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Policy Perspective

India's curious stand at the WTO

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Summary

India refused to sign the Trade Facilitation Agreement (TFA) at the World Trade Organisation's (WTO) General Council meeting in Geneva on 31 July 2014. Since the WTO works through consensus, the meeting collapsed without any agreement. India's stand was harshly criticised across the world.

Global disapproval of India's action was heightened especially because the TFA was a part of the Bali Declaration, to which India is a signatory. The Bali Declaration of December 2013 was the first agreement reached as part of the 12-year-long Doha Round of trade negotiations.

However, **only the TFA was picked** out from the original Doha package while all the other components of the 'Doha Development Agenda'—such as agriculture, cotton trade, and market access for agricultural products, among other issues—were deferred.

Also on the back-burner was a decision on how much public stockpiling of food grains (considered by the WTO as a trade-distorting measure) will be allowed to developing countries such as India for meeting their food security requirements. Called the 'Peace Clause', it essentially insulates countries from being challenged till a permanent solution is found by 2017. However, analysts writing on the Bali outcome claimed that the U.S. Trade Representative at the Bali ministerial insisted on adding riders in exchange for agreeing to the clause.

After Bali, the **'Peace Clause' promise was soon forgotten.** Most of the WTO meetings prior to July were focused on expediting the TFA, without paying much attention to seeking a permanent solution to agricultural and other pending issues. Even WTO's printed work programme was loaded in favour of the TFA. Commerce Minister Nirmala Sitharaman's statement to Parliament confirms this. It led India to believe that developed countries were only interested in getting the TFA signed, and subsequently they were likely to abandon the Doha Round.

India insisted that it was not opposed to the TFA *per se*, but wanted WTO members to also keep their promise of discussing a permanent solution to food security issues. In fact, India has already implemented many of the TFA's requirements.

India is also insisting that the WTO must change its method of calculating government support to farmers. The WTO is using the average global food grain prices of the 1986-88 period as the external price benchmark. India's contention is that prices have risen seven-fold since then. And during 1986-88, the U.S. and Europe were dumping food grains on the world market, leading to a fall in the price of rice and wheat. This makes the **benchmark doubly suspect.**

India is also contending that the entire system of food procurement through the payment of a minimum support price to farmers is focused on the domestic market and, therefore, cannot be considered as "trade distorting."

Finally, New Delhi found itself isolated at Geneva with even traditional supporters among developing and poor countries crossing the floor on the TFA. **India will have to introspect on the proximate causes for this isolation,** including a review of its communication policy. It is likely that the country was overly focusing on food stockpiling at the expense of other development issues, giving its allies reason to feel that it too was interested in a single-point agenda.

India will have to adapt a **three-point strategy** to not only counter the global tide of bad publicity but also as a bargaining chip for allowing the TFA. **One,** improve the training schedule of its trade negotiators. **Two,** push for a change in the external benchmark of 1986-88. **Three,** bring back the issue of freer cross-border movement of professionals back to the trade agenda.

Policy Perspectives from Gateway House give an overview of a global issue that has implications for India's policy-making and business community. Each perspective summarises the criticality of the issue, lists the dimensions to be considered for analysis, and outlines how a policy can be designed or executed.

Introduction

India has been vilified globally over the past few months for derailing an opportunity to free up global trade that could have, purportedly, brought prosperity for people across the world. The western media has been censorious and most free-market thinkers are baffled by the Modi government's stand.

India was uncompromising in its refusal to sign the Trade Facilitation Agreement (TFA) at the World Trade Organisation's (WTO) General Council meeting—held in Geneva on 31 July 2014—unless it was taken up in conjunction with issues related to agriculture subsidies and food stockpiling. Ultimately, the meeting collapsed without reaching any agreement, because the WTO works on a consensus basis and even one dissenting note is enough to disrupt talks. [1]

India's stand invited opprobrium, with many perplexed western observers finding the country's actions at odds with Prime Minister Narendra Modi's avowed support of free markets, foreign investment, and economic reforms. Although Commerce Minister Nirmala Sitharaman later clarified that India was not opposed to the TFA, subject to India's concerns also being addressed, the tide of resentment has not turned.

The TFA will again come up for discussion among WTO members this month. Public posturing meanwhile seems to suggest that India has softened its stand somewhat, but is unlikely to relax its opposition unconditionally.

India's opposition to any agreement on the TFA has left many questions unanswered, and it is important to understand the country's position. This policy perspective discusses some likely scenarios that can provide clues to India's strategy and standpoint.

Background

At the Bali ministerial in December 2013, WTO members managed to reach an agreement, which had eluded the WTO for 12 years since the Doha Round of Trade Negotiations, or the Doha Development Agenda (DDA), was launched in November 2001. The Bali round was the ninth biennial since the launch of the first ministerial meetings in Singapore in 1996.

Developed countries, including some advanced developing countries (such as China), managed to reach an agreement on only trade facilitation—an accord designed to simplify global customs procedures and facilitate trade of goods across borders. But the TFA was supposed to be part of an overall package, which included agriculture and other development issues. However, through hard-nosed negotiations, industrialised countries put together a final agreement that plucked out only one issue (TFA) from the DDA and managed to push all the others (including agriculture) down the road.

On agriculture, it was decided to defer judgement till 2017 on how to treat developing countries pursuing food security through public stockholding of food grains. In short, developing countries, including India, cannot be challenged through the WTO Dispute Settlement Mechanism for stockpiling grains till a permanent solution is negotiated by 2017. This has been called the 'Peace Clause'.

However, some additional conditions were slipped into the final text of the Bali declaration, which tie the hands of developing countries. These are discussed later.

Discussion on a host of other development issues—such as market access for cotton products from least developed countries (LDCs) or export subsidies—were all mothballed till the next ministerial. Ironically, the export subsidies on agricultural goods are mostly provided by rich countries to their farmers, and they have been reluctant to entertain any discussion that aims to phase out the regime.

Why is India upset?

So why is India upset, especially since the country was also a signatory to the Bali agreement? And why did some of the other large developing countries—such as China, Brazil, and South Africa—cross the floor, isolating India?

Here are some probable reasons for India's principled stand at the WTO General Council meeting in Geneva on 31 July 2014.

What caused the turnaround: As part of the Bali agreement, meetings were scheduled to be held between December 2013 and July 2014 to discuss the TFA, as well as all the contentious issues on agriculture and on how to proceed with discussions on finding a permanent solution. However, India claimed that most of the discussions in this period centred on the TFA and there was very little progress on agriculture. This gave India reason to believe that the **developed countries were only interested in pushing the TFA through,** leaving agriculture and other development issues unresolved.

In a statement to Parliament on 5 August 2014, Commerce Minister Nirmala Sitharaman said: "In contrast to their efforts on Trade Facilitation in the WTO, some developed countries have been reluctant to engage on other issues. Seeing the resistance to taking forward the other decisions, the apprehension of developing countries was that once the process of bringing the Trade Facilitation Agreement into force was completed, other issues would be ignored, including the important issue of a permanent solution on subsidies on account of public stockholding for food security purposes. India, therefore, took the stand that till there is an assurance of commitment to find a permanent solution on public stockholding and on all other Bali deliverables, including those for the Least Developed Countries (LDCs), it would be difficult to join the consensus on the Protocol of Amendment for the Trade Facilitation Agreement." [2]

Western trade negotiators have instead portrayed India's decision as a last-minute, arm-twisting tactic to wrangle trade concessions in agriculture, leading to a distorted narrative in the western mainstream media and by U.S.-based think tanks.

An example of this deliberately mangled narrative is an interview with Gary Clyde Hufbauer, Reginald Jones Senior Fellow at Peterson Institute for International Economics, in Washington D.C., soon after the Bali Declaration, in which he said: "…India led a group of countries which wanted, essentially, a buyout from disciplines on agricultural subsidies. It's as straightforward as that. They called the agreement Food Security. I think that's a mis-label. But what they want and what they got is that for an indefinite period of time—to be reviewed in 2017—they can subsidise whatever they wish for the so-called purpose of stockpiling essential foodgrains, whatever that means." [3]

What's paradoxical here is that the DDA was scheduled to end by 2005 but steamrolling by the U.S. and the European Union has vitiated and prolonged negotiations.

WTO's role as an arbiter: In a detailed summation of the Bali ministerial proceedings, an article in the *Economic and Political Weekly* describes how WTO director general Roberto Carvalho de Azevedo created conditions at Bali, through closed-door meetings and hardball negotiations, which convinced developing countries to support developed countries on the TFA. [4]

In addition, Azevedo was possibly under pressure from different national groupings —such as Friends of the System (members include: Australia, Canada, Chile, Mexico, Norway, Switzerland, South Korea, Singapore, Turkey, Hong Kong, Colombia, Costa Rica, and Pakistan)—to somehow stitch together an agreement that could bring some finality to the Doha Round. A general sense of disappointment and an air of futility has surrounded the Doha talks since their inception and Azevedo was keen to showcase some success, even if it meant pushing a few pending issues under the carpet. Cynics have presaged the end of the WTO and of trade multilateralism; WTO officials were hard-pressed to prove them wrong.

But isn't the TFA supposed to benefit all? It is time to bust some myths about the agreement. One of them is that the TFA will increase global GDP by $1 trillion and create 21 million additional jobs. This has been described as a highly exaggerated estimate. While the figure's provenance is disputed, it is believed that a 2013 paper first put a number on the purported gains from trade facilitation. [5] Senior fellow at the Peterson Institute for International Economics, Arvind Subramanian, has questioned the number in one of his columns and said, "Gains from TFA have been grossly overstated." [6]

Other experts have also questioned the conclusion. Jeronim Capaldo of Tufts University in Boston finds the figure implausible: "…its expected gains of $1 trillion dollars for the global economy are largely overstated as they are based on a set of unjustifiable assumptions…" [7] Columnists in leading western publications surprisingly bought into this mythical figure unquestioningly. [8]

Trade is a good economic tonic: The other myth about the TFA is of the enormous change it will occasion in developing countries by improving trade infrastructure. A closer look at the agreement shows how it is only meant to cut down time-to-market for imported goods; in short, all the changes—including in port infrastructure and customs processes—will only help importers, which are mostly developed countries, to reach markets faster, thereby improving turn-around times and reducing costs.

But, for this to happen, many countries (both developing and LDCs) will have to incur additional capital expenditure to expand their port handling capacities, hire additional staff, and upgrade hardware and systems. This is expected to hit LDCs the hardest. The developed countries had agreed to defray some of the costs, but this has been insufficient. Besides, some of these cost items become fixed in nature (such as an enlarged wage bill), translating into a high-cost infrastructure that does not necessary help the economy. A one-time refinancing does not solve this problem, especially for the LDCs.

But, importantly, the **TFA contains nothing**

which will help either developing countries or the LDCs to export more or help them gain enhanced access to developed markets. The entire benefit is expected to flow to the developed countries, which can now use the TFA to prise open new markets.

In any case, India is believed to have already implemented many of the conditions of the TFA, which makes India's opposition to the passage of the agreement at Geneva look all the more principled.

India's stand on agriculture: Strategically, India's tactic on July 31 has brought agricultural issues back to centre-stage. India has consistently sought to highlight its sovereign right to provide food security for its citizens, just as the U.S. has a right to build up energy security for its inhabitants. As an extension of this prerogative, India has consistently defended its right to buy food grains from farmers at a higher price, to stockpile grains as a strategic instrument to keep domestic food prices under check, as well as to supply these grains at subsidised rates through the public distribution system (PDS) to meet the minimum food requirements of 40% of the population.

This food security platform is bookended by subsidies on both sides—when farmers are paid a minimum support price which is higher than the market price, and when consumers are sold grains at a price lower than the market price. But that perspective changes when viewed from the PDS end, or the sovereign compulsion to feed the country's poor at affordable rates. To enable food sales through the PDS network, the government needs to buy grains. And to do so it must pay a price higher than market rates.

According to the WTO's Agreement on Agriculture, providing a minimum support price to producers—which is higher than the market price—for buying grain is viewed as trade distorting and is subject to limits. India—and, indeed, many other developing and poor nations—has a problem with the way this limit is calculated.

India and other developing countries are expected to maintain their "aggregate measurement of support" (AMS), or the subsidy paid for procuring grains, within 10% of the value of agricultural production. Here is how it works:

First, the value of production is calculated by multiplying the minimum support price offered to farmers with the total crop produced in that particular food grain. Next, the value of AMS is calculated by multiplying the total volume of that crop with the difference between the support price and a fixed, external reference price. Under the limit, or in WTO language *de minimis* rules for developing countries, AMS should be within 10% of the value of agricultural production.

The **problem is with WTO's choice of an external reference price,** which is the average of the prices prevailing during 1986-88. The benchmark is meaningless on two counts. One, it is 28 years old and does not take inflation into account. Grain prices have increased by at least seven times in the interim. Consequently, the gap between the minimum support price and the historical benchmark is so wide that India (and probably many other large developing nations) always runs the risk of breaching the 10% limit. Two, the choice of timeline further skews the benchmark because in those years both the U.S. and Europe were dumping grains on the world market and thus average prices were pushed to artificially low levels. [9, 10]

The moot question here is: why did the WTO arbitrarily select 1986-88 as the benchmark years?

India and many other countries have been asking for a revision of the fixed external reference price. However, any move to discuss such a change was blocked by the U.S. at Bali, as well as in earlier ministerial meetings. Given the compelling need to provide for food security, without a permanent solution to this weird mathematical formula developing countries will always remain vulnerable to trade pressures from the rich countries.

There are other oddities in the agricultural face-off:

1. The messiness with the external reference price has additional complications. In case the country is a net grains exporter, the benchmark becomes f-o-b (free-on-board) prices; for net importers, it is c-i-f (cost-plus-insurance-plus-freight) prices.

2. While the 'Peace Clause' does provide some breathing space, the WTO has sought to bind developing countries in other legalese. The Bali declaration text states: "Any developing Member… shall ensure that stocks procured under such programmes do not distort trade or adversely affect the food security of other Members." This **shifts onus of proof—that they are not indulging in trade distorting practices—on developing countries,** thereby giving rich countries another handle to browbeat developing countries. This strong language was apparently inserted by the U.S. Trade Representative while agreeing to the 'Peace Clause'.

3. India's food stockpiling is conducted exclusively within the domestic confines of its borders. Therefore, raising the bogey of trade distortion seems to be stretched.

4. The U.S. doles out a far higher volume of subsidies to its farmers, but it was able to move these subsidies to the category of non-trade-distorting. This happened in the 1980s and 1990s when developing countries and LDCs lacked negotiating muscle but were keen to foster a multilateral trading regime. Ironically, most of the subsidies actually are used by agricultural activities that are export-oriented, such as livestock management, and cultivation of corn and soya.

5. It is well known that India's food subsidy programme is defective and riddled with myriad leakages and corrupt practices. It is also true that direct cash transfers to targeted beneficiaries induce economic efficiencies and engender systemic savings. However, it takes time to move from the current subsidy system to direct cash transfers, given the vast population base to be covered and the inherent complexities involved.

Standing alone: India's stand was visibly non-obstructionist, and yet it was isolated at the General Council meeting, finding support from a rump group of countries comprising Bolivia, Cuba, and Venezuela. It is mystifying why some of the large beneficiaries of agriculture issues at the WTO—China and Brazil, among others— switched sides at the last moment. It can only be conjectured that they were lured away with the promise of quid pro quo.

China's role at Bali and later, at July's General Council meeting, is illuminating. It abandoned its support for India's cause—which, incidentally, also helps China—and put its weight behind the TFA. That is understandable: China sees itself as one of the world's trading giants. [11]

Strangely, if India does manage to get its way on food security at the WTO, China will be among the largest gainers. It, therefore, seems that China is content to sit back and watch India wage this lonely war on behalf of developing countries. Even South Africa and Brazil seemed to be arm-twisted into not supporting India.

Then there's politics: The Bharatiya Janata Party followed up its ascension to power in May 2014 with a scrutiny of major international agreements signed by the previous Congress government. They are not satisfied with the **text of the Bali agreement which, Modi's government believes, was left ambiguous** by former commerce minister Anand Sharma. [12]

In fact, in December 2013, Arun Jaitley, then Leader of Opposition in Rajya Sabha (and now the finance minister), had raised questions about India agreeing to only the TFA while postponing a permanent settlement on agriculture.

Conclusion

Under the circumstances described above, India may be justified in holding the TFA hostage till a permanent solution on agriculture is finalised.

What is the way forward? Here are some suggestions:

1. Part of the reason that India is struggling to maintain its food security issues—critical to the country's well-being—is because of the naiveté Indian negotiators displayed during the Uruguay Round (1986–1994) in Punta del Este of trade negotiations. A lot of ground was ceded to the U.S. and Europe during those negotiations, partially in good faith and partially because Indian officials were not familiar with trade niceties. [13] Even in subsequent years, India's negotiation strategy has invited adverse comments from academia and other stakeholders. It is, therefore, absolutely necessary that India's commerce and external affairs ministries hire skilled negotiators, preferably from the private sector. In addition, it is also absolutely imperative that the government puts its diplomatic corps and trade officials through a training process.

2. India has to ensure that the external price benchmark of 1986-88 is updated and shifted closer to a current time-frame. To do this, it will need support from a large number of developing and poor countries. India will have to retrospect on how it got isolated at Geneva in July. It looks like **India did not communicate its position well,** and was only interested in sorting out the logjam over food stockpiling, whereas the other developing and poor countries have many other pending issues. Communication has to be key—India will have to call in all favours and ensure that a permanent solution to the food security issue, as all as to other development issues, are sorted out as a pre-condition to signing the TFA.

3. One of India's original bargaining chips in the Uruguay Round was services and cross-border movement of trained professionals. Somewhere along the line, these two issues got dropped. This might be a good time to put these chips back on the table.

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