

**India-Japan Economic Partnership: Potentials, Promises and Prospects**

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## **India-Japan Economic Partnership: Potentials, Promises and Prospects**

### **Abstract:**

*When India started the process of negotiating the Comprehensive Economic Partnership Agreement (CEPA) with Japan, this was New Delhi's first Free Trade Agreement (FTA) negotiation with a developed economy. India so far had relied on the WTO led-multilateral trade system. Various interpretations have been given regarding India's departure from its policy of multilateralism and entering into various bilateral and regional FTA negotiations and implementation. There is a general consensus among the economists that India went with the global trend, what they term as the "Spaghetti Bowl" phenomenon: signing bilateral and regional FTAs following the weakening of WTO-led multilateralism. India in this process signed various FTAs. Japan was one such country with which it signed FTA.*

*However, the fact cannot be ignored that when it comes to the India–Japan FTA, in addition to the global trend, it was driven by political compulsions to uplift the abysmally low trade volume between the two strategic partners and it was decided that the economy would be the "bedrock" in the bilateral partnership. This realization led the two countries to forge a stronger economic partnership which will not only be limited to trade in goods but will encompass trade in services, investments and promotion of people-to-people partnership. This study in this context looked into the India–Japan economic partnership, especially after the CEPA coming into effect in 2011. It looks into various questions such as how it has performed, what kind of expectations various stakeholders have had vis-à-vis the CEPA, what it promised to them, what are the potentials of the CEPA and what are their expectations as the CEPA enters into its final phase of tariff elimination.*

*The Study examines two key official documents: the Joint Study Group, which suggested the signing of the CEPA, identifying various complementarities between the two economies and the India–Japan CEPA documents which commit to eliminating various tariffs and offers various incentives for each other's investors. The study finds that the CEPA has achieved mixed results. While on the one hand, the volume of bilateral trade has increased, the Japanese FDI flow towards India is on the rise and so is the number of Japanese companies, on the other hand, the gap in the bilateral trade has widened and the concerns in the media have emerged of the low share of India's*

*trade in bilateral trade volume. At the political level and in the policy circles, concerns of Japan imposing 'non-tariff barriers' have come to the fore. There have been similar concerns about India's performance in other FTAs (such as with South Korea, Singapore and Malaysia) signed around the same time. Concerns have also been raised in various studies conducted by different institutes in India, and some of them have been asking New Delhi to review the FTAs and give a pause to the various bilateral and regional FTAs which are under negotiation. These issues have been analysed in this study below and have been backed by statements and statistics.*

## 1. Introduction

Despite having geographical proximity, a factor that helps propel trade and flow of capital between the two economies, India–Japan economic engagement, especially in the post-war period, was not as robust as it was expected. Various domestic and external factors have been blamed for weak trade and economic links between the two Asian economies. These include India’s decision to put the economy under state control and Japan opting for a liberalized economic system: putting the two Asian economies at odds with each other. India’s tilt, as perceived by Japan, towards the USSR and Japan joining the US-led capitalist world, the diagonally opposite political system, is also blamed as an intervening factor impeding the economic ties between the two countries. However, post 1990s, when India liberalized its economy, and this coincided with USSR’s collapse, it was expected that trade flow will increase manifold between Japan, a major trading power, and a newly liberalized India. But the trade between the two countries remained stagnant and so were the investment flows from Japan towards India.

As Japan was identified as “an important source of both investment and technology,”<sup>1</sup> when India adopted the liberalization process, stagnation in bilateral trade and flow of Japanese FDI, was a cause of concern in New Delhi’s policy circles. In this context, both Indian and Japanese governments constituted a Joint Study Group consisting of various stakeholders, government officials and academic experts to identify the complementarities between the two countries and suggest ways to uplift the bilateral economic ties.

The Study Group after its detailed deliberations identified that there remains a lot of “potentials” between the two countries and if harnessed properly both countries can forge a complementary economic relationship. The Study Group suggested the signing of an Economic Partnership Agreement by the governments of India and Japan. The Economic Partnership Agreement, which concluded in 2010 and came into effect in 2011, was full of “promises” including elimination of tariffs and trade barriers, opening up trade in services and promoting investments. Since it was the most comprehensive Free Trade Agreement New Delhi had ever signed, it generated lots of expectations especially in India. The simulation studies conducted by various economists generated hope about a sizeable jump in the bilateral trade volume. However, almost after a decade of the bilateral CEPA coming into effect, the partnership does not seem to be as bright as projected.

Various concerns, mostly in India from government, policy circles and various stakeholders have been raised including widening trade gaps between India and Japan as well as imposition of various non-tariff barriers by Japan. Since the India–Japan CEPA has not worked up to the expectations of India, it seems cautious to forge such similar bilateral and multilateral agreement, including the RCEP. Naturally, the “prospects” of the CEPA do not look that bright. The paper, in this context tries to understand the evolution of India–Japan economic partnership and identifies the problems it faces and speculates its future.

### **1.1. The Structure of the Paper**

Given the fact that the direction to forge a complementary economic partnership came from a high-level joint committee of the India–Japan Study Group (JSG), the paper examines the recommendations given in the JSG. Then it looks into the CEPA document to compare the recommendation and implementation part as well as the measures the CEPA adopted to promote trade in goods, investment and trade in services between the two countries. Consequent upon examining the two primary sources, the paper looks at various studies to examine what kind of expectations the economists and experts had about the CEPA and how they look at its impacts after it came into effect. In addition to this, the paper maps the narratives that have come to the fore regarding the India–Japan CEPA especially in India and examines the political statements, policy documents and studies conducted by different stakeholders. Since both the JSG and CEPA hoped that following the India–Japan bilateral Free Trade Agreement, India will enter into various regional trade agreements, a section of this paper looks at India’s endeavours to forge similar bilateral and regional FTAs. As many readers may be curious to know the state of trade ties between India and Japan before the CEPA, the paper starts with giving a snapshot on India-Japan trade relations highlighting the evolution of bilateral economic ties. The author employs a political-economy perspective to study the subject which will be useful for policy planners studying this topic.

## **2. India-Japan Trade and Economic Relations in Retrospect**

Even though India signed a Comprehensive Economic Partnership Agreement with Japan in 2011, Japan’s economic ties with India can be traced back to 1894 when the two countries signed a trade

convention. India at that time was still under British administration. The 1894 agreement gave fillip to the cotton trade between the two Asian nations. The trade convention also paved the way for the opening up of the regular ocean transport between India and Japan.<sup>2</sup> By the mid-1910s, India became the third leading trade partner for Japan after the United Kingdom and the United States. In terms of Japanese exports, India by the 1920s became the fifth largest market after China, the United States, Hong Kong and the United Kingdom.<sup>3</sup> The trade and economic ties were mainly driven by resource supply. Apart from the iron ore, other raw materials included supply of raw jute and raw cotton to Japan.<sup>4</sup> In short, much before the onset of World War II, India and Japan had already established complimentary and interdependent economic ties. It was because of the interdependent nature of Indian and Japanese economies that developed during the pre-war years that India wanted to see an economically resurgent Japan following World War II.

Various sources suggest that India was keen for on the economic revival of Japan and offered its raw materials including iron ore needed by Japanese war-weary industries. Indian Prime Minister Jawaharlal Nehru, while meeting a Japanese trade mission, assured them that India would assist as much as possible in sending “raw materials to Japan.”<sup>5</sup>

As mentioned earlier, the domestic and external factors have impacted the growth of India-Japan relations. Despite the good beginning in the early 1950s, both the countries could not take their relations to an upper trajectory as their investors and traders had a very different perception towards each other. The Japanese believed that India has tilted towards the Soviet Union and has adopted a socialist economy<sup>6</sup> and the Japanese businessmen viewed Indian economic policies as “un-realistic and non-pragmatic.”<sup>7</sup>

Sakutaro Tanino, a Japanese ambassador to India beautifully summed up the nature of the bilateral economic relations that existed during the entire Cold War period. Tanino noted that India’s special relationship with the USSR and Japan’s security engagement with the US “eventually resulted in the cooling-off of the great enthusiasm of the 50s.”<sup>8</sup> The Official Development Assistance (ODA)<sup>9</sup> and the entry of some of Japanese companies into the Indian market, including Suzuki,<sup>10</sup> are the only examples which sustained the bilateral economic relationship during the Cold War period.

As India initiated economic reform in 1991,<sup>11</sup> “Japan was identified as one of the most important sources of both investment and technology by the government of India.”<sup>12</sup> The Japanese side also



viewed “economic liberalization” as a “return to the inspiring phase” of India-Japan relations.<sup>13</sup> But Japanese investors were not satisfied with the pace and extent of India’s economic liberalization and thus there has been no “quantum jump in Indo-Japanese economic relations. In fact, expansion and growth patterns have been cautious and gradual.”<sup>14</sup> Japanese automotive firms such as Honda and Toyota set up factories in India in 1994 and 1997, respectively. But the Japanese electronics giants did not show similar enthusiasm in the Indian market.<sup>15</sup>

Despite the slow paced growth in economic and trade ties, political partnership between the two Asian nations was growing at a much faster pace. A “global partnership” envisioned during Japanese Prime Minister Yoshiro Mori’s New Delhi visit in 2000, transformed into a strategic and global partnership during Prime Minister Junichiro Koizumi’s visit in 2006. The economic relationship was an essential component of this partnership.<sup>16</sup> A joint statement signed by Japanese Prime Minister Koizumi and his Indian counterpart Manmohan Singh noted that “a strong, prosperous and dynamic India is in the interest of Japan and vice versa.”<sup>17</sup> But the economy still remained a weak link and Indian Prime Minister Manmohan Singh acknowledged in his address to the Japanese Diet that economic ties should be the “bedrock”<sup>18</sup> of the Indo-Japan relationship. He also noted that economic ties between the two countries remain “well below the potential.”<sup>19</sup> As a result of strategic talks, the Indian and Japanese governments agreed in 2005 to set up a Joint Study Group to study areas in which both the countries could complement each other and give fillip to their stagnant economic ties.

### **3. The Prelude to CEPA: The Potentials Identified by Joint Study Group**

The Joint Study Group consisting of government officials, stakeholders and academic experts had rounds of discussions to assess the status of India-Japan bilateral economic relations and evaluated its future potential. It also studied hurdles in free trade between India and Japan and recommended the possible remedies to overcome those hurdles. It found that there exists immense potentials in the fields of trade, investment and other areas of bilateral cooperation.

The JSG, in its findings, noted that the economies of both the countries are “highly complementary in terms of factor endowments, capabilities, demographic profiles, convergences and specializations.”<sup>20</sup> Moreover, it hoped that India’s “cost-effective human resources may complement growing labour scarcity and rising wages.”<sup>21</sup> It also highlighted complementarities in

India's software prowess and Japan's strong capacity in IT hardware. It also noted that "India's capabilities in pharmaceutical industry, biotechnology, and auto components usefully complement Japanese competence in heavy engineering, automobiles, machinery and chemical industry."<sup>22</sup> The group also pointed to the complementarity between India and Japan given that the earlier is a major producer of agricultural products and the latter "imports more than 50% of its food requirements."<sup>23</sup> It also looked into India's huge infrastructure requirements and observed that Japan can establish a complementary relationship in this field "facilitating trade, investment and technology transfer between them."<sup>24</sup> As regards the FDI, the Joint Study Group stated that FDI is "an instrument for economic development." Even though it is growing since 1991, it constitutes only 7% of the total FDI flow to India, and added in the report and expressed concern that it is "far less than the actual potential."<sup>25</sup> Further, it noted that "the huge size of the market and skilled manpower available in India can provide a fertile ground for FDI by the capital abundant economy of Japan."<sup>26</sup>

Notably, as regards the trade, the JSG found that even though the bilateral trade between India and Japan is on the rise (approximately USD 6.8 billion in 2005), the trade figure was not "commensurate with the two countries' economic size and potential."<sup>27</sup> It also noted that bilateral trade has stagnated "despite unilateral trade liberalization in India" and noted that "there is a great deal of potential for expanding bilateral trade in goods."<sup>28</sup> Given the high tariff in India, the JSG suggested "tariff reduction and possible elimination"<sup>29</sup> consistent with the WTO rules. It hoped that these measures will "increase market access opportunities for both countries."<sup>30</sup> The JSG also noted that the Indian side expressed strong interest in the expansion of market access for the agricultural and food products in which "India has competitive edge."<sup>31</sup> To facilitate trade in the agricultural sector, the JSG suggested various measures including "customs cooperation," utilizing "Export Inspection Council of India," and more importantly "exploring the possibility of... a new mechanism on SPS-related issues in a joint consultation group..."<sup>32</sup>

As regards the trade in services sector, the JSG identified "enormous potential" between the two countries and suggested both the governments to "remove barriers to trade in services" adding emphasis to cover "all services sectors and all modes of supply in GATS."<sup>33</sup> It also highlighted that "services liberalization should be designed to enhance the competitiveness of each economy"

and special emphasis should be given on areas such as “IT, financial services, telecommunication services, construction services and transportation services.”<sup>34</sup>

As India was interested in attracting more FDI from Japan, the JSG also noted “tremendous investment opportunities in India” for Japanese companies and recommended both governments conclude an “investment agreement to address a wide variety of issues including national treatment, transparency, facilitation, investment promotion, protection and dispute settlement.”<sup>35</sup>

The JSG noted that the lack of human exchange between the two countries and suggested both governments enhance “people-to-people exchanges” hoping that it will provide a basis for “stronger bilateral economic ties.”<sup>36</sup>

In the light of their comprehensive study and existing trade potentials, the JSG suggested conclusion of a Comprehensive Economic Partnership Agreement which will provide a “proper architecture for bilateral economic engagement” between the two countries. The JSG, without naming RCEP, also hoped that “an EPA/CEPA will also serve as a building block for an even larger regional economic integration.”<sup>37</sup>

In its final recommendation, the JSG suggested the negotiation of a CEPA covering trade in goods and in services, measures for trade promotion, liberalization of investment flows and other areas covering a comprehensive economic partnership between India and Japan.

#### **4. India-Japan Economic Partnership Agreement: The Promises**

Following the recommendation of the Joint Study Group, India and Japan formally started discussing the modalities of an Economic Partnership Agreement (EPA) also termed a Comprehensive Economic Partnership Agreement (CEPA). As it covered wider areas and were not limited to trade in goods, it took a long time to be concluded. The negotiation on the CEPA concluded in 2010 and both the countries formally signed the CEPA in Tokyo on February 16, 2011 which came into effect from August 1, the same year. The CEPA covered trade in goods and services, movement of natural persons, investment, intellectual property rights, custom procedure and other trade-related issues.<sup>38</sup> The areas covered in the India-Japan CEPA were almost identical to the areas suggested by the Joint Study Group which saw many complementarities and potentials between the two countries in these fields. Notably, the CEPA’s preamble states that India-Japan

“bilateral relationship will be enhanced by forging mutually beneficial economic partnership through liberalization and facilitation of trade and investment.”<sup>39</sup> Moreover, the CEPA noted that “the economic partnership will create larger and new market, enhance attractiveness and vibrancy of their markets, and contribute to improving efficiency and competitiveness of their manufacturing and service industries.”<sup>40</sup> The document hoped that the CEPA will “open a new era of relationship” between the two countries and would “contribute to expanding trade and investment not only between the two parties but also the region.” The reference to the “region” here was an apparent reference to East Asia and the creation of a trade bloc of ASEAN + 3 + 3 (later named RCEP) of which the two countries are important members. In this context, some of the important objectives identified by the countries in the CEPA are as follows:

- a) to liberalize and facilitate trade in goods and services
- b) to increase investment opportunities and strengthen protection for investment and investment activities
- c) to ensure protection of intellectual property
- d) to promote cooperation for the effective enforcement of competition laws
- e) to improve business environment<sup>41</sup>

The agreement made a commitment to “eliminate or reduce its custom duties on originating of other Party”<sup>42</sup> and laid the terms and conditions for the elimination of the custom duties. The document has classified goods traded between the two countries in separate schedules and has divided them into seven categories. The goods are marked as A, B5, B7, B10, B15, Pa/Pb and X. Custom duties on goods identified as “A” has been eliminated from the date of entry into force of the CEPA, that is August 16, 2011. The custom duties on goods identified as “B5,” “B7,” “B10,” “B15,” will be eliminated in 6, 8, 11 and 16 years, respectively. The custom duties on goods identified as Pa and Pb shall be reduced in accordance with the terms and conditions set out in respective notes indicated in the Schedule of India. However, there would be no duty elimination on goods indicated as X.<sup>43</sup>

Some of the goods on which both countries will remove tariff in phases have been indicated in Table 1.

**Table 1. Selected list of goods on which tariffs would be eliminated gradually**

| Period over which tariff has to be reduced | Goods Description  |  |
|--|--|--|
|  | Schedule of India  | Schedule of Japan  |
| Immediate                                  | <ul style="list-style-type: none"> <li>• Most textile products including yarn and fabric</li> <li>• Computer printers, PCs and other automatic data processing machines</li> <li>• Cell phones and other types of phones, networking equipment and SIM cards</li> <li>• Capacitors, diodes, specified measuring instruments</li> </ul> | <ul style="list-style-type: none"> <li>• Specified petroleum products</li> <li>• Ores, slag and ash</li> <li>• Inorganic chemicals and specified organic chemicals</li> <li>• Machines – mechanical and electrical and parts thereof</li> <li>• Most textile and textile products</li> </ul> |
| Seven years                                | <ul style="list-style-type: none"> <li>• Lubricating oil</li> </ul>  | <ul style="list-style-type: none"> <li>• Specific types of fish and fish meat</li> </ul>   |
| Ten years and above                        | <ul style="list-style-type: none"> <li>• Specified petroleum products</li> <li>• Most metals and articles thereof</li> <li>• CDs, DVDs, watches, musical instruments</li> <li>• Arms and ammunition</li> <li>• Certain types of furniture</li> </ul>   | <ul style="list-style-type: none"> <li>• Specified iron and steel products</li> <li>• Certain fruits like oranges, apples, grapes</li> </ul>   |

**Source: CEPA pages 105 to 961/CII Study on India-Japan relations**

As a result of the CEPA coming into effect, some 17.4 % of the tariff lines have been reduced to 0% by India while the Japan side has put 87% of its tariff lines under immediate reduction to zero.<sup>44</sup> The official CEPA document has laid down rules for elimination of custom duties in Article 19.<sup>45</sup> It may be noted that Japan was already putting low tariffs on various products to comply with WTO norms.

To attract Japanese investment in India, the CEPA has given Japanese investors a kind of “national treatment” in the areas of goods (Article 18) in accordance with GATT,<sup>46</sup> in market access (Article 60) as well as in the investment. The provision related to investment in the CEPA states:

Each Party shall accord to investors of the other Party and to their investments treatment no less favourable than that it accords like circumstances to its own investors and to their investments with respect to investment activities in its Area.<sup>47</sup>

In addition to the National Treatment, both the countries have granted The Most Favoured Nation status to each other’s investors (Article 86)<sup>48</sup> under the CEPA. It seems, it was a calibrated move by the two governments to give this status given the fact that Japanese investors had largely been confined to East Asian and Southeast Asian countries. With the national treatment extended to

each other's investors, the investors now enjoy access to courts and tribunals of the host country in case of a trade and investment-related dispute.<sup>49</sup> This simply means that a foreign investor can now enjoy the right to sue the government if their rights and profit are infringed upon.<sup>50</sup> In case they are not satisfied with the domestic arbitration process they can approach the international bodies for adjudication (Article 96 of CEPA).<sup>51</sup>

The CEPA has also removed any performance-related requirement for the investors in the host country. The bilateral document notes that no party can impose requirements related to export at a given level or percentage of goods or services. Moreover, they cannot be forced to achieve a given level of domestic content.<sup>52</sup> Ranja Sengupta argues that “countries usually impose performance requirements on foreign investment such as limits on ownership, board membership, and on exports; compulsory local content, etc. But under the CEPA, these restrictions are no longer permissible.”<sup>53</sup>

As the CEPA was under discussion, it was being speculated that Japan may grant some relaxation to India in terms of Technical Barriers to Trade (TBT) and in terms of Sanitary and Phyto Sanitary (SPS) measures. But the final CEPA maintained that the TBT and SPS will apply as per the WTO Agreement.<sup>54</sup> But both the parties agreed to form a sub-committee which will undertake “consultations on issues related to technical regulations.” The committee will also undertake consultations to “identify and address specific issues that may arise from the application of SPS measures.”<sup>55</sup> Considering India's demand to allow access of its generic medicine in the Japanese market, the bilateral agreement noted to “exchange information concerning generic medicine” adding that the two parties would promote cooperation in this field.<sup>56</sup>

India had been demanding from a long time from Japan to allow its rice including basmati rice to Japan but during the negotiations, New Delhi agreed to put rice sector under the “exclusion” list. In the concluded CEPA, rice has been put in “X” category meaning there would be no tariff relaxation for India.<sup>57</sup> However, a similar FTA signed with Malaysia, India has successfully bargained for allowing rice imports into Malaysia. It seems India considered the sensitivities of Japanese farmers who remained opposed to opening these sectors. As India and Japan were negotiating the CEPA, Japan was considering joining the Trans Pacific Partnership (TPP). The Japanese farmers were opposing Japan's participation in the TPP as they were wary that the

multilateral trade treaty will allow inflow of cheaper rice from the TPP member countries, affecting their livelihood.

Another concession India made was related to nurses and caregivers. Even though the CEPA allows movement of natural persons and highly skilled persons, India was expecting that Japan will allow entry to its nurses and caregivers into Japan with a long-term work permit. New Delhi was demanding treatment to its caregivers at par with Indonesia and Philippines, with whom Japan has also signed Economic Partnership Agreements. But the Japanese side asked India to wait as it is facing some problems as the nurses from these countries have not been able to pass the necessary language tests after their two-year probations. The CEPA in this regard noted that “Japan shall enter into negotiation with India... regarding the acceptance of Indian qualified nurses and certified care workers by Japan, with a view to reaching a conclusion of the negotiations within one year if possible, but not later than two years, after the entry into force of this Agreement.”<sup>58</sup> More than seven years have elapsed ever since the signing of the CEPA, but both the parties did not renew their negotiation. This means that India lost the opportunity to forge a strong people-to-people contact that could have resulted following the conclusion of this agreement. As mentioned earlier, the JSG had suggested that both the governments enhance “people-to-people exchanges” hoping that it will provide a basis for “stronger bilateral economic ties.” Even though the Japanese government was reluctant to accede to India’s demand in this regard, a section of the Japanese media had urged its government to make “concessions” to India on this point. The *Yomiuri Shimbun* in its editorial demanded that “to deepen economic partnership between this country and India, Japan should make concessions.”<sup>59</sup> The CEPA, however, facilitates the flow of “natural persons” and paves the way for employment opportunities in Japan and India for each other’s citizen. Subsequent upon this development, both the countries signed a Social Security Agreement in May 2012. Under this agreement, the Japanese and Indian workers employed on short-term contracts in each other’s territory need not pay into the pension schemes of both the countries. This had hampered the human exchange “imposing an additional burden on individuals and corporations.”<sup>60</sup>

On India’s part, it demanded stricter rules of origin apparently not to allow the benefits of the CEPA to a third country. It allowed the goods of originating countries (India and Japan in this case) but restricted the goods produced using non-originating materials having value content less

than 35% and a change in tariff classification at the six-digit level of the Harmonized System.<sup>61</sup> This criterion is not applicable to all products. Different rules are applied on some products under the product-specific rule. This makes the rule of origin criteria more complex. Japan's Ministry of Economy Trade and Industry (METI) has brought to the notice of officials in New Delhi about the problem faced by Japanese exporters in getting Certificates of Origin because of this strict criteria and has demanded to ease such restrictions.<sup>62</sup>

## **5. CEPA: The Prospect**

Both the Indian and Japanese leaderships have attached high hopes to the bilateral economic partnership engagement. This is evident from the joint statement issued by Indian Prime Minister Manmohan Singh and his Japanese counterpart Naoto Kan in October 2010 after the conclusion of the CEPA agreement. The statement expressed confidence that bilateral agreement “will develop areas of potential mutual complementarity, further strengthen the bilateral economic relationship, and promote economic development by increasing the cross-border flows of goods, persons, investment and services.”<sup>63</sup> Moreover, both were hopeful that the agreement will “strengthen the foundation for the economic development of India and Japan.”<sup>64</sup> Both the leaders exuded confidence that India and Japan “will be able to make maximum use of respective competitive advantages to promote the development of both economies. This will bring about increased prosperity and stability to the peoples of both countries, and thus, contribute to the peace and prosperity of the Asian region and the international community.”<sup>65</sup>

Consequent upon the expectations raised by the CEPA, various simulation studies projected high potentials of CEPA. One of the simulation studies based on Computable General Equilibrium (CGE) analysis concluded that “tariff reduction will increase India's export to Japan by 18.25%, while for Japan it will be only 4.65%.”<sup>66</sup> As for the welfare effect, the Study noted that “simulation results suggest a positive net welfare gain for both countries with an expected gain of USD 1198.67 million and USD 120.27 million for India and Japan, respectively.”<sup>67</sup> India will gain more than Japan if CEPA is materialized by 2020, the study emphasized.

B.S. Raghavan, a columnist with the *Business Line*, argued that “there is a great responsibility cast on both India and Japan to make a success of it so that it becomes a path setter for CEPAs with other developed countries.”<sup>68</sup> He cites a simulated computer study to suggest that India's GDP can

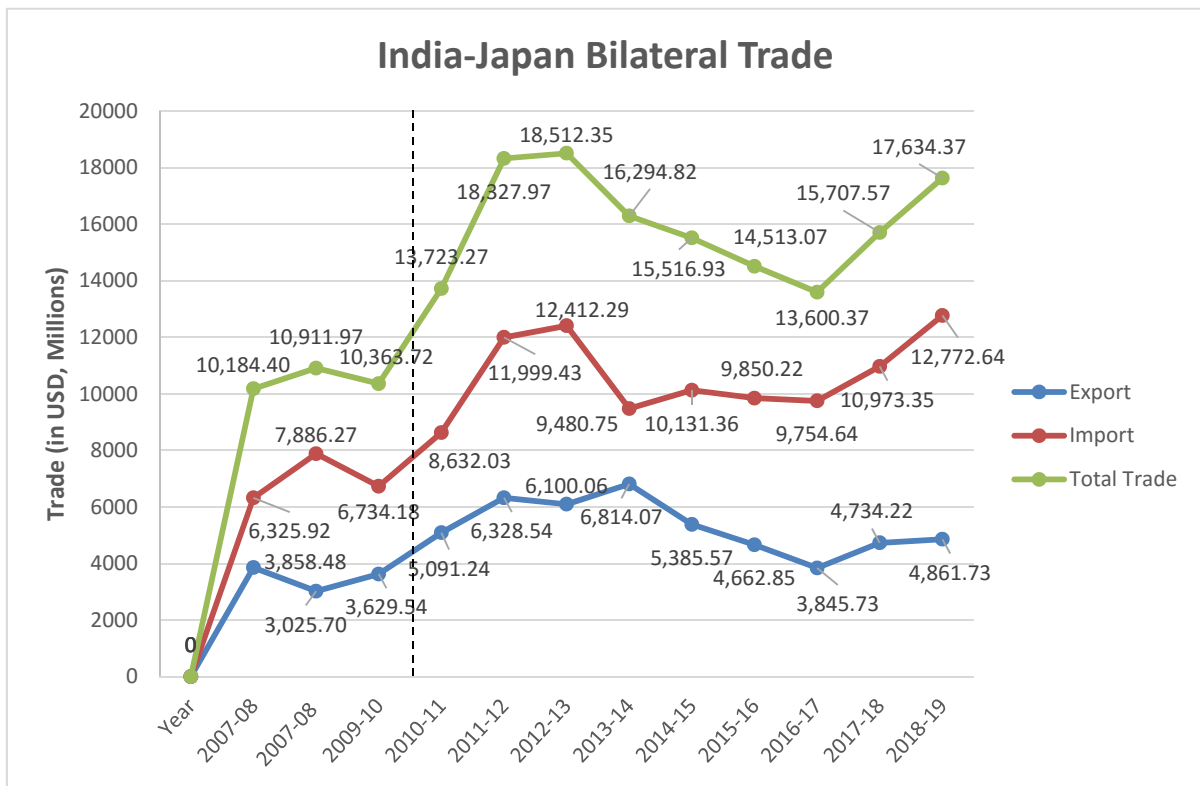


grow by as much as 3.45% if New Delhi signs similar agreements with ASEAN countries and its dialogue partners.<sup>69</sup> C.P. Ravindaran, however, was of the view that the gains from the India-Japan CEPA “will come eventually through competition with more efficient producers on the one hand and in demanding markets, on the other.” He adds that the CEPA, through its free trade provisions, holds such possibilities for India.<sup>70</sup>

Other experts, however, cited some caution on over-optimism and expectations related to the CEPA. They noted that despite the CEPA easing the duties on goods, Indian exports will continue to face some non-tariff barriers such as standards and technical barriers. The Indian producers will have to match with standards set by Japanese importers.<sup>71</sup> Geethanjali Nataraj, points that “Japan’s Sanitary and Phytosanitary Measures (SPS) standards are major barriers for Indian exports of poultry, meat, tuna, shrimp, marine products and fruits”. She suggests that both the countries should share and facilitate “the underlying technology” to help improve Indian products sanitary standards.<sup>72</sup> Similarly, Kaliappa Kalirajan and Swapan Bhattacharya noted that there remain “behind the border” constraints in India-Japan trade and the growth in trade can take place when these constraints are eliminated.<sup>73</sup> Ambassador Arjun Asrani, who was part of India-Japan Joint Study Group which recommended negotiation on a CEPA between the two countries, however, believes that the inclusion of a large number of goods in the negative list would remain an impediment in the wider trade flows between the two countries.<sup>74</sup>

The most positive impact of the CEPA on India- Japan relations could be seen in the trade and investment fields. The CEPA has certainly boosted bilateral trade which was well below potential. In FY2010-11, trade between the two countries stood at around USD 13.4 billion. However, in FY2011-12, within months of the CEPA coming into effect, it touched USD 18.3 billion (See graph 1 below). It saw some downward trends two years after the CEPA’s implementation. But during the last two fiscal years it has witnessed an upward trend and at present stands at USD 17.63 billion. As the CEPA is entering into the final phase of tariff elimination, the bilateral trade is likely to grow further.

**Graph 1: India-Japan Export and Import Data**















**Source: Ministry of Commerce and Industry, Government of India**

**(The dotted vertical line indicates the year of CEPA’s implementation)**

The positive impact of the CEPA could also be seen on the growing Japanese investment in India. As the CEPA promises lots of incentives including national treatment that has been mentioned in the above section, various Japanese companies have been established or are keen to establish their production bases in India. Various surveys conducted by Japan Bank of International Cooperation (JBIC) suggest that India maintains the top position as the future investment destination for Japanese investors. A 2018 survey conducted by JBIC suggests that India maintains the second most favoured destination by the Japanese investors in the medium term followed by China. The gap between the two, however, remains only of 6%. (See table 2 below)

**Table 2: Promising Countries/Region for Business Development for Medium Term – FY2018**

**Results**

| Ranking |   |      | Country/Region<br>(Total) | No. of Companies |             | Percentage Share (%) |      |
|---------|---|------|---------------------------|------------------|-------------|----------------------|------|
| 2018    | ←   | 2017 |                           | 2018<br>431      | 2017<br>444 | 2018                 | 2017 |
| 1       | —   | 1    | China                     | 225              | 203         | 52.2                 | 45.7 |
| 2       | —   | 2    | India                     | 199              | 195         | 46.2                 | 43.9 |
| 3       |    | 4    | Thailand                  | 160              | 153         | 37.1                 | 34.5 |
| 4       | —   | 3    | Vietnam                   | 146              | 169         | 33.9                 | 38.1 |
| 5       | —   | 5    | Indonesia                 | 131              | 147         | 30.4                 | 33.1 |
| 6       | —   | 6    | US                        | 124              | 116         | 28.8                 | 26.1 |
| 7       | —   | 7    | Mexico                    | 59               | 81          | 13.7                 | 18.2 |
| 8       | —   | 8    | Philippines               | 43               | 47          | 10.0                 | 10.6 |
| 9       |    | 9    | Myanmar                   | 37               | 40          | 8.6                  | 9.0  |
| 10      |   | 12   | Malaysia                  | 36               | 26          | 8.4                  | 5.9  |
| 11      |  | 16   | Germany                   | 25               | 13          | 5.8                  | 2.9  |
| 12      |  | 10   | Brazil                    | 24               | 28          | 5.6                  | 6.3  |
| 13      | —   | 10   | Korea                     | 22               | 28          | 5.1                  | 6.3  |
| 14      |  | 14   | Taiwan                    | 19               | 17          | 4.4                  | 3.8  |
| 15      |  | 13   | Russia                    | 16               | 19          | 3.7                  | 4.3  |
| 16      |  | 14   | Singapore                 | 15               | 17          | 3.5                  | 3.8  |
| 17      |  | 20   | Cambodia                  | 13               | 9           | 3.0                  | 2.0  |
| 18      |  | 18   | Australia                 | 12               | 10          | 2.8                  | 2.3  |
| 19      |  | 17   | Turkey                    | 9                | 12          | 2.1                  | 2.7  |
| 20      |  | 23   | Laos                      | 7                | 5           | 1.6                  | 1.1  |
| 20      | —   | 32   | France                    | 7                | 2           | 1.6                  | 0.5  |

Source: JBIC

Interestingly, when it comes to “long term” investment destination, India becomes the top most destination surpassing China. The gap between India and China in terms of being a long-term investment destination also remains high. It is more than 12% (See Table 3). As India was keen to draw more FDI as a result of the CEPA, it seems the bilateral trade is serving that objective seen from the Indian perspectives.

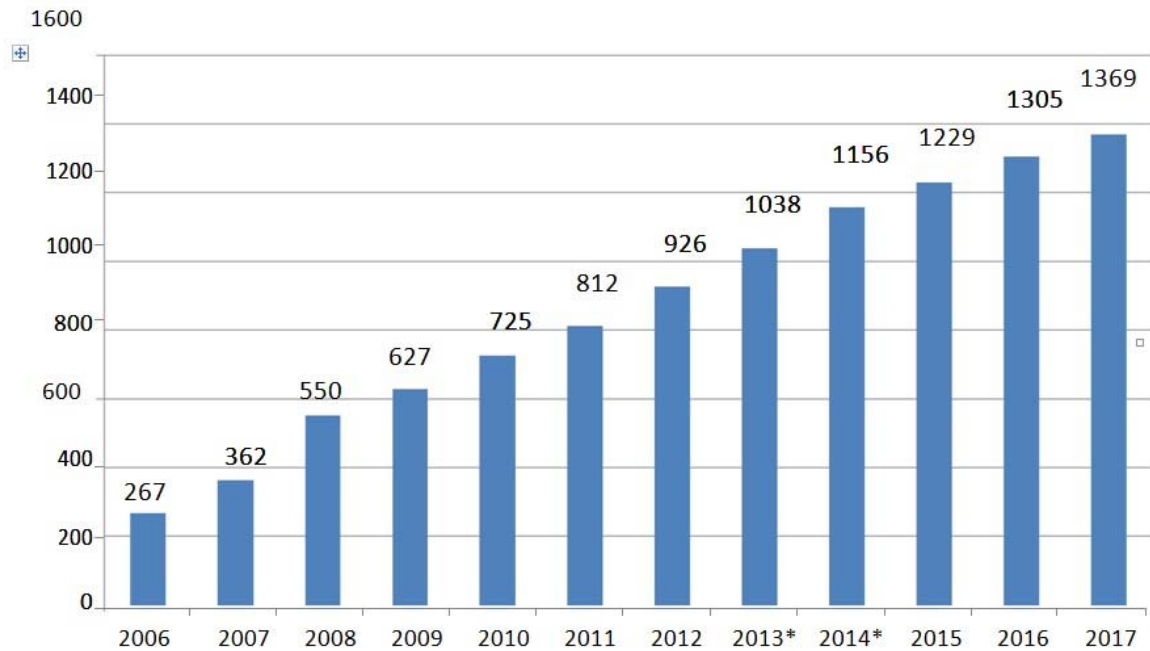
**Table 3: Promising Countries/Region for Business Development for Long Term – FY2018 Results**

| Ranking |        |    | Country/Region<br>(Total) | No. of Companies |             | Percentage Share (%) |      |
|---------|--------|----|---------------------------|------------------|-------------|----------------------|------|
| 2018    | ← 2017 |    |                           | 2018<br>350      | 2017<br>337 | 2018                 | 2017 |
| 1       | —      | 1  | India                     | 205              | 214         | 58.6                 | 63.5 |
| 2       | —      | 2  | China                     | 164              | 146         | 46.9                 | 43.3 |
| 3       | —      | 3  | Vietnam                   | 115              | 115         | 32.9                 | 34.1 |
| 3       | ↑<br>— | 4  | Indonesia                 | 115              | 109         | 32.9                 | 32.3 |
| 5       | —      | 5  | Thailand                  | 105              | 80          | 30.0                 | 23.7 |
| 6       | —      | 6  | US                        | 76               | 78          | 21.7                 | 23.1 |
| 7       | —      | 7  | Myanmar                   | 41               | 48          | 11.7                 | 14.2 |
| 7       | ↑<br>↑ | 8  | Mexico                    | 41               | 45          | 11.7                 | 13.4 |
| 7       | —      | 9  | Brazil                    | 41               | 43          | 11.7                 | 12.8 |
| 10      | —      | 10 | Philippines               | 30               | 33          | 8.6                  | 9.8  |

**Source: JBIC**

The JBIC survey seems consistent with the actual investment and the growing number and presence of Japanese companies in India. The number of Japanese companies have been increasing ever since the signing of a bilateral strategic partnership in 2006, albeit slowly. The 2017 figure, released by the Japanese embassy in India, shows that the number of these companies touched 1369. However, this is a positive trend, as in 2006, there were only 267 Japanese companies in India. The signing of the CEPA, which promises lots of incentives to the Japanese establishments, seems to have generated Japanese interests in the Indian market and as a result Japanese companies in India are growing.

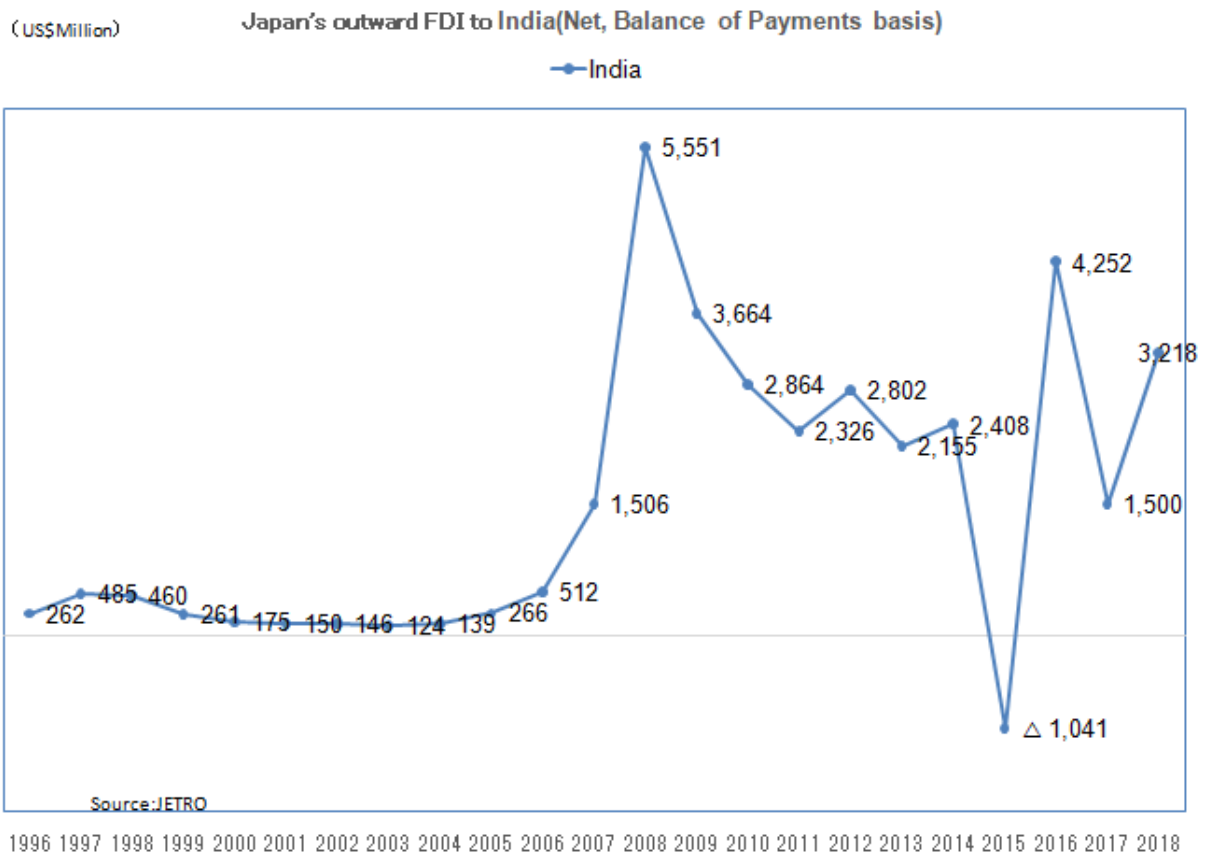
**Graph 2: Number of Japanese Companies in India**



**Growing Japanese industrial footprint in India (Source: Embassy of Japan, New Delhi)**

In terms of the actual flow of Japanese Foreign Direct Investment towards India, there has been inconsistency. In 2001, India attracted Japanese FDI of USD 150 million. Gradually, it reached a peak of USD 5551 million by FY2009. In FY2016–17, India attracted Japanese FDI of USD 4709 million. But by the year 2018, it again dipped to USD 3218 million. Despite the fluctuation in Japanese FDI towards India, Japan continues to maintain its position among the top investors of FDI in India. But India still would have to compete with ASEAN countries in attracting Japanese FDI. Japanese investors find the corporate rate of ASEAN countries much more attractive. The corporate rate in Thailand is only 20%. Naturally, the flow of Japanese FDI is towards the ASEAN countries because of this reason. Even though the Indian government has reduced the basic corporate tax rate from 30 to 25%, under certain conditions, this is less attractive than some of the ASEAN countries corporate tax rate.<sup>75</sup>

**Graph 3: Japan's FDI towards India**



**Source: JETRO**

Another positive development in India-Japan trade, which is not directly related to the CEPA, is bilateral currency swap agreement which continues to grow in volume. In 2011, India and Japan upgraded their currency swap arrangement from the earlier USD 3 billion to USD 15 billion. In 2018, both the countries further upgraded the agreement up to USD 75 billion.<sup>76</sup> The currency swap agreement will help both countries in managing short-term liquidity problems. Seen from the investors' point of view, it will help maintain financial stability, especially for India, which foreign investors as well as Japanese investors want.

Apart from the positives, the CEPA has also generated some negative optimism. Concerns about growing trade imbalance in Japan's favour have also started surfacing. Indian media reports suggest that India-Japan merchandise trade grew 38% from August 2011 to March 2012. Japanese

exports to India grew by 40.96% while India's export to Japan managed to grow only 18.39%. A year before the CEPA, Indian exports to Japan had grown by 43% and imports had grown by only 28%. Concern in Indian business circles that the CEPA has increased the trade balance in Japan's favour has started surfacing.<sup>77</sup>

Some concerns about the CEPA also came to the fore at the political and diplomatic levels. Indian media quoted the Commerce, Industry and Textile Minister conveying to his Japanese counterpart that India's generic medicines' share in Japanese markets is less than 1% of the total Japanese market and urged Japan to remove "non-tariff barriers" on the Indian drug companies. The then Commerce Minister Anand Sharma, who coincidentally is one of the signatories of the bilateral CEPA, requested the Japanese government to start negotiations on nursing and healthcare.<sup>78</sup> Sharma's successor, Nirmala Sitharaman has had similar concerns. In a seminar organized by New-Delhi-based think tank; the RIS, the Commerce Minister expressed satisfaction over growth in bilateral trade post-CEPA. However, she expressed concern over the growing trade deficit between India and Japan post-CEPA. In her words, the "trade deficit of India with respect to Japan has also increased from USD 3.1 billion pre-CEPA to USD 5.2 billion post-CEPA."<sup>79</sup> She was of the view that both the countries must look at ways and means to address this "skewed trade." She suggested that this problem can be addressed by increasing India's exports to Japan and increasing the pharmaceutical export to Japan could be one option adding that "the share of India in the Japanese drug market continues to be below par."<sup>80</sup> The Japanese experts, however, point that the low share of consumption of Indian pharmaceuticals is due to Japanese "business customs" and not necessarily due to "non-tariff barrier" as has been complained by India.

Echoing a similar line of concerns expressed by the Indian leadership, the Indian Embassy in its note on Japan-India relations observed that "the negative or slow growth in trade with Japan is a matter of concern for India, in view of the fact that there is a high potential for faster progress on goods and services trade."<sup>81</sup>

India's Foreign Trade Policy Statement 2015 in a guarded response to the India-Japan CEPA observes that "projected gains for India...have not materialised to the extent expected."<sup>82</sup> It also points towards NTBs being applied by Japan. It notes that "access to the Japanese market remains constrained by NTBs."<sup>83</sup> It further observed:

While on the one hand, the Japanese market has not seen growth in the product areas of India's interest, Indian business entities are facing problems in market access. These problems can be briefly said to be arising out of language constraints faced by Indian companies in Japan, highly demanding product and service standards, regulations that require business modalities making market access a costly venture, and a relative lack of intensive effort on the part of Indian business.<sup>84</sup>

To overcome the problem it suggests:

The other route of access of India's export sectors into Japan will require language proficiency, negotiating a simplified framework for market access and continuous trade promotion efforts on the part of businesses and the government.<sup>85</sup>

The Foreign Trade Policy Statement also talks of the need to "intensify outreach work"<sup>86</sup> on bilateral trade agreement with Japan.

Since India's objective to find a complementarity with Japan has not achieved its stated goals, some policy planners have also examined the trade agreement critically. For example, a semi-official policy paper by the government think tank NITI Ayog pointed that India's trade deficit with Japan has "widened" post-CEPA. The authors are not particularly critical of the Japan CEPA but almost all the FTAs signed by India. They have observed that the "utilization rate of India's FTA is very low."<sup>87</sup> The report cites, the "lack of information on FTAs, low margin preference, delays and administrative costs associated with rules of origin, non-tariff measures,"<sup>88</sup> as major reasons for this underutilization which impacts the export outflow from the country towards the FTA partners. In the context of Japan, he cites that import into India "increased more than exports."<sup>89</sup>

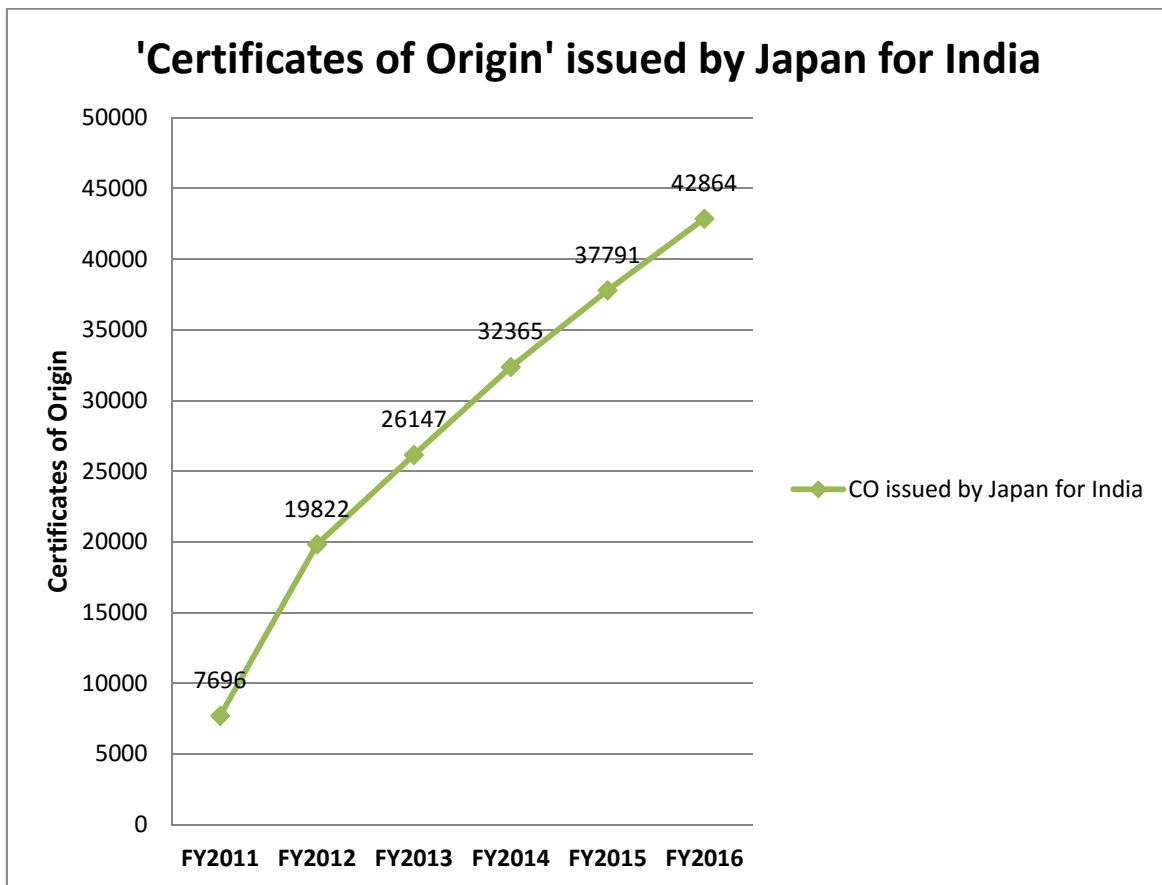
Despite consistent efforts by the Indian and Japanese governments, bilateral trade, which was projected to touch USD 20 billion by 2010, missed the target. Trade between India and China, however, touched around USD 75 billion around that time despite having no FTAs and with no visible political backing to improve trade relations with Beijing. But why did the bilateral trade not cross the USD 20 billion mark? The experts have different views on it. Masanori Kondo believes that the reduction of tariffs on many items will take place in the "final tenth year"<sup>90</sup> and



thus “there will be no benefit during the first nine years.”<sup>91</sup> Moreover, he points that “there is a large number of items excluded from tariff reduction”<sup>92</sup> including automobiles and automobile parts. The Japanese manufactures had high hopes of tariff elimination and this could have led to jump in Japanese automobiles export to India.<sup>93</sup>

Kohei Shiino, Associate Professor at Takushoko University, blames the stricter “rule of origin” criteria that restrict flow of goods between India and Japan impacting the bilateral trade volume. He points out that while other FTAs have kept the rules of origin simpler, the India-Japan CEPA puts the restriction of a 35% value-added criterion and change in HS code at six-digit level as a general rule. If these two criteria are not met simultaneously, Certificates of Origin at the exporting country cannot be issued and the exporters cannot get any tariff concession despite the India-Japan CEPA. He also points that the stricter rule of origin policy takes longer transaction time and increases transaction cost.<sup>94</sup> Japanese exporters, however, have been able to effectively utilize the Rule of Origin routes. This is evident from the number of Certificates of Origin (CO) issued by Japan for goods to be exported to India (see Graph 4 below)

**Graph 4: Certificates of Origin issued by Japan for India under CEPA**



**Source: METI, Japan**

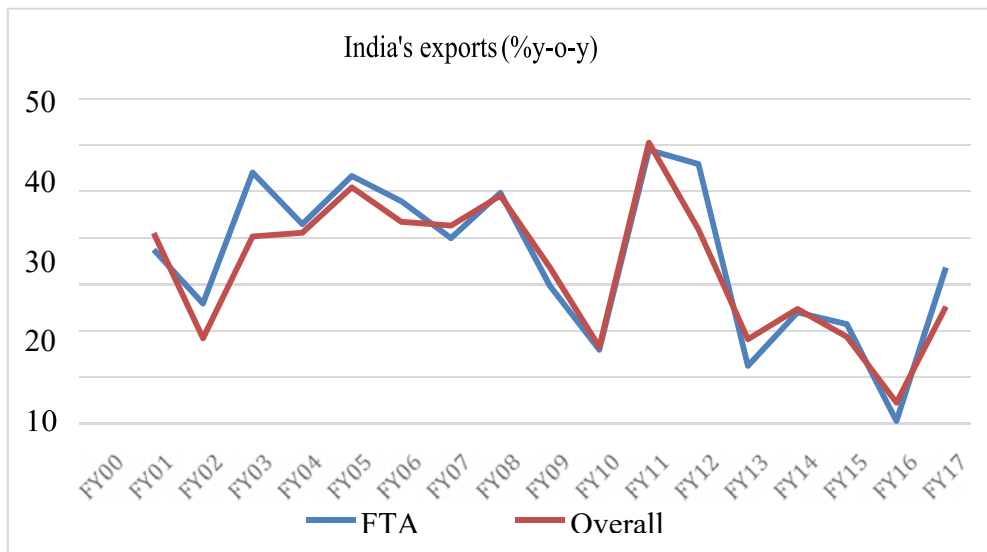
No such CO data is publically available from India to ascertain how many COs have been issued by Indian authorities to utilize the India-Japan CEPA. A study led by V. K. Saraswat at NITI Ayog also points that Indian exporters are not effectively utilizing COs for their exports. The Study notes that because of the time-consuming process, the Indian exporters take the normal route rather than utilizing COs under bilateral RTAs. The study points that “Complex rules of origin criteria, lack of information on FTAs, higher compliance costs and administrative delays dissuade exporters from using preferential routes. The compliance cost of availing benefits under these FTAs is so high that exporters prefer using the normal route. India has actively pursued FTAs with several major trading partners in the past without benefitting much.”<sup>95</sup>

When it comes to bilateral trade with Japan, there are other expectations from India. One such expectation is to achieve complementarities in goods and services. But finding such complementarities with Japan is difficult since Japan is an ageing society and consumerism remains low in Japan. India, on the other hand, has a growing economy and a society with a large consumer base. So in this scenario, it would be difficult to find complementarities and a trade balance which remains in Japan's favour is likely to grow further. Thus, it will be a challenge for both economies to achieve a balance in trade. But surely, a trade conflict between India and Japan is not likely to emerge as was seen between the US and Japan during the late 1980s because India is offering trade relaxation to Japan with an objective that goes beyond the economic dividend. India wants to minimize its growing dependence on China and signed FTAs with East Asian and Southeast Asian countries including Japan, South Korea, Malaysia, Singapore, etc. in quick succession while denying similar treatment to China using trade gap as a pretext.

### **India's Regional Economic Integration Post India-Japan CEPA**

As pointed above, both India-Japan Joint Study Group and the India-Japan CEPA mentioned that the bilateral comprehensive partnership agreement with Japan will lead to more regional and bilateral partnership, it is pertinent to examine whether India is actually keen to go for more regional agreement including much talked about Regional Comprehensive Economic Partnership. It may be noted that both India and Japan are members of the RCEP which is under negotiation. Conclusion of this agreement will pave the way for the Japanese and Indian traders to use either the CEPA or the RCEP route for their exports to each other's markets. But as the concerns grow about the under-utilization of the FTAs and the results show that India's export to FTA's and non-FTAs countries/groups do not show much difference (see the graph 5), India is treading cautiously to conclude further bilateral and regional FTAs, including the RCEP.

**Graph 5: India's export to FTAs and Non-FTA countries**



**Source: V.K Saraswat /NITI Ayog**

China is also one of the reasons of India's slow approach as China is also one of the negotiating partners, with which India's trade gap is widening. It will widen further once RCEP is implemented.<sup>96</sup> A NITI Ayog note in this regard has gone on suggesting that "given India's inability to negotiate a good deal in services in the past, RCEP negotiations especially with China need a second thought."<sup>97</sup> A similar study by an independent trade chamber argues that "India's move to enter into regional trade agreements has to be judged from the view point of promoting trade with economies with similar economic structure and to create more stability and level playing ground among its peers."<sup>98</sup>

It is pertinent to note here that among the bilateral FTAs India has signed, its trade balance has been positive only with neighbouring countries. It includes Nepal, Sri Lanka, Bhutan and Afghanistan. India has not gained much in terms of trade balance when it comes to Southeast Asian, East Asian or European partners, with which it has signed the FTAs. These include Japan, South Korea, Singapore, Malaysia, the Netherlands, etc. Trade balance with these countries has widened further and India's balance in trade shows negative. (See table 4)

**Table 4: India’s bilateral FTAs and overall trade performance**

| Serial No. | Partner Countries | Years of Enforcement | India’s Exports FY2018–19 | India’s Import FY2018–19 | Total Trade FY2018–19 | Trade Balance FY2018–19 |
|------------|-------------------|----------------------|---------------------------|--------------------------|-----------------------|-------------------------|
| 1.         | India–Nepal       | 1999                 | 7,763.60                  | 503.51                   | 8,267.11              | +                       |
| 2.         | India–Sri Lanka   | 2000                 | 4,708.50                  | 1,472.83                 | 6,181.33              | +                       |
| 3.         | India–Afghanistan | 2003                 | 715.44                    | 435.44                   | 1,150.89              | +                       |
| 4.         | India–Singapore   | 2005                 | 11,571.14                 | 16,281.64                | 27,852.78             | –                       |
| 5.         | India–Bhutan      | 2006                 | 657.33                    | 369.53                   | 1,026.86              | +                       |
| 6.         | India–Chile       | 2007                 | 989.80                    | 1,237.55                 | 2,227.35              | –                       |
| 7.         | India–Finland     | 2009                 | 256.12                    | 1,124.08                 | 1,380.20              | –                       |
| 8.         | India–Korea       | 2010                 | 4,705.07                  | 16,758.76                | 21,463.83             | –                       |
| 9.         | India–Japan       | 2011                 | 4861.73                   | 12772.64                 | 17634.37              | –                       |
| 10.        | India–Malaysia    | 2011                 | 6,435.25                  | 10,818.60                | 17,253.85             | –                       |

**Computed by the author from Ministry of Commerce, Government of India EXIM data**

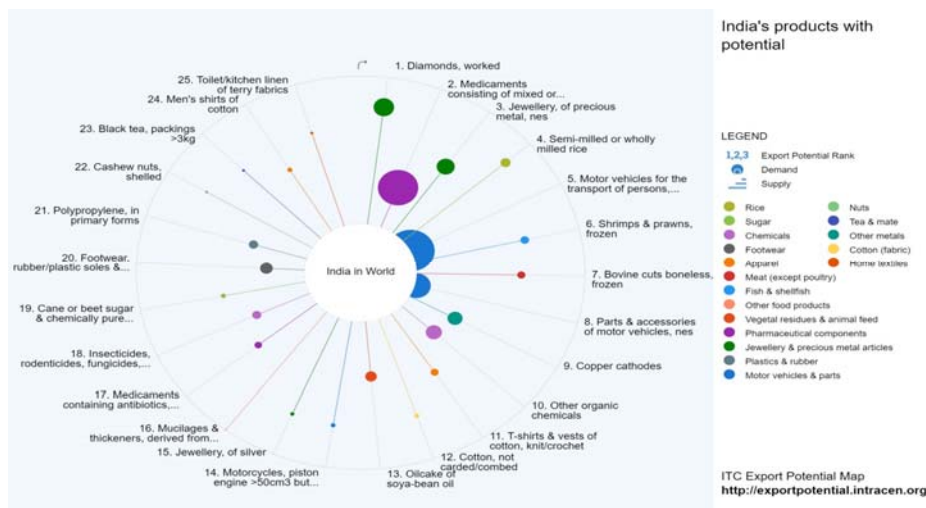
The NITI Ayog’s analysis shows that India’s export to RTAs and non-RTA countries remains almost the same. Even though there has been growth in India’s overall export, it is largely due to diversification of the export basket both in terms of destination and commodities. In the context of these developments, India seems to be leaning towards adopting strategy to sign FTAs/RTAs focusing on “product and services with maximum export potential.”<sup>99</sup>

Apart from the NITI Ayog, other stakeholders also have similar views as they believe that “India is not reaping any cost advantage while importing from its respective partners.”<sup>100</sup> Without mentioning Japan, a study by India’s PHD Chambers points that “Trade arrangements with some developing countries have also fallen short of expectations in terms of the elimination of tariff and nontariff barriers.”<sup>101</sup>

The partnering countries have not adhered to comparative advantage theory, the core principle of trade agreements, notes that report.<sup>102</sup> Against this backdrop, the trade body suggests “caution in application” of trade arrangements given the ambiguity involved in the RTAs/FTAs. The report notes that “hastily negotiated agreements have only disappointed India’s export growth story.”<sup>103</sup>

Saurabh Sanyal, Secretary General of India’s PHD Chambers, suggests that the Government of India should “strengthen its product strategy” and the focus should be on promoting export of high-value products with a strong domestic manufacturing base.”<sup>104</sup> The ITC has developed a trade potential map identifying the trade potential of 25 commodities (See the map 1).

**Map 1: India’s Export Potentials**



**Source: ITC Export Potential Map**

As various stakeholders’ analyses of India’s FTAs are coming to the fore, there has been growing realization that India’s FTAs have not yielded expecting benefit. As a result, demands are growing not to sign further FTAs and RTAs. NITI Ayog’s note suggests in this regard that “before getting into any multilateral trade deal India should first review existing FTAs in terms of benefits to various stakeholders like industry and consumers, trade complementarities and changing trade patterns in the past decade.”<sup>105</sup> Demand to review the FTAs by default applies to the Japan-India CEPA as well.

## 7. Conclusion and Suggestions

The analysis above suggests that economic and trade ties between the two countries have deepened ever since India and Japan signed the Strategic Partnership in 2006 following which the decision to negotiate a CEPA was made. But the CEPA has yet to achieve “complementarities” as was envisioned in the India-Japan Joint Study Group and CEPA documents analysed above. As noted above, the leaders of both the countries took a political decision to uplift the abysmally low

bilateral trade volume between the two Asian economies by signing a Comprehensive Economic Partnership Agreement (CEPA) in 2011. Moreover, India termed this agreement as an “alliance between Japanese technology and capital and a young Indian labour force.” Both the countries decided to take the low trade volume of USD 10 billion to USD 20 billion by 2012, as various sources suggest. But even after eight years of effective implementation the bilateral trade volume stand at USD 17.63 billion at the end of FY2018–19. This is evident that they have missed the USD-20-billion target. Kohei Shiino, an Associate Professor at Tokushoku University, believes that one of the reasons of this low trade volume is that the Japanese companies remain concentrated in ASEAN and conduct trade from there with India.<sup>106</sup> Norio Kondo believes that Japan has signed similar such FTAs with other countries and all the countries are competing for market access and increase their trade share. Thus, the advantages to the Japan-India CEPA have been wiped away.<sup>107</sup> Professor Makoto Kojima who was part of India-Japan Joint Study that suggested the signing of the India-Japan CEPA observes that the impact of the CEPA on bilateral trade has “disappointing.” He believes that trade in pharmaceuticals and agriculture has great scope and it can lift the bilateral trade. There remains SPS concerns about India’s agricultural products and those can be addressed with further efforts from both sides including the sharing of the technology by the Japanese side to uplift the SPS standards of Indian products. He is also of the view that as various Japanese companies including Uniqlo and Rakuten are entering into the Indian market, there are chances of export of their products back to Japan increasing India’s trade share.<sup>108</sup>

Moreover, as a result of the CEPA, the trade balance has grown in Japan’s favour. The gap in India-Japan bilateral trade has grown up to USD 8 billion. Before the CEPA came into effect in 2011, the trade gap between the two countries was roughly USD 3 billion. The growing trade gap is becoming a cause of concern both in political and policy circles in India. The critics blame that because of some “behind the border” barriers imposed by Japan, the inflows of Indian goods in Japan remain limited even though the investment flows from Japan as well as increasing number of Japanese companies setting up their industry in India are encouraging signs. However, a comprehensive and complementary economic relationship, which was envisioned by the leaderships of the two countries, has yet to be achieved. The section below, in this regard, offers some suggestions to give a new fillip to the economic and trade relationships between India and Japan.

One of the many objectives of the India-Japan CEPA was to exponentially enhance the bilateral trade volume between the two countries and deepen the economic ties. The CEPA did bring impressive results and within a year of this agreement coming into effect in 2011, the bilateral trade touched USD 18.32 billion in the FY2011–12 as compared to USD 13.72 billion in 2010–11. However, after two consecutive years of touching new heights, the bilateral trade started decelerating causing alarm that the CEPA’s objectives would be defeated if it continues to plummet. It has started accelerating again during the last two fiscal years. This gives cause of some optimism also as both the countries are close to entering into the third stage of tariff elimination and would eliminate the promised tariffs by 2021. However, the bilateral trade figure still remains below the 2012 level (USD 18.32 billion) and the call for review of FTAs by India is growing within the domestic constituencies in India.

Keeping this in mind, both Indian and Japanese governments should find ways to make the CEPA much more relevant and should consider a few options in this context. One of the options could be to activate various sub-committees that the CEPA document mentions, and in addition to this, form a select core group which should analyse the shortcomings of the CEPA and suggest remedial measures to both governments.

The second option could be to give a rethinking of “inconclusive” parts of the CEPA signed in 2010. Even though the three-year period to conclude India’s nurses and care workers entry into Japan as mentioned in the CEPA document has expired, it may be reminded that Japan has signed a similar CEPA (known as EPA in Japan) with Indonesia and Philippines, where it has allowed nurses and care workers to work in Japan as part of the EPA. India was also asking similar treatment for its nurses and caregivers in the India-Japan CEPA. Japan, in principle, had agreed to give the same treatment to Indian workers, but sought more time, as it found that majority of the nurses and care workers were finding it difficult to attain language proficiency after their two years of internship in Japan. Passing the language test was a pre-requisite to starting fully-fledged work in the service sectors catering to the medical requirements of Japan’s ageing society. However, Japan has revisited this policy and has simplified the language tests for expats,<sup>109</sup> which has resulted in a large number of those expats clearing the Japanese language test. Since Japan is no more facing the difficulties it cited to India, it should revisit this “inconclusive” aspect of the India-



Japan CEPA. This will allow more Indians to work in the Japanese service sectors, as the CEPA promises trade not only in goods, but also in services.

It is pertinent to mention here that a study based on “Revealed Comparative Advantage index” finds lots of complementarity in India and Japan in service sectors. The Study finds that Japan has “comparative advantage in transportation, construction and royalties and license fees services, while India has the comparative advantage in commercial services, other business services and computer and information services.” The study concludes that “both the countries can complement each other.”<sup>110</sup>

Here it is important to mention that the JSG noted that the lack of human exchange between the two countries and suggested both governments to enhance “people-to-people exchanges” hoping that it will provide a basis for “stronger bilateral economic ties.” Given the complementarity in service sector the simulation-based study has noted, and the JSG has pointed out, before the signing of a CEPA, both India and Japan should think of more ways to cooperate in service sectors.

Thirdly, India and Japan should look at the new avenues and openings in Japan in service sectors and should try to tap these opportunities. Recently, Japan has announced a policy of allowing unskilled and low skilled workers to work in Japan.<sup>111</sup> Since the CEPA promises trade in services and assures flow of human resources between the two countries, it would be pertinent for India to request Japan to give preferential treatment to countries with which it has signed a CEPA. Moreover, India should ask Japan to fix a quota for Indian high-skilled and semi-skilled workers under this scheme.

It may be recalled that the India–Japan strategic partnership was aimed at creating a “win–win” situation for both countries. However, in the field of economy and trade, it has brought more advantage to Japan than to India. The trade balance continues to grow in Japan’s favour and concern about growing trade gap is emerging in India and this is not limited to media but has percolated into policy, political and diplomatic circles. The efforts should be made to increase India’s trade share in the bilateral trade so that it does not lead to “trade frictions” between the two countries in future.

Japan has allowed the entry of some Indian vegetables, fruits, poultry and fish. However, some of the Indian agricultural produce as well as fisheries and shrimps do not come up to the Sanitary and

Phyto Sanitary (SPS) measures applied by Japan. There are reports that suggest that some of the Indian shipments to Japan had to be taken back as they could not come up to the Japanese SPS standards. Similarly, India's generic medicines' share in Japanese markets is less than 1% of the total consumption of generic drugs. It is said that the packaging of Indian medicines does not match with that of the Japanese ones; because of this, the local consumers shy away from buying these medicines. Therefore, till India overcomes these Non-Tariff Barriers (NTBs) on its food products as well as generic medicines, it would be difficult to gain access to the Japanese market and, in that case, it would be difficult to achieve a trade balance with Japan. Technology could be a great enabler in this context. To overcome these NTBs put in place by Japan, India should ask Japan to share and facilitate the technologies, application of which would lead to improvement in Indian products' SPS measure standards as well as Indian medicines being able to match the requirements of Japanese generic medicines.

Needless to say, Japan has acknowledged that "a strong, prosperous and dynamic India is in the interest of Japan and vice versa." Both the governments have undertaken various measures to upgrade their economic relations. However, there is vast potential and opportunities, some of them cited above, which remain untapped. Collaboration in these fields between the two countries will certainly impart momentum to their economic growth and prosperity.

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<sup>1</sup> J.N Dixit, "My South Block Years: Memoirs of a Foreign Secretary", UBS Publishers and Distributors, New Delhi, 1996, p.254.

<sup>2</sup> T.R. Sareen, "India and Japan in Historical Perspective" in Rajaram Panda and Yoo Fukuzawa (eds) *India and Japan in Search of Global Roles*, Promila and Company Publishers, New Delhi ( 2007), p.30.

<sup>3</sup> Purnendra C.Jain and Maureen Todhunter, "India and Japan: Newly Tampering Relations", in Purunendra C. Jaain ( ed.) *Distant Asian Neighbours: Japan and South Asia*, Sterling Publishers Private Limited, New Delhi, 1996, p.87.

<sup>4</sup> For a detail account of items traded between the two countries during the pre-war period, please refer to P G Rajamohan, Dil Bahdur Rahut and Jabin T. Jacob, " Changing Paradigm of Indo-Japan Relations: Opportunities and Challenges, Working Paper No.212, Indian Council for Research on Economic Relations, New Delhi, 2008.

<sup>5</sup> Selected Work of Jawaharlal Nehru, Vol. 6. p 481, as quoted in Hiroshi Sato, India Japan Peace Treaty in Japan's Post-War Asian Diplomacy, *Journal of the Japanese Association for South Asian Studies*, Vol. 17, 2005, p.10.

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