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**Tariff Liberalization and India-ASEAN Bilateral Trade-A Review****Mohd Kashif\* and Prof. NUK Sherwani\*\***

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**Abstract**

*AIFTA is a free trade agreement between the India and ASEAN which was signed on 13 August 2009 and implemented on 1 January 2010. The basic purpose of this agreement is to reduce tariff barriers and to expand the bilateral trade between India and ASEAN countries. Trade is a major mechanism of India and ASEAN economic integration. The objective of the present study is to analyse the existing literature available on the impact of tariff liberalization under AIFTA on India-ASEAN bilateral trade relationship. For the present paper, exhaustive literature review was done, with a framework to gain all important information available through articles and papers published in journals of repute. As such, all related literature have been analyzed to examine the effect of tariff liberalization under AIFTA on price, output mix, employment and trade and to measure the welfare and revenue effects associated with these tariff reductions. The literature available on the subject does not provide a satisfactory picture on India-AIFTA trade relations. Infact, tariff liberalization under AIFTA had a negative impact on many Industrial sectors. The tariff reduction caused a fall in tariff revenue and welfare loss to India.*

*This research paper is part of my PhD research work on "A Study on Indo-ASEAN Trade Relationship"*

**Key Words:** AIFTA, ASEAN, Tariff liberalization, Revenue Effect, Welfare Effect, Trade Creation, Trade Diversion

**Introduction**

A Free Trade Agreement (FTA) is a form of economic integration in which member countries have agreed to reduce tariff barriers to increase the trade of goods and services with each other (O'Sullivan & Sheffrin, 2003). To achieve the benefits of FTA, the five well known countries of South-East Asia namely Indonesia, Malaysia, Philippines, Singapore and

Thailand created a FTA on 8<sup>th</sup> August 1967 in Bangkok, Thailand which is popularly known as Association of Southeast Asian Nations (ASEAN) (Gupta, 2016). Within a short duration, the membership of ASEAN has expanded as in the year 1984, Brunei become the member of ASEAN, Vietnam take membership in the year 1995, Laos and Myanmar take membership in 1997 and Cambodia take the membership of ASEAN

in the year 1999 (www.nti.org). Thus, the membership of ASEAN has extended to ten at present. There is a tremendous growth in ASEAN economy during the last few decades. In 2016, the ASEAN as a single economy has ranked on 6<sup>th</sup> place as largest GDP in the world and ranked on 3<sup>rd</sup> place in Asia (Strengthening ASEAN- India Partnership: Trends and Future Prospects, 2018).

India is a dominant trade partner of ASEAN. India initiates its Look East Policy in the year 1990. In the year 1992, India-ASEAN relations emerged as sectoral dialogue partnership which was turn into full dialogue partnership in the year 1995 (Strengthening ASEAN- India Partnership: Trends and Future Prospects, 2018). Since then trade relationship between India and ASEAN countries are upgrading. The India-ASEAN trade relationship was upgraded to summit level and accordingly the first India and ASEAN Summit was held in the year 2002 in Cambodia (Gupta & Shah, 2015). During the second summit in 2003, India and ASEAN signed a framework agreement on Comprehensive Economic Cooperation (CECA) (Gupta & Shah, 2015). The India and ASEAN has started negotiations on trade in goods in March 2004 and finally India and ASEAN signed a free trade agreement on 13 August 2009 which is

popularly known as ASEAN India Free Trade Agreement (AIFTA). This agreement put into effect on 1 January 2010. Tariff liberalization is the basic objective of signing the AIFTA.

### **Objectives Of The Study**

The objectives of the study are:

- To furnish a conceptual framework on the tariff liberalization under AIFTA.
- To critically examine the literature available on the impact of tariff liberalization under AIFTA on India-ASEAN bilateral trade relationship.

### **Framework Of Tariff Liberalization Under AIFTA**

The ASEAN-India FTA divides the tariff lines into five groups which are Normal Track, Sensitive Track, Highly Sensitive Track, Special Products and the Exclusion list (Joseph, 2009). In case of normal track, the tariff rates will be reduced to zero. In case of sensitive track, the tariff lines will be reduced to 5%. There is no tariff reduction in case of exclusion list (Bhattacharyya & Mandal, 2016). India has removed 489 products from the tariff concession list. This is also known as negative list. In case of highly sensitive goods the tariff reduction is divided into three categories. In first category, the tariff rates are to be reduced to 50%. In the second category, the tariff rates are to be reduced by 50% and in third

category it is to be reduced by 25% (Joseph, 2009). Special products involves Crude and Refined Palm Oil, Coffee, Tea and Pepper and for these products reduction in tariff will be at more gradual rate than normal or sensitive track (Veeramani & Saini, 2011).

### **Impact of Tariff Liberalization Under Aifta On India-Asean Bilateral Trade Relationship**

The main motive of this study is to highlight some of the important findings on India-ASEAN trade relationship. There is enormous availability of literature on the subject and some significant work has been included in the present study.

**Joseph (2009)** in his article made an attempt to analyse the impact of AIFTA on India's plantation sector and estimating the relationships between tariff rate and import on one side and import and domestic price on the other side. In the study, the author opposed the simple static analytics which says that a fall in tariff rate will harm the interest of both domestic producer and seller and increase imports which result in price crash. The author support the dynamic approach which reveals that tariff reduction is not only impact import but import is also dependent on productivity, market structures and exchange rate.

**Ahmed (2010)** in his research article made an attempt to analyse the sectoral

dimensions of AIFTA. Global Trade Analysis Project (GTAP) model and SMART model has been used in the study. The author is examining the effect of tariff liberalization on price, welfare distribution, output mix, employment and trade with the help of GTAP model and estimate the welfare and revenue effects associated with tariff liberalization through SMART model. It is found from the study that India's employment and wages of the people working in convenience food products, agricultural items and fisheries sectors might be negatively affected by the increasing ASEAN's exports in these sectors. The result reveals that trade creation arises due to the AIFTA is confined to limited tariff lines. The result also indicate that AIFTA will have a negative affect on trade balance and revenue loss for India which might adversely affect the public health, education and government gains which have an important portion in budgets of country. On the other hand, it is also found AIFTA will provide a significant impact on the convenience food items, grain crops, textile and wearing apparel, light manufacturing and heavy manufacturing sectors.

**Francis (2011)** in her article made an attempt to provide an overview on the structure of India's trade with the world in addition to ASEAN nations. The author

pointed out that ASEAN member nation will acquire remarkable market access in India in various semi-processed or processed agricultural products. The reduction in tariff proposed under FTA between India and ASEAN will provide a negative effect on the Small and Medium Enterprises of India engaged in agricultural products and food items as well as intermediate products and light manufacturing goods.

**Veeramani & Saini (2011)** in their research article analyse the impact of ASEAN-India Preferential Trade Agreement on specified plantation commodities which are Coffee, Tea and Pepper. Single Market Partial Equilibrium Modelling Tool (SMART) model and Gravity model are used in the study to analyse the trade creation and trade diversion effects on import, to measure the welfare and revenue effects associated with tariff reduction and to estimate the import under different tariff reduction conditions. It is analysed from the study that preferential trade agreement between India and ASEAN would lead to significant rise in plantation commodities from ASEAN nations to India. It is further observed that trade creation is the main cause of import growth in India than trade diversion. Trade creation helps to improve the welfare because the new imports from ASEAN replace costly domestic production of India. The study

reveals that the proposed reduction of tariff under the ASEAN-India PTA may cause some tariff revenue loss to the Government of India. However, reduction in domestic price and fall in dead weight loss result the gain in consumer surplus which outweighs the tariff revenue loss leading to net welfare gain.

**Chandran & Sudarsan (2012)** in their research article made an attempt to analyse the impact of AIFTA on India's fisheries trade. Partial Equilibrium Simulation Method (SMART) has been used in the study. The result of SMART simulation indicates that tariff reduction is responsible for the trade creation and marginal welfare increases with a reduction in nominal tariff revenue. The study also argues that India should take necessary steps against large scale dumping to protect its marine sector.

**Mondal, Sirohi & Thorat (2012)** in their research article made an attempt to find out the impact of AIFTA on India's dairy trade. Partial Equilibrium Model (SMART) has been used to analyze the effect of tariff on the trade. The study concluded that in ASEAN region there is a significant trade potentiality exists for India in dairy market. By applying the SMART model, it is found that by signing the AIFTA India has created an additional scope to enlarge its exports volume in dairy to ASEAN member nations.

It is further argued that Indian dairy industry can be benefitted by entering in those markets where tariff has been eliminated through AIFTA. It is very difficult to detain large market share in those countries where tariff is already removed. They also pointed out that India's tariff elimination creates a little opportunity for ASEAN member countries to enlarge their market shares in India.

**Ratna & Kallummal (2013)** in their article made an attempt to study the effect of FTA on products related to agriculture like fisheries, tea and coffee. The study period has taken from 1996 to 2008. Pearson Correlation is used in the study to analyse the impact of India's tariff on fisheries, tea and coffee with variables like employment, prices, production, productivity, exports and imports. It is found that in fish sector the production and prices have risen due to the rise in tariff. It is presumed that production and prices in the fisheries sector in India protected by a rise in tariff upto a level. Secondly, India being a crucial participant for exports of processed fish to the globe fulfils its requirements by imports. In case of tea, it is observed that imports, production and cultivation region extend with the increase in tariff but auction prices and employment decline in the sector. Thus, a rise in tariff in tea was not successful to

restrict the tea import, protecting yield, auction price and domestic employment. Secondly, Tea imports from Indonesia and Vietnam are low priced which might be a warning to the producers of the country. In case of Coffee sector, it is observed that high tariffs are unable to provide much protection to Coffee industry in India. A fall in tariff will not threaten to the domestic sector. The main problem of coffee industry in India lies in domestic incompetency not with tariff liberalization.

**Bhattacharyya, R., & Mandal, A. (2014)** in their study tries to find out the industries that are supposed to be affected negatively or positively due to the implementation of AIFTA during the study period 1989 to 2009. The authors used Gravity model is in the study to estimate the values of import (India) from country j (the six ASEAN members) with respect two different situations which are without tariff and with tariff and Gross Domestic Product which is actually income level of India and ASEAN. It is found that industries that are affected adversely by AIFTA are electric machinery, ores, slag and ash, nuclear reactors, aluminium and articles thereof, rubber and articles thereof, organic chemicals, iron and steel, manmade textiles materials, woods and articles of wood, vehicles other than railway. On the other hand industries that

are favourably affected because of the reduction in tariffs resulting from AIFTA are Organic chemicals, iron and steel, electric machinery inorganic chemicals, glass and glassware, nuclear reactors, mineral fuels and toys, games and sports requisites.

**Yean & Jia Yi (2014)** conducted a research study to compare the effect of AIFTA on India's exports of manufacturing items to ASEAN and ASEAN's export of manufacturing items to India and to contrast the role of trade liberalization to other variables in the exports of manufactured products between India and ASEAN. Augmented Gravity Model has been used in the study to estimate the impact of GDP, Distance, Tariff, colony, real effective exchange rate and FDI on the export of manufactured products between ASEAN and India. The study reveals that ASEAN is more benefitted from the tariff liberalization than India. Secondly, distance variable is highly affecting the ASEAN manufacturing exports to India. The effect of tariff reduction is very low on the export of manufacturing goods between India and ASEAN. The study suggests that the AIFTA will have to build up various measures to facilitate the trade which help in to raise the volume of exports of manufactured goods between India and ASEAN.

**Bhattacharyya & Mandal (2016)** in their research article tried to analyse the ex post effects of India- ASEAN FTA. After the evaluation of ex post effect of AIFTA, it is revealed that trade and tariff concessions provides more benefits to ASEAN than India. As far as welfare is concerned, it is found that during the starting two years of AIFTA both India and ASEAN benefitted in welfare but these benefits has decreasing over the period of time. It is also pointed out that there is a sharp fall in imports of both India and ASEAN which caused a fall in revenue from tariff from the rest of the world. The article suggest that Indian government can avoid the negative surplus either by more tariff liberalizing to elastic goods or by signing a similar agreement with other countries of the world.

**Mandal (2018)** in his article made an attempt to examine the welfare impact of AIFTA. Global Trade Analysis Project (GTAP) model is used in the study to estimate the impact of tariff liberalization on the welfare distribution. It is found from the study that ASEAN will be benefitted in terms of welfare due to AIFTA but AIFTA will have a welfare loss for India. The India's welfare loss emerges due to the deterioration in trade. On the other hand, main reasons for ASEAN welfare gain are

allocative efficiency and positive trade effect.

### **Conclusion**

The findings of the present study suggest that in comparison to India, the ASEAN countries receive much more benefits from AIFTA. Tariff liberalization has not been in the favour of India as was anticipated in the beginning of AIFTA. Some of the studies opine that tariff liberalization under AIFTA will have a negative impact on the Indian SMEs engaged in agricultural and allied activities as well as those engaged in the business of intermediate goods and light manufacturing goods. AIFTA will have a negative affect on trade balance and revenue loss for India which might adversely effect the public health, education and government gains, which is a serious threat. The tariff liberalization also effects the employment and wages of people working in various sectors in India like processed food industry, agricultural and fisheries sectors. In case of tea, it is observed that imports have increased due to tariff reduction but there is a fall in auction price and domestic employment. Tea imports from Indonesia and Vietnam are low priced which might be a warning to the producers of the country. In

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case of Coffee sector, falls in tariff will not a concern for domestic sector. The main issue of coffee industry in India lies in domestic incompetency not with tariff liberalization. Further, industries that are affected adversely by AIFTA are electric machinery, ores, slag and ash, nuclear reactors, aluminium and articles thereof, rubber and articles thereof, organic chemicals, iron and steel, man-made textile materials, woods and articles of wood, vehicles other than railway. On the other hand, industries that are favourably affected due to tariff reduction resulting from AIFTA are organic chemicals, iron and steel, electric machinery inorganic chemicals, glass and glassware, nuclear reactors, mineral fuels and toys, games and sports requisites.

As far as welfare is concerned, it is found that during the starting two years of AIFTA both India and ASEAN benefitted in welfare but these benefits has been decreasing over the period of time. A sharp fall in imports of both India and ASEAN countries caused a decrease in tariff revenue from the rest of the world. ASEAN benefitted more in terms of welfare due to AIFTA but AIFTA has a welfare loss for India.

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