

Commonwealth Trade Case Studies: India

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Summary

- India is an extremely large and diverse market – this creates both opportunities and challenges for potential exporters
- India is a high-growth market, but is also marked by poverty. At present there is a limited market for the high-value exports that the UK specialises in
- The Indian market has extremely high tariff and non-tariff barriers, which are particularly severe in some of the markets that West Midlands manufacturers specialise in (e.g. automotive)
- Scope to reduce tariffs may be limited by entrenched domestic interests and political lobbying
- Infrastructure is poor and patchy, increasing both market fragmentation and distribution costs
- Corruption, uncertainty around the application of rules (including tariffs and import rules) and ad-hoc changes (often by official administrative fiat) may make India an extremely challenging market for many British firms

Overview

As the most populous country in the Commonwealth and one of the largest economies in the world, India is a natural target for enhanced trade and economic links post-Brexit. One of the arguments put forth in favour of Brexit is that the UK should seek to decouple from a “moribund” European economy (often characterised as suffering from “eurosclerosis”). Having done so, the UK would allegedly be freer to engage with the dynamic and rapidly growing economies of Asia. The example of India suggests that this vision may be more challenging to execute than has been envisioned.

There is enormous scope for tariff reduction were a free trade agreement (FTA) between the UK and India to be signed. One example of this are the real prospects for enhanced exports of whisky to India. At present, whisky is subject to applied duty of 150%, which is likely to be an area of contention during any negotiationsⁱ. Scotch accounts for some 22% of all British exports of food & beveragesⁱⁱ and as India is by some measures the world’s largest whisky market, the potential stakes for the food & drink industry are significant.

Nevertheless, given that food & drink combined accounted for only 6% of British goods exports in 2016 (and in the region of 3.4% of total British exports), this impact ought not to be overstated. One of the difficulties in establishing a free trade agreement with India is that tariffs are often used for domestic political purposes. For example, in April 2008 India substantially reduced import duties for a number of agricultural products in an effort to reduce inflation. Tariffs on many of these were subsequently raised again. There are powerful entrenched domestic political interests that would be disadvantaged by any reduction in tariffs and it may be difficult to negotiate a settlement, particularly given that any FTA would have to cover “substantially all” of the trade between the UK and India in order not to fall foul of WTO rulesⁱⁱⁱ.

An outline of India's present tariff regime

India is a comparatively closed market relative to European standards and there are numerous challenges to doing business and exporting. In its guidance to exporters, the UK Department of International trade notes that import duties and additional taxes are “likely to be a minimum of 35%”^{iv}. India's system of tariffs and fees is both complex and relatively opaque. In general, it consists of customs duty, an “additional” or “countervailing” duty, a “special additional duty” and an education assessment.

Of these, additional duty is applicable to all imports except alcoholic beverages. The special additional duty is a 4% surcharge (levied ad valorem) and applies to all imports, except those explicitly exempted via an official customs notification. Finally, the education assessment is a further 3% surcharge on the post-duty price, and is applicable to most imports (once again, except those officially exempted). Further to this, there is a landing fee of 1% included in the valuation of all imported products except those exempted through special notification.^v

In addition to its complexity, the Indian tariff system is characterised by uncertainty, ad hoc alterations and changes by administrative fiat. In part, this is due to the large disparity between the theoretical maximum that it can apply, under its commitments to the WTO (its “bound” rates) and the rates that it currently applies (the MFN applied rates). As a result of this, India is able to increase tariffs (up to their bound maximum), or reduce them with minimal notice, leaving exporters uncertain as to the tariff rates their goods will face. India's average “bound” tariff rate is currently 48.5%, whilst its average MFN applied rate was 13.4% in 2016, according to the WTO. Some 25% of all goods are not covered by WTO binding, leaving India free to levy tariffs as it sees fit.

India maintains a “negative list” of goods subject to additional non-tariff barriers. These include items that require an import license (notably livestock & a number of chemicals). Other goods can only be imported by the government or certain monopoly providers (some pharmaceuticals fall into this category) and are typically subject to approval by the government in both timing and quantity. Once again, this system is largely opaque. Import of used or refurbished items are typically restricted still further (sometimes with additional tariffs, as in the case of motor vehicles, and sometimes by outright prohibition.

India requires import license for all remanufactured goods at the present time. This is often burdensome for businesses with delays in processing licenses and quantity limitations on certain parts being particular problems^{vi}. Even the largest companies at times fall foul of licensing restrictions, with Apple being refused permission to import used iPhones into the Indian market^{vii}.

An example: tariff and non-tariff barriers to automotive imports

Of particular interest for the West Midlands region, India's present MFN applied rate for motor cars is 60% and is currently an unbound industry. India further operates a number of duty exemption regimes for imports. These are opaque in nature and eligibility is typically subject to a number of conditions (often including an obligation to export from India).

India's automotive lobby, the Society of Indian Automotive Manufacturers, is vociferously opposed to reducing tariffs on motor cars, commercial vehicles and many component parts. In 2015, it commented on the prospect of a free trade agreement with the EU, stating, “FTAs with competing countries do not benefit Indian automobile industry”, arguing that “it is against the concept of 'Make

in India' for local value addition and local employment"^{viii}. As of today, diesel buses, motor cars (petrol and diesel), trucks, two wheelers and engines (petrol and diesel) are all on the list of items that SIAM seeks to exclude from FTAs^{ix}.

In addition to this, India maintains substantial non-tariff barriers on the import of motor vehicles. In particular, they can only be imported direct from the country of manufacture (thus preventing the storage or warehousing of cars en-route). Moreover, new vehicles can only be imported through 3 ports, namely Chennai, Calcutta and Nhava Sheva in Mumbai. The restrictions on importing used vehicles are yet more stringent and apply to any vehicle that has been sold, leased or loaned prior to importation into India or has been registered (for use) in any country prior to being imported. This is true irrespective of whether the vehicle has actually been used. The vehicle must be 3 years old or less. In this case, two testing certificates are required (issued by a testing agency), one confirming that at the point of export, the vehicle complies with all Indian regulations and the second confirming that it conforms to its original homologation certificate.

On arrival at port, it must be submitted for testing by the appropriate agency in order to be granted a certificate from said agency confirming compliance with Indian Motor Vehicles Act (1988) and subsequent legislation. Moreover, used vehicles can only be imported through the port at Mumbai. All used vehicles that are imported must have a minimum roadworthiness period of 5 years and this needs appropriate certification^x.

General Barriers to Trade

The most recent Trade and Investment Barriers Report^{xi} found that India (alongside China and Brazil) had the second highest number of barriers to trade of countries surveyed (split almost evenly between barriers at the border and those 'behind the border'). Moreover, India has put the second highest number of new barriers in place over the past year (behind Russia), suggesting that trade distorting measures continue to be an active policy tool for the Indian government and bureaucracy. Of particular interest given the difficulties faced by Britain's steel sector in 2015 and 2016 is the imposition of minimum import pricing for steel products (measures extended in late 2016). Mandatory certification (by the Bureau of Indian Standards) of steel products was also extended in scope last year.

Medical devices (such as scanners etc.) are regulated as drugs in the Indian market. One result of this is that remanufactured equipment is completely prohibited. Similarly, "landing charges" are imposed for textile imports (in addition to a 60% tariff) and the regulations regarding alcoholic beverages differ substantially from international standards (thus increasing costs for those seeking to export to the Indian market, in addition to an extremely burdensome tariff regime). The Trade and Investment Barriers Report also finds significant and substantial regulation on imported telecommunications equipment (which are not applicable to domestic producers). Tellingly, the admission that FTA negotiations with India have come to an impasse is explained by "a mismatch of the level of ambitions"^{xii}.

India ranks 130th on the World Bank's "Ease of doing business" rankings^{xiii}, similar to Nicaragua, Tajikistan and Cambodia. Whilst India ranks relatively highly for its protection of minority investors, getting electricity and ease of gaining credit, it presents particular problems for companies that need to deal with construction permits, pay taxes or enforce contracts. India also ranks 143rd out of 190 countries for trading across borders.

Further barriers within the Indian market that are likely to constrain the growth of British exports there in the future include its fragmented nature. India is a patchwork of 36 state and union territories with considerable autonomy as regards a wide variety of important matters (including transport, transfer of non-agricultural land, contracts, bankruptcy, economic planning, labour welfare, stamp duties and many others). Although English is widely used in officialdom, the official language also varies by state. States additionally vary enormously in size from Sikkim with a population of less than 1 million to Uttar Pradesh with a population of around 200 million. Exporters will want to concentrate their focus on a certain number of selected markets.

In its own advice for exporters, the British government notes that “[c]orruption is well entrenched in India and pervades many aspects of daily life”^{xiv}. This poses a significant barrier to trade and doing business. As government advice notes, “[p]oliticians, bureaucrats and law enforcement officials often wield significant discretionary power and notable abuses have been brought to light.” Particular problems include judicial and police corruption, with payments frequently changing hands in order to influence court decisions. This is compounded by corruption in terms of land administration and customs. Businesses find corruption at the border (in addition to burdensome import procedures) to be amongst the biggest obstacles to importing into the Indian market.

India’s infrastructure is extremely poor, most notably with regard to transportation. As a result, importing is often more difficult and costly than many businesses are used to in more developed markets. The fragmented legal and administrative landscape also means that transport within India can vary substantially in terms of its efficacy and as a result, local target markets need to be chosen with considerable care.

India also imposes numerous restrictions on ownership with, for example, limitations on capital investment for both foreign companies and their domestic partners. Similarly, direct investment in the banking sector is subject to heavy restrictions and the state owns a large majority of both banking assets and branches. Restrictions also exist on foreign accounting firms and lawyers. Telecoms and retail further face tremendous barriers to trade and investment. Investment and some services-related trade face another obstacle (although one that is less acute for manufacturers seeking to export to India), namely poor protection of intellectual property.

The US government notes that “India remains one of the world’s most challenging major economies with respect to protection and enforcement of IP”. In common with problems pertaining to bribery and corruption, lax (or non-existent) enforcement is a problem even when the overarching legal framework is in place. Further issues surround the interpretation and application of patent law. India has no statutory protection of trade secrets. Some action is now beginning to be taken at a state level, although the scope and extent of this remains unclear at the present time.

ⁱ Ryan, C. ‘Cheaper whisky takes the edge off Brexit’ *Bloomberg*, [online] 3rd August 2017, Available at: <https://www.bloomberg.com/news/articles/2017-08-03/u-k-sees-lower-tariffs-on-whisky-as-path-to-brexit-trade-deals> [Accessed on 5th October 2017]

ⁱⁱ HMRC, 2017, ‘UK Overseas Trade Statistics: June 2017’, *UK overseas trade statistics and regional trade statistics*, [online]. Available at: <https://www.uktradeinfo.com/Statistics/BuildYourOwnTables/Pages/Home.aspx> [Accessed on 5th October 2017]

ⁱⁱⁱ General Agreement on Tariffs and Trade, Oct. 30 1947, 61 Stat. pt. 5 T.I.A.S. 1700 55 U.N.T.S. 194

- ^{iv} Department for International Trade 'A guide for British businesses interested in selling goods and services in India.' *Exporting country guides*, [online], 12th November 2016, Available at: <https://www.gov.uk/guidance/exporting-to-india> [Accessed on 5th October 2017]
- ^v <https://ustr.gov/sites/default/files/2013%20NTE%20India%20Final.pdf> ???
- ^{vi} <https://ustr.gov/sites/default/files/2013%20NTE%20India%20Final.pdf> ???
- ^{vii} T. Worstall, 'India's Very Strange Ban On Apple's Used Phones', *Forbes*, [online] 5th April 2016, Available at: <https://www.forbes.com/sites/timworstall/2016/04/05/indias-very-strange-ban-on-apples-used-phones/#7b89a8c57a22> [Accessed on 5th October 2017]
- ^{viii} The Economic Times, 'Auto sector inclusion in India-EU FTA against 'Make in India'', *India Times*, [online] 13th April 2015, Available at: <http://economictimes.indiatimes.com/industry/auto/auto-sector-inclusion-in-india-eu-fta-against-make-in-india/articleshow/46906368.cms> [Accessed on 5th October 2017]
- ^{ix} Society of Indian Automobile Manufacturers, 'SIAM Sensitive Items List for FTAs/PTAs at 6 Digit Classification: To Be Put in Negative List', [online], Available at: <http://www.siamindia.com/cpage.aspx?mpgid=16&pgid1=26&pgidtrail=73> [Accessed on 5th October 2017]
- ^x NOTIFICATION NO. 4(RE-2001)/1997-2002, (Issued by the Government of India, Ministry of Commerce & Industry, [online], Available at: <http://dgft.gov.in/exim/2000/not/not01%5Cnot0400.htm> [Accessed on 5th October 2017]
- ^{xi} European Commission, *Report from the Commission to the European Parliament and the Council on Trade and Investment Barriers, 1 January – 31 December 2016*, [online], Available at: http://trade.ec.europa.eu/doclib/docs/2017/june/tradoc_155642.pdf [Accessed on 9th October 2017]
- ^{xii} *Ibid.*, p. 16
- ^{xiii} The World Bank, *Ease of Doing Business Rank*, [online], June 2016, Available at: <http://www.doingbusiness.org/rankings> [Accessed on 9th October 2017]
- ^{xiv} Department for International Trade, 'Overseas Business Risk – India' [online] (Updated 4th August 2017), Available at: <https://www.gov.uk/government/publications/overseas-business-risk-india/overseas-business-risk-india> [Accessed on 9th October 2017]