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U.S. Withdrawal of GSP Benefits to India

Need to look at the bigger picture

The United States of America has unleashed another trade irritant by terminating the benefits of the Generalised System of Preferences (GSP) to India (and Turkey). While it has been in the news for more than a year, its potential implications are likely to go beyond bilateral trade frictions and may have deleterious impact on Indo-U.S. 'economic and strategic partnership'.

This Policy Note analyses potential economic and strategic implications of this development. It argues that both countries should look at the bigger picture of their current and emerging relationship, and avoid such trade irritants. Otherwise, the goal of achieving US$500bn Indo-U.S. bilateral trade by 2025 will remain elusive.

Introduction

The U.S. decision to withdraw benefits under the Generalised System of Preferences (GSP) to India and Turkey appears that the Trump Administration is following a quixotic trade policy that does not take into account economic and strategic priorities of the United States. It is likely to take similar action against Indonesia and Thailand – two important countries in the Indo-Pacific region.

It can potentially put a significant brake to the objective of enhancing the Indo-U.S. bilateral trade from the current level of US$126bn to US$500bn by 2025. Similarly, it will undermine the growth of Turkey-U.S. bilateral trade from the current level of US$21bn to US$75bn in the next decade.[1]

At the same time, it is worth mentioning that the Indo-U.S. strategic partnership continues to expand at a sustained pace. In 2018, both countries signed the Communication, Compatibility, and Security Agreement. The U.S. recognises India as a strategic partner in its new ''Free and Open Indo-Pacific'' strategy, which is articulated in the Asia Reassurance Initiative Act, 2018.

Therefore, this decision to withdraw GSP benefits can impact both parties to strive for equilibrium while balancing their economic and strategic goals.

U.S. Decision and its Impact

The U.S. categorically stated that its decision to end the GSP benefits came after extensive engagement with India to seek ''equitable and reasonable access'' for the U.S. products particularly in dairy and medical devices. The U.S. is of view that India's trade policy regime is becoming more restrictive as its recent policy stance on e-commerce and price cap on stents and other medical devices can severely hurt commercial interests of American companies.

Given the fact that India is the largest beneficiary of the U.S. GSP regime as 1900 products are covered under it, this withdrawal will impact India's annual export of US$5.6bn to the U.S., which is approximately 10 per cent of its total export to that country. The total value of duty concession under GSP is US$190mn per year for Indian exporters.

[1] US decision to remove Turkey from GSP contradicts $75bn trade target, https://www.dailysabah.com/economy/2019/03/06/us-decision-to-remove-turkey-from-gsp-contradicts-75b-trade-target

Key sectors such as organic chemicals, parts of vehicles, furniture, leather goods, textiles and apparel, electrical apparatus, stone, sand and cement, plastic material, rubber, bedding mattress, wood, glass and nuclear fuel materials will be affected. This is not a positive development because India's growth of export intensity is declining and its share in global export is stagnant.

India's official response to the U.S. decision is that it will not have much adverse impact on its export. However, as pointed out by several sectoral bodies such as the Council for Leather Exports of India, micro level implications to labour intensive goods export, which play an important role in India's employment generation and socio-economic development, can potentially result in job losses, a current hot issue in India and engaging much attention on the eve of the General Elections.

India and the U.S. to avoid trade irritants for strengthening their economic and strategic partnership in the Indo-Pacific region

Secondly, many Indian exports under the U.S. GSP regime constitute intermediate goods, which are used by American manufacturers to produce their final products with relatively high competitiveness. As a result of this decision, other than direct negative impacts on Indian producers and American consumers, American manufacturers will also get adversely affected.

Will it be a Gain for China?

There are a number of GSP eligible products on which India and China are competing in the U.S. market. Commenting on this development, Agra Footwear Manufacturers and Exporters Chamber stated that the impact would be significant on leather goods exports to the U.S. at a time when made in India items are facing stiff competition from China (and Vietnam).

Futhermore, potential effects could be seen in other labour-intensive sectors such as intermediate bulk bags, industrial bags, garments, engineering goods, plastics and chemicals, where India and China are competing in the U.S. market.

Therefore, this U.S. decision will undermine its own economic priorities as it will affect its import diversification strategy through which it wants to replace China with other possible sources. The U.S. must understand that such irritants to Indo-U.S. trade should not result in benefits to others with which it is already competing on trade, technology and strategic fronts.

Way Forward

Keeping the above-stated factors in mind, it is important for India and the U.S. to not allow bilateral trade irritants to dominate their strategic partnership. They should resolve this matter within 60 days of its announcement so that it does not come into effect.

It is true that, amidst trade tensions, the U.S. had a robust strategic partnership with Germany in 1970s and with Japan in 1980s. So both could exist as today with Turkey which is a member of the NATO. However, given various geo-economic, geo-political and geo-strategic developments, which are taking place in the Indo-Pacific region, both India and the U.S. cannot afford to face such a situation.

Therefore, it is time for a mutually acceptable bilateral trade deal. This can be done by devising better treatments in a number of areas. First, India can reconsider its policy stance on e-commerce as it limits fair competition and encourages trade and technology distortion.

Secondly, both countries can identify products on which there can be mutual market access without any major negative fallout on their economic interest. The U.S. should look at products which it is importing from China but can be easily imported from India through necessary adjustments in technical regulations. Similarly, India should look at products which are otherwise being imported from China and can be imported from the U.S.

This would help both to reduce their respective trade deficit with China and can significantly boost the growth of their bilateral trade. Above all, this would strengthen their 'economic and strategic partnership' in the Indo-Pacific region, which will, in turn, help shaping new rules on the emerging global economic and political order.

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