Should India Review or Re-negotiate the existing RTAs/FTAs with Japan, Korea and ASEAN; the Steel Perspective.

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India's experience with RTAs/FTAs has not been very encouraging over the years. The country has recorded a trade deficit in all major trade agreements with the only exception of South Asia Free Trade Agreement (SAFTA). Based on different studies it was found that India's exports to FTA countries has not outperformed overall export growth or exports to rest of the world. India's trade deficit in all products with ASEAN, Korea and Japan has widened significantly in post-FTAs period and has remained one-sided from its inception stage till date.

In terms of the steel, Japan and Korea, pose serious challenges for Indian steel industry. Both the countries have large surplus capacities in steel making. The two countries also have a very high exports to production ratio. Exports of semi-finished and finished steel products as a percentage of crude steel production is recorded to be as high as 40 percent. Japan and South Korea has witnessed demand saturation, where the demand for steel products is expected to decline in both medium and long run.

Production, Consumption and Exports of Japan and South Korea

(Value Million Metric Tonnes)

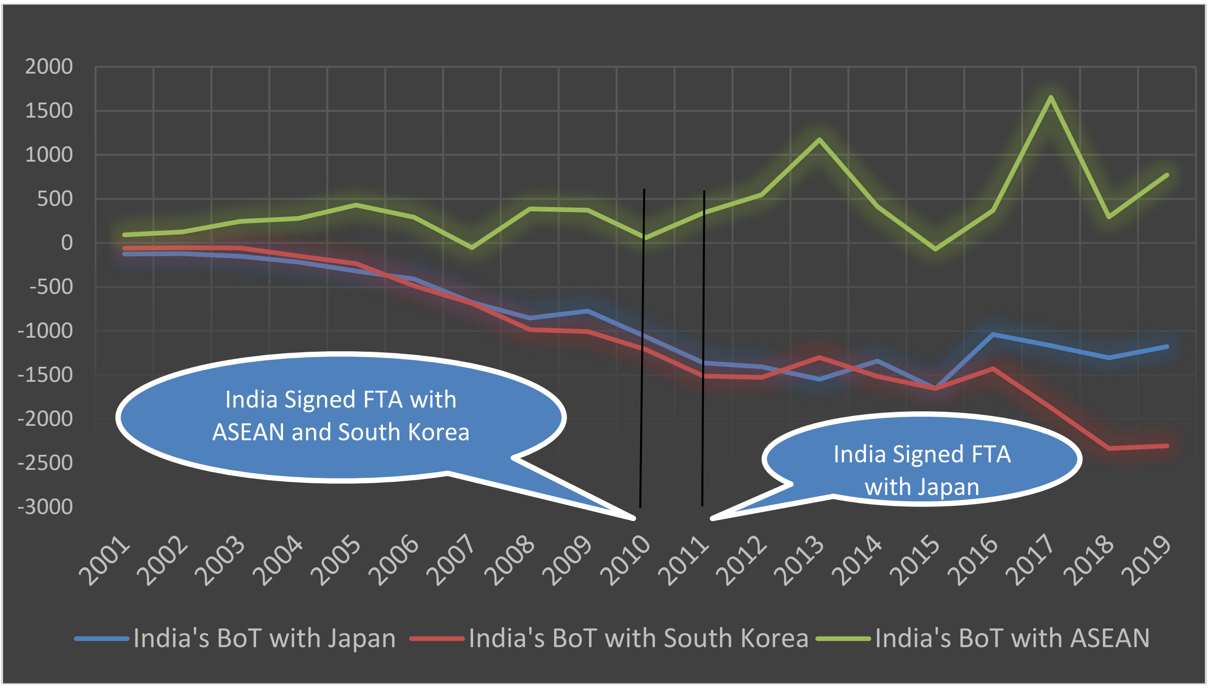
	Global Ranking in Terms of Crude Steel Production (2019)	Crude Steel Production (2019)	Apparent Steel Use (Consumption) (2019)	Surplus	Exports of Semi-finished and Finished Steel Products (2019)
Japan	3	99.3	69.8	30%	33.1
South Korea	5	71.4	55.4	22%	30.0

Source: Authors calculation based on the data of World Steel Association

Post-FTA, combined steel exports from Japan and Korea to India recorded an increase of around 71 percent to 3.8-MnT in 2019-20. On the other hand, exports from India to both Japan and Korea have remained insignificant. The figure below depicts the clear picture with respect to the one-sided steel trade with Japan and Korea in Post FTA period. In the figure the Balance of Trade (BoT) in steel products has deteriorated since the inception of the FTAs with both Japan and Korea.

Balance of Trade in Steel Products* with Japan, ASEAN and South Korea

(Value in USD Million)



Source: Authors Calculation based on ITC Trade Maps Data

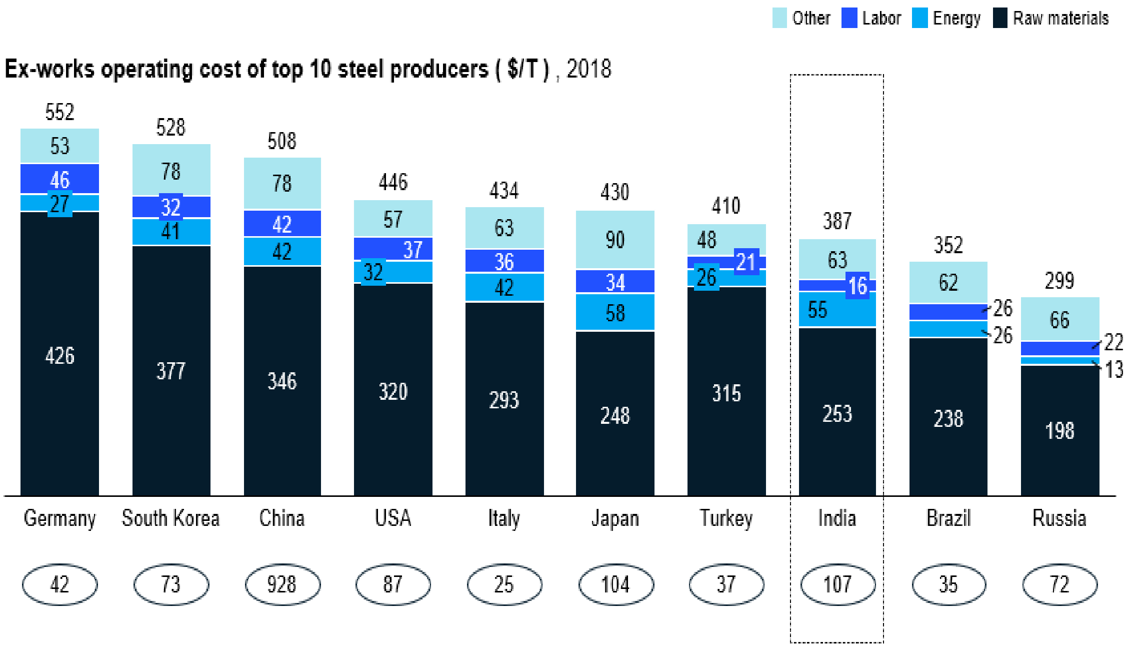
**For calculating the BoT in steel products, selected products at HS 4-digit level were chosen (From HS: 7206 to HS: 7306) as mentioned in the EXIM bank's occasional paper no. 172 titled "Indian steel industry: export prospects"*

It is also argued that more than 90% of these imports from Japan and Korea are within the capacity and the capability of Indian steel industry and imports are purely a fallout of price differentials.

With respect to the ASEAN India has a surplus trade in steel products, however there are concerns with respect to the compliance of rules of origin and high Chinese investment in steel plants in ASEAN countries. Apart from that India has a disparity of tariff concession with ASEAN. India has reduced its duty to NIL on all imports from ASEAN under Chapter 72 (Iron and Steel), however, ASEAN countries have not reciprocated the same treatment for exports from India. This disparity of duty concession has results in a disadvantage to exports from India to ASEAN.

The Indian steel industry is considered highly competitive up to the factory gate. In 2016, World Steel Dynamics ranked India second in terms of cost of conversion of iron ore to steel, after Ukraine. Indian mills were found to be more cost efficient in converting iron ore to steel than their counterparts in China, Japan or Korea.

Ex-works operating cost for India is lowest among top steel producers in the world



Source: NITI Aayog

Despite being more efficient India is still saddled with various structural deficiencies in the form of; high cost of finance and power, cost of logistics, incidence of various non-creditable taxes and duties. All these deficiencies cumulate to a cost dis-advantage of approx. US$80-100 per tonne as per NITI Aayog. For details see the table below.

Cost Difference for Indian Steel Mills vis-à-vis Other Countries (USD/Ton)	
Logistics and infrastructure	25–30
Power	8–12
Import duty on coal	5–7
Clean Energy Cess	2–4
Taxes and duties on iron ore	8–12
Finance	30–35
Total cost disadvantage	**80–100**

Source: NITI Aayog

Most of the industry experts believe that there is a need for Level Playing Parity for Indian Steel Industry vis-à-vis Imports.

Apart from the cost difference the need to review or re-negotiate the existing RTAs/FTAs with Japan, ASEAN and Korea also arises due the following;

Price Arbitrage: There exists a strong possibility of price arbitrage due to tariff differential between FTA and Non-FTA partners. In India the FTA has offered market access at a tariff arbitrage ranging between 10% to 12.5% vis-à-vis Non-FTA countries. For example, currently, the tariff arbitrage for HR Coil imports from Japan / Korea works out to US$69 per tonne or approx. ₹5000 per tonne (based on the import price of HR Coil (base grade) @ US$550 per tonne (CFR-India).

Lenient Rules of Origin: Rules of Origin (ROO) is a critical part of the FTA's for conferring the originating status of goods being exported, thereby qualifying for concessional duty under the FTA. Currently the negotiated FTA's have lenient ROO's. For instance, the Indo-Japan / Korea FTA has a Product Specific Rule (PSR). This PSR requires change in Customs Tariff Sub-Heading (CTSH) at 6-Digit level without any value-addition requirements under the general ROO's. Whereas Indo-ASEAN FTArequires value-addition of 35 percent along with change in CTSH at cumulative level across all ASEAN countries irrespective of minimum value-addition in the country of export. The presence of lenient ROO's could be leveraged by non-FTA countries to channelize their exports via these FTA countries by capitalizing the concessional tariffs without adequate value addition.

Safeguard Provision under FTA: It is believed that the safeguard mechanism has been leniently negotiated by India. For instance, the transitional period for bilateral safeguard measures under India-ASEAN FTA was kept only 5-years from the date of duty elimination. It is argued that the transitional period for safeguard under FTAs should be negotiated for a longer period.

It is also argued, that to protect the domestic industry, India can also re-negotiate for the inclusion of the auto-trigger safeguard mechanism to check drastic import surges with its FTA partners. This auto-trigger safeguard mechanism was also proposed by India in RCEP negotiation. According to this mechanism, in case there is a flood of imports, (From the FTA partners) after reaching a certain threshold, the auto-trigger of safeguard duties on the import of concerned product will be initiated. These thresholds can be mutually decided by the two parties in the process of re-negotiation. For instance, South Korea in some of its FTAs has included sector specific safeguards mechanism to protect its agriculture sector. This mechanism provides Korean government the authority (and not to the other FTA partner) to impose the safeguard measure[1] when the aggregate volume of imports of certain identified agricultural products exceeds a trigger quantity set out in the agreement. Another example of the inclusion of trigger safeguard mechanism is of the Free Trade Agreement between the Eurasian Economic Union and the socialist republic of Viet Nam[2].

Further the existing FTA's provide for a cap on safeguard duty to lower of the applied MFN tariff applicable at the time of signing the FTA's or the prevailing applied tariff. This cap should be modified to minimum at prevailing MFN tariff. In addition to the above issues, the exports of seconds and defective steel from the FTA partners qualify for the same level of concessional tariff.

In conclusion, it can be said that FTAs with Japan, Korea and ASEAN have been one-sided from the date of inception. In Post-COVID scenario, the situation has further aggravated, which has adversely impacted millions of jobs at the back of an unprecedented economic meltdown. Given the current situation the government can suspend all such one-sided FTAs till the situation gets normalized with the recovery of economic growth up to certain level.

To suspend the trade through FTA route the government can exercise its powers under Article 11 of India-Japan CEPA, Article 2.9 of India-Korea CEPA and Article 12 and 13 of India-ASEAN CECA by invoking general and security exceptions available under WTO 's GATT framework.

[1] See WORKING PAPER No. 54, Republic of Korea and its Growing FTA Network A study of provisions in Korea's FTAs on access for merchandise goods into its market by V. S. Seshadri
Link: http://wtocentre.iift.ac.in/workingpaper/WorkingPaper54.pdf
[2] See: https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/3455/download