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REGIONAL TRADING BLOCS AND THEIR IMPLCATIONS FOR THE INDIAN ECONOMY

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REGIONAL TRADING BLOCS AND THEIR IMPLICATIONS FOR THE INDIAN ECONOMY

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The aim of this paper is to analyse the likely consequences on India of the formation of two trading blocs : The EC (European Community) and the NAFTA (North American Free Trade area). The paper surveys the institutional background to the formation of the trading blocs and tries to prognosticate on the future evolution of their trading policies vis a vis less developed countries in general and India in particular. Our analysis shows that the EC has strong trade creating effects whereas those of NAFTA are strictly limited. Trading blocs should not be perceived as throats to India's export prospects, rather they present several opportunities for export expansion, if proper domestic policies are pursued. Our paper also surveys the gamut of issues related to South-South trade and concludes that the time is not yet ripe for Southern countries to form an effective regional trading bloc on their own.

The end of the Second World War not only witnessed the emergence of the US as the new economic hegemon but also a complete disillusionment with the doctrine of protectionism amongst industrialised countries. Multilateralism became the new catch word and "free" but fair trade" the new key phrase. The new Multilateralism was initiated by the former allied powers under the aegis of the GATT and held, more or less, unchallenged sway over the new world trading order for the next two decades. But protectionist tendencies, even during GATT’s heydays, were not entirely subdued. As Winters (1990) has noted, the successive rounds of GATT negotiations have involved a subtle interplay of bilateral and multilateral elements. Article XXIV of the GATT explicitly admits Customs Unions and Free trade areas under certain conditions, and preferential trading arrangements such as the ECSC (European Coal and Steel Community), EEC (European Economic Community) and the EFTA (European Free trade Association) all emerged during the late 1950s and early 1960s.

The mid sixties marked a turn in the tide of fortune of Multilateralism and the next decade and a half, saw the emergence of strong protectionist sentiments all over the industrialised world, especially marked in the US. The sources of this new protectionism have been extensively analyzed. Bhagwati (1988,1991) attributes it to the Diminished Giant Syndrome of the US viz., to its loss of national competitive advantage in high- technology sectors to Japan and Korea, which put pressure on the US to protect its industries via trade related measures. To this general trend, one must add at least three specific factors:-

(i) The two oil price shocks of the 1970s depressed world markets and imposed large and accelerated structural adjustment on the US and other developed economies.

(ii) The Reagan administration's strategy of running,huge budget deficits and then disinflating via huge real interest rates subjected the US balance of payments to enormous strains.

(iii)public support for protectionist policies in the industrialised countries was cleverly gained by holding out to organised workers the threat of loss of jobs from foreign competition and by the general appeal to xenophobic sentiment (Corden (1974) and Stoeckeletal(1990)).

The protectionist tendencies got reflected in three distinct sets of measures adopted by the industrialised world:

(1) aggressive unilateralism, especially, by the US
(2) multilateral initiatives at the various GATT fora, and
(3) formation of regional trading blocs.

Aggressive unilateralism by the US first evidences itself in the 1974 Trade Act and culminates with the Special 301 provisions of the 1988 Omnibus Trade Act. On the GATT front, even though an appreciable reduction in tariff levels was achieved over successive rounds, the advanced countries managed to have instituted in their stead, several kinds of non tariff barriers (NTBs), which, because of their discriminatory and mis-allocative nature, were far more insidious than the tariff barriers they replaced. The recently concluded Uruguay Round of the GATT represented a major triumph for the protectionist forces in the industrialised world, since their long standing demand to strengthen intellectual property laws and investment measures and to bring trade in services within the GATT discipline were not only conceded but trade retaliation (under certain circumstances) was admitted as a legitimate weapon to enforce adherence to the regime. Recent years have also witnessed the emergence of a number of regional trading blocs and these are the subject matter of this paper. Trading blocs, in the view of their opponents, are a manifestation of protectionist tendencies, though ' their proponents justify these arrangements as a substitute for the multilateral liberalisation of trade, which the GATT failed to usher in.

The plan of this paper is as follows. Section 2 presents some general considerations about the EC and the NAFTA, whereas Section 3 concerns itself with a review of the broad trading arrangements that India has with these two blocs. Two special schemes -the GSP (Generalised System of Preferences) and the MFA (Multi Fibre Agreement)-are discussed at length in Sections 4 and 5 . The impacts of the EC and the NAFTA on India's trade prospects are discussed in Sections 6 and 7 with the South-South trade possibilities explored in section 8. Section 9 concludes the paper.

EC AND THE NAFTA: GENERAL CONSIDERATIONS

The term "Trading Bloc" is somewhat elastic and in a generic sense can be used to refer to any of the following four arrangements (which are listed here on an ascending scale of integration).

1) Preferential Trading Arrangement (PTA): The term PTA applies to an arrangement whereby a country applies lower tariffs to imports from a designated group of countries or where a group of countries applies reciprocally and mutually, lower tariffs within this group.

2)Free Trade Area(FTA): Members in this arrangement maintain their individual trade regimes against non members but tariffs are completely eliminated for trade between members

3)Customs Unions (CUs):This arrangement applies when an FTA also has a common external tariff.

4)Common Market(CM):In addition to being a CU, a common market eliminates all barriers to internal trade in goods services as well as to labour and capital movements between member countries.

Whereas the EC is well on its way to becoming a common market, the NAFTA represents a much looser kind of an arrangement, being closer to an FTA, than a common market. Three explicit differences might be noted between the EC and the NAFTA:

> Firstly, EC members have significantly ceded national sovereignty over economic affairs to regional bodies such as the European Court of Justice, the European Commission and the European Parliament. No such willingness to cede national sovereignty to regional bodies is evident among the three NAFTA countries (Grinspun’and Cameron (1993)),
>
> Secondly, unlike the EC, the NAFTA does not provide a formal system of free labour mobility (Hufbauer and Schott (1992))
>
> Thirdly, a single European currency and common monetary and exchange rate policies are important goal for die EC! NAFTA, on the other hand, has eschewed consideration of these issues. As a matter of fact, changes in the real exchange rates will be relied upon as an essential adjustment mechanism in the NAFTA member countries

The fact that NAFTA represent a much looser union than the EC has important implications for non member Whereas in the case of the EC, future negotiations (whether via WTO or bilateral) relating to trade restrictions (and preferences) will have to be on a community vide basis, similar negotiations relating to NAFTA countries will be dominated by (NAFTA)- member-specific considerations. Secondly, with the EC, both trade creation and trade diversion are likely to be significant, whereas with the MAFIA trade creation is likely to be much less in comparison to trade diversion.

TRADING ARRANGEMENTS

In order to analyse the possible impacts of the EC on India's trade prospects, it is necessary to review the trade arrangements between India and the two blocs and to have some idea about the direction and composition of this trade. We turn to the latter aspect first.

The EC is India's largest trading partner accounting for 28% of India's total exports, NAFTA comes second accounting for 16% of India's exports with OECD Asia (Japan, Australia and New Zealand) and East Asia accounting for about 10% each. (Figures are from the UN COMTRADE data base and pertain to yearly averages over 1990-1993). Thus the EC and NAFTA together account for nearly 40% of India's total exports. So far as the composition of exports is concerned, manufactures accounted for 84% of total exports to the EC and 79% of total exports to NAFTA. Within manufactures, the most prominent items were textiles, clothing, chemicals, leather and footwear. India is also a marginal exporter of food products, ores *&.* metals and fuels. Table 1 presents a detailed composition analysis of exports to the EC and the NAFTA, Let us now turn to a review of the trade arrangements with the EC and the NAFTA members.

MFN DUTIES

The MFN duties and the GATT ceiling duties are shown in Table 2. Because of the EC's Common Agricultural Policy (CAP), MFN duties on agricultural products are higher than in the US and Canada. For industrial products, US duties are lowest and Canadian duties the highest with the EC duties closer to the US levels.

PRICE CONTROL MEASURES

There are three types of price control measures viz. anti-dumping duties, countervailing duties and variable charges. The EC and all NAFTA members impose anti-dumping and countervailing duties within the GATT framework '. Variable charges however are levied only in the EC and the US .Under the CAP of the EC, a number of temperate agricultural products are charged with variable levies which raise their price to the domestic support level. These goods include live animals, meat, dairy products, cereals, vegetables, oilseeds and fruits. In the US variable charges are referred to as "Section 22 fees" and levied on sugar, molasses and syrups.

TECHNICAL MEASURES

Most health and safety regulations are set at the national level of the EC member countries and are implemented by the national authorities. The most commonly covered products under such regulations are meat/fish products . soaps, cosmetics, detergents medicines, pesticides , plants, fertilizers etc. Health and Hygiene measures in NAFTA countries are similar.

A number of other measures are in operation, such as seasonal duties, customs surcharges, internal taxes, advance payment requirements, automatic and non automatic licensing etc. But we do not discuss them in detail here. Instead we focus attention on two aspects of particular relevance to less developed countries viz., Generalised Scheme of Preferences (GSP) and the Multi Fibre Agreement (MFA): a highly institutionalised system of export restraints).

GENERALISED SYSTEM OF PREFERENCES

GSP IN THE EC

The EC operates three preferential trading agreements (PTAs)[2] of which the GSP is of prime relevance from India's point of view. The scheme was introduced on 1st July 1971 mainly with a view to providing developing countries greater access to the EC markets. The GSP scheme covers both agricultural and industrial goods. Under this scheme, imports from beneficiary countries are allowed into the EC at preferential lower tariffs upto a certain level (GSP ceiling). Imports beyond the ceiling are permitted but do not qualify for the GSP tariff. For agricultural. products, tariff concessions of about 20-60% are granted, for about 700 items. For manufactured goods, the products from developing countries must pass a" Rules of origin" test i.e.

(i) they should be completely manufactured within the exporting country or have gone though sufficient processing, and

(ii) they should be directly transported from the exporting country.

In the EC, the GSP scheme extends to all dutiable manufactured and semi-manufactured goods, except for some sensitive products (such as iron and steel, textile etc.)The iron and steel products are treated under specific regulations under the GSP scheme and imports of textiles are contingent on the MFA.

The GSP scheme was revised in 1981 and further modified in 1986. A new GSP for manufactured goods was introduced on 1st January 1995 and will remain in force for the four-year period 1995-98. For agricultural products the revised GSP will come into effect on 1st January 1996. The new revised GSP for manufactured goods is based on two complementary mechanisms viz., tariff modulation and the graduation mechanism. Under the first of these, all quotas and ceilings have been abolished. Instead all manufactured products are divided into four categories (i) very sensitive (ii) sensitive (iii) semi- sensitive (iv) non-sensitive. The GSP margin of preference on these categories would be respectively 15%,30%,65% and 100%. Under the new policy of graduation, the degree of competitiveness of a beneficiary country is measured in terms of an entire industrial sector, and not in terms of a specific product as before. Graduation occurs in two phases - in the first of which the margin of preference is reduced by 50% and in the second, abolished altogether. The phases come into operation on the basis of a Specialisation Index, and the EC has given an assurance that this index will be objective and transparent. The graduation mechanism for India will apply to the following sectors (i) textiles (ii) leather, raw hides and skins and (iii) leather articles and furskins.

GSP IN NAFTA:

UNITED STATES:

The GSP Scheme in the US has been in operation since 1976 and provides for duty free entry to about 4100 items . The GSP scheme is reviewed periodically and a previous beneficiary country may be excluded as it advances economically and/or as its trade becomes competitive. Product exclusion occurs when the value of a country's shipment of a given product exceeds 50%(or sometimes 25%) of the total US import of the product or surpasses a predetermined dollar value. Similar rules of origin apply, as in the case of the EC, except that in the US case, it is specifically laid down that the cost of material and processing operations in the exporting country must equal at least 35% of the value of the finished product.

CANADA:

Canada introduced a General Preferential Tariff (GPT) for developing nations in 1974. Initially the preferences were granted for selected agricultural products and for all industrial inputs and manufactured goods with the exception of certain chemicals, plastics, textiles, footwear and electronic goods. Since 1988, the GPT scheme has been extended to almost all industrial products and over 240 agricultural items. Rules of origin require that (i) the foreign material content must not exceed 40% of the value of the good. However, cumulative origin is allowed so that materials and parts obtained from one beneficiary country and processed in another would be treated as " Domestic Content" (ii) the goods must be consigned directly from the exporting country.

In addition to GPT preferences, the developing country members of the Common wealth also benefit from the British Preferential Tariff (BPT) for various agricultural and manufactured products.

MEXICO:

This country does not grant any GSP privileges, but because Mexico is a signatory to the 1971 Protocol of (he GATT covering 17 developing countries (including India), some mutual tariff concessions and preferences on specified items are in operation.

MULTIFIBRE AGREEMENT

The Multi Fibre Agreements , after some initial precursors, came into force formally on 1st January 1974 as MFA I. The MFA I established formally the principle that restrictive trade agreements could be imposed in order to prevent market disruption but on the whole was not unfavourable to the less developed countries point of view, especially, as the coverage was quite limited excluding such products as handloom fabrics and handicrafts from the scope of bilateral quotas. These arrangements were accentuated and tightened in successive MFAs , till by the time the MFA IV (1986-1991) came into operation, trade in textiles and clothing was subject to a maze of restrictions and severely constrained the export prospects of one of the developing countries' leading export sector. By the mid 1980s about 36% of the textile exports to the EC and 46% of apparel exports to the EC from the developing countries was restricted (i.e. subject to bilateral quotas). In the course of this evolution, the concept of" Market Disruption " as originally defined in ANNEX A of MFA I (to apply to loss of production and employment in the developed country due to low priced imports) had been considerably extended to implicitly include lower input prices due to Changes in technology and tastes.

As far as India is concerned,13 categories of textiles and clothing Come under current MFA (MFA IV) restrictions - 4 in Textiles and 9 in Clothing. for Textiles, items subject to quota restrictions are - Category I (cotton yarn), Category 2 (cotton fabrics), Category 20 (bed linen) and Category 39 (table, toilet and knit wear other than terry). For Clothing, the quota items are Category 4(T-Shirts), Category 5 (jerseys), Category 6 (woven trousers), Category 7 (ladies blouses), Category 8 (gents shirts), Category 15-B (ladies jackets), Category 26 (ladies dresses) Category 27 (ladies skirts) and Category 29(ladies co-ordinate suits). In the US market textile quotas apply to seven items, whereas, about 23 clothing items come under MFA quotas or consultations. Among these quota items the major products are (i) woven cotton fabrics (ii) made up textile articles (iii) carpets and rugs (iv) travel goods and handbags (v) clothing accessories (vi) knitted clothing and (vii) clothing of textile fabrics. Items (i),(iii),(vi) and (vii) are also under the MFA restrictions in Canada.

Textiles and doming are an extremely important item of Indian exports accounting in the 1990s for 32% of its total exports to NAFTA and for 42% of total exports to the EC. Thus the future evolution of the MFA is, of more than a passing, significance for India. The recently concluded round of the GAIT specifies a phase out of MFA over a ten year period beginning 1st January 1995. The Phase out would be spread over three stages viz., I (1995-1998), II (1998-2002), III (2002-2005) with growth factors of 16%, 25% and 27% to be applied in these stages respectively ; this arrangement will integrate about 18% of total imports (under MFA) into the GATT by the end of Phase I, 51% by the end of Phase II and complete integration into the GATT is proposed by the end of Phase III i.e. by 1-1-2005. LDCs in general are worried as to whether the phase-out timetable will be strictly adhered to or whether old protectionism will somehow re-emerge in new guises. From the point of view of further analysis, it is important to note that, with the formation of the EC on 1 1-93, country quotas have been replaced by EC-wide quotas.

An argument frequently resorted to in developed countries is that quotas are non restrictive because quota utilisation for many countries are less than 100%. The internal allocation of Country/Category quotas can often be inefficient, making these quotas binding, even at lower rates of utilisation. The argument applies with particular force for clothing, and we try to explain below in brief the policy followed by India in allocating quotas internally among domestic producers. This policy is administered by the Apparel Export Promotion Council (AEPC). The AEPC works out a minimum export price for each Category of garment to a given destination on the basis of manufacturing costs and world prices. These prices are then treated as floor prices for all exporters. Firms can seek a quota allocation against a confirmed export order backed by an irrevocable letter of credit.

Two types of allocations prevail in India for garments -closed and open. Closed allocations represent 75% of total allocations and are based on criteria such as past performance, manufactured capacity and exports to non quota countries. The remaining 25% of *he allocations belong to the so-called Open Category and are distributed on a First-Come-First-Serve (FCFS) basis.

The reasons for underutilisation of quotas are manifold. Firstly, as noted by Kumar and Khanna (1990), low aggregate quota utilisation rates may reflect a situation in which certain categories impinge on their limits and other categories are of little interest to exporters, so that Indian firms may suffer from binding constraints in categories in which they are competitive (even when aggregate utilisation rates are low). There is of course a 7% "swing" provision across categories but, as it comes into effect after the annual quotas have been exhausted , it is of little use when quota exhaustion occurs during subperiods, as is usually the case with many goods facing seasonal demand. Secondly, the Indian regime introduces inefficiencies of its own creation on the quota system. In the allocation of closed quotas, there is a further disaggregation via the system of reservation for manufacture - exporters , public sector exporters, handloom exporters etc. which in effect depresses the utilisation rate. For the open allocations, the AEPC uses the " Cut-Off " price as a rationing device. The scramble for quotas in certain categories saw firms making applications under several registration "aliases" as also inflating their unit prices. A final source of inefficiency results from firms entitled to close allocations, using these to cross subsidies their sales under the Open allocation system (see Government of India (1993-94) and ICICI (1994)).

EC IMPACT ON INDIA

To appreciate the economic significance of EC for India's trade,we need to know the likely impact of the common market on the EC economy itself. The most famous report dealing with this aspect is that by Cecchini et al (1988) which estimated the impact of EC 92 as being in a band of 4.25% to 6.5% of EC GDP. Using this set of estimates, analysts have attempted to project the impact of EC 92 on world trade in general and on specific countries or regions, in particular. At the aggregate level, three sets of factors may be distinguished:

(i) trade creation because of increasing import demand due to stimulus to EC GDP consequent upon integration

TRADE BLOCS IN THE SOUTH:

There is a very pervasive strand of thinking among intellectuals and policy makers in LDCs about the possibility of forming trading blocs among groups of LDCs. This viewpoint derives sustenance from several distinct but related influences:

(1) Possibly the first and dominant influence is the strong appeal that the "dependency theory" has had on economic theory of the South.The hard core proposition of the dependency school is of course the Singer-Prebisch thesis that LDCs face a secular decline in their terms of trade and therefore North-South trade is iniquitously biased in favour of the North.

(2) In a seminal contribution W.A.Lewis (1980) strongly makes out a case for trade as an engine of growth and postulates a stable long run relationship between growth in the industrialised countries and the LDCs. This relationship coupled with the stagnation in growth of the industrialised countries since the 1980s leads Lewis to emphasise South-South trade as the only mechanism which can sustain growth among LDCs.

(3) The 1980s have also witnessed the emergence of new protectionism in the North, especially an increasing resort to Non tariff barriers (NTBs) (See Section 1). It is generally agreed that the North's capacity to absorb the South's goods is severely constricted - what Bhagwati (1988) has called the "Second Export Pessimism".

(4) Finally, South politicians have always been enamoured by slogans such as " Third World Solidarity" and "Southern Self Reliance" and hence the idea of Southern trade bloc is not without an emotive appeal.

In practice however, achievement of Southern solidarity has made little headway. South -South trade[9] in 1990 accounted for 2.9% of total world trade. So far as India's exports to LDCs are concerned, their share (in India's total exports) has come down from 23% in 1960 to about 11% in 1990. Tariff levels in several LDCs continue to be high (under the Special and the Differential treatment of the GATT) and various types of non tariff barriers are in existence. The idea of removing such tariff and non tariff barriers on a reciprocal basis by LDCs has naturally been a very attractive one. An initial effort in this direction was made under the auspices of the GATT and a protocol was signed by sixteen countries and came into force on 1lth February 1973. Some of the major members of the protocol are Brazil, India, Pakistan, Egypt, Chile and Korea. However for various reasons, the protocol has had only a limited effect on trade and welfare in the third world. These reasons were threefold - the number of signatories was limited, the package was confined only to tariffs and non tariff barriers and only 740 tariff positions were covered. The protocol was strengthened and revived under a new preferential trading system which was signed by 46 members of the G-77 group of the LDCs. The main point of action of the new system is a Global System of Trade Preferences (GSTP) among LDCs (Linneman (1992)).

The GSTP essentially comprises of three features

(1)a uniform tariff cut of 10-20% on an MFN basis to be applied to all imports from participating members. Exceptions to these cuts will be granted for sensitive products but limited to between 100 to 200 tariff positions per country

(2) to be guarded from misuse, such tariff concessions should be subject to "Rules of Origin". The chosen rule of origin is the So called " BTN jump" criterion- i.e. the imported imports must have undergone a specified transformation process or have been transformed to such an extent that the processed inputs are classified differently from the unprocessed inputs (according to the Customs Co-operation Nomenclature). A cumulation provision may be applied that takes into account the process of transformation in all signatory countries and

(3) Safeguard measures which allow exemptions to the tariff concessions in countries facing balance of payments difficulties and threat of serious injury to domestic producers. However, the importing country should consult its trading partners in advance, and demonstrate the likelihood of the injury or threat and also compensate its trading partners.

The agreement recognises the special problems of the least developed countries and they are not required to make concessions on a reciprocal basis [10]. New negotiations rounds will be needed to make the GSTP more broad based in terms of products and also deepen the tariff cuts. The impact of the GSTP on trade preferences of the LDCs have been estimated by Erzan and Yeats (1988). For the proposed tariff cuts of between 10-20% , South-South trade is projected to increase between 1.7-3.4 %. Even if tariff cuts are as high as 50% (a rather unlikely outcome) the study estimates the gain in trade at a modest 8.5%.

EC-wide quotas prevailing in 1993 with the (aggregate of) the national quotas of 1992 adjusted for growth factors. In both textiles and clothing , the new quota regime is more liberal (though only slightly so) than the old quota regime. Table 5 also shows that predictably , quota utilisation rates have improved after the switch-over to EC-wide quotas for both textiles and clothing.

However, too much, of course should not be read into this analysis. The quotas are subject to periodic revisions and the possibility of introducing quotas afresh cannot be ruled out (as a matter of fact that is exactly what happened in the case of textiles Category 9 (Terry Towels)). More importantly, the calculus of qualified majority voting introduced in EC decision making in 1986 means that one small and two large countries can block any liberalising proposal, enhancing the protectionist possibilities of EC 1992.

In the final analysis one can say that with the successful completion of the GATT round the forces of liberalisation have gained considerable ground but that protectionist tendencies are never absent and can surface at any moment. One tiling is certain however, the formation of a trading bloc leads to a possibility of a quick and organised retaliation by one trading bloc against actions of another. This " balance of terror" could be an important restraint on protectionist sentiments in any one bloc getting out of hand.

NAFTA IMPACT ON INDIA

In contrast to the EC, NAFTA is only a free trading area covering the US, CANADA and MEXICO and has thus raised genuine concerns among LDCs about the likely trade diverting consequences. While quantitative assessments of the likely impact of the NAFTA on LDCs based on detailed models, are lacking at the moment, some indications of likely scenarios are available in Hufbauer and Schott (1992), Erzan and Yeats(1992), World Bank (1992) and Safadi and Yeats (1993). From the Indian perspective, the last named study is particularly important and we critically discuss its methodology and conclusions below. As a backdrop to the discussion, it is as well to remember that India's trade with the NAFTA is heavily concentrated towards manufactures (which account for 79% of India's total exports to the region) with the single sector, textiles and clothing accounting for 40% of the manufacturing exports. NAFTA (absorbing currently about 16% of India's total exports) ranks second in importance to the EC (corresponding figure being about 28%) as a trading bloc for India.

Safadi and Yeats (op.cit) specify two preconditions for trade diversion to take place:

(1) firstly, trade diversion would emerge only for those products for which trade barriers currently apply for imports into the US from Canada and Mexico, and

(2) the NAFTA countries should be viable competitors for products traditionally imported from S.Asia.

In order to assess the overall impact of NAFTA, trade diversion possibilities have to be examined in each of the three member country markets. Of course the US is the major market ($5.4 billion imports from S.Asia, as compared to $0,348 billion for Canada and $0,067 billion for Mexico) but the Canadian-Mexican market is more vulnerable. For the US market, trade diversion was considered a real possibility in the case of 12 S.Asian exports. For the Canadian and Mexican markets trade diversion possibilities were serious for 5 and 2 products -espectively[7].

Using a partial equilibrium trade projection model developed by UNCTAD(1989), the authors project a trade diversion loss OP account of NAFTA of $35 million to S.Asia with India's share in this loss being $17.1 million (about 43% of the S.Asian loss). Sector wise speaking, India's greatest loss is in the field of clothing accessories (2.2% of its current exports) followed by woven cotton fabrics (1.8%) and clothing of textile fabrics (1.3%). This loss is hardly significant, especially, when juxtaposed against the projected gains from the Uruguay Round liberalisation (under the 30% and 50% liberalisation scenarios the gains are estimated to be $1780 million and $2970 million). If these figures are right as Safadi and Yeats write "NAFTA is almost a non event from the S.Asian perspective".

However, the study of Safadi and Yeats makes several simplifying assumptions. They assume away the phasing out period of trade barriers of more than 15 years, and also that all trade and non trade barriers facing the NAFTA members will be removed (when in fact certain key barriers such as rules of origin and transformation for Mexico are likely to be permanently in place). The study also proceeds on the assumption that Mexico (from which the trade diversion effects for S.Asian exports originate)faces no domestic supply constraints when in fact these are likely to be significant.

Bui all these restrictive assumptions mean that the NAFTA effects are likely to be overstated than otherwise . So on balance, their basic conclusion, about NAFTA no affecting S.Asian exports significantly, is unlikely to be challenged by more detailed analyses.

(2) trade diversion to Intra-EC sources because of abolition of Internal trade barriers and also because of cost efficiency in EC industries, and

(3)terms of trade effects because of price reductions in EC exports.

However the aggregate picture needs to be supplemented with several specific sectoral details. Non-tariff barriers are very much in evidence for several sectors. VERs are one common form of barriers and apply to textiles and clothing (under the MFA), footwear, iron and steel , leather products etc. Internal taxes, harmonisation requirements and technical standards (including health regulations) also act as NTBs. Among studies which have attempted to assess the impact of EC 92 on LDCs, special mention is owing to Davenport and Page (1991), Stoeckel et al (1990), Pohl and Sorsa (1992) and World Bank (1992). The standard methodology seems to be one of analysing the aggregate consequences via econometric or systems models and then capture the impact of NTBs via a Scenario- building exercise. This paper differs from the previous studies in that it is specifically focussed on India and it goes into a detailed Sectoral analysis. From the DGCI&S (Directorate General and Commercial Intelligence and Statistics) data , the following 26 commodities were identified as being of importance to India in the EC market:

(1) Textiles (2) Animal and Vegetable oils (3) Apparel (4) Chemicals (5) Coffee (6) Cotton manufactures (7) Crude fertilisers (8) Crude animal and vegetable materials (9) Electrical machinery (10) Fruits and vegetables (11) Floor coverings (12) Footwear (13) Iron and steel (14) Jute manufactures (15) Leather (16) Metal manufactures (17) Non electrical machinery (18) Oil meals (19) Spices (20) Tea (21) Transport equipment (22)Tobacco (23) Pearls, Precious and Semi-precious worked or unworked (24) Marine products (25) Metalliferrous ores (26) Non ferrous metals. Trade creation and trade diversion was estimated for each of these 26 categories using the trade projection model of UNCTAD (1989). Terms of trade effects (which emerged insignificant in most of the cases) were estimated via the method suggested by Davenport and Page (1991). The net impact in trade is presented in Table 3. The tabulated figures need careful interpretation; in particular they are based on three underlying assumptions:

(1) Article 115 prohibiting transshipment under certain conditions, of goods imported in one country to another, will be abolished, so that EC national restrictions on third country members will either be replaced by EC- wide restrictions or fall into disuse

(2) Trade barrier will continue at existing levels with national barriers replaced by equivalent EC-wide restrictions.

(3) The MFA **will** be phased out strictly in accordance with the time table agreed to in the Uruguay Round of the GATT(See Section 5).

Under these assumptions Table 3 indicates the aggregate impact of $705.09 million under the assumption of 4.25% growth in EC GDP and $978.23 million on the assumption of a 6.5% growth. Note that nearly 68% of the total effect is attributable to three sectors viz., textiles, apparel and pearls (precious and semiprecious, worked or unworked). The income elasticities for these three sectors are 2.18, 13.28 and 9.82 respectively [A]. The elasticity for apparels is very high and not surprisingly, the MFA restrictions become binding for the same in our model (though the MFA restrictions for textiles are non binding). If the MFA restrictions were not binding on apparels the gains in exports would have been $ 1153 million (4.25% of EC growth) and $1757 million (6.5% EC growth). These would have been comparable with predicted gains of $ 1750 million from a 30% liberalisation in the GATT as projected by the World bank (1992).

Our analysis is contingent on the assumption that the protection levels in EC 92 will remain unchanged at existing levels. Opinion on this is strongly divided. Stoeckel et al (1990) feel that " Fortress Europe" is a strongly likely outcome and adduce the Common Agricultural Policy, increased levels of antidumping and the increased concentration of industry as factors favouring this view point. They also cite the famous "Poitiers case " of October 1982 relating to Japanese VCR imports into France to show how easily VERs (Voluntary Export Restraints) can arise from pressures exerted by domestic producers and politicians. Pohl and Sorsa (1992) on the other hand prognosticate a liberal trading regime emanating from EC 92, based on the argument that it is in Europe's own interest to liberalise, rather than otherwise.

From India's point of view any likely impacts are tied up in a few critical sectors especially textiles and clothing , (pearls precious and semiprecious worked and unworked) and leather & leather products. We have already seen (Section 3) that textiles and leather and leather products are likely to be phased out of the GSP under the graduation scheme. The MFA is likely to be phased out in 2005. Nevertheless, textiles and clothing sector will continue to face restrictions in the interim period. However , since 1st January 1993, national quotas have been replaced by community wide quotas. From a purely logistics point of view the replacement of national quota by an equivalent (i.e. simple aggregation of national quotas) EC-wide quotas would lead to better quota utilisation. But it is not necessary that the EC-wide quotas is a simple aggregation of national quotas , it could be less or more. Table 4 compares the

Even though the slow progress of the GSTP negotiations are often blamed for the tardy growth of South-South trade, these also seem to be certain fundamental reasons for this latter feature. The traditional basis for predicting trade flows is the Hecksher-Ohlin theory, which states that countries will specialise in the export of those commodities that use their relatively abundant factor more intensively. The theory seems to receive considerable empirical support in predicting North-South Trade flows (Leamer(1984), Tharakkan ((1984)) etc. However, as Linder (1961) has observed , the narrowing of income differences between any pair of countries seems to expand rather than diminish trade- the phenomenon of Intra-Industry trade. The works of Balassa (1966J Verdoorn (1960) etc. also found that within EC industry specialisation was growing and trade flows in similar manufactured goods was expanding. Intra-Industry trade (in the mid-1980s) accounted for 59% of the total merchandise trade between industrial countries, whereas for the NIEs (Newly Industrialising Economies) it was 42% and only 15% for the South countries. Thus Intra-industry trade becomes increasingly dominant as income levels converge between trading partners. One can thus say that for countries at dissimilar levels of development, trade will be guided by factor endowments but for countries at similar levels of higher incomes Intra-industry trade will be the dominant factor. At the current low levels of similar development, the Southern countries have low possibilities of trade among themselves (their similarity precludes trade based on factor endowment differences while their low incomes mean that they are not yet ripe for Intra-industry trade). It will be a long time before these countries attain sufficiently high incomes for Intra-industry trade to become important. Only then can South-South Trade come into its own and trading blocs become a viable option in the South.

CONCLUSIONS:

This paper has tried to assess the emerging global trading environment for India's trade in the coming decade and has focused on the impact of the EC and NAFTA. The overall scenarios which emerge are not too bleak and certainly no cause for alarm from India's point of view. So far as NAFTA is concerned its impact on India will only be minimal whereas EC is expected to augment Indian exports considerably. Whether the projected gains from the EC (as also from the Uruguay Round of liberalisation) are actually realised would depend on India's successfully overcoming its domestic supply constraints most of which can be traced to the sluggishness of its ongoing structural reforms.

The current domestic situation in India reflects a strong attempt by a section of the intelligentsia and politicians to paint the global environment as a sinister threat from the developed world to the less developed. Our analysis shows the fallacy of this perception. It is in India's interests to remain an active participant in the global economy and to concentrate on removing those domestic barriers that inhibit this process. In particular an angry retreat into autarkic policies could spell economic "hara-kiri". There are not very sanguine prospects in South-South trade either. India' best bet is to meet the challenges posed by the new global trading order by pressing ahead with the structural reforms process. The stance of India's policy will only become clear , however, after the general elections of 1996.

NOTES:

1 According to GAIT, Antidumping measures may be invoked when the investigating authority is satisfied that dumping has occurred with material injury to the domestic industry. Countervailing duties are imposed on the basis of a finding of countervailing subsidies granted on experts.

2 These are respectively (i)Lome convention for the ACP countries (ii) Mediterranean preferences and (iii) GSP.

3 The growth factors have to be applied to augment the quota growth rates embodied in the current bilateral MFA agreements.

4 Our estimated elasticities for India in the case of textiles (2.18), clothing (13.28),leather (152) and metal manufactures (8.55) can be compared with those of Alizadeh and Griffith-Jones (1991) - textiles and clothing (2.5), leather (3.7) and metal manufactures (3.4). Their figures represent some kind of an LDC average.

5 Since the 1986 switchover to qualified majority voting, a commission proposal can be passed with 54 out of 76 votes. The vote distribution is as follows : United Kingdom (U.K), France, Germany and Italy (10 votes each), Spain (8), Belgium, Greece, the Netherlands and Portugal (5 each), Denmark and Ireland (3 each) and Luxembourg (2).Thus one small country (say with 2 or 3 votes) and 2 big countries (say 10 votes) can block any liberalising proposal.

6 The 12 products are (i) Nitrogen function compounds (ii) Synthetic organic dyestuffs (iii)Woven cotton fabrics (iv) Madeup textile articles (v) Carpets and rugs (vi) Universal and Plates of iron (vii) Travel goods and handbags (viii) Clothing of textile fabrics (ix) Clothing accessories (x) Leather apparel (xi) Knitted clothing and (xii)Footwear

7 The 5 products in the Canadian market are (i) Clothing of textile fabric (ii) Knitted clothing (iii) Leather clothing (iv) Carpet clothing and (V) Woven cotton fabrics. The two products in the Mexican market are (i) Leguminous vegetables and (ii) Oilseeds and nuts.

8 One indication of supply constraints in Mexico is the low import penetration of Mexican textiles (0.22 %) and clothing (0.45%) in North American markets. This contrasts with the corresponding figure for South Asia of 0.65% and 1.5% (the reference years are 1986-1991).

9 The term South is being used here to exclude the Newly Industrialising Economies and Eastern Europe.

10 The participants in the agreement are Algeria, Angola, Argentina, Bangladesh, Benin, Bolivia, Brazil, Cameroon, Chile, Colombia, Cuba, Ecuador, Egypt, Ghana, Guinea, Guyana, Haiti, India, Indonesia, Iran, Iraq, Libya, Malaysia. Mexico, Morocco, Mozambique, Nicaragua, Nigeria, N. Korea, Pakistan, Peru, Philippines, Qatar, Romania, Singapore, S. Korea, Sri Lanka, Sudan, Tanzania, Thailand, Trinidad and Tobago, Tunisia, Uruguay, Venezuela, Vietnam, Yugoslavia, Zaire and Zimbabwe.

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TABLE 1: PRODUCT-WISE COMPOSITION OF INDIA'S EXPORTS TO THE EC AND NAFTA (1990)

'	EC		NAFTA	
	US $Mn	%% of Export To EC	US $	%of Export to NAFTA
ALL ITEMS	4874.55	100.00	3658.90	100.00
FOODS	522.44	10.72	341.20	900
AGRICULTURAL MATERIALS	26.20	0.54	108.80	300
ORES AND METALS	97.97	2.0!	17.90	—
FUELS	—	—	299 .20	8.00
ALL MANUFACTURES	4097.02	84.00	2897.40	79.00
CHEMICALS	323 79	6.64	115.50	3.00
LEATHER	474.33	9.73	62.20	2.00
TEXTILES	8559I	17. 59	350.40	10.00
CLOTHING	1190 34	24.42	801 .70	22.00
FOOTWEAR	89.60	1.84	50.00	1.00
MISCELLANEOUS MANUFACTURES	89 12	1 .83	111. 60	3.00

NOTE: PRODUCT GROUPS ARE DEFINED AS FOLLOWS: (SITC)

(i) ALL ITEMS 0 TO 9
(ii) FOOD(0+1+4+22))
(iii) AGRICULTURAL MATERIALS (2-27-28)
(iv) ORES AND METALS (27+26+68)
(v) FUELS (3)
(vi) All MANUFACTURES (5+8+68)
(vii) CHEMICALS (5)
(Vii) LEATHER (61)
(ix) TEXTILES (66)
(x) CLOTHING (84)
(xi) FOOTWEAR (85)
(xii) MISCELLANEOUS MANUFACTURES (89)

TABLE 2: MFM DUTIES AND GATT CEILING DUTIES

	MFN DUTIES		GATT CEIUNG DUTIES	
	AGRICULTURE	INDUSTRY	PERCENTAGE OF Agricultural PRODUCTS	PERCENTAGE OF INDUSTRIAL PRODUCTS
EC	12.1%	6.4%	65.00	100.00
CANADA	0%	9-25%	98.50	95.90
Mexico	0-10%	0-20%	VARIABLE	VARIABLE
US	3%	5%	90.00	100.00

Source: UNCTAD Directory of Import Regimes Part II. 1994

TABLE 3:NET TRADE AUGMENTATION OF INDIA'S EXPORTS TO THE EC

	(FIGURES IN MILLION US DOLLARS	
COMMODITY	Net Trade Augmentation	
	4.25 % EC GROWTH	6.5% EC GROWTH
TEXTILES	80.72	12347
ANIMAL AND VEGETABLE OIL AND FATS	-3 44	-5.27
APPAREL	174.53	174.53
CHEMICALS	-8.77	-13.41
COFFEE	033	0.5 .
COTTON MANUFACTURES	49.52	75 73
CRUDE FERTIUSERS AND CRUDE MINERALS (EXCL COAL PETROLEUM AND PRECIOUS	-8.84	-13 51
CRUDE ANIMAL AND VEGETABLE MATERIALS	111	1 72
ELECTRICAL MACHINERY, APPARATUS AND APPLIANCES	119	1821
FRUITS AND VEGETABLES	-731	-11 18
FLOOP. COVERINGS	21 36	3268
FOOTWEAR	72.03	110.17
IRON AND STEEL	-353	-5 4
JUTE MANUFACTURES	-1 13	-1 74
LEATHER, LEATHER MANUFACTURES RES AND DRESSED FUR SKINS	22.55	3449
MANUFACTURES OF METALS N E S	3991	53 39
MACHINERY OTHER THAN ELECTRIC	17 12	26.2
OIL MEALS	1 84	281
SPICES	-0 95	-1 46
TEA	6 3	9 63
TRANSPORT EQUIPMENT	2296	35.12
TOBACCO	-85	-1301
PEARLS AND PRECIOUS STONES UNWORKED OR WORKED	227.54	347.6
	9 711	1485
MARINE PRODUCTS		
METALL1FERROU3 ORES AND METAL SCRAP	-11 91	-1821
NON FERROUS METALS	0.04	0 32
TOTAL	705.09	978 23

Table 4 A: QUOTA COMPARISONS FOR THE PRE AND POST EC 92 (TEXTILES)

(FIGURES IN METRIC TONNES)

CATEGORY	AGG. NATIONAL QUOTAS ADJUSTED FOR GROWTH FACTOR 1992	EC WIDE QUOTA 1993
1	33423	33599
2	46319	48150
. 9	NR	6950
20	11506	11664
39	3007	3062

NR: NON RESTRICTED

SOURCE: Cotton Textiles Export Promotion Council (TEXPROCIL)

TABLE 4B: QUOTA COMPARISONS FOR THE PRE AND POST EC 92 - (APPAREL)

	AGG. NATIONAL QUOTAS ADJUSTED FOR GROWTH FACTOR	EC WIDE QUOTA
Category	1992	1993
4	35566	36505
5	22596	23134
6	5146	5269
7	48426	48779
. 8	33676	34044
15-b	3831	3939
26	11474	11584
27	10354	10553
29	6286	6436

Source: Apparel Export Promotion Council (AEPC).

TABLE 5A: QUOTA UTILISATION RATES PRE AND POST EC 92 PERIODS (TEXTILES)

Category	1987	1988	1989	1990	1991	1992	I993
1	NR	0.45	0.43	1.08	0.99	1.03	1.08
2	1.01	0.86	0.82	1.11	1.01	1.01	1.12
9	NR	NR	NR	NR	.	NR	0.67
20	0.45	0.66	0.66	1.04	1.04	1.10	1.12
39	0.14	0.19	0.18	0.28	0.32	0.41	0.61

NR; NON RESTRICTED

SOURCE : Cotton Textiles Export Promotion Council (TEXPROCIL)

TABLE 5B: QUOTA UTILISATION RATES PRE AND POST EC 92 PERIODS (APPAREL)

Category	1987	1988	1989	1990	1991	1992	1993
4	1.06	0.94	1.17	1.24	1.06	1.10	1.09
5	NR	NR	0.84	1.04	1.04	1.01	1.06
6	1.00	0.98	1.06	1.09	0.89	0.85	0.97
7	1.08	0.95	1.03	1.13	1.03	0.99	1.04
8	1.09	1.09	1.55	1.08	1.08	1.05	1.10
15-b	0.68	0.63	0.5	0.37	0.35	0.27	0.23
26	1.05	0.79	0.73	0.89	1.02	1.04	1.04
21	1 10	1.08	0.97	0.98	0.79	0.73	0.96
29	1.14	0.98	1.03	0.99	0.68	0.42	0.31

NR : NON RESTRICTED

Source: Apparel Export Promotion Council (AEPC).

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