance and investment.

3.1 Trade Patterns Between India and the EU

3.1.1 General Overview

At the time of the BTIA negotiations initiation, the EU was India's biggest trade partner with an overall share of 19.5 per cent of exports and imports (Ecorys 2009: 27). In 2008 India imported 18.2 per cent of its total share from the EU and exports 21.7 per cent to the EU. Vice versa, India is a rather small trading partner for the EU. The share of total trade (exports and imports) exchanged with India accounts for only 2.1 per cent of the EU's total trade flows, up from 1.5 per cent in 2002 (My dataset, p. 4). The EU imports 1.8 per cent of its goods and services from India and exports 2.4 per cent to India.

However, the former trend of increases in the trade share of the EU for India has been changing over the past years: EU-India trade flows show a decline compared to previous years as well as to the respective partner's trade share with the rest of the world. Thus in 2012 the total trade of India with the EU declined to 13.2 per cent (European Union, Trade in goods with India 2013: 9).

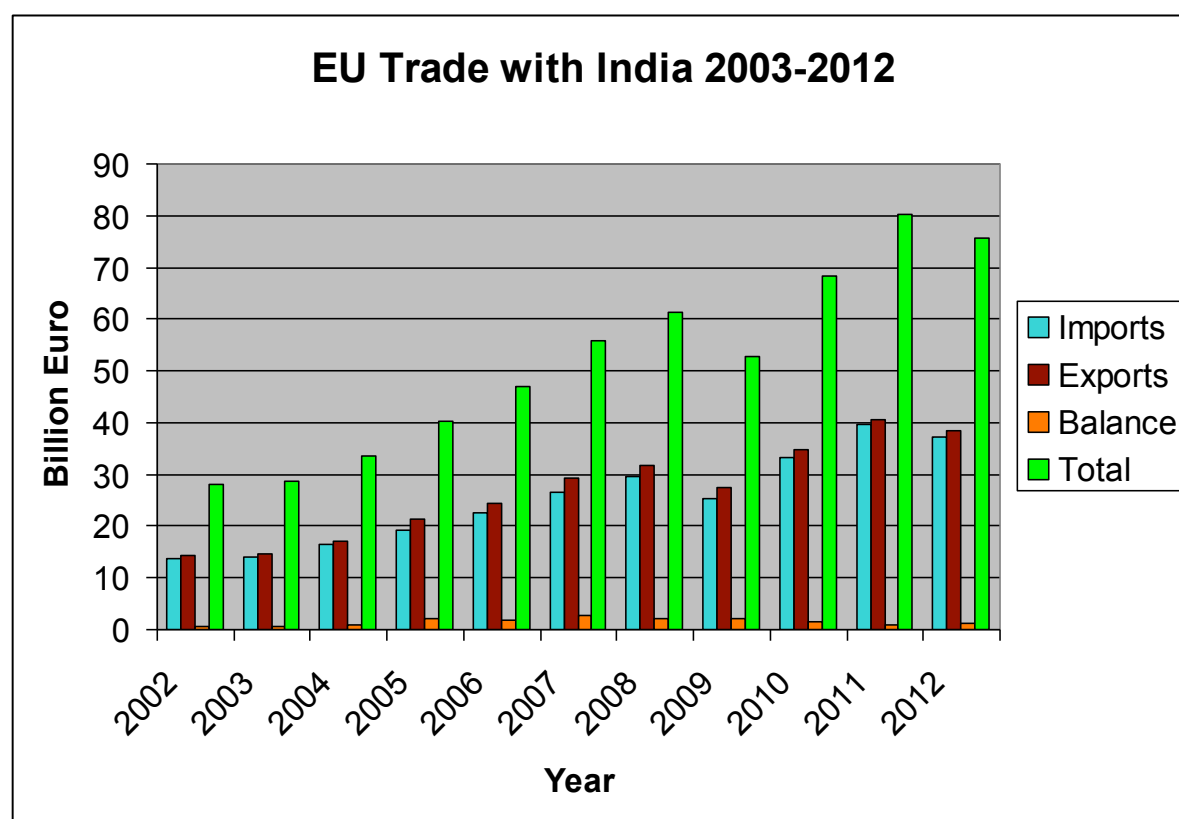
Although the EU remains the number one trading partner in all respects, i.e. imports, exports and total trade, the share has declined, as trade with other countries, such as China or the United Arab Emirates has gone up (European Union, Trade in goods with India 2013: 9). These patterns are not reflected on the European side of the partnership, where the total trade share of India remained almost the same at 2.2 per cent in 2012 (European Union, Trade in goods with India 2013: 10).

With regards to the absolute amount of trade a clear pattern can be identified in Graph 1. Whilst the mutual trade flows did not reach 30 bn. Euro in 2003, the total trade amounted to 76 bn. in 2012; the highest absolute level meanwhile was reached in 2011 with more than 80 bn. (European Union, Trade in goods with India 2013: 4). So it is evident that the figures imply a general upward trend in total trade between India and the EU, which suggests that both partners have an interest in expanding their cooperation.

3.1.2 Trade Balance

As Graph 5 also illustrates, the trade balance is almost even. Although the EU consistently exports more than it imports, the difference between the two is not noteworthy. In 2007 it reached its high, but has been levelling off since and in 2011 the balance was less than one bn. Euro.

Graph 5: EU Trade with India 2003-2012



Source: European Union, Trade in goods with India 2013.

3.1.3 Trade Composition

Evidently there are some common industries where trade between the two partners is most pronounced. Fortunately the latest figures cover the year of 2012. In this year the EU mainly imported textiles (amounting to 6.3 bn. Euro), mineral products (5.4 bn.) and chemical products (4.9 bn.). Combined these account for about 40 per cent of the EU's imports from India (European Union, Trade in goods with India 2013: 8). A trend that can hereby be identified is that the absolute amount of textiles has been almost constant in the last few years, but that the trade of chemical products has increased by over 60 per cent since 2008.

On the other side, the EU's exports mainly rely on machinery (11.6 bn.) and precious metals (8.3 bn.), which amount to over half of the exports into India with a rising trend for precious metals. To illustrate this summary, please see the following two tables containing the EU's imports and exports to and from India.

Table 6: Imports from India 2006

Products	Million Euro	%
TOTAL	26,262	100
Manufactured goods classified by material	8,325	31,7
Miscellaneous manufactured goods	6,875	26,2
Machinery and transport equipment	3,033	11,5
Chemical and related products	2,781	10,6
Food and live animals	1,527	5,8
Mineral fuels, lubricants and related materials	1,220	4,6
Crude materials inedible, except fules	695	2,6
Animal and vegetable oils, fats and waxes	140	0,5
Commodities and transactions	109	0,4
Beverages and tobacco	82	0,3

Source: Eurostat, Trade: 31.

Table 7: Exports to India 2006

Products	Million Euro	%
TOTAL	29,481	100
Machinery and transport equipment	10,873	36,9
Manufactured goods classified by material	9,399	31,9
Chemical and related products	2,325	7,9
Miscellaneous manufactured goods	1,585	5,4
Crude materials inedible, except fuels	1,208	4,1
Commodities and transactions	499	1,7
Mineral fuels, lubricants and related materials	126	0,4
Food and live animals	109	0,4
Beverages and tobacco	76	0,3
Animal and vegetable oils, fats and waxes	14	0,0

Source: Eurostat, Trade: 31.

3.2 Foreign Direct Investment

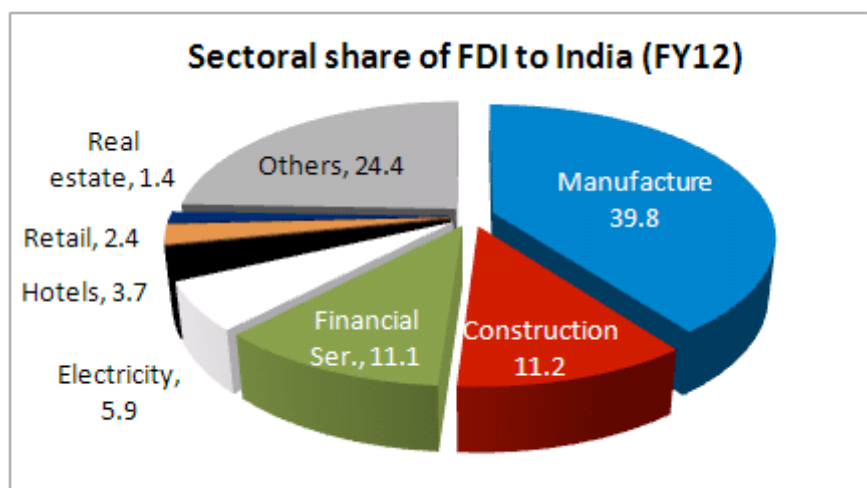
Of all countries investing in India, the EU-27 provides the largest amount of FDI. The direct investments have been steadily increasing over the last decade, as can be seen in table 8. The increase between 2006 and 2007 is especially noteworthy, but unfortunately I could not get hold of any more recent figures.

Table 8: FDI Flow from the EU-India

	2004	2005	2006	2007
FDI outflows to India	1.6	2.5	2.5	10.9
FDI outward stock in India	9.1	11.1	13.4	24.4
FDI inflows from India	0.0	0.5	0.5	9.5

Source: Ecorys 2009: 31.

Graph 6: Sectoral share of FDI to India



Source: Equitymaster 2012.

Most of the money that is invested goes into manufacturing with construction and financial services also boasting more than 10 per cent of the incoming FDI in India (Equitymaster 2012). Among the European Union the most prominent investors are Germany, Great Britain, the Netherlands and France (Ecorys 2009: 32).

4. Free Trade – Theory and Practise

In order to fully comprehend the BTIA between India and the EU, it is crucial to deal with the basics of trade theory and international trade. The latter involves the international organization dedicated to free trade, the World Trade Organization (WTO), which similarly requires a basic understanding.

In this chapter, I provide an introduction to trade theory and the gains from trade, and international trade. It will explain the institutional concept behind free trade, the World Trade Organization (WTO) and bilateral and multilateral trade agreements. Thereafter, I describe free trade as well as free trade agreements in the WTO setting. A special focus is on free trade in the context of development. At the end of the chapter, I describe both the EU's and India's foreign trade policies.

4.1 Trade and Trade Theory

Usually, it is considered broad consensus that some trade, particularly international trade, is beneficial to a country. Not many will oppose that Austria should import its bananas rather than grow them themselves. In trade theory, the exchange of tangible and non-tangible goods between two countries is to the mutual benefit of both parties.

In media, however, the prevalent opinion denounces trade as threatening to domestic economies, the job market and wages. Opponents of trade criticize disparities between countries engaging in trade, which leave weaker countries at a disadvantage. Such disparities do not occur often and if they do, they are short-termed and the benefits surpass the harms, proponents reply (Krugman, Obstfeld, Melitz 2012: 11 ff.).

As a matter of fact, international trade can cause internal distortions, forcing people out of their profession if they cannot compete with the new competition and leaving them in unemployment. The deepening of social inequality across the world – in developed as well as developing countries – is on-going, with real wages of unskilled workers decreasing steadily. Income distribution has altered as well, as larger groups of the population are pushed into labour and less people are concentrated in the more lucrative class of capital owners. Without doubt, these real-world policy problems require adequate solutions, but where does the strong discrepancy between trade proponents and opponents stem from? What are the patterns of

trade and how much trade is *healthy*? Is international trade in its most liberal form – free trade – worthwhile for developing countries and developed countries equally?

The very basic concept of trade “involves multiple parties participating in the voluntary negotiation and then the exchange of one's goods and services for desired goods and services that someone else possesses.” (Investopedia Definition of Trade 2013). The exchange usually takes place in a market. In addition to goods and services, trading can also involve financial goods – securities – which are exchanged in financial markets.

4.1.1 What Do We Trade?

Worldwide, primary goods form 7.02 per cent of world trade, secondary goods make up 54.73 per cent, services are 19.77 per cent and fuels and mining adds up to 18.48 per cent (Krugman, Obstfeld, Melitz 2012: 18). Not too long ago, it was primary goods, which dominated world trade heavily. Particularly developing countries were the primary exporters of natural resources. It is widely prognosticated that services will become more and more important (Krugman, Obstfeld, Melitz 2012: 20).

Several factors can influence the level of trade between two economies, the most common of which are the size of the economy²⁰, the geographical distance, business cycles, wars as well as protectionist barriers such as borders (Krugman, Obstfeld, Melitz 2012: 17).

4.1.2 History of Trade

Trade has existed for centuries as a form of exchange between human beings. Whereas early societies engaged in bartering, the emergence of currency as the main mean of transaction enforced the exchange of goods and services for money. The basic concept, however, remained the same: one thing is given in exchange for another.

From the well-known Silk Road in the 4th century AD to Vasco da Gama's sail around the Cape of Good Hope, societies soon discovered the benefits for their economies from trade with one another and increasingly engaged in it. In the 16th century, Portugal and Spain dominated international trade largely, and the Dutch followed later. It was the British Empire,

²⁰ E.g. the gravity model provides empirical evidence, see Krugman, Obstfeld, Melitz 2012, 15).

which consolidated much of the trade links and established further through their various colonies. The East India Company, which administrated the trade between India and the British Empire should be mentioned at this point (Carpenter, Dunung 2011).

Image 1: The silk road connecting the Mediterranean with Asia



Source: Carpenter, Dunung 2011

4.2 International Trade

Unlike trade within a country, international trade is “(...) the concept of exchange [of goods and services] between people or entities in two different countries.” (Carpenter, Dunung 2011). Several theories explain the principles of international trade. Among the most commonly known are Mercantilism, Adam Smith’s absolute advantage, David Ricardo’s relative comparative advantage as well as the Heckscher-Ohlin Model. One should bear in mind that these theories remain theoretical concepts, which assist economists and governments to better understand international trade. Nevertheless, they cannot be always fully applied to the real world (Carpenter, Dunung 2011).

4.2.1 International Trade Theories

4.2.1.1 Mercantilism

In the late 17th century, Europe was fragmented and awaiting a wave of revolutions. **Mercantilism** was the predominating trade doctrine and France its most prominent proponent. This approach aimed at a positive current account by promoting exports and protecting the economy from imports by applying (high) tariffs. This doctrine unleashed interstate tensions and led to intensified imperialism and colonialism (Carpenter, Dunung 2011). Mercantilism, along with other theories, hypothesizes trade from a country's perspective; therefore it can be categorized as a classical theory.

Table 8: Trade theories

Classical Theories	Modern Theories
Mercantilism	Country Similarity
Absolute Advantage	Product Life Cycle
Comparative Advantage	The Competitive Advantage
	Heckscher-Ohlin

Source: personal research, notes.

4.2.1.2 Absolute Advantage

In the British Empire, **Adam Smith** developed his theory on the benefits of specialisation for countries in his paper “Wealth of Nations.” (Smith 1776). It opposed mercantilism and promoted free markets. It was Adam Smith who proposed that as little government intervention in markets as possible, referring to the invisible hand, would support markets in regulating themselves and increase every nation's welfare. He defined the wealth of nations as the national income rather than the king's treasury. His theory of **absolute advantage** hypothesizes this by explaining that a country (country A) should specialize in the good it produces most efficiently due to, e.g., technology advances, and export the good to another country (country B), which produces the very same good less efficiently. In turn, country B exports the goods it is specialized in to country A (Krugman, Obstfeld, Melitz 2012: 621).

4.2.1.3 Comparative Advantage

In “Principles of Political Economy and Taxation” (1817), David Ricardo extended the concept of comparative advantage by the element of the relative production costs of goods compared to each other. According to Ricardo, a country ought to produce a good if the opportunity costs of producing it are lower than vice versa²¹. To provide a textbook example, we could consider the United States and its comparative advantage in computers. During major holidays, like Valentine’s Day, the United States would import their flowers (winter roses) from other countries that can produce them at a lower production cost, e.g. South America, Colombia (Krugman, Obstfeld, Melitz 2012: 24 ff.). The logic behind this stems from the two main reasons countries engage in international trade in the first place: first, countries benefit from their advantage in comparison to others, and secondly, countries trade in order to achieve economies of scale, that is, only a limited number of goods are produced at a larger scale and more efficiently (Krugman, Obstfeld, Melitz 2012: 137 ff.).

In our example, Colombia has a comparative advantage in producing winter roses because of climatic conditions as well as because of the labour productivity, which is lower than in the US. The US, on the contrary, is better off by producing computers since growing winter roses in heated greenhouses is expensive and not energy efficient. Besides, the US has a comparative advantage in producing computers – the know-how and further resources being placed in the US makes it cost efficient to produce them at the expense of other goods. In this case, both countries benefit from specializing in one good and trading it to one another, and so does the world economy.

Sticking to this example, let’s suppose the US grows 10 million roses for Valentine’s Day in order to meet the increased demand. This extra effort costs it 100.000 computers, which could have been produced instead (opportunity cost of 10 million roses is 100.000 computers). On the other hand, Columbia produces 10 million roses and 30.000 computers. If both countries decided to specialize in the good they produce most efficiently – Colombia grows roses and the US produces computers – not only could they have benefitted from economies of scale but the so could have the world, since international output would have increased (see table 9). Consequently, international trade increases world output because it allows countries to specialize in the production of goods they have a **comparative advantage** in.

²¹ Economists use the term “opportunity costs” to describe trade-offs (Krugman, Obstfeld, Melitz 2012, 25).

Table 9: Hypothetical Changes in Production

Changes in Production	Million roses	Thousand computers
United States	-10	+100
Colombia	+10	-30
Total	0	+70

Source: Krugman, Obstfeld, Melitz 2012: 26.

4.2.1.4 Theories in Practise

In theory, an increase in world output increases everyone's standard of living if countries export their good of comparative advantage. In practise, however, reality often looks different: there are more countries than just two; also there is no independent, objective authority that takes the decision as to which good is produced, and finally countries do not produce what makes another country better off, but rather what will make themselves better off (Carpenter, Dunung 2011).

4.3 Free Trade

Trade constitutes a significant part of a country's output, which is reflected in the formula for the Gross Domestic Product²²:

Image 2: GDP explained

GDP = C + G + I + NX Where: C stands for consumption and is equal to private consumption or consumer spending in an economy; G stands for the sum of all government spending; I stands for investments of the country's business spendings on capital NX stands for total net exports (total exports minus total imports).

Source: Krugman, Obstfeld, Melitz 2012: 297 ff.

²² The Gross Domestic Product reflects a country's output Y, the monetary value of all finished goods and services (Krugman, Obstfeld, Melitz 2012, 11).

Depending on the size of the country, domestic trade can be equally important as transit trade and international trade. In the EU, for instance, trade in goods within the Single Market was valued at € 2 804 131 million in 2011 compared to extra-EU trade of € 3 267 467 million (Eurostat International trade in goods 2012). This high amount of trade and the subsequent welfare in the European internal market is owed to the free movement of goods, capital, services, and people within the member states (European Commission Single Market 2013). Such conditions are usually reached by abolishing protective measures, namely import tariffs or quotas. The complete abolition of said measures leads to free trade, which is defined as: “The unrestricted purchase and sale of goods and services between countries without the imposition of constraints such as tariffs, duties and quotas.” (Investopedia Free Trade 2013).

World wide, few countries perform completely free trade. The city of Hong Kong according to Krugman et al (2012, 213 f.), may be the only “country” without tariffs or import quotas. Many others have eliminated tariffs and quotas on certain products and for certain countries. Nevertheless, the debate is lively, and there are proponents as well as opponents of free trade. In the following, I introduce the most common arguments.

4.3.1 Advocates of Free Trade

Arguments in favour of free trade can be organized into two categories – economical and political. The focus in this subchapter is on the economical arguments.

The most crucial economical argument in favour of free trade is the principle of mutual gains from trade through the exploitation of comparative advantage. This argument is quantifiable, as I explained earlier (see 4.2.1.3 on comparative advantage). The second quantifiable argument looks at efficiency losses from protectionism. It is commonly accepted that free trade helps avoiding production and consumption distortions due to tariffs and quota. Such distortions often lead to welfare losses (Krugman, Obstfeld, Melitz 2012: 211).

A famous example for efficiency losses through protectionism is India’s widespread practise of rent seeking. In the 1950s and 1960s, the government allocated licenses with the right to import products to Indian companies according to their installed capacity. This face of India’s license raj led to large inefficiencies since several investing countries overinvested in order to be able to accrue a larger number of import licenses. In economic terms, the resources used to

build this idle additional capacity reflect the costs of protectionism and a loss to the Indian economy (Krugman, Obstfeld, Melitz 2012: 211 f.). Table 10 illustrates the effects of various trade policies on producers, consumers, the government's budget and on the overall nation. This table certainly does not promote interventionist trade policies and emphasizes the negative effects on consumers and the at best ambiguous effects on national welfare.

Table 10. Effects of Trade Policies

Actors in the economy	Tariff	Export Subsidy	Import Quota
Producer Surplus	é	é	é
Consumer Surplus	ê	ê	ê
Government Revenue	é	ê	–
National Welfare	≈	ê	≈

Source: Krugman, Obstfeld, Melitz 2012: 211.

Estimations of gains from free trade predict the gains for developing countries to be higher than for developed countries. Since the latter generally have lower tariffs and quotas, a move to worldwide free trade would not mean gains as high as for developing countries, which usually maintain a higher level of protectionism (Krugman, Obstfeld, Melitz 2012: 209).

Further gains from free trade may not be quantifiable but are equally important to be considered: economies of scale and incentives for innovation (Krugman, Obstfeld, Melitz 2012: 221). These so-called dynamic gains support industries in gaining efficiency and refrain from losses. Protected markets often aid firms in entering sectors despite the possibility of inefficiencies. Consequently, narrow domestic markets may be distorted, leading to unutilized potential and inefficient scale. Competition is reduced and profits are artificially raised. The abolition of quotas and tariffs, however, allows the right amount of firms to enter a market and produce at their highest potential, leading to economies of scale. On a similar note, protectionism leads to fragmentation and distortion internationally as well (Krugman, Obstfeld, Melitz 2012: 221 f.).

It is often cited, yet difficult to quantify, that more competition leads to increased incentives for innovation. Trade without barriers increases the level of competition for firms with new imports as well as for exports. The opportunity for increased export provides larger markets for companies as well as diversified consumer pools, which, in turn, requires domestic firms

to learn and innovate their products. Consumers are said to profit from the resulting diverse products at competitive prices.

4.3.2 Opponents of Free Trade

Economists opposing free trade argue that under restrictions, free trade can be the least harmful policy. This argumentation leaves room for interpretation with regards to the reasoning for less protection in developed countries compared to developing countries, which, historically, went as far as to perform import-substitution (ISI). Developing countries often face political and economical fragility and instability, which requires them to undertake some sort of protection. Most such measures those governments undertake are aimed at the protection of particularly vulnerable interest groups (Krugman, Obstfeld, Melitz 2012: 257).

Another argument in favour of protective measures and a nation's welfare is the terms of trade argument for a tariff²³. According to Krugman et al, a tariff lowers the price of imports and thus generates a terms of trade benefit in large countries (Krugman, Obstfeld, Melitz 2012: 218). Usually, such big countries are able to affect the prices of foreign exporters and therefore can influence the terms of trade in their favour. Nonetheless, this benefit must be higher than the costs of a tariff – namely the producer and consumer distortions.

Economists opposed to free trade argue that failures in a country's domestic market are a valid argument against the promotion of free trade. An example is malfunctioning industries, which do not yield enough knowledge or technology spill over to other sectors, leading to a marginal social benefit. Such a loss or non-existing benefit may be used as justification for protective measures (Krugman, Obstfeld, Melitz 2012: 218).

The protection of infant industries is highly relevant in countries, which try to establish new industries and push for innovation. Economists argue in favour of the protection of such infant industries in order to allow them the development to a point where they are capable of competing in the world market (Krugman, Obstfeld, Melitz 2012: 258).

John Stuart Mill's argument on the risk of monopolies evolving from free and unregulated trade hypothesizes the potential power of monopolies to influence prices. This risk of a

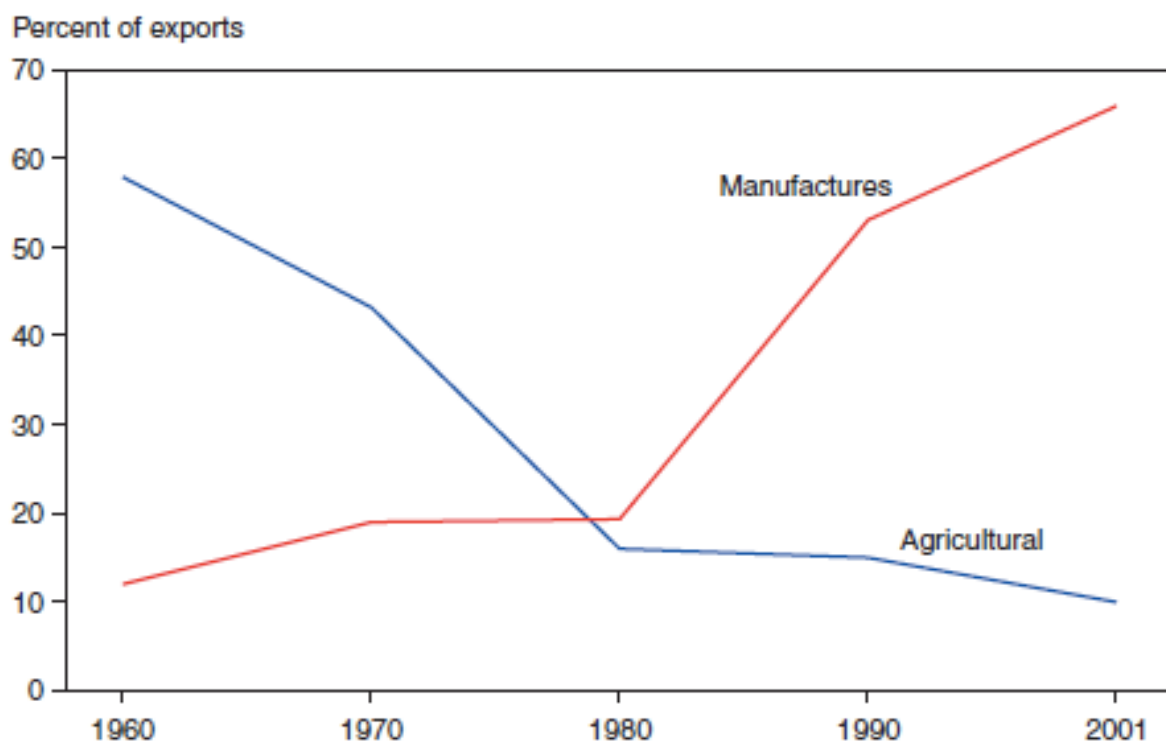
²³ The terms of trade is the ratio of the price of a country's exports divided by the price of its imports (Krugman, Obstfeld, Melitz 2012, 218).

manipulation of the terms of trade by certain powerful companies through for instance the unfair maintenance of tariffs is usually met by government regulation (Krugman, Obstfeld, Melitz 2012: 160).

4.3.3 Free Trade in the Context of Development

Over the past decades, many developing countries have shifted from exporting primary goods to now mainly exporting manufactured goods (Krugman, Obstfeld, Melitz 2012: 25). Up until the late 1970s many of the world's poorer countries were primarily involved in the export of minerals, crude oil, coal and agricultural products. The United Nations Council shows their shift towards the export of manufactured goods in the following graph:

Graph 7: The changes in the composition of developing country exports



Source: UNCTAD 2013

As mentioned earlier, Simon Kuznets underlines this change with his theoretical findings on tendencies in terms of sectorial changes. He notes that countries experience a monotonic drop in the share of primary goods, followed by a – at first – rise in the share of secondary goods. The latter peak and drop as countries reach a high-income status, which is when services are already rising and continue to do so.

The economic development of Asian countries has generally followed this so-called “Kuznets process”. A study by the Asian Development Bank (Asian Development Bank 2009) tested the tendency of Asian countries to follow this development path and confirmed the Kuznets process for most Asian countries. Those countries, which were emerging economies, had higher shares of manufacturing and lower of services. Exceptions are the Philippines and India, whose shares of manufactures are lower and services are higher.

4.3.3.1 India and its Development Path in the Tertiary Sector

Over the past years, India has proved to be a strong partner in providing services for domestic and foreign companies. The tertiary sector’s share in India’s GDP is striking and it contributes strongly to India’s growth. In the context of the Kuznets process, however, one might ask whether India is able to maintain and increase its high level in the services sector and skip the phase of a high level in manufacturing. According to Lemoine et al, three arguments oppose the current Indian path to growth (Lemoine et al. 2007: 41): first of all, the growth of the past years has been so-called “jobless-growth”: India has failed to generate a high number of jobs, the job creation potential in fast growing and productive sectors has been and remains low. Secondly, Lemoine argues that India’s comparative advantage and the accompanying growth in the service sector may be due to distortions in the economic system, which may fade in the coming years. Lastly, India has a large and growing workforce (Lemoine et al. 2007: 41).

In order to ensure sufficient employment, the country must ensure sufficient labour intensive manufacturing production. In lights of a decreasing demand of labour in the agricultural sector (according to the Kuznets process), the redistribution of labour becomes even more essential (Kochhar et al 2006; Lemoine et al. 2007: 41).

4.3.3.2 Export Subsidies

Countries participating in the General Agreement on Tariffs and Trade (GATT) and later the World Trade Organization (WTO) ought to refrain from non-tariff barriers, such as export subsidies. However, a substantial exception had been granted to the USA in the early stage of the GATT, namely subsidies on agricultural products (Krugman, Obstfeld, Melitz 2012: 204). Also the EU and other developed countries subsidize their agricultural sectors heavily and protect it against competition. The question arises, particularly in a developmental context,

whether such subsidies hurt developing countries and their economies and should therefore be removed (Krugman, Obstfeld, Melitz 2012: 204).

As developing countries import products at a lower price (as a consequence of subsidies), consumers profit from such subsidies. They are able to purchase products cheaply compared to their home country prices. Additionally, producers of alternative goods, such as coffee, can produce and export without fearing subsidies. The bloc of developing countries and other opponents of this barrier, however, criticize the preservation of agricultural subsidies during the Doha round²⁴. Their argument underlines the negative effects on their industries, which are hurt and prevented from competing at world prices. Developing countries are denied market access since they cannot compete at subsidized price levels despite the often given comparative advantage in the primary sector²⁵. Agriculture is particularly important for developing countries since large portions of their populations live in rural areas and make their living from agricultural activities. By applying subsidies, developed countries uphold production beyond what the market would usually sustain and create heavy market distortions – something that developed countries claim to eradicate (Harborth 1992: 232). Domestic farmers are forced out of the market and the lack of competition may – in some cases – even lead to higher international prices instead of lower prices, which initially justified the subsidies (Harborth 1992: 232 f.). Not only do developing countries lose export potential, labour working in and around the agricultural sector loses a fair amount of income. Studies have argued that this practise harms the development process and increases poverty, particularly in primary sector-dependent least developed countries (LDCs): the missing output decreases available government income and consequently leaves less possibilities for welfare investments in health, education, infrastructure (Harborth 1992: 236 ff.).

Proponents of subsidies predict that the abolishment of subsidies could hit developing countries in general and African nations²⁶ in particular heavily and make them even worse off. In this argumentation, the negative effects of higher food prices for domestic consumers

²⁴ “The Doha Round is the latest round of trade negotiations among the WTO membership. Its aim is to achieve major reform of the international trading system through the introduction of lower trade barriers and revised trade rules” (WTO Doha Round).

²⁵ The comparative advantage in the primary sector of developing countries is often due to the large supply of labour.

²⁶ African nations in particular because the EU exports a large amount of its subsidized products to this region.

would offset the gains from higher prices for their agricultural products (Krugman, Obstfeld, Melitz 2012: 238).

4.4 Free Trade Agreements in the WTO-Setting

„In addition to their commitment to multilateralism, WTO members may contemplate bilateral agreements: this is a way to further or quicker liberalise trade, as well as to negotiate on issues not covered by the multilateral agenda.“ (Indo European Journal).

After having described the roots, benefits and advantages and disadvantages of trade and free trade, it is time to look at the mechanisms more closely. It is worthwhile to discuss the path from a country's desire to reduce tariffs in order to avoid production and consumer distortions to the actual realization of the plan. It is often advisable for countries to engage in mutual agreements rather than change their tariff or quota policy unilaterally since such agreements increase the support for free trade – and thus counteract protective measures - more broadly (Krugman, Obstfeld, Melitz 2012: 228). Support may be raised by, for example, domestic exporters, who count on gaining access to foreign markets if they lobbied for and supported such agreements.

Usually the path to an agreement leads through a number of bilateral or multilateral trade negotiations. In the following I will provide a brief summary of the history of international trade agreements as well as the different types of agreements.

4.4.1 History of Trade Agreements

According to Krugman et al, the United States was the first country to systematically advocate trade agreements. In the 1930s they pushed for “internationally coordinated tariff reductions” (Krugman, Obstfeld, Melitz 2012: 230). In a direct and bilateral approach, they successfully negotiated mutual tariff reductions with specific industries in a number of countries.

Soon after WWII it was the allies and their diplomatic corps that envisioned a multilateral forum where impediments to trade would be discussed and abolished. Corresponding to the zeitgeist and establishment of institutions like the World Bank and the International Monetary

Fund, the International Trade Organization (ITO) was proposed to be established to deal with trade affairs (WTO history 2013). However, a number of countries initiated their negotiations under a “provisional set of rules”, the General Agreement on Tariffs and Trade (GATT)²⁷ (Krugman, Obstfeld, Melitz 2012: 230). The permanent secretariat was placed in Geneva, Switzerland. This agreement was effective until 1995, when a permanent organization, the World Trade Organization (WTO) was created. In the end, the ITO was never established and the negotiations and rules performed under the auspices of the GATT-governed international trade for a period of 48 years. Even after the initiation of the WTO, the GATT guidelines continued to be in place. In its self-description, the WTO talks about itself as “the only global international organization dealing with the rules of trade between nations.” (WTO history 2013). The core of the organization’s work is the facilitation of trade agreements, which are negotiated and signed by its member governments and ratified in their parliaments (WTO history 2013).

4.4.1.1 The WTO

The WTO’s main purpose is the promotion of free trade and “to help producers of goods and services, exporters, and importers conduct their business.” (WTO history 2013).

Bound tariffs and the prevention of non-tariff barriers are the two tools the WTO uses in order to achieve its goal. The former stands for tariffs, which a country is committed to and cannot increase and it is the less preferred alternative to tariff cuts. The abolishment and prevention of non-tariff barriers, on the other hand, is another step towards free trade. However, as it has been already mentioned, the United States and the EU enjoy the exception of agricultural product subsidies - an evident counter development to free trade reveries.

4.4.2 Bilateral and Multilateral Trade Agreements

Since the 1990ies more and more countries have been engaging in bilateral trade agreements. This has not always been the case – FTAs were frozen in the late 1990ies in favour of the WTO and the promising Doha Round (European Policy Center 2009: 16 f). However, the Doha Rounds were not equally successfully for all its members. Therefore many countries continued searching for alternative bilateral and multilateral ways to reach decreased trade barriers.

²⁷ There were no “member states” of the GATT but only “contracting parties”.

This development challenges the WTO's mission to ensure worldwide free trade by reducing tariffs and barriers for WTO members, since bilateral trade agreements are negotiated between two parties. Such parties consequently provide each other preferential treatment under so-called free trade agreements (FTAs) or preferential trade agreements (PTAs). They pose an important alternative to multilateral negotiations. PTAs "(...) include Generalized System of Preferences schemes (under which developed countries grant preferential tariffs to imports from developing countries)" (WTO Preferential Trade Agreements 2013). Some bilateral and multilateral trade agreements may include the liberalization of investments. This is the case between India and the EU, who are negotiating the BTIA.

Another form of trade agreements is Regional Trade Agreements (RTAs) (WTO Regional trade agreements 2013). The objective behind the roughly 379 Regional Trade Agreements (RTAs) that are in force is mainly to improve entry to new markets as well as eased access to them.

Table 11: Types of trade agreements

Type of Agreement	Changes
Bilateral Trade Agreements	Elimination of customs and non-customs barriers on trade between two countries
Multilateral Trade Agreements	Elimination of customs and non-customs barriers on trade between multiple countries
Customs Union	Free trade area between member countries; adoption of Common External Tariff
Common Market	More integrated customs union: free movement of goods, services, capital and labour
Economic Union	Integration of all economic policies

Source: WTO Preferential Trade Agreements 2013, private notes.

Unlike WTO treaties, in which non-WTO members are discriminated over those who are members, such two-party-agreements allow outside parties to actively involve in better trade conditions for themselves as well as the second party. These reciprocal trade agreements include free trade agreements and custom unions and are „(...) notified under Article XXIV:7

of the GATT 1994, and paragraph 2 (c) of the Enabling Clause, and Economic Integration Agreements under Article V:7 of the GATS.“ (WTO Scope of RTAs 2013).

The WTO puts clear restrictions on WTO members who sign PTAs and RTAs. Under the WTO, countries are usually bound to the Most-Favoured-Nation (MFN) treatment, which constrains countries to treat every member state equally in terms of granting lower tariffs and fewer barriers, facilitate market opening as well as the flow of investments (WTO Scope of RTAs 2013). The MFN rule is part of all three main agreements of the WTO: the General Agreement on Tariffs and Trade (GATT), the General Agreement on Trade in Services (GATS), and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). RTAs challenge this rule, therefore they underlie restrictions: Parties involved must show established free trade within the regional area within ten years. To avoid potential discrimination against WTO members, parties are obliged to keep tariffs against outside parties constant and ensure complementarity with WTO standards (WTO Scope of RTAs 2013).

Over the past few years, FTAs and RTAs have become more the rule than exception. Above all, the comparably faster handling of negotiations and the prevention of lengthiness are considered striking arguments in favour of FTAs. Negotiations in multilateral settings are often lethargic and less productive in terms of quick outcomes and do not seem to gain much enthusiasm recently (Modwel, Singh 2012: 2 f).

Some countries believe very strongly in FTAs and RTAs and have a significant number of such agreements in place or in negotiation. The EU is part of 34 RTAs (with further three in negotiation) whereas a large number of the RTAs are agreements with future candidates to the EU (European Commission Trade Agreements 2013). Chile follows the EU closely with 22 RTAs, and the US has 13 RTAs. A look into the WTO RTA database shows the diverse composition of partners in RTAs, where developed countries, developing countries and regional unions and associations negotiate and agree on tariff reductions (WTO RTAs Database 2013).

4.5 The EU's Foreign Trade Relations

The EU realized that over the next decade, the largest portion of demand will be generated outside Europe. This development makes it necessary for the EU to pave the way for its businesses by gaining market access to foreign markets and opening up its market to other countries (European Commission Trade Agreements 2013). As part of the *Global Europe Strategy* (2006), the EU put forth a stronger emphasis on FTAs and RTAs (European Commission 2006: 2).

"What do we mean by external aspects of competitiveness? We mean ensuring that competitive European companies, supported by the right internal policies, must be enabled to gain access to, and to operate securely in, world markets. That is our agenda." – EU Trade Commissioner Peter Mandelson, 2008.

On October 4th 2006, the EU published its first draft of a "Global Europe Strategy", aiming at an economically stronger and more competitive EU. In the foreword of this communication, the strategy plan is described as a necessary tool in order to ensure growth, prosperity and wealth in the EU. Globalisation brings along new challenges, which the EU seeks to face by having forward-looking and cohesive trade policies. Since the plan puts great emphasis on bilateral trade, similar virtues are expected from the EU's partners: the abolishment of protectionism in the EU must go hand in hand with "(...) activism in creating open markets and fair conditions for trade abroad." (European Commission 2006: 7). Reducing tariffs and opening markets for European companies is considered important for a stronger cooperation with EU trade partners.

In a bilateral context, the EU does not only aim at facilitating trade relations and investment flows. Negotiations often follow a holistic path of integrating the service sector by securing new market openings in banking, insurance, retail trade, and business services (European Policy Center 2009: 16 f.). In the very interest of the EU is the enhanced protection of intellectual property rights (IPRs) in order to meet the basic protection measures at the least. IPRs include the pharmaceutical sector and the EU advocates strong protection beyond the TRIPS agreement (European Policy Center 2009: 16 f.). Fair and transparent government procurement depicts another area of "deep interest" the EU has when negotiating with FTA partner countries.

Considering the EU's late perception of the benefits of FTAs especially in Asia, it has caught up incredibly fast. Since then the EU has been at the forefront of FTA arrangements and ranks at the top of parties involved in FTAs and RTAs. Regarding the EU's regional focus, FTAs with the European neighbourhood have proven successful in the past. Nevertheless, with growing competition, the EU targets new markets with large growth potential, low tariffs against EU exports and protection against EU competitors. Asian countries are clearly at the top of the priorities in FTAs. Among the prioritized negotiation partners are South Korea with which negotiations endured from 2007 to 2011 until consensus was reached“(...) to reciprocally liberalise all trade in goods and services and to tackle existing and future non-tariff barriers to trade.“ (European Commission Free Trade Agreements 2013). It is the most recently signed FTA, which provisionally went into force on July 1st 2011. The negotiations of the Transatlantic Trade and Investment Partnership (TTIP) between the EU and the United States have been cancelled on October 4th 2013 due to the US administration shutdown (European Commission Trade Agreements 2013).

Graph 8: The EU's trade relations worldwide



Source: European Commission Trade Agreements Map.

4.5.1 Strategies to Enhance Trade

As mentioned earlier, the EU was a late-starter in exploring the potential for trade with Asia. Therefore, it was all the more important to establish a sound strategy. The Global Europe Strategy consists of an action plan with concrete steps by the European Commission in order to maintain their competitiveness in the world market. The Global Europe Strategy consists of an internal and external agenda, outlining the EU's long term plans coherently. The focus is on goods, services, investment and government procurement liberalisation, competition policy, intellectual property rights enforcement, and non-tariff barriers. Soon after the strategy plan became public, the *Market Access Strategy* was brought forward in April 2007 (European Commission 2006: 13).

Internal Agenda

“Internally we will:

- Make sure that internal policy proposals, while furthering European standards, fit with global competitiveness challenges.
- Make sure the benefits of trade opening are passed on to citizens by monitoring developments in import and consumer prices.
- Equip people for change through the new generation of cohesion policy programmes and the European Globalisation Adjustment Fund.” (European Commission 2006: 15).

The internal agenda of the strategy emphasizes the EU single market's potential to compete internationally. The international market, however, does not always comply with rules and regulations crucial to prosperous business activities and relations. Since the EU is most certainly a forerunner with regards to compliance, it counts on bilateral and international co-operation in the compliance with rules and regulations. In order to maintain competitiveness, EU businesses are required to show flexibility without downgrading their own rules (European Commission 2006: 9).

Further, the internal plan recognizes the adaption to globalisation processes, such as rationalization, as inevitable. For the very reason that artificial protection of sectors that are affected by globalization-induced, increased competition is not sustainable, revisions and adaptations must be undertaken, e.g. by modifying the Customs Code for EU-internal trade and introducing e-customs (European Commission 2006: 10).

External Agenda

- “Maintain our commitment to the Doha Trade Round and the WTO as the best way of opening and managing world trade.
- Make proposals on priorities in trade and investment relations with China as part of a broad strategy to build a beneficial and equal partnership.
- Launch a second phase of the EU IPR enforcement strategy.
- Make proposals for a new generation of carefully selected and prioritised FTAs.
- Make proposals for a renewed and reinforced market access strategy
- Propose measures to open procurement markets abroad.
- Conduct a review of the effectiveness of our trade-defence instruments.” (European Commission 2006: 15).

From the strategy paper, it is evident that the EU is highly committed to the WTO and its mechanisms for managing world trade.

With regards to trading partners, China is recognized as new challenging partner requiring a broad strategy. Intellectual Property Rights are a pressing issue requiring attention especially during negotiations with Asian countries. The opening of developing country markets gives the EU access to public procurement, which has to be regulated accordingly. The strongest emphasis is put on FTAs. Such agreements are considered vital for enhancement within the WTO – they could enforce multilateral negotiations and a decrease in world trade barriers – and also beyond the WTO. FTAs must be “comprehensive and ambitious in coverage, aiming at the highest possible degree of trade liberalisation including far-reaching liberalisation of services and investment.” (European Commission 2006: 11). Vice versa, the EU expects quite something from its potential bilateral partners too: non tariff barriers, the implementation of the EC Enforcement Directive for IPR protection, full parity if there are EU competitors and good governance in financial, judicial and social areas. Also, the EU commits herself to paying special attention to the needs of negotiation partners from developing countries (European Commission 2006: 11).

4.5.2 Global Europe Strategy – an Effective Strategy?

The Global Strategy, while leaving room for criticism, can overall be seen a pro-active approach. After the Lisbon strategy in 2005, the Global Strategy Paper contributed to the clear formulation and communication of the EU's trade goals in the short- and long-term future. It seems that such a strategy was necessary – worries about loss of market share, the increasing oil price and fight for raw materials, the growing market share of Asian countries in Africa, as well as about successful trade agreements of competing economies were and still are self-evident. The EU faced internal concerns too: its trade deficit was growing and some sectors (e.g. intensive labour sectors) became increasingly more competitive. Therefore, the Global Strategy paper suggests a combination of internal and external measures to go hand in hand and promote reforms on each level. Critics, however, consider the strategy to be misleading. Developing countries might face more disadvantages from stronger cooperation under the strategy than they do today. For example, harsh trade liberalisation, as promoted by the EU, might have a negative impact on the quality of jobs abroad and in the EU. Furthermore, the aspiration for privileged national treatment for European corporations, in addition to easy, non-tariff-based market access for those corporations is considered problematic.

Demands and requirements articulated specifically towards the completion of FTAs are comprehensive and require strong commitment from the EU's partners. The eradication of tariffs together with free market access and the influence on the political space through implementation of certain EU directives interfere with the single countries' sovereignty. At the time of the publication, however, negotiations over a few Free Trade Agreements were in progress. Asia was especially in the EU's focus, but along with Korea and ASEAN-member states, one of the countries targeted as well is India.

4.6 India's Foreign Trade Relations

Similar to many countries, India faced a slowdown of its economy after the global financial crisis but was able to recover its merchandise exports in the period 2010-11²⁸. As mentioned earlier, India is facing a growing current account deficit, which has to be brought under control. To do so, the Ministry of Commerce and Industry has developed a "(...) *Strategy*

²⁸ In 2010-11, merchandise exports accounted US\$ 250 bn., a growth of 40 per cent compared to a growth of negative 3.5 per cent in 2009-10 (Department of Commerce India 2013).

Paper for doubling merchandise exports in three years from US\$ 246 bn. to US\$ 500 bn. in 2013-14.” (Department of Commerce India 2013). It is part of the Indian Foreign Trade Policy (FTP) 2009-2014, which the Department formulates. The Indian government is aware of the interdependence of Indian exports and the global economy but is confident to reach their goal and defines the following goal: “The long-term vision of the Department is to make India a major player in world trade by 2020, and assume a role of leadership in international trade organizations commensurate with India’s growing importance.” (Ministry of Commerce & Industry 2011: 3).

4.6.1 Strategies to Enhance Trade

Table 12 shows the strong disparity between India’s exports and imports. In comparison, imports have been growing faster than exports, leading to a growing trade imbalance.

Table 12: Projections of Exports and Imports as per cent of GDP

(values in US \$ billion)							
Year	GDP at Market Price	Exports	Imports	BOT	X as % of GDP	M as % of GDP	BOT as % of GDP
2010-11	1592.6	246.0	360.0	-114.0	15.4	22.6	-7.2
2011-12	1836.3	292.9	448.7	-155.8	15.9	24.4	-8.5
2012-13	2117.3	348.7	559.2	-210.5	16.5	26.4	-9.9
2013-14	2441.2	415.1	696.9	-281.8	17.0	28.5	-11.5

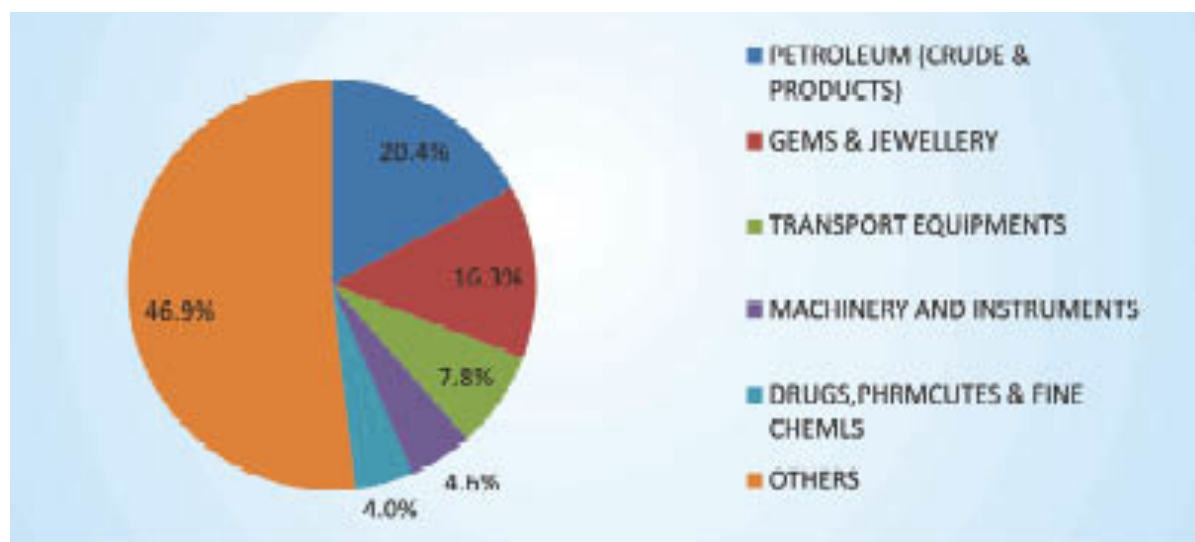
Source: Ministry of Commerce & Industry 2011: 7.

Trade in crude products, textiles and gems and jewellery has been performing well but there seems to be growth potential across the sectors. Gems and jewellery, for instance, remains important for the Indian market due to its high volume that it contributes to exports, despite its low value added (Ministry of Commerce & Industry 2011: 10).

More critical industries for growth are engineering goods, which accounted for 20 per cent of India’s total exports in 2011. India’s average share in the heavy machinery and transport

equipment sector was as low as 0.3 per cent²⁹ and it sees huge potential in this sector due to high international demand. A traditionally strong sector, focus shall also be on drugs and pharmaceuticals as well as chemicals. In terms of natural resource sector, the agricultural sector as well as plantation crops is considered as helpful to increasing the country's exports (Ministry of Commerce & Industry 2011: 10).

Graph 9: The top five export commodities, 2011-12



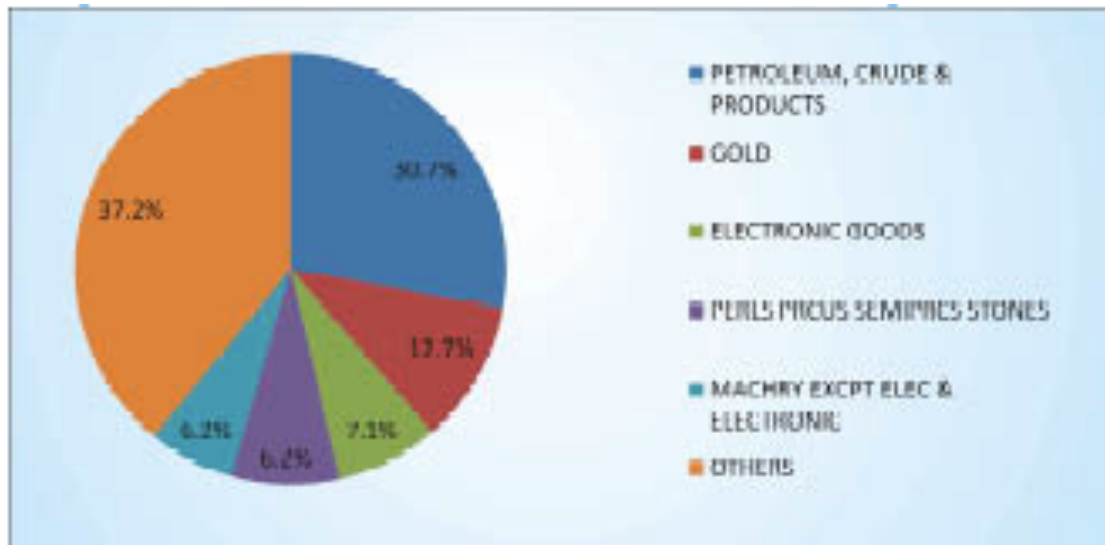
Source: Department of Commerce India 2013.

Undoubtedly, India is aiming at a substantial long-term increase in its exports. It expects not only a positive trade balance but also various spill-over effects. The country's manufacturing industry shall be strengthened, technology and research and development enhanced, quality raised and consequently new consumers and markets accessed. Entrepreneurs' exposure to international markets would increase their competitiveness and therefore India's exports.

Complementarily, the strategy aims at decreasing its imports. Currently India's import composition looks as shown in graph 10:

²⁹ Weighted average 2003-2007 (Ministry of Commerce & Industry 2011, 11).

Graph 10: The top five import commodities, 2011-12



Source: Department of Commerce India 2013.

Potential for a reduction of imports is particularly seen in the agricultural sector (pulses and edible oils), fertilizers and the pharmaceutical industry. Nevertheless, India's energy dependence requires its largest imports and can be reduced. Particularly coal and petroleum are largely imported and are due to ineffective pricing, waste in energy supply and energy losses heavy on India's trade balance. The Strategy Paper emphasizes the necessity for an import reduction of these goods as well as a focus on the development alternative energy sources (Ministry of Commerce & Industry 2011: 14 ff.)

4.6.2 India's FTAs

Even though India relaxed its protective measures strongly since the 1990s, some restrictions remain. Compared to similar emerging markets, India is said to have comparably high tariffs and restrictive investment norms. They are often considered impediments to trade negotiations. Even though non-agricultural tariffs are below 15 per cent, agricultural tariffs average at a high 30-40 per cent level (World Bank India Foreign Trade Policy 2013).

Nonetheless, India is involved in plentiful trade negotiations and has been pushing for more liberal international conditions for example in services. It has a number of FTAs in force and a similarly high number of agreements in progress. Most of the existing FTAs approach countries in India's neighbourhood and are aimed at enhancing Asian regionalism – a rising

trend amongst Asian countries (Petri 2010). Other than its involvement in bilateral agreements, India is also increasingly – even though still hesitant - engaged in large FTAs. Being an ASEAN³⁰ member, it is negotiating the Regional Comprehensive Economic Partnership (RCEP), which consists of the 10 ASEAN member states plus Australia, China, India, Japan, South Korea and New Zealand. The ambitious goal is to conclude this agreement by the end of 2015. Another similarly large project is the Comprehensive Economic Partnership for East Asia (CEPEA/ASEAN+6). It includes the following 16 members: Australia, New Zealand, Japan, India, China, South Korea, Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Viet Nam (Petri, Plummer, Zhai 2011: 5).

The following chapter introduces the exception to India's focus on Asia: the Broad-Based Trade and Investment Agreement with the European Union.

³⁰ Association of Southeast Asian Nations (Asean 2013).

5. The Broad Based Trade and Investment Agreement

The preceding chapters gave the background to how the idea of an FTA between the EU and India developed. With the launch of the Global Europe Strategy in 2007, the EU kicked off a new trade strategy. The emphasis on RTAs and FTAs, especially in Asia, allowed a new focus in EU foreign trade. This new approach was aimed at mending the EU's past failures to secure access to emerging markets as well as acquiring a safe stance against other big competitors such as China. A Free Trade Agreement with one of the biggest untouched markets with a large growth capacity seemed like "the coup". In addition there was India's strong relationship with the EU, its aim of increasing exports and restoring high growth. In this context, the Broad based Trade and Investment Agreement between the EU and India was born.

5.1 The BTIA in Retrospect

In 2005, the first India-EU summit on economic cooperation took place and gave the starting signal to first steps towards a free trade agreement, involving "concrete steps of cooperation through with the EU and India could strengthen their influence on global political, economic and social developments" (Luif: 47). Leaders on both sides indicated serious interest in an agreement and moreover, a group was formed in order to explore means and the compatibility for a deepened trade and investment relationship. The High Level Trade Group (HLTG) consisting of government and industry officials assessed both parties' effective gains from a BTIA. It examined the actual shape of an agreement between both partners (Report of the EU-India High Level Trade Group to the EU-India Summit 2006). The HLTG conducted research over a one-year period and presented the outcomes on October 13 2006, only a few days after the publication of the EU's Global Strategy Paper.

In the report, the group strongly recommends the negotiation of the BTIA. On the basis of both partners' strategic partnership, existing at the time of the report's publication, further deepening of their trading and investment relationship was recommended. (Ecorys 2009: 27). Throughout the paper, the group underlines the commitment shown by both sides to the WTO, the Doha Development Agenda (DDA) and the route of multilateralism. The EU and

India are considered two parties strongly positioned as advocates of multilateralism, so it might be surprising that they put this much energy towards agreements between two parties. The argument, especially from the EU, points at the complementary character of bilateral trade agreements, like in the form of FTAs. Such agreements may function as necessary supplements to multilaterally negotiated treaties (Report of the EU-India High Level Trade Group to The EU-India Summit 2006: 5).

The report defines specific areas, which should be covered in an FTA in order to start the negotiations. Possible obstacles are also included, bearing in mind the different interests present on both sides. The group discussed “(...) trade in goods, trade in services, investment, trade facilitation, public procurement, intellectual property rights, competition and dispute settlement” (Report of the EU-India High Level Trade Group to The EU-India Summit 2006, 1). All in all, the report includes a recommendation for more transparency regulations for both parties and their economies (Report of the EU-India High Level Trade Group to The EU-India Summit 2006: 5). Moreover, the report suggested that further talks could lead to a successful completion and that both parties should be willing to invest in this agreement.

5.2 Areas

As mentioned in the introduction, there is little information available on a concrete agreement paper. The following area definition is hence based on a literature review and own identification of key issues.

5.2.1 Trade in goods

The eradication of tariffs between the negotiating parties is highly prioritized in FTAs. The HLTG suggests a 90 per cent elimination of tariffs reached within a time period of seven years after an agreement is signed. The recommendation is sensitive to the fact that there might be only partial liberalisation due to certain ineligible product fields (Gasiorek et al 2007: 5).

5.2.2 Trade in Services

The EU's as well as the Indian service sector are of great importance as they make up significant shares of both economies. Thus the liberalisation thrives for the elimination of all discrimination between the parties. In this context, the General Agreement on Trade in Services (GATS) plays a vital role: the HLTG suggests further liberalisation of the four modes of supply, which are at the heart of the treaty and are as follows (Gasiorek et al 2007: 6):

Table 13: Four modes of supply

Mode	Meaning	Example
Mode 1 Cross-border trade	Trade from country A into country B	Supply of information via internet: e-banking
Mode 2: Consumption abroad	Services of country A are consumed by citizens of country B	Tourism
Mode 3: Commercial presence	Services of country A are supplied in country B	Hospital, school in country B
Mode 4: Movement of natural persons	Citizens of country A move to country B to provide a service (temporarily)	Lawyer, language school teacher

Source: WTO Services GAT 2013.

5.2.3 Investment

The Indian subcontinent has received Foreign Direct Investments (FDIs) from the EU for many years – as mentioned earlier. The target in the BTIA is an increase in capital flow from both parties. However, bilateral investments require flawless access for investors and transparency over the investments embedded in effective regulations - which are not quite in place (Gasiorek et al 2007: 6).

5.2.4 Trade Facilitation

The long-term effects of efficient trade facilitation lead to higher revenues (e.g. customs) as well as a secure, trustworthy business environment. In the lights of a FTA, the HTLG promotes the simplification and better organisation of trade. (Gasiorek et al 2007: 7).

5.2.5 Technical regulations – TBT and SPS

Enhancement in the areas of technical barriers to trade (TBT) and sanitary and phyto-sanitary measures (SPS) is especially required in order to facilitate trust between India and the EU. Along with the elimination of barriers, both sides shall work towards mutual understanding (Gasiorek et al 2007: 8).

5.3 Obstacles

While this section provided a timeline of the BTIA, the stage is set for an examination of the obstacles to the agreement. Since a holistic listing of the obstacles is not possible due to a lack of literature and information, the following description is based on a personal assessment of crucial challenges faced during the negotiations. The selection was made with regards to providing a range of challenges – both of tariff and non-tariff nature.

5.3.1 Scope

Naturally, a large number of obstacles accompany the trade negotiations. First and foremost, the BTIA intends to include the European Union, which currently consists of 28 member states and India, the second most-populous country, in one free trade area. The mere scope of the agreement brings along severe challenges in terms of the involved interests, costs, and the administrative effort. Especially the differing interests of the different stakeholders make the process of finding consensus in controversial issue areas even more difficult.

5.3.2 Foreign Direct Investment

The area of Foreign Direct Investment (FDI) has also proven to be a challenge. India is hesitant about allowing large investment inflows and has capped the investment amount on

services in the country. In addition, the license acquisition procedures in India are affected by India's red tape, which makes it difficult for foreign businesses to operate in India.

5.3.3 Automobile sector

The integration of the vehicle and automobile sector impacts negotiations with respect to tariff and non-tariff barriers. India and the EU differ regarding customs procedures, investment restrictions, technical standards and intellectual property right standards (Ecorys 2009: 96 f.). India protects its automobile sector by applying high tariffs to imports as well as granting tax reductions to domestic production (Ecorys 2009: 96). The EU's average tariff rates are lower, however, the automobile production is also more advanced and experienced than India's. Naturally, the EU wants access to the Indian market and export at lower tariff rates.

5.3.4 Intellectual Property Rights

The data exclusivity clause, stricter IPR enforcement and TRIPS compliance are the main difficulties with regards to intellectual property right protection. While India is complying to its obligations with the WTO, the BTIA negotiations require going beyond them. India is therefore hesitant to include stricter measures.

5.3.5 Government Procurement

The area of government procurement poses another challenge to the negotiations. The European Commission wants fair access to Indian procurement for its businesses and treatment according to WTO guidelines of non-discrimination and national treatment (Eberhardt, Kumar 2010: 27). This is problematic for India, as the economy believes in favouring domestic suppliers in order to strengthen their businesses.

Intellectual property rights and government procurement serve as key issues in the case analysis of the next chapter.

6. Case Analysis

6.1 Introduction of Method

The former chapter gave an overview of the effects of tariff-barrier liberalisation. Trade liberalisation bears the possibility of a welfare gain and loss, depending on the extent of government regulation. In the absence of appropriate governmental measures or precipitous liberalisation, countries may experience losses from opening up.

This chapter presents an in-depth analysis of two non-tariff barrier areas, which play a substantial role in the BTIA negotiations. The examples have been chosen on the basis of literature reviews as well as an analysis of official EU and Indian documents. I conduct a systematic case analysis of Intellectual Property Rights and Government Procurement – both of which are areas of negotiation and conflict in the FTA. The first part of the case analysis consists of a background assessment. By doing so, the institutional and regulatory environment of the issues is provided. At the same time, I will assess India's and the EU's compliance record by comparing the current status to their regulatory frameworks. In order to illustrate the contentious points, I identify several challenges with regards to an integration of the issue into the BTIA. Those challenges illustrate the potential problems that could arise if Intellectual Property Rights and government procurement were included in the BTIA in their current condition. The last part of the case consists an impact analysis. This analysis hypothesizes the integration of the two issues and assesses their impacts on an economic, social and environmental level.

Following the analysis the findings are organized and summarized. A key issue area matrix is used in order to assess the likeliness of an integration of the areas. A SWOT matrix method complements the findings chapter. The method assists in the evaluation of the particular strengths, weaknesses, opportunities and threats of the agreement according to the findings of the case analysis and this thesis.

6.2 Case 1: Intellectual Property Rights

6.2.1 Background

In April 2013, India's Supreme Court of India adjudicated against the appeal of Novartis in the case "Novartis AG vs. Union of India & Others" (Supreme Court of India 2013). Novartis had filed an appeal about an earlier rejected challenge against India with regards to an amendment to India's Patents Act, which went into effect on January 1st, 2005 (Abbott 2013). The company had argued that the amendments to the Patents Act were unconstitutional and also not compatible with the WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS) (Gasiorek et al 2007: 50). The first challenge by Novartis was rejected in by the High Court in Madras in 2007 and the court also rejected Novartis' second appeal.

The basis of the court's decision is the Indian Patents Act of 1970, which was amended on January 1st 2005 with special regards to Section 3 (d). It was proposed by the Indian government and targets the patent protection of newly introduced pharmaceutical products that lack substantial technological changes. The Indian Parliament then adopted Section 3 (d) amendment, which poses "a requirement that patents for new forms of known substances should only be granted on the showing of a significant enhancement in known efficacy" (Abbott 2013). The motivation behind this decision was to guarantee the availability of medicines for the Indian population as well as developing countries and prevent pharmaceutical companies from filing patent application for medicines without insubstantial technological changes.

6.2.2 Intellectual Property Rights (IPR)

What is particularly striking about the April 1 2013 decision is the wide ranged media coverage and criticism. It sent strong signals to pharmaceutical companies, especially to those operating - or planning on operating - in India (Abbott 2013). Intellectual Property Rights (IPR) regimes are per se a field of controversy since they incorporate the fundamental question of the balance between public and private interests. By definition, intellectual property (IP) "refers to creations of the mind: inventions, literary and artistic works, and symbols, names, images, and designs used in commerce." (WIPO 2013).

Generally, IP is divided into two categories: the first includes all kinds of industrial property, dealing with inventions (patents), trademarks, industrial designs, and geographic indications of source. The second category deals with copyright, which includes literary and artistic works such as novels, poems and plays, films, operas, musical works, artistic works such as drawings, paintings, photographs and sculptures, and architectural designs (WIPO 2013). The diverging stances touch on both categories where on the one hand people believe intellectual property to be a common good, and on the other hand, people demand protection of it. The claim for unrestricted availability of knowledge is based on the idea of common knowledge and its potential benefits for society. It is considered immoral to exclude certain parts of the public from utilizing knowledge (WIPO 2013). A slightly more moderate view considers the affordable allocation of intellectual property as justified. The contrasting position not only questions the necessity to allocate knowledge but also considers it economically problematic. Intellectual property rights ought to incentivize innovation and thus economic and social development. Taking away this spurring element would result in a lack of spirit of discovery and thus innovation and economic progress (WIPO 2013).

It is debatable if ideas and information are property and, more importantly, who possess the right to own it. In international law, however, this issue has been regulated in favour of the second camp, which claims intellectual property belongs to the producer and thus believes in patents and copyright. The World Intellectual Property Organization (WIPO), an international organization, is the United Nations agency “dedicated to the use of intellectual property (patents, copyright, trademarks, designs, etc.) as a means of stimulating innovation and creativity.” (About WIPO 2013). The self-prescribed mission is the promotion of innovation and creativity for the economic, social and cultural development of all countries, through a balanced and effective international intellectual property system.“ (About WIPO 2013). With 189 member states and its headquarters in Geneva, Switzerland, WIPO administers international treaties in the area of intellectual property rights.

International controversy ignited when the discussions on intellectual property ended with the TRIPS Agreement at the end of the Uruguay Round in 1994³¹. The WTO TRIPS agreement came into force on January 1st 1995 and remains the most comprehensive and hence key

³¹ The Uruguay Round (1986-1994) was the largest trade negotiation ever and the outcome included i.e. the TRIPS Agreement (WTO The Uruguay Round).

agreement in the area of intellectual property. Therefore it plays an important role in most free trade negotiations and constitutes a bone of contention.

6.2.3 Legal situation

Compliance with the TRIPS agreement is obligatory for WTO members, although some of them signed it later than others. At the time of its negotiation, it was an unprecedented international agreement laying down legal regulations for dealing with intellectual property as a WTO member towards the nationals of other WTO members states. The objective is “The protection and enforcement of intellectual property rights should contribute to the promotion of technological innovation and to the transfer and dissemination of technology, to the mutual advantage of producers and users of technological knowledge and in a manner conducive to social and economic welfare, and to a balance of rights and obligations”. (TRIPS Agreement Article 7 1994). The agreement itself is limited in its scope and only lays down minimum standards and basic rules for dealing with intellectual property (TRIPS Agreement 1994).

Moving on to health and nutrition, the main principles of the agreement require their members - when formulating or amending their laws and regulations – to “adopt measures necessary to protect public health and nutrition, and to promote the public interest in sectors of vital importance to their socio-economic and technological development, provided that such measures are consistent with the provisions of this Agreement.” (TRIPS Agreement Article 8, paragraph 1 1994). Signatory countries shall take appropriate measures, which „may be needed to prevent the abuse of intellectual property rights by right holders or the resort to practices which unreasonably restrain trade or adversely affect the international transfer of technology.“ (TRIPS Agreement Article 8, paragraph 2 1994). These main principles evidently lay down ground rules for intellectual property rights but refrain from restricting their members too much in terms of the applied measures. In Article 3 paragraph 1, signatories accept to accord “the nationals of other Members treatment no less favourable than that it accords to its own nationals with regard to the protection of intellectual property, (...)“ (TRIPS agreement Article 3, paragraph 1 1994). Since the agreement performs under the aegis of the WTO, the most favoured nation treatment applies as well: „With regard to the protection of intellectual property, any advantage, favour, privilege or immunity granted by a Member to the nationals of any other country shall be accorded immediately and unconditionally to the nationals of all other Members.“ (TRIPS agreement Article 4, paragraph 1 1994).

Under TRIPS, all those WTO members who at the time the agreement came into force (i.e. in 1995) did not comply with it, were given 10 years of time to do so. However, “India’s Patents Act from 1970 exempted food or medicine or drug from product patenting” (Chaudhuri 2002: 3354), which is why the country had to put changes into place.

6.2.4 IPR System in India

The next two sections take a closer look at India’s and the EU’s IPR regimes and their compliance records. In the case of India, the development of the IPR legislation and the institutional framework are also analysed.

Following the WTO membership and the necessity to follow TRIPS rules, the Indian government performed amendments under the Patents (Amendment) Act (Trademarks Act and Copyright (Amendment) Act) in 1999 and the possibility of “Exclusive Marketing Rights” (EMR) was provided (Chaudhuri 2002: 3354). This step was one of a number of steps in order to harmonize the Indian Patent law and its administration with India’s obligations under the TRIPS agreement.

After 1999, companies could apply for patenting in the formerly restricted areas but processing of grants was frozen until 2004. Exceptions existed, granted a patent had been approved in another WTO member state and the application complied with the Indian Patent Act. After another amendment in 2002, the 2005 amendment to the Patent Act proved highly controversial for domestic producers as it initiated a process patent regime (Gasiorek et al 2007: 51). Henceforth, India’s new patent regime— it had been undertaken in order to comply more closely with TRIPS – required producers to obtain compulsory licenses. Even though such compulsory licenses would enable Indians to produce and export generic drugs (as long as they were licensed), reality proved more difficult: the process of purchasing such a licensing is tedious and bureaucratic and very few licenses have been granted (Gasiorek et al 2007: 51).

Although its process has been commonly criticized, the Indian Patent law provides data exclusivity. This system prevents the acceptance of a medicine’s generic version registration during the medicine’s patenting process. The use of the registration files of the original medicine in order to register a generic version of that medicine is also prohibited under the

data exclusivity clause (Gasiorek et al 2007: 51). Further major legislation in the field of IPR include “the Trademarks Act, 1999; the Copyright (Amendment) Act, 1999 which has been amended to protect computer programmes as literary work; the Patent Act 1970 as amended most recently through the Patent (Amendment) Act 2005; the Designs Act of 2000; the Semiconductors Integrated Circuits Layout-Designs Act, 2000; a sui generis legislation for the protection of plant varieties called the Protection of Plant Varieties and Farmers’ Rights Act, 2001 (the PVP Act); and the Geographical Indications of Goods (Registration & Protection) Act, 1999.” (Ecorys 2009: 260).

India has expanded its administration and established the Department of Industrial Policy and Promotion (DIPP), which deals with legislation relating to patents, trademarks, designs and geographical indications. The “Intellectual Property Appellate Board” (IPAB) functions as an appeal contact against the decisions of Registrar of Trademarks, Geographical Indications and the Controller of Patents (Ecorys 2009: 260). The legal amendments did not go unseen as the number of patents filed show. Leaving China behind, India managed an increase of 365 per cent between 1995-2004. Foreign investors and companies have contributed to a 105 per cent increase, leaving India with the 7th largest increase among WTO members (Ecorys 2009: 260).

Evaluating the efforts undertaken by India it can be concluded that the country has room to further establish its statutory and administrative framework for IPR protection. The DIPP puts strong efforts into enforcement improvement. An inter-ministerial committee has also been set up specifically to increase the enforcement of IPR protection and deal with counterfeiting, piracy, data protection, and the like (Ecorys 2009: 260).

6.2.5 IPR System in the EU

The EU, a knowledge-based Single Market, puts great emphasis on sound IPR and their enforcement. The European Commission is in charge of monitoring the protection of intellectual property within the EU and the progress being made in this field. The harmonisation process of the different member states provisions is ongoing. An important enforcement instrument is the recent Directive 2004/48/EC, which censures “unnecessarily complicated or costly (...)“ civil procedures or such that „entail unreasonable time-limits or unwarranted delays“ before the European Court of Justice (Ecorys 2009: 259). The directive

deals mainly with enforcement issues in counterfeiting and product piracy as well as “procedural issues regarding evidence, standing, interlocutory measures, damages, judicial publication” (Ecorys 2009: 259). The EU has made notable progress in harmonising national and EU IP, however, patent law remains problematic and requires an improvement in the procedures. The number of languages spoken in the EU adds to the difficulties for the implementation of community-wide patents and hence consequently hampers an effective enforcement.

Towards its partners, the EU has emphasized compliance with the TRIPS agreement as a starting condition. Some of the previous FTA negotiations, however, went beyond compliance with the TRIPS agreement but asked potential partner countries to ensure effective protection and enforcement of IP. In a number of agreements, the EU specifically mentions treaties and conventions to which their negotiation partner has to conform. Such TRIPS+ requirements, e.g., are laid out in the EU-Mediterranean Agreements and the EU-Chile Agreement and have been specifically mentioned in the EU-India negotiations (Ecorys 2009: 51).

6.2.6 Challenges

The protection of intellectual property is a challenge to the EU and India. Both concede that they have problems in guaranteeing a transparent and balanced IPR legislation between protecting IPR and preventing the creation of monopolies, as well as with putting adequate enforcement mechanisms in place. India and the EU share their intentions to promote innovation and investment as economic stimulus for employment, growth and progress, specifically for international traders and investors, who wish to be at ease when doing business abroad.

Despite the mutual understanding between the two negotiation partners, there are several challenges ahead. In the following I identify several challenges with regards to an integration of Intellectual Property Rights into the BTIA. They illustrate the potential problems that could arise if Intellectual Property Rights were included in the BTIA.

6.2.6.1 Challenge #1: TRIPS+ Compliance of India

In previous FTAs and RTAs, the EU insisted on their partner countries to not only comply with TRIPS but with treaties and conventions going beyond what is laid out in the WTO agreement. In the EU-India BTIA negotiations, the EU requires India to go beyond TRIPS. There are examples for IP related treaties, which India is a part of, such as the Patent Cooperation Treaty (PCT) and the Budapest Treaty on the International Recognition of the Deposit of Microorganisms for the Purposes of Patent Procedure (WIPO Budapest Treaty 2013).

However, one of the difficult treaties for India to accept is the International Convention for the Protection of New Varieties of Plants (UPOV) 1991. “India approved the Protection of Plant Varieties and Farmer’s Rights Act 2001 in place, which follows the UPOV version of 1978 and incorporated parts of UPOV 1991 (Gasiorek et al. 2007 Annex 4: 67). This Indian version of UPOV aims at a better balance between breeders and farmers rights. The UPOV version of 1991, however, is said to determine which practices “undermine the right of farmers to save, use, exchange and sell IPR protected seeds“ (Eberhardt, Kumar 2010: 36). India’s position in this regard is rather practical and points at the successful implementation progress made with the TRIPS agreement. This process is still ongoing, therefore the commitment to and implementation of additional multilaterall agreements is considered to be unrealistic in terms of costs and success.

Furthermore, at present, India lacks the necessary amount of staff, e.g. patent examiners³². Qualified IPR attorneys are also scarce, even though, ideally, a judge should have at least background knowledge in chemistry, pharmaceuticals or biotechnology (Gasiorek et al. 2007 Annex 4: 67). At the moment, India is not creating enough IPR professionals to meet their demand.

³² 3500 in the US; 4000 in China and 275 in India (Gasiorek et al. 2007 Annex 4: 67).

6.2.6.2 Challenge #2: IPR Enforcement in India

Both Indian as well as European investors criticize the lack of IPR enforcement in India, which inevitably creates a major barrier to market access. Even though the necessary legislation is present, the implementation is poor. One good example is the enforcement of copyright law: until today, the establishment of the Copyright Enforcement Advisory Council (CEAC) has not proved to be very successful. It was set up in 1991 “to review the progress of enforcement of Copyright Act periodically and to advise the Government regarding measures for improving the enforcement of the Act” (Ministry of Human Resource Development 2013). However, its record concerning the better awareness for and enforcement of copyrights remains poor. Necessary, well-informed and trained staff (police, prosecutors) is neither available nor trained, so are judges. This lack in human resources and awareness results in thousands and thousands of pending cases and a stuck enforcement process. Another example is the pre-grant opposition procedure, which has been in force since the Indian patent law amendment of 2005. Now, in addition to post-grant, pre-grant opposition can be filed, which in turn lead to massive delays in the issuance of patents and a growing number of competitors and cases.

It is evident that the sluggish and idle IPR enforcement system reduces trust in India as a safe place for investment. As a result, not only domestic investors and inventors prefer foreign markets, also foreign direct investment (FDI) flows into the country have declined over time. The country lacks the indispensable manpower and investment in the enforcement in order to recreate confidentiality in India as a safe haven for invention, investments and progress.

6.2.6.3 Challenge #3: Patent Law in the EU and Trademark Law in India

The EU Single Market harmonized its IPR legislation over the past years and, in addition, gained significant experience in the protection of IPR. Despite the efforts, Indian exporters face several problems when inventing and investing in the EU. While the fields of designs, trademarks, copyrights and enforcement procedures of IPR are well protected; patent law still seems to be subpar. As a consequence, national IP laws of member states apply to Indian exporters, which can be an impediment (Gasiorek et al. 2007 Annex 4: 71). Different EU member states vary for the most part in calls for speed, type of relief, cost and the potential

drawbacks of legal actions. The language barrier and the difficult accessibility of knowledge and understanding of the EU system aggravate these procedural differences in IP litigations. Consequently, Indian firms are confronted with high costs of obtaining and enforcing patents and trademarks as well as enforcing copyrights. Litigation costs and attorney fees are also considerably higher compared to the domestic market (Gasiorek et al. 2007 Annex 4: 71).

6.2.6.4 Challenge #4: Data Exclusivity

The EU has emphasized its desire to include a data exclusivity clause in the FTA, ensuring the protection of registration files for a fixed period of time. According to the clause, regulatory authorities are obliged to protect the data of a patent applicant from being used to register a generic version of that very medicine (Gasiorek et al. 2007 Annex 4: 51). As the review of a patent application can take a longer time, the clause hinders the development of generic pharmaceuticals in the meantime and leads to delays in the supply of affordable medicine for the poor. In addition, the clause obliges India producers of generic drugs “to repeat the innovator companies’ costly and time-consuming tests because public authorities could no longer rely on their test data to approve the generic drug.” (Eberhardt, Kumar 2010: 18).

The Indian government took a rather oppositional stand on this issue and set up an inter-ministerial committee in order to assure TRIPS compliance in this matter. The Indian Commerce and Industry Minister and chief negotiator for the FTA, Mr Anand Sharma, assured in 2011 that India would reject any efforts to include data exclusivity in bilateral trade agreements (Third World Network 2011). Consistent pressure from Indian and international groups and NGOs, as well as from the Indian government induced the European Commissioner for Trade to back away from this clause in 2012 (MSF 2012). However, several stakeholder groups remain alarmed about the EU’s efforts of finding alternative ways to push the clause through. The NGO Médecins Sans Frontières (MSF) assumes that the EU is putting pressure on India and its domestic drug law (MSF 2012).

Another aspect of this issue concerns Indian business process outsourcing (BPO). In the past years, more and more Western multinational corporations have outsourced a significant part of their services to India and its call centres. The lack of data protection, however, has increased the pressure on India to adapt its legislation. Particularly the incident of the

Citibank data theft³³ forced India to act. The EU has taken a serious stand in this matter since European businesses are obliged to comply with Directive 95/46/EC on data privacy (Directive 95/46/EC 1995). The directive prohibits business in countries where no adequate protection of personal data is guaranteed.

So far, India has been working on a data protection law, as it is evident that the lack of data protection goes to the expense of India's share in the outsourcing market. Such a law would go beyond India's TRIPS agreement requirements.

6.2.6.5 Challenge #5: The Mutual Problem of Piracy

Counterfeiting and piracy, as well as the resulting economic damages are considered to be a mutual problem. Despite adequate legislation, both partners have to deal with copyright infringement and piracy of audio, film, books, and software and – particularly problematic in India – cable signals. The use of pirated products is widespread and lead to a domino effect in the whole picture market. The movie industry laments the distribution of pirated DVDs and VCDs way before the theatrical release, posing a major problem and high costs to the whole industry.

6.2.7 Impact Analysis

An impact analysis is conducted in order to assess the possible impacts of IPR laws and enforcement as construed in the FTA. Since the exact wording and positions are not available, this analysis is based on a qualitative analysis as well as literature review. Most of it is published by non-governmental organizations. Since this chapter deals with challenges of the integration of non-tariff barriers, the impact value of their changes will be analysed qualitatively.

³³ Citibank customer data was stolen by workers at an Indian call centre (Gasiorek et al. 2007 Annex 4: 70).

6.2.7.1 EU

Economic Impacts

It is evident that a harmonisation in the domestic IP law will be beneficial to the EU economy. Certain parts of EU IP law is already harmonized, but others are either incomplete in their implementation or not even implemented legally. The stronger emphasis on EU IP law harmonisation will increase investor trust in the EU market and consequently reduce non tariff barriers to free trade.

In the FTA, the EU insists on stronger IP protection and from an economic point of view, this will impact the EU positively in its growth. It has been mentioned earlier that IP and its protection is considered a trigger of innovation and progress. The economic impact of IP protection can be different from sector to sector but it is typically high in a knowledge-based economy, which the EU certainly is. Consequently, it is ought to profit from free trade with a market, which, on the one hand, provides adequate IP protection, and on the other hand, functions as market.

Starting from the assumption that India complies only with the provisions necessary to fight both parties' mutual challenge, namely piracy and counterfeiting, the EU will still benefit from it (Ecorys 2009: 262). The economic damage from counterfeiting and piracy can be reduced – particularly for small and medium sized enterprises. The indirect damage of discouraged innovation can be reduced as well and in turn lead to increased R&D efforts and investments in the EU.

Social Impacts

The effects on the social structure in the EU can range from positive, employment stimulating outcomes to rather negative ones. The latter may occur in case of the encouragement of establishing subsidiaries in India instead of producing in Europe. This could be the case if India decided to facilitate such steps further – not only through their IPR law but also through tariffs and investment facilitation (Ecorys 2009: 17).

On the other hand, considering the market size of India, the EU-India FTA could encourage higher exports to India. The country is currently blessed with a growing, consumption-

friendly middle class. Even though the American culture is dominant among the foreign cultures in India, the EU stands the chance of positioning themselves as a partner of exquisite taste, class and style. This would spur the demand for European high quality products.

Environmental Impacts

There are no exact figures available but the impacts of the EU-India FTA on CO₂ emissions and other environmental factors in the EU are expected to be little and insignificant. Increased trade between the two economies will increase the consumption of energy, so will the increased air and marine transport. The resulting increase in direct Global Emissions by Gas emissions, however, will be rather small and negligible (Ecorys 2009: 18).

6.2.7.2 India

Economic Impacts

IPR protection is one leg of improving innovation conditions in a country. IP protection can foster entrepreneurial spirit and R&D efforts, but may also impede the diffusion of knowledge and technology as well as the development of monopolies. So far, Indian producers have taken the opportunity of India's TRIPS compliance and consider it a positive development for India. This trend can be observed in the growing number of patent applications in India. Another sign illustrating the positive reception of stronger IP protection in India are investments in R&D as well as in the key sectors of information technology and pharmaceuticals.

The increased access and strengthened intellectual property regime within an FTA between the EU and India is very likely to promote capital inflows from foreign companies as well as trade. Increased trust in India's IP protection can also stimulate technology transfer and thus spill-over – crucial for a country like India, which is a knowledge follower (Ecorys 2009: 265).

The impact on FDI attraction and thus GDP growth can be measured with the help of an OECD index and is said to be significant for India. The index shows the correlation between the improvement of IP legislation and growth. Thus, a 1 per cent increase in the Patent Right Index leads to a 1.3 per cent increase in imports and 1.6 per cent increase in FDI for a

developing country (cite! See Park, W.G. and D.C. Lippoldt (2008), “Technology Transfer and the Economic Implications of the Strengthening of Intellectual Property Rights in Developing Countries”, OECD Trade Policy working Papers 62, OECD Trade Directorate.). However, it must be noted that patent right enforcement and protection diminish positive effects on trade and FDI since it involves costs to establish such a framework. The output increase due to IP protection is likely to stimulate total factor productivity³⁴.

To sum it up, the economic effects of a strengthened IPR legislation and enforcement is likely to foster innovation and R&D and thus growth as well as FDI and trade.

Social Impacts

With regards to the social impacts, the effects of a potentially tightened patent regime could be hazardous for India, as the production of generic drugs – as it is done now – would become illegal. Currently, India supplies generic drugs at low prices not only India-wide but also to many developing countries, especially in Sub-Saharan Africa. HIV/Aids treatment as well as expensive drugs against cancer are largely produced in India at a low-cost and aim at providing affordable medical care. If the production and subsequent distribution of generic drugs fall under the BTIA, fewer producers will take the risk of running generic drug factories. Together with a supply shortage of such drugs, many jobs affiliated with the generic drug production would be at stake. Above all, however, is the threatened health of many people in India and abroad. Repeating Sen’s (2013) point of view on the necessities for development, health is crucial to a successful and prosperous human life. Healthy people are more productive in their lives and thus states should support measures that lead to good health. Médecine Sans Frontier has a similar point of view and actively opposes the integration of IPR in a FTA between India and the EU. „As an organisation that sources 80 per cent of its HIV treatment medicines from India, MSF is also concerned at the intellectual property enforcement provision and investment mandate that remain.” (MSF 2012).

More rigid compliance with restrictions in the agricultural sectors may also be disadvantageous for India. Not only would the full implementation of the UPOV regulations be expensive, but it could also lead to adverse effects on farmers and their rights. Particularly

³⁴ TFP is a variable that accounts for results in total output that are not caused by the common inputs of labour and capital.

small farmers would be affected by the regulations as the protection of new varieties of plants and thus the reuse of seeds could be aggravated.

In these respects, therefore, the intellectual property rights contain serious risks on a social scale. This will presumably motivate Indian representative to push hard for some form of compromise that does not undermine the generic industry; in the least it is plausible to expect some form of transition period that allows India adapt to the new regulatory framework.

Environmental Impacts

Environmental impacts resulting from IPR changes could stem from a reduced rate of piracy products. A large number of such products do not comply with safety and health standards; often they do not comply with environmental standards as well. Illegal production sites have sometimes proven to be hazardous to the surrounding ecosystem, as regulations are not followed. Some factories harm the local water resources, leading to subsequent damages of the soil and air. Even though the large environmental and ecological influences of a tightened IPR regime might not have great impacts, even a small reduction of India's carbon footprint would be a success (Ecorys 2009: 19).

6.3 Case 2: Government Procurement

India's trade policies regarding non-tariff barriers are an essential issue for negotiation, particularly in the field of government procurement. This second case is constructed like the first one and examines background, legal status and impacts of an integration of government procurement in the BTIA.

6.3.1 Background

Government or public procurement is the procurement of goods and services on behalf of a government authority. The procurement process is different from country to country whereas most systems require some sort of bidding for projects. Such public tender (call for bidding) aims at reducing fraud, corruption, waste and protectionism, which could occur otherwise. The WTO defines the necessary requirements for an efficient procurement system as "the attainment of value for money, public access to information on government contracts, and fair opportunities for suppliers to compete for government contracts." (WTO Government Procurement General Overview 2013).

The significance for a well-set and transparent procurement system stems from various reasons. First and foremost, the government is able to provide public goods and services as well as those that allow the government to function properly. What is more, a fair and transparent procurement process reduces waste of taxpayers' money and thus enhances public confidence in good governance. Lastly, the sector is not negligible in economic terms. In fact, government procurement amounts for 10-15 per cent and roughly 20 per cent of GDP in developed and developing countries respectively. Consequently, as government contracts often require international goods and services, government procurement fosters international trade. It goes without saying that multinationals as well as international companies are interested in bidding for such projects. The rules of the competitive market would allow this if there were a comprehensive set of rules. Procurement, however, had been excluded from multi- or even bilateral trade negotiations (within the framework of the WTO) until recently. GATT and later WTO members negotiated the multilateral Government Procurement Agreement (GPA), started talks on government procurement in services within the GATS agreement (Article XIII: 2 of GATS) and established a working group on transparency in government procurement in 1996.

This setting fostered the internationalization of procurement as well as the desire of international firms to bid in foreign markets. Bilateral trade agreements as well as preferential arrangements evidently included some sort of government procurement regulations, which allowed bidding in the partner country.

In the BTIA, the EU demands mutual access to government procurement, along with further improvements of the Indian system. The EU would like India to comply with international standards and open up their lucrative procurement sector for the EU. As of now, India is not a signatory of the GPA agreement under the aegis of the WTO.

6.3.2 Legal Situation

The only international agreement on government procurement is the multilateral Government Procurement WTO agreement³⁵. It deals with goods and services and explicitly includes construction services. The main targets being transparency and non-discrimination, the agreement calls upon its signatories for maximum openness in their national procurement systems. This non-tariff barrier is therefore targeted at the reduction of procurement barriers, particularly in bilateral preferential trade agreements.

The agreement regulates “national treatment and non-discrimination for the suppliers of Parties to the Agreement with respect to procurement of covered goods, services and construction services as set out in each Party’s schedules and subject to various exceptions and exclusions that are noted therein.” (WTO Government Procurement General Overview 2013). Further, it encompasses procedural aspects of government procurement, which requires full transparency and a fair competition on the grounds of non-discrimination between the bidding parties. Since the procurement process attracts irregularities, members of the agreement agree to apply the WTO Dispute Settlement Understanding. Members also oblige to „the availability and nature of domestic review procedures for supplier challenges which must be put in place by all Parties to the Agreement.“ (WTO).

³⁵ However, not all WTO members are bound by this agreement.

The first Agreement on Government Procurement, covering government entities and goods only, was signed in 1979 (went into force in 1981), after efforts within the OEC had been made to agree on an international set of rules. An amendment version of this agreement went into was implemented in 1988. The signatory states demanded further amendments with regards to the scope of the agreement. This new Agreement on Government Procurement was signed on April 15th 1994 in Marrakesh and went/came into force on January first 1996. It included purchases by sub-central government entities and other public enterprises as well as services and construction services. The first result was strong: it was estimated that the value of procurement subject to international competition, had increased ten-fold³⁶. The number of countries joining the agreement has expanded since then, leading to a growing value of it. The latest changes to the agreement were formalized on March 30th 2012, at the same time when the Decision on the Outcomes of the Negotiations under Article XXIV: 7 of the Government Procurement Agreement was formalized (WTO Government Procurement General Overview 2013).

The EU (EU-28) has signed the agreement, the other signatory countries of a total of 43 are: Armenia, Canada, Hong Kong, China; Iceland; Israel; Japan; Korea; Liechtenstein; the Kingdom of the Netherlands with respect to Aruba; Norway; Singapore; Switzerland; Chinese Taipei and the United States (WTO Government Procurement General Overview 2013). 22 countries (all WTO members) and four intergovernmental organizations³⁷, have observer status, one of which is India (WTO Government Procurement General Overview 2013). According to the OECD “Total government procurement worldwide is estimated to be roughly equivalent to 82.3% of world merchandise and commercial services exports in 1998.” (OECD Newsroom 2013: 8). This figure illustrates the economic relevance of the procurement sector.

³⁶ Annual value under 1979 agreement: US\$30 bn.

³⁷ These organizations are the International Monetary Fund (IMF), the International Trade Centre (ITC), the Organization for Economic Cooperation and Development (OECD) and the United Nations Conference on Trade and Development (UNCTAD) (WTO Government Procurement General Overview 2013).

Table 14: The three main areas of work on government procurement in the WTO

The three main areas of work on government procurement in the WTO			
	Plurilateral Agreement on Government Procurement	General Agreement on Trade in Services	Working Group on Transparency in Government Procurement*
Type of work	administration of existing WTO agreement	negotiations based on <u>Article XIII:2 of GATS</u>	study and elaboration of elements for inclusion in an appropriate agreement
Main principles	transparency and non-discrimination	transparency and possibly non-discrimination	only transparency (preferences not affected)
Scope of work	goods and services, including construction services	only services	government procurement practices
Participation	plurilateral (not all WTO Members are Parties)	multilateral (all WTO Members involved)	multilateral (all WTO Members involved)

Source: WTO Government Procurement General Overview 2013.

6.3.3 Government Procurement in India

Obtaining a transparent and clearly structured procurement system is a challenge common to many developing countries. India is one of those countries, which face the challenge of balancing social and sustainable objectives of supporting domestic and particularly small and medium sized enterprises and high growth rates as well as a high quality public sector infrastructure in an effective manner (Srivastava 2012).

Albeit a WTO member, India is not a signatory but an observer of the GPA. The main differences between the GPA and the Indian Government Procurement system are preferential treatment of domestic enterprises (mainly micro and small enterprises), transparency and review mechanisms. The legal basis of central government procurement in India is the General Financial Rules (GFR) of the Ministry of Finance (Ministry of Finance, Government of India 2013). Firstly formulated in 1961, the GFR were revised in 2005 and since then, provide general principles and regulations of public buying: “Every authority delegated with the financial powers of procuring goods in public interest shall have the responsibility and

accountability to bring efficiency, economy, transparency in matters relating to public procurement and for fair and equitable treatment of suppliers and promotion of competition in public procurement.” (GFR 2005 Rule 137: p. 27). Inventory costs resulting from excess purchase are to be avoided as well and the procurement procedure also requires clearly spelled out specifications of the good or service in question. Bidders meeting these criteria, “should be invited following a fair, transparent and reasonable procedure;” and convince the procuring authority by fulfilling the requested criteria and providing a reasonable balance between price and quality.

The Directorate General of Supplies and Disposal (under Department of Supply) is the central purchasing organization of the Government of India; it ensures the purchase of goods and services in the most efficient and economic manner (Gasiorek et al. 2007 Annex 4: 30). The standard mechanism of procurement is to obtain bids in either an advertised tender enquiry, limited tender enquiry or a single tender enquiry (rule 149). Generally, the GFR based centre government’s procurement mechanism is - even if only broadly - compatible with requirements of most free trade agreements.

Legally, the rules governing the centre differ from the state and municipal level in terms of a systematic set of rules. Whereas the central government and the state of Bihar follow the revised GFR of 2005, the other states’ regulations are based on the 1961 version (Ministry of Finance, Government of India 2013). The main differences between the centre (and Bihar) and the other states are the preference system and the average number of tenders (which is significantly lower on the state level). While price preferences exist on the state level, the centre has purchase preferences for small-scale units and village enterprises. Among states, there is a correlation between states with good governance and advanced procurement legislation. Karnataka and Tamil Nadu for example have introduced state legislation and e.g. transparency rules for procurement (Gasiorek et al. 2007 Annex 4: 30; Ministry of Finance, Government of India 2013).

The procurement of governmental contracts is a very lucrative sector in India and estimated at around US\$156 bn. (12-14 per cent of GDP) (cite). However, little reliable data is available for an estimation of the procurement sector in India. Srivastava estimates the total value between 3.5 and 5.7 per cent of GDP³⁸ (1998-2001) (Srivastava 2012).

³⁸ Only with competitive bidding.

6.3.4 Government Procurement in the EU

The European Single Market system induced progress towards a harmonized European procurement system comparably early (Bovis 2007). Discrimination or barriers are prohibited on the grounds of the European Single Market and the Four Freedoms. In addition to primary legislation, the EU undertook efforts to harmonize the member states' legislation. Currently, the government procurement sector in the EU accounts for an estimated 16 per cent of GDP (European Commission, Public Procurement 2013).

The EU considers government procurement as an essential part of trade agreements – irrespective of the agreement being a preferential trade agreement or not. First and foremost, she (the EU), values the opportunities that EU businesses can accrue (or that occur), along with the stimulation of the EU economy and job creation. In negotiations, the EU points out the fact that its companies and firms are highly competitive in many sectors and would benefit the partner country's economy by providing high quality work.

The EU argues for competitive and open procurement markets, particularly in her partner economies, and criticizes protectionist policies, which may have or will hurt EU businesses (e.g. US, Brazil, China, Turkey, Russia, certain States in Australia are said to having applied such measures (European Commission, Public Procurement 2013).

6.3.5 Challenges

6.3.5.1 Challenge #1: Corruption

Fraud, bribing, bid rigging – these are just three faces corruption can adopt/take within the government procurement sector. Both the EU and India are affected by such criminal incidents, which lead to substantial losses of quality and public money every year. According to the Confederation of Indian Industries survey³⁹, a bribe of two to 25 per cent of the contract price is said to be average in order to secure a public contract (Gasiorek et al. 2007 Annex 4: 56).

³⁹ World Bank survey

Despite the EU system's flaws, India is in the position where there is more room for reforms in the procurement methods. An example is India's single stage two envelope bidding system. In this system, bidders for a contract submit two envelopes simultaneously: One contains the technical proposal, the other one the price proposal. Both envelopes are enclosed together in another envelope, whereas the technical proposal is ought to be opened first. This ensures the evaluation of the bid before knowing the price and prevents from hasty decision-making based on the price.

In India, this system has proved not to be effective in some cases, leading to delays in the processing of bids and decision-making and an undermined process, since price envelopes are opened first and the lowest bidders receive the contract award. By performing price preference, bidders may receive the contract even though they do not offer the best solution and public resources are inefficiently spent. Another aspect is a lack of transparency, manifested in little public information about bids, decisions and justification of those decisions.

6.3.5.2 Challenge #2: Procurement Process

In contrast to the EU, the Indian procurement system lacks certain procedural aspects, which would enhance a fair and transparent process. Despite India's tendency to red tape, the procurement sector is not equipped with standardized bidding documents, administrative documentation of bids and awards or a harmonized dispute settlement mechanism. Problematic consequences lead to distorted competition and delayed requests (amongst others) and promote corruption.

6.3.5.3 Challenge #3: Pressure on Bidder

An issue that may not necessarily affect the free trade agreement but has significant effects on the Indian procurement system is pressure on bidders. In some cases, authorities may put bidders under pressure to adapt the bid price and offer a lower one. Bidders may get into dire straits when put under pressure to eliminate costs but keeping other variables of the contract constant. Particularly the retaining of quality becomes a difficult endeavour (Gasiorek et al. 2007 Annex 4: 58).

6.3.6. Impact Analysis

We can say that India complies with the EU's requirements in theory and it will limit national treatment requirement only to purchases made by the central government and exclude the state and municipal level.

To many experts, the real problem for India lies in the procurement methods. India's attitude here is that procurement methods do not have an impact on transparency. Others would argue differently (Gasiorek et al. 2007 Annex 4: 55 ff.).

6.3.6.1 European Union

Economic Impact

Generally speaking, it can be said that the EU has experienced large benefits from domestic standardization in government procurement. Many companies are specialized in working with governments and delivering their services to them. If government procurement were included in the FTA the way the EU is hoping for, European companies could hope for substantial gains. India's size and large number of projects would open various new possibilities to businesses in Europe. Especially the infrastructure sector offers great potential for growth and thus for professional businesses since the Indian government has put great emphasis on public-private partnerships (PPPs). Infrastructure projects are henceforth realized in a partnership between the government – be it the central government or state governments – and private companies. Such partnerships give businesses the security to recover their investment, whereas the government can provide the guarantee that the project is realized under governmental supervision.

With this in mind, it is reasonable to suggest that standardization in the Indian procurement system would benefit European business and contribute positively to the EU's growth. The lack of standardization in India hinders EU companies to bid for Indian projects, since the variation across the country makes it difficult for foreign competitors.

Hence the EU is a great supporter of standardization in government procurement. In negotiations for better procurement systems, they have argued that it “enhances government abilities to obtain better value for money and increases efficient use of public resources; is a

powerful tool to fight corrupt practices; [and] increase transparency and legal certainty.“ (European Commission, Public Procurement 2013).

As there is little information on the actual negotiation status of this issue, it is difficult to assess if the EU is really willing to offer equal access to their market in return. Their official position certainly promises compliance to procurement regulations. The European Commission commits itself to opening their market: “(...)the EU advocates for an ambitious opening of international public procurement markets outside the EU and has committed itself to granting market access to its public procurement market for certain foreign goods, services and companies. The EU negotiates both bilateral/regional and plurilateral international agreements.“ (European Commission, Public Procurement 2013).

However, it could be to the EU’s disadvantage if India, in turn, wanted equal access to the EU’s government sector. Increased competition from Indian businesses is an expressed fear, even though the actual economic impact is expected to be little. Distorting effects of competition would only arise if the EU’s procurement system was fragile and European businesses were not be able to compete.

Clearly, there are discrepancies between the EU’s and India’s position: the EU wants India to open the sector and grant the EU’s businesses access; India on the other hand is hesitant and – even if – will probably only comply under the condition that the EU opens their sector as well. In sum, both partners face the same trade-off: opening up business opportunities abroad vs. protecting domestic firms from foreign competition. So far it has not become clear how the negotiations will go.

6.3.6.2 India

Economic Impacts

A number of positive and negative consequences are possible for India if it standardized its procurement system and granted the EU access to it. First and foremost, a better-regulated system would benefit the domestic system in various ways. More Indian companies would have access to projects and would diversify the biddings. The competition between the companies would increase the quality of their services offered to the authorities. Consequently, the central and local governments would have more companies offering their

services and could in turn offer their citizens “more bank for their buck”. An improvement of work quality is particularly important in infrastructure projects, which often cost large sums but do not return equal quality.

Additionally, there are benefits to the government’s reliability and its perception. Entrepreneurs would have trust authorities and could count on them as a constant factor rather than an instable, unpredictable one. Increased transparency would allow a substantial boost of entrepreneurship because a lack of governmental regulations would not pose a cost and risk factor any more. Consequently, this development would spur economic growth in India.

As discussed earlier, India is very interested in gaining access to the European market. Clearly, this would create the opportunity for Indian businesses to expand their horizon and offer their services to a new, larger market. Even though European competition is strong, open procurement would allow Indian businesses to learn from their European colleagues and improve their businesses.

Costs affiliated with required changes in the Indian procurement system are a negative impact on India’s economy. The abolition of corruption and implementation of improved bidding procedure mechanism will require substantial investments by the Indian government. In a similar vein, the e-procurement initiative of the Indian government has been costly without providing significant improvements for procurement (Gasiorek et al. 2007 Annex 4: 15 ff.). Delays and corruption have also proven exacerbating factors.

Another factor, which has been analysed from the EU’s perspective earlier, is the potential negative impact from increased competition of European countries. Compared to India, the EU has well-established and experienced businesses. The quality of the work is high and so are the demands for high standards. Although, in case of the integration of procurement in the BTIA, European businesses will have difficulties with adapting to the rules of the Indian market; nevertheless they have the lead in quality and experience. Such a development, if allowed too abruptly, would create distortions among Indian businesses and eventually force a significant number of them out of the market.

Social Impact

From a democratic-theoretical perspective, governmental initiatives aimed at decreasing corruption and improving transparency lead to increased trust in the authorities. Especially in India, where corruption is omnipresent, any measure targeted at more transparency would have positive impacts.

Furthermore, initiatives such as the e-procurement system help the country modernize faster as information is available online and to larger population groups. India is already strong in using online sources and offering information to its population using technological communication. Open and online access to procurement regulations will certainly contribute to the information of more people (Gasiorek et al. 2007 Annex 4: 16).

Hence breakthroughs in the procurement sector could have notable positive social impacts, which would assist India on its path of development.

7. Summary of Findings and Possible Solutions

7.1 Summary

The conducted impact analysis hypothesized the integration of intellectual property and the area of government procurement and allowed an assessment of its effects on the EU's and India's economy and their society and environment.

It has become clear that the negotiation parties have varying interests in the process and that those interests are mainly organized around the economic advantage. Impacts on the social, environmental and developmental sphere also weigh in the assessment of the negotiation positions, nonetheless, their role is subordinated and rather marginal.

Under the increased access and strengthened intellectual property regime caused by a trade agreement, there would be smaller direct and larger indirect effects on the respective economies. The effects resemble one another in that they are difficult to monetize. One significant challenge is the area of generic drugs production. The recently completed Novartis case sent a strong signal to pharmaceutical companies about India's sternness with regards to its IP regime (Abbott 2013). The data exclusivity clause illustrates parts of the challenge in detail and poses a great hurdle to the EU the businesses it represents. This clause would prevent the acceptance of a medicine's generic version registration during the medicine's patenting process. Also, the use of clinical data is prohibited during the patenting process. The Indian Ministry of Commerce has set up an inter-ministerial committee in order to ensure compliance with their TRIPS obligations, it is not clear whether data exclusivity will be implemented. Since European pharmaceutical companies fear a potential lack of protection of their data, this remains a bone of contention.

On the other hand, India is well aware of not only its moral obligation to produce and provide affordable generic drugs, but also the economic importance of doing so. The expected positive effects on the health of millions of people are exorbitant. The same goes for the indirect impacts on the economies of generic drug importing countries, which will lose cure for their patients and subsequently productive labour potential.

The time frame has also shown to be relevant in the course of the impact analysis: In the short term, the countries cannot expect significant improvements or aggravations since an integration of IPR is a long process. In the long-term, positive effects are possible, particularly in the form of increased innovation, reduced infringement and an overall positive contribution to production and economic growth. In this case, however, IPRs must be implemented and enforced in a good timely manner. Strict enforcement, attention to developments in the international sphere as well as monitoring are also crucial measures to both India and the EU's path towards harmonized IP regimes and an integration of the two in their FTA.

The overall impacts of the harmonisation of government procurement under the EU-India FTA can be valued as positive, whereas improvements are required from both involved parties. Overall it can be said that India and the EU have to standardize their systems in order to increase mutual trust within the FTA. This is the first and key step, especially from India's side, as there are difficulties for businesses in the procurement market. As a result, the Indian economy could benefit from a quality increase, economisation of costs and spill-over effects on civil society trust through increased transparency and lower corruption. In addition, if Indian businesses gained the same access to European procurement, Indian entrepreneurs can step into new markets and increase the quality of their services by benefitting from European businesses' experiences. As can be seen from this analysis, the points of controversy remain numerous and both parties will need to make some concessions to ensure that the deal can go through.

7.2 Solutions to Challenges

A closer look at the challenges that were analysed in the previous chapter, allows the suggestion of a number of solutions.

One of the larger questions that arose from the analysis does not concern India's ability to stick with their full compliance with their TRIPS obligation, but rather India's desire to go beyond TRIPS. As of now, India is legally obliged to comply with TRIPS and its regulations and the country seems determined to do so.

In the long-run, India will have to make a choice. If the country is interested in engaging in free trade arrangements with Western countries or even RTAs with Asian countries, they have to provide trustworthy, predictable protection of intellectual property. Not only will such a framework protect Indian businesses from fraud and illegal copying, it will also set a precedent for India's advancement in entrepreneurship (Gasiorek et al. 2007 Annex 4: 67).

The question remains if India wants to go beyond the basic TRIPS framework. Future agreements of the scope of the BTIA will certainly require India to do so. The scope of the BTIA, however, shifts parts of the responsibility to the EU as well. Since the two partners are very different in some parts, mutual assistance could be an option in order to come closer in the negotiation process. In the case of intellectual property protection in India, technical and financial assistance is a viable option that could lead to fast compliance and speed up the BTIA negotiations. Similarly, the combating of corruption and the improvement of India's procurement process could be handled with assistance of the EU. India can offer European companies better business environments and the EU grants technical and financial support in return. In the same vein, India would benefit if it realized the advantages of a well-functioning procurement framework. This is especially the case, as quality improvements and public savings are indisputably in its own interest.

The EU's efforts are also required with regards to the harmonization of the EU's patent law. As Indian businesses require access to the European market as well, the EU has to send strong signals of their will to provide it. Cooperation could also be the key in the combating of product piracy. Thus, reciprocal arrangements and mutual rapprochement of both parties are promising methods that could lead to a successful completion of the negotiations in the areas of intellectual property rights and government procurement.

7.3 Key Issues Assessment

In Table x I provide an overview of the key issues in the FTA and the level of concessions that both sides are likely to make. This matrix is based on the personal assessment of the factors and considerations outlined above.

Table 15: Key issue areas projected level of agreeability according to impact analysis

Key Issues	India	European Union
IPR		
Government Procurement		
Tariffs		
Movement of labour		

Source: Thesis outcome.

Based on the impact analysis, the case of IPR suggests that India has been complying with its WTO and TRIPS obligations and is determined to continue doing so. The compliance with additional provisions, which would limit or harm Indian production, exports, commodity prices or innovation sector seems unlikely at this point. The EU, on the other hand, seems adamant about its demands in the negotiations. However, ultimately it will have to respect India's position of not going beyond TRIPS.

Government procurement is highly in India's interest in order to improve procurement processes and increase project quality. In the recent years, public private partnerships have proved to be a successful way of handling government projects, especially in the area of infrastructure important. The latter is crucial to India's economic and social development and it requires large investments. In the current five-year plan the Indian government is planning on investing US \$1114.93 billion countrywide in order to improve infrastructure conditions (Embassy of India, Washington DC, 2013). Especially in the lights of the current economic state of India, the recovery of these investments is crucial and makes Indian efforts in procurement improvement more likely. The EU on the other hand, is highly interested in access the Indian procurement market. This interest could be met by providing similar access to competitive Indian firms, as compromises are inevitable.

Since India's opening of its economy in the early 1990s, it has increasingly proved its readiness for tariff reductions and decreased protectionism. According to the World Bank "average non-agricultural tariffs have fallen below 15 per cent, quantitative restrictions on imports have been eliminated, and foreign investments norms have been relaxed for a number of sectors." (World Bank India Foreign Trade Policy 2013). The EU is willing to grant tariff reductions as well – even though the agricultural sector is still highly protected and is likely to remain so for reasons beyond the scope of this paper. The movement of labour between the two parties seems more in the interest of India than of the EU. India has asked for the free movement of skilled labour to the EU, however, the EU remains hesitant (Mukherjee, Goyal 2013: 2)

7.4 SWOT Analysis of BTIA

Table 16: SWOT Analysis

Internal	Strengths Increase in trade volume Diversification of trade Gains from trade Diplomatic relations	Weaknesses Reciprocity Lack of transparency
	Opportunities Knowledge spill-over Technical advancements Scope of agreement FDIs Market access	Threats Rigidity Scope Public information

Source: Thesis outcome

The results that the analysis has yielded are included in the table. It shows that the strengths and opportunities predominate the BTIA, despite threats and weaknesses.

8. Conclusion

“We will need to ensure that we share similar ambitions with our prospective partners at the outset in order to avoid negotiations later stalling because of a mismatch of expectations.” (Global Strategy: 12).

8.1 Conclusion of Thesis

This thesis analysed obstacles in the free trade agreement Broad-based Trade and Investment Agreement (BTIA) negotiations between India and the European Union. Besides the parties' large sizes, the scope of the agreement has proven to be an obstacle to the negotiations. The FTA intends to include multiple areas and to eradicate both tariff and non-tariff barriers. The magnitude of the intended “deep integration” is unprecedented in a bilateral trade agreement and poses a challenge to the involved parties. This is further compounded by the fact that a large number of stakeholders with frequently conflicting interests remain entangled in the treaty negotiations. The European Commission is forced to juggle between the EU's interests and foreign trade policy goals on one hand and the varying interests of EU member states on the other. Achieving agreement between the 28 EU member states without seriously diluting the treaty's goals remains an uphill battle in the negotiations. In much the same way, India is being forced to seek compromise as the country's various trade policy stakeholders work to exert their influence. A tendency for state pushback on federal policy only aggravates the situation further. The fact that India remains very much a developing country with its large number of poor and sizeable domestic challenges only work to complicate decisionmaking. The Ministry of Commerce is conducting a sensitive balancing act of not only negotiating the best possible outcome for the Indian economy, but also assuring the Indian population that the agreement will benefit all.

By providing detailed political and economic profiles, the two parties' negotiation positions have been isolated and put into perspective of their potential gains and losses from the FTA. The question is not whether the FTA will be completed but rather what elements the final agreement will contain. If the two economies want to benefit from the two major gains from trade – an increase in production efficiency and an overall decrease in consumer prices – the

speed and extent to which trade integration occurs is crucial. As the party more vulnerable to trade distortions, India will need thoughtful regulation if it is to achieve a smooth transition.

Ecorys (2009) suggests that the free trade agreement “will bring India and the EU mostly economic benefits (welfare gains, production, international trade, wage increases, productivity increases).“ (Ecorys 2009: 269). According to their economic analysis, the benefits are the largest if the FTA is far-reaching and allows for deep integration. The figures also support this thesis’ outcome regarding short-term versus long-term gains: “India is expected to gain €4.9bn in the short run and €17.7bn in the long run, while the EU is expected to gain €4.4bn in the short run and €1.6bn in the long run. In percentage terms, this amounts to an additional 0.3 per cent growth for the Indian economy in the short run, and 1.6 per cent additional growth in the long run.” (Ecorys 2009: 269).

This aligns with the outcome suggested by this thesis: that the integration of intellectual property right protection and government procurement, in spite of their controversial nature, will eventually benefit both parties. The impacts and spill-over effects are numerous and likely to affect the economic, social, and environmental spheres. It was shown, however, that while India is likely to be affected to a larger extent by the FTA, it will need to implement domestic policies that increase foreign parties’ trust in its economy and foster the growth of Indian businesses. Similarly, the timely rollout of regulations, monitoring, and supervision are crucial. At the same time, the EU has a greater responsibility to make concessions and to bridge gaps in the negotiations. Fairness and flexibility will remain key success factors in the realization of the BTIA, so that the strengths and opportunities illustrated in the SWOT table can be fully utilized.

In some ways, the two parties share common challenges. Both are tackling economic downturns amidst evolving political climates. In India, a potentially transformative general election set for May 2014 is being overshadowed by a significantly weakened currency and growth rates well below their potential. In The EU, the debt crisis lingers on with the 2014 growth forecast recently being revised down to 1.1 per cent (European Commission Press Release 2013c). Consequently, both could use a free-trade induced economic boost.

8.2 Outlook

Geopolitically, the BTIA is of interest to India as it has been left by the wayside of South East Asian economic integration. Political constraints mean that India has few realistic options for economic cooperation with direct neighbours. Enhanced trade with the EU is not an obvious choice but provides great economic opportunities. The EU, on the other hand, is well aware of the opportunities arising from greater access to the large Indian market.

Regarding the question of whether the BTIA can gain momentum and overcome conflicting interests, the literature analysis suggests that a series of mutual concessions could eventually foster a final agreement. That said, it is worth recalling that both India and the EU have alternatives to the BTIA and that they could turn to them if negotiations falter. India could still pursue regional integration, mimicking other South and South East Asia countries, and foster trade relations within the RCEP. Alternatively, India could redirect its focus from Europe to Central Asia, bearing in mind that it already invests heavily in the region and imports fractions of its energy demand from the region (Chaudhury 2013). In conclusion, it remains to be seen if the two negotiating parties make concessions and support the negotiations to reach consensus in the Broad based Trade and Investment Agreement.

9. Appendix

9.1 Abstract

The aim of this paper lies in the thorough analysis of the current negotiations of the India-EU Broad Based Trade and Investment Agreement (BTIA). Hereby it attempts to illustrate various facets of the nature of the negotiation, namely the sectors, which will be included in a deal, the trade-offs each partner will face, and their impacts on the negotiation parties' economic, social and environmental spheres. A crucial aspect to be considered is the negotiating powers of each side and their effects on the outcome. Both economies have been confronted with the consequences of slow business cycles, which shifted priorities towards domestic consolidation. The question at hand is whether India and the EU will both recognize the BTIA as a contribution to their path out of slow growth and therefore whether the BTIA can gain momentum again.

The method that is used is a case-analysis. Using in-depth knowledge of the two partners and their economic circumstances, the pertinent issues are identified. In the next step a theoretical framework is applied and the effects of key issue areas on the treaty is analysed. Moreover, potential solutions are provided and a – merely speculative – comment on the feasibility is given.

The data that I use are administrative reports of the two partners as well as academic articles on the subject as secondary sources assisting the analysis. What is more, publications from international organizations like the WTO and the Asian Development Bank have also provided some insights and perspectives. In the course of my analysis I have identified the following results: intellectual property rights and government procurement were extracted as important issues and the analysis yielded the following rank of important challenges: TRIPS+ compliance of India, IPR enforcement in India; patent law in the EU; data exclusivity, and the mutual problem of piracy for intellectual property as well as corruption, procurement process and pressure on bidders for government procurement. The areas were analysed with regards to their impacts on the negotiation parties' economic, social and environmental spheres. The results exposed monetary effects, particularly on India. In order to ensure positive effects, careful regulation and monitoring will be necessary.

9.2 Zusammenfassung

Das Ziel dieser Arbeit ist die umfassende Analyse der aktuellen Vertragsverhandlungen über den Freihandelsvertrag Broad Based Trade and Investment Agreement (BTIA) zwischen der Europäischen Union und Indien. Dabei versucht sie verschiedene Aspekte der Verhandlungen zu untersuchen. Konkret geht es um die Bereiche, die im Vertrag verankert werden, die Kompromisse, die die Partner eingehen müssen sowie deren potenzielle Einflüsse auf die Wirtschaft, Gesellschaft und Umwelt der zwei Vertragsblöcke.

Ein bedeutender Aspekt ist die Verhandlungsmacht beider Seiten sowie deren Einfluss auf das Ergebnis. Fernerhin werden die Problemthemen identifiziert und aufgrund ihrer Bedeutung bewertet. Außerdem werden potenzielle Lösungen erörtert und eine – wenn auch spekulative – Beurteilung der Erfolgsmöglichkeit dargelegt.

Die verwendete Methode ist eine Fallstudie. Mit Hilfe von fachkundigem Wissen der beiden Partner und deren wirtschaftlichen Voraussetzungen werden die Problemfelder identifiziert. Im nächsten Schritt wird ein theoretischer Ansatz verwendet um die Vertragsverhandlungen und die Effekte der definierten Schlüsselbereiche auf den Freihandelsvertrag zu analysieren.

Diese Forschungsarbeit gründet sich zum einen auf offizielle Berichte und Stellungnahmen der beiden Verhandlungspartner sowie auf akademische Beiträge zu diesem Thema. Darüber hinaus werden Publikationen von internationalen Organisationen wie der WTO oder der Asiatischen Entwicklungsbank zu Hilfe gezogen. Im Zuge meiner Analyse stieß ich auf folgende Ergebnisse: Ich habe den Bereich der geistigen Eigentumsrechte sowie der öffentlichen Auftragsvergabe als Kernbereiche der vertieften Handelsintegration definiert und die Analyse erbrachte, dass folgende Herausforderungen in den Verhandlungen zentral sind: TRIPS+ Einhaltung seitens Indiens; die Durchsetzung geistiger Eigentumsrechte in Indien; das Patentrecht in der EU; Datenexklusivität und das gemeinsame Problem des Datendiebstahls. Im Bereich der Auftragsvergabe nannte die Analyse insbesondere Korruption, das Vergabeprozedere und Druckmittel auf Unternehmer. Diese Kernherausforderungen wurden im Anschluss auf ihre Effekte auf Wirtschaft, Gesellschaft und Umwelt beider Partner analysiert. Es stellte sich heraus, dass die monetären Effekte auf Indien überwiegen und diese vorsichtiger Regulierung bedürfen.

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Vorsitzende Debattierclub und Consultant **September 2011-August 2012**
- Planung und Durchführung der „Meisterschaft im Deutschsprachigen Debattieren 2012“ in Wien mit 220 internationale Gästen
- Erstellung der Marketingstrategie sowie Zusammenstellung des 40-köpfigen Teams
- Planung und Moderation von 70+ Debatten, Podiumsdiskussionen und Konferenzen zu Wirtschaft und Politik
- India Vision Foundation, Kiran Bedi** **Neu Delhi, Indien**
Praktikantin **Februar 2010**
- Mitarbeit an dem Projekt „Safer India“: Erstellung von Strategien zur Verbesserung der Zusammenarbeit zwischen Exekutive und BürgerInnen
- Evaluierung des Projekterfolgs und Erstellung eines Maßnahmenkatalogs für Sponsorenakquisition
- Verein Personenkomitee „Gerechtigkeit für die Opfer der NS-Militärjustiz“; Praktikantin** **Wien, Österreich**
Juli 2009-Oktober 2009
- Recherchetätigkeit in historischen Archiven für die Rehabilitation der Opfer der nationalsozialistischen Militärjustiz
- Mitgestaltung der Ausstellung „Was damals Recht war...“ – Soldaten und Zivilisten vor Gerichten der Wehrmacht

AUSSERCURRICULARES ENGAGEMENT (AUSZUG) UND WEITERE INFORMATIONEN

Peer Mentorin für Studenten an SAIS, Washington, DC

Gastautorin in der SAIS Wochenzeitung "SAIS Observer"

Vizepräsidentin, Initiativgruppe Wien Alpbach: Organisation diverser Podiumsdiskussionen

Tutorin und Mentorin, Universität Wien: Begleitung von StudentInnen durch das erste Studiensemester

Gründungsmitglied des Model United Nations Club Wien: Mitbegründung des Clubs; Organisation, Vorsitz und Teilnahme an mehreren Verhandlungssimulationen

Sprachkenntnisse: Deutsch, Punjabi (Muttersprachen), Englisch (Muttersprachenniveau), Hindi, Urdu (exzellent), Französisch (gut), Niederländisch (Grundkenntnisse)

Interessen: Rhetorik, Laufen (Halbmarathon und Leitung einer Laufgruppe), Tanzen (Tanzclub SAIS Bologna)

Auszeichnungen: Stipendium der Stadt Wien; Stipendium der Universität Wien; Österreichische Debattiermeisterin 2011; Beste Rednerin des „Redewettbewerb Alpbach 2011“; Stipendium der Stiftung Zukunft Berlin



Rupinder Kaur Rai,
Wien/Washington, DC, Dezember 2013

9.5 Eidesstattliche Erklärung (Deutsch)

Ich erkläre hiermit eidesstattlich, dass ich die Arbeit selbständig angefertigt, keine anderen als die angegebenen Hilfsmittel benutzt und alle aus ungedruckten Quellen, gedruckter Literatur oder aus dem Internet im Wortlaut oder im wesentlichen Inhalt übernommenen Formulierungen und Konzepte gemäß den Richtlinien wissenschaftlicher Arbeiten zitiert, gekennzeichnet bzw. mit genauer Quellenangabe kenntlich gemacht habe.

Die Diplomarbeit wurde bisher weder publiziert noch einer anderen Prüfungsbehörde vorgelegt.

Rupinder Kaur Rai

Wien/Washington DC, Dezember 2013