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ASEAN-India Free Trade Agreement and India's Trade Competitiveness: An Assessment

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As a part of the strategic and economic plan looking for new business opportunities and encouraging investment environment throughout the world, the countries are pursuing regional economic cooperation which focuses on the arrangement for preferential trade among the members. India is also in aggressive pursuance of this type of trade integration which resulted into a number of bilateral and multilateral agreement with the member countries of the Asian region.

During last two decades, the stalemate in multilateral trade negotiations under the framework of World Trade Organisation (WTO) regime has provided impetus to the establishment of regional trade blocks all over the world. The economic reasons behind these trade agreements are to allow the regional members the benefit from economic cooperation and comparative advantages of trade and make them less dependent on necessary imports from more distant countries. It generates sufficient economic activity, improve efficiency, heighten competition, attract investments, and thus create jobs in the trade area. More over they are expected to maintain peace and stability in the region.

We may have different forms of regional integration, classifying them by a rising degree of intensity. They mainly include Preferential Trade Agreement (PTA), Free Trade Area (FTA), Customs Union (CU), Common market (CU) and

Economic and Monetary Union (EMU). When PTA is formed with the reduction of custom duties (mainly tariffs) on trade among members relative to those on trade with non-members, FTA eliminates tariffs and quotas on the trade among member countries. CU, which goes a step further than the FTA as in addition to free trade within the union; there is a common external tariff (CET) against non-members. While CM is a Customs Union that allows for the free movement of factors of production among member countries, EMU the extreme form of integration where we can perceive a common market in which there is a single currency and monetary policy, and in which major economic policies (particularly fiscal policy) are coordinated or harmonised. Often, there is a compensation policy, which involves transfer of income to poorer or disadvantaged members of the Union.

Reflecting the diversity of economies and their histories, regional integration follows distinctly different patterns across the world. Europe has a long history of regional integration, underpinned by a strong institutional framework. By contributing more than 20 per cent of world GDP 27 member country group European Union proved the most successful integration of this world. It could make dominance over US in the many of the international trade and financial matters. North America has chosen a free trade area arrangement 'NAFTA' between USA, Canada and Mexico that does not foresee the creation of supranational institutions. The agreement brought in painful economic restructuring and unemployment to relatively weak member 'Mexico.' In Latin America, MERCOSUR's initial objectives of a common market and coordinated economic policies have suffered setbacks caused by financial turbulence in the region in the late 1990s, and the grouping is yet to recover momentum. In Asia, trade integration has progressed at a rapid pace based on the exploitation of intra-regional comparative advantages.

Regional Economic Integration in Asia

East and south Asia are home to breathtaking economic diversity. At one end of the spectrum are the advanced economies of Japan, South Korea, Taiwan, Hong Kong and Singapore and on the other end least-developed economies such as Nepal, Bangladesh, Cambodia, Laos and Myanmar. Low-income, but fast developing countries from the region, especially China and India are also going ahead with strategic alliances with their trade partners such as Sri Lanka, Indonesia, Philippines, Thailand, and Malaysia. Huge differences in politics, institutions and historical legacies overstress the diversity. Hence it is not surprising that Asian economic integration, even in "globalising Asia is rather weak. (*Emerging Asian Regionalism,* Asian Development Bank, 2009, pp. 10-12.). Major regional integration agreements entered between the countries in the Asian region include Association of South East Asian Nations (ASEAN), South Asian Free Trade Agreement (SAFTA), Asia Pacific Economic Community (APEC), etc.

ASEAN India Free Trade Agreement (AIFTA)

As a part of its liberal and genial approach to East Asia India has started to make strategic trade integrations with countries of South East Asia. In August 2009, India has entered Free Trade Agreement, ASEAN India Free Trade Agreement (AIFTA) for goods with the ten member association of south East Asian nations. This agreement takes a number of measures to improve trade flow between the regions and to share each country's strategic advantage with others. The success stories of many of the regional integrations of the world such as European Union reveals that trade competitiveness of the member countries of the trade block shall bring them synergy in promotion of both inter regional and intra regional trade. There are apprehensions that ASEAN countries are more competitive in sectors like agriculture, textiles, auto components and electronics and India will face negative consequences by the agreement. More over there is a general view that India's unsatisfactory export performance can be attributed to low export competitiveness. At this juncture it is imperative to analyse the trade competitiveness of India thereby one can make out whether India could be really benefitted by this agreement?

Measures of Trade Competitiveness

Competitiveness may be defined as gain in price, quality, product design, reliability, salesmanship etc. In our paper we have given thrust only on price competitiveness. This is because non price competitive factors are intangible and so difficult to measure without rigid assumptions. More over by measuring the price competitiveness one can indirectly identify the country's strategic control in supply of resources, capacity to bring cost efficient production and ability to maintain quality thereby reliability in their products in international market. This ultimately leads to the competitiveness of the producer in non price terms also.

For the purpose of the study we have computed the following indices:

1. REP (Relative Export Price Index): The ratio of the unit value index of Indian exports to a weighted average of unit price of exports of its competitors. REP index below unity indicates higher competitiveness of exports of India compared to its competitors.
2. RWPI (Relative Wholesale Price Index): India's whole sale price index divided by a weighted average of the indices of its competitor's whole sale prices, which is a practical proxy for domestic costs. A relative WPI of India below unity shows its competitiveness in the domestic cost of export production.
3. PEI (The profitability of Exports Index): It is the ratio of India's export unit value to its whole sale price index. The assumption behind this measure is that higher export prices relative to whole sale prices means that producers are more likely to export rather than sell in the domestic market. But the time gap between the production and the export sale is much longer than lag between the production and domestic sale. This definitely poses a problem in determining the validity of this index. A PEI of above 1 indicates higher profitability and below 1 indicates lower profitability.
4. RPE (The Relative Profitability of Exports Index): This is the ratio of profitability index of India to weighted profitability index of her competitors. RPE value of more than unity indicates India's export profitability is better than its competitor's profitability.

5. IPC (The Index of Import Price Competitiveness). India's WPI divided by its unit value index of imports. This is a measure of competitiveness of import substitutes for domestic products. An index of IPC below 1 indicates greater competitiveness of imports and above 1 indicates lower competitiveness.

For constructing the index of relative export prices, we have used the unit value index of overall exports of India. In this paper we have taken ASEAN 5 countries – Singapore, Malaysia, Indonesia, Thailand and Philippines as major competitors of India in world market.

The weight given to each competitor of India for averaging purposes is calculated based on the following formulae:

$$\frac{W_j = \sum X_{ix} \sum Y_j}{jk}$$

Where W_j is the weight of the j^{th} country; X_i is the export share of India to the world exports; Y_j is the export share of competitor to world exports. The weight given to each competitor reflects the relative importance of that country in India's overseas markets weighted by the importance of that market to India. This paper used last 8 years trade data available from the database of International Financial Statistics maintained by International Monetary Fund.

Table 7.1 gives a bird eye view of the economic performance of India and major five ASEAN countries. In terms of GDP India's economic growth is far ahead of its competitors. Our GDP was grown from 3.89 per cent in 2001 to 9.82 per cent in 2006. None of its competitors from the ASEAN region was able to achieve such amasing growth with in this short span of time. When three countries among the group (Malaysia, Singapore and Thailand) received negative growth in 2009, the growth rate of Philippines was nominal only. Indonesia is the only one country in the region which could relatively consolidate its position even in the facet of global melt down. Economic performance of India too, was badly affected by the crisis, but at a scale which is much lesser than that of its competitors.

Table 7.1: GDP Growth (per cent) of India and Competitors—a Comparison

Year	India	Indonesia	Malaysia	Philippines	Singapore	Thailand
2001	3.89	3.64	0.52	1.76	-2.37	2.17
2002	4.56	4.50	5.39	4.45	4.11	5.32
2003	6.85	4.78	5.79	4.93	3.77	7.14
2004	7.90	5.03	6.78	6.38	9.30	6.34
2005	9.21	5.69	5.33	4.95	7.31	4.61
2006	9.82	5.50	5.85	5.34	8.35	5.23
2007	9.37	6.28	6.18	7.08	7.77	4.93
2008	7.35	6.06	4.63	3.84	1.15	2.59
2009	5.36	3.99	-3.63	0.99	-3.33	-3.46

Source: IMF Financial data series.

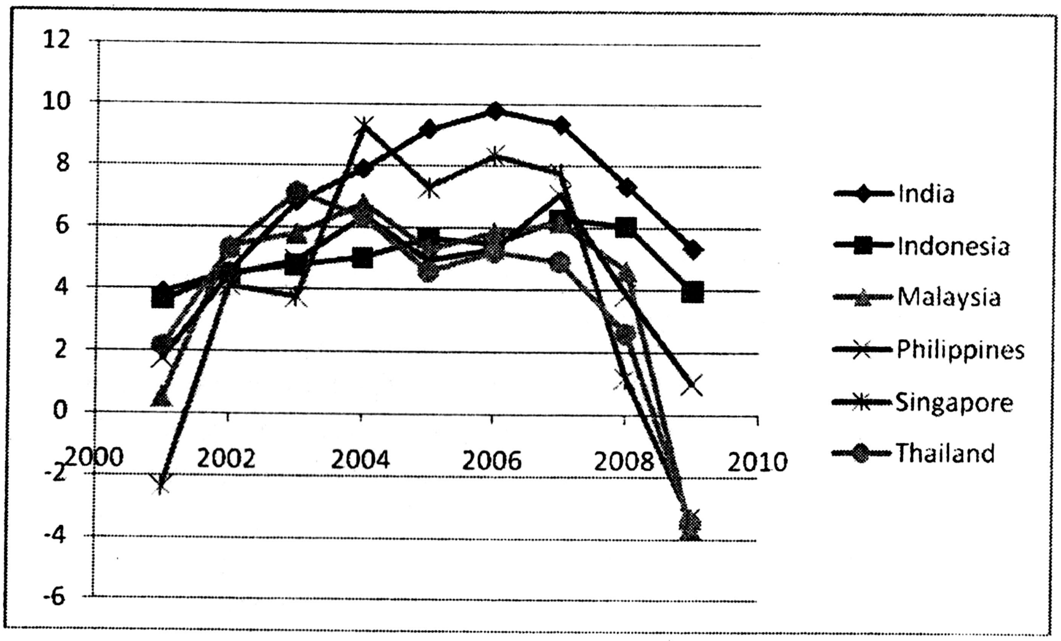

Figure 7.1: GDP Growth Rate of Selected Countries

However our economy has expanded by an average of 8 per cent between 2003-04 and 2008-09. This figure can be taken as a measure for judging the strength of India even during the financial tsunami shattered days of the global economy.

Table 7.2: Export Performance of India and its Competitors (in USD Millions)

Year	India	Indonesia	Malaysia	Philippines	Singapore	Thailand
2001	43361.1	57360	88005.3	32664.3	121751	64918.8
2002	50372	59164	93265	36501.9	125177	68108.2
2003	58962.9	64107	99369	36229.2	144181	80323.6
2004	76648.6	70767	125744	39680.4	198637	96248.2
2005	99619.6	86996	140870	39879.3	229649	110178
2006	120861	103486	160573	47415.8	271807	130803
2007	145393	118728	176025	50270.2	299272	153100
2008	175513	147640	209673	49025.3	338202	172857

Source: IMF Financial data series.

Table 7.2 explains the trends in export earnings of India and its ASEAN major competitors the value of India's exports rose from 43361.1 millions (in dollar terms) to 175513 millions during the last 8 years. Initially all ASEAN countries except Philippines had higher export earnings than India. But later years it could surprisingly perk up its earnings from overseas market and was able to keep its position in third place behind Singapore and Malaysia. Such incremental growth in its earnings from global market can be attributed to the surge in service exports, especially export of softwares and electronics.

Table 7.3: Imports of India and its Competitors (in USD Millions)

Year	India	Indonesia	Malaysia	Philippines	Singapore	Thailand
2001	50392.3	37534	73866.1	34920.9	116000	61959.9
2002	56516.8	38340	79869.1	37179.9	116448	64645.3
2003	72557.7	42244	81948	39501.9	127939	75824.3
2004	99775.4	54877	105298	42344.6	163854	94409.8
2005	142842	75533	114411	46963.8	200047	118158
2006	175242	80333	131080	54081.1	238710	128723
2007	215241	93088	146773	57707.7	263155	140795
2008	276944	129767	164410	N.A.	319780	178771

Source: IMF Financial data series.

India is the largest importer following Singapore among the selected south East Asian nations over the study period. In 2001 it was in 4th position in imports after Singapore, Malaysia and Thailand. But by the end of 2008 its import payment increased about 5 times of its payments during initial years and such a trend could not be perceived in the import trade of any other countries in the group.

During the initial years India's export share in the world export was lower than its competitors (Table 7.4). Only Philippines was exception to this at that time. However, India could consolidate its position later years and surpassed Thailand and Indonesia in terms of its contribution to world exports. On an average 1 per cent of total world export is constituted by export from India. One remarkable point to be noticed here is that when trend in share of world exports by all the competitors from the region exhibited volatility, India could expand its share significantly year after years.

Table 7.4: Share of India and its Competitors in World Exports (per cent)

Year	India	Indonesia	Malaysia	Philippines	Singapore	Thailand
2001	0.71	0.94	1.44	0.53	1.99	1.06
2002	0.78	0.92	1.45	0.57	1.95	1.06
2003	0.79	0.86	1.33	0.48	1.93	1.07
2004	0.84	0.78	1.38	0.43	2.18	1.05
2005	0.95	0.83	1.35	0.38	2.20	1.06
2006	1.00	0.85	1.33	0.39	2.24	1.08
2007	1.05	0.86	1.28	0.36	2.17	1.11
2008	1.11	0.94	1.33	0.31	2.14	1.10

Source: IMF Financial data series.

In terms of share of imports India occupy the second position in the region after Singapore. On an average 1.2 per cent of the world exports is routed through this country. In parity with the growth in share of world exports, India's share in world imports is also increasing year by year. (See Table 7.5)

Table 7.5: Share of India and its Competitors in World Imports (per cent)

Year	India	Indonesia	Malaysia	Philippines	Singapore	Thailand
2001	0.79	0.59	1.16	0.55	1.83	0.98
2002	0.86	0.58	1.21	0.56	1.77	0.98
2003	0.95	0.55	1.07	0.51	1.67	0.99
2004	1.06	0.59	1.12	0.45	1.75	1.01
2005	1.34	0.71	1.07	0.44	1.88	1.11
2006	1.43	0.66	1.07	0.44	1.95%	1.05
2007	1.53	0.66	1.04	0.41	1.87	1.00
2008	1.70	0.80	1.01	N.A	1.97	1.10

Source: IMF Financial data series.

Compiled from International Financial Statistics Published by IMF

Values of indices used for measuring the trade competitiveness of India is explained in Table 7.6. Indices were computed only for the first 5 years of observation (i.e.. 2001 to 2005) as the required data were not readily available for the rest of the period. REP of India during the study period found greater than unity which indicates lower competitiveness of Indian exports compared to that of its competitors. However the value of relative WPI of India obtained less than unity which shows that India is more competitive than its competitors in terms of cost of production of goods exported. A sizable portion of our exports constitute IT exports. As India is abundant with human capital possessing high level knowledge and expertise in development and application of Information Technology, the cost of production of this service component is much cheaper than the production cost of any other product. Due to this India gain competitiveness in cost of production of exports relative to its competitors. But the benefit of this cost efficiency could not be fully capitalised by the country and Indian exports remained less profitable till 2005 as the values of its PEI were less than unity until the year. Never the less India's export profitability compared to its competitors in the region has considerably improved later years of the study as revealed by the trend in index values of REPI. India's import was found competitive only in 2004 since its IPC values were above unity in all other years of the study.

Table 7.6: Trade Competitiveness of India-Indices

Year	REP	PEI	IPC	REPI	RWPI
2001	1.21	0.9	108.71	1.38	0.97
2002	1.20	0.85	103.69	1.33	0.97
2003	1.33	0.92	104.93	1.70	0.97
2004	1.45	0.96	89.43	1.77	0.95
2005	1.67	1.03	102.07	2.05	0.90

Concluding Remarks

Even though the absolute value of India's exports and also its share in world exports is increasing year by year the competitiveness of Indian exports is yet to improve. Infact we are competitive in terms of domestic cost of production, still our export is less profitable. However there is significant improvement in India's export profitability compared to its competitors which signals the fruitfulness of the measures taken by the Government in promotion of trade and investment in the country. But when we look in to the possible impact of AIFTA on Indian economy and also on its trade regime we cannot expect the same scale of benefits from it. This is because one of our principal exports is Information Technology (IT) or IT enabled services for which we are mostly depending on the U.S and European market. At present the contribution of ASEAN countries in India's software exports is insignificant. So what growth we have received in our foreign earnings during the last few years is extensively attributed to the export of this service component. More over about 57 per cent of India's GDP was constituted by service sector in 2009. So through this agreement we cannot expect any positive impact on service sector without finalising the liberalisation of trade in services between India and ASEAN, which is presently outside the scope of AIFTA. Similarity in natural vegetation and aquatic conditions between India and ASEAN region the free trade agreement shall carry far reaching effect on both agriculture sector (especially plantation sectors) and marine sectors of the country. ASEAN countries like Malaysia and Indonesia where agriculture productivity is relatively high which makes them leading producers of certain agricultural crops such as rubber, tea, coffee, spices etc. Under this agreement India shall force to import these agriculture produce which shall negatively affect the poor farmers of the country. Cheaper imports of marine products may bring the sea food industry in more vulnerable conditions. Moreover, when the countries binding by this agreement is advanced in to more degree of integration such as common market or customs union India shall be forced to follow common trade policy towards the non members of the trade block. Then this will place India at the risk of losing its overseas market also as the competitors from the region can dictate the trade terms now due to their strategic position which they command in the region.

No doubt, trade liberalisation which is based on inter sectoral trade leads to winners and losers. There should be transition of wealth from gainers to losers in order to reach the distinct object of overall welfare of the region. Here the role of the Government is more important than anything else. Ultimate gain of the trade agreement is critically decided by the ability and bargaining power of the government to adopt measures and policies for easing the lumber shifted on the shoulders of the weaker segments. Thus we can conclude that the strategic position that a country command in the trade block is the crucial factor deciding the scope and pattern of benefits it can pick through the integration.

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