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Challenges in negotiating the India-UAE CEPA

Author

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Cover Photographs:

Union Minister for Commerce and Industry Piyush Goyal and UAE Minister of State for Foreign Trade Dr. Ahmed Al Zeyoudi address a joint press briefing at the launch of negotiations for Comprehensive Economic Partnership Agreement on September 22, 2021. Source: ANI

Union Minister for Commerce and Industry, Shri Piyush Goyal, inuagrates India Pavillion at Expo 2020 Dubai site on October 1, 2021. Source: Ministry of Commerce and Industry, Government of India

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Introduction

On September 22, India and the United Arab Emirates (UAE) launched negotiations to conclude an FTA in the genre of a Comprehensive Economic Partnership Agreement (CEPA), with the first round of talks being held shortly thereafter.[1] The two countries have also conveyed their intention to wrap up the negotiations quickly, possibly by December this year, so that the CEPA can be signed in March 2022 after the necessary internal procedures. This brief looks at the favourable factors for forging such an FTA and certain distinctive factors in bilateral economic ties that may need to be suitably addressed if it is to bring commensurate benefit to both countries. It also makes an evaluation of the challenges based on the UAE's existing FTA portfolio which is limited in scope, even though the UAE is now known to be negotiating with several other countries.

The conducive factors

India's current economic engagement with the UAE has both width and depth. The UAE has been India's second or third largest export destination and import source for most of recent years[2]. The two way trade covers several sectors, going significantly beyond the jewellery and petroleum sectors that had earlier dominated. Even in bilateral services trade, the span is wide covering transport, travel, construction, IT, education, health, hospitality, media and financial services. Before the onset of COVID, more than 1000 flights used to operate between the two countries every week.

Indian investments in the UAE are estimated at around US$ 85 bn. The UAE is the ninth largest investor in India with cumulative inflows totalling US$ 11.5 bn[3]. The UAE is the top destination for Indians seeking work abroad[4] and their current number is estimated at around 3.3 mn. This diaspora includes not just blue collar workers but also white collar experts and professionals. Annual

[1] See the joint press statement https://pib.gov.in/PressReleasePage.aspx?PRID=1757061
[2] Bilateral trade figures as per DGCIS for select years is given in Annex 1 to this brief
[3] These investment numbers have been taken from the websites of the Indian Embassy in Abu Dhabi and India's Department for promotion of Indian industry and internal trade
[4] See the newsitem which quotes India's minister of state for external affairs Shri V. Muraleedharan, https://www.arabianbusiness.com/politics-economics/466617-uae-named-top-destination-for-indian-workers-abroad-says-minister

remittances from the UAE to India have been adding up to US$ 15 bn. In sum, the economic exchanges between the two countries substantially cover the movement of goods, services, capital and labour.

Politically too, India and the UAE have developed close ties, with frequent high level visits. Bilateral relations have been elevated to a comprehensive strategic partnership in recent years. As per the Indian Embassy's website, there are some 44 MOUs signed between the two countries in a range of areas since 2014[5]. A CEPA between the two countries could provide a further boost to bilateral relations. Together with the United States and Israel, India and the UAE have also become part of a new quadrilateral economic forum inaugurated on 20th October.

These are decisive moves. At a time when India is finding a pressing need to expand its market access abroad and boost exports, the UAE could be a partner in furthering these goals. This is particularly so since the UAE has also come to be regarded as a gateway to Africa, Central Asia and other parts of the world in view of its efficient ports, airports and logistic arrangements.

The UAE could also be considered a suitable FTA partner because of the substantial level of complementarity between the two economies. The UAE is oil rich and non-agricultural. Its significant diaspora population is a ready consumer of several Indian goods and services. As a trading hub for gold and diamonds, the UAE has become a supplier of gold metal and diamond roughs for the diamond cutting and gold processing industry in India, creating a value chain.

Certain unique characteristics that need consideration

The UAE has, however, certain unique characteristics that will also need consideration. In a population close to 10 million, local Emiratis number less than 12% and the rest comprise expatriates. Among the latter, Indians top the list (27%) followed by Pakistanis (13%). The rest are made up by nationals from Bangladesh, Philippines, Iran, Egypt, Nepal, Sri Lanka, China and others. Extending rights under the FTA to natural persons and juridical persons who are not Emirati nationals will therefore need close scrutiny.

Secondly, UAE has zero corporate and income taxes[6] which is very attractive to investors. Indian entrepreneurs are no exception and have substantially

[5] https://www.indembassyuae.gov.in/bilateral-agreement.php
[6] The UAE does not levy income tax on individuals. However, it levies corporate tax on oil companies and foreign banks. See https://u.ae/en/information-and-services/finance-and-investment/taxation

invested in the country. It has also been alluring for resourceful Indians looking to park funds, including in the form of real estate purchases, or to relocate families with more easy access to education and other facilities. Whether an FTA will encourage more such movements is an important aspect to keep in view.

Third, the UAE is a significant trading and re-export hub[7]. This is apart from being part of the customs union with the other five GCC countries. A good part of its imports are re-exported. While precise re-export statistics are not immediately available for the country as a whole, its two major emirates, Dubai and Abu Dhabi, have reported that around 50% of imports by each of these emirates are re-exported[8]. There can be little doubt that several products exported from India to the UAE get re-exported to Pakistan, Iran, Iraq, central Asian and African countries. In several instances they could bring an additionality to India's exports. But they could also be a source of competition in building India's direct exports to those destinations. On the reverse side, India would also be a recipient of re-exports from the UAE, whose sources of origin are third countries including China, which is the UAE's largest source of imports. Items like gold metal, diamond roughs, cashew kernels, essential oils and copper items which figure among significant imports into India from the UAE are all likely to be sourced from third countries.

Fourth, the UAE is also keen to expand its non-oil business. Its minister of state for foreign trade, Al Zeyoudi, stated in New Delhi at the launch of CEPA negotiations on September 22, 2021 that the UAE was seeking to double non-oil trade with India to as much as US$100 bn over five years, as part of its efforts to boost ties with fast growing economies beyond the Middle East (two way non-oil bilateral trade has been around US$ 40 bn, even as this experienced a dip in 2020-21). The UAE already has an expanding industrial base covering construction materials, metals, chemicals, autos and consumer electronics, and it will be seeking to build and broad base these sectors further. It will continue to leverage its ease of doing business, special economic zones and zero tax policies in attracting investments, including from India. Whether and how the global minimum tax agreed to recently will impact this in the coming years remains to be seen.

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[7] UAE:A Business Manual by Ambassador Mahesh Sachdev is a detailed book about the country, its economy, the business opportunities, the regulatory regime and ways to navigate it for interested businesspersons., Published by Eco Diplomacy and Strategies, New Delhi, 2016

[8] See https://www.dubaicustoms.gov.ae/en/tradestatistics/Pages/default.aspx. and https://indd.adobe.com/embed/db3c782d-4e0c-4851-af03-0b790f5e30b4?startpage=1&allowFullscreen=true

The UAE's existing FTA portfolio

The UAE is party to a customs union among the six GCC countries (Bahrain, Kuwait, Oman, Qatar and Saudi Arabia are the other five) that came into force in 2003. Earlier, in 1998, it also became a member of a free trade arrangement among 16 Arabian countries (Pan Arabian Free Trade Agreement). Further, it is also party to the GCC's FTA arrangements with EFTA countries (in force from 2013) and Singapore (2014).

While the UAE is now negotiating the CEPA with India on its own, and not through the GCC, it is not clear if the UAE will rely on the GCC template, as it did in the agreements with EFTA and Singapore, for its negotiations with newer partners. However, in this brief, they are taken as reference points for drawing comparisons. Also, in addition to India, the UAE is keen to finalise comprehensive economic agreements with the UK, Turkey, South Korea, Ethiopia, Indonesia, Israel and Kenya[9].

Market Access benefits from the CEPA

The average MFN import tariff of the UAE is 4.7%[10]. Several items in India's export basket to that country, be it refined petroleum products, iron and steel items, chemicals, garments, cut and polished diamonds, gold jewellery or automobiles, carry a uniform duty of 5%[11]. Any reduction or elimination in this regime will be in India's interest, particularly since the UAE's current FTA partners are still somewhat limited in number. This will, however, require that all these items get included among the items which will see duty reduction/elimination coverage by the UAE in the CEPA under negotiation. It will further require that the rules of origin are carefully crafted, ensuring that even items like jewellery, cut and polished diamonds and refined petroleum products, which have limited value addition in percentage terms but require substantial investments, qualify.

There are also certain items of significant export by India such as rice, shrimps, pharmaceuticals, gold coins and ships, boats and floating structures which attract zero duty in the UAE . The CEPA will have to ensure they continue to remain so for India.

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[9] See https://www.dailysabah.com/business/economy/uae-seeks-quick-trade-talks-with-8-countries-eyes-deals-soon
[10] See page 37 of the WTO Trade policy review at https://www.wto.org/english/tratop_e/tpr_e/s338_e.pdf
[11] The tariff data has been verified from the WITS website

The benefits secured by the UAE from the CEPA may be substantially more in view of India's market size and its higher MFN tariff levels, averaging around 14%[12] (for non-agricultural products it is 12%). It will be in India's interest to ensure that the tariff reduction/elimination coverage is largely similar to those extended to ASEAN, Korea and Japan. But grant of duty concessions in the petroleum, petrochemical and jewellery sectors will need very careful assessment since they can be hugely distorting for the domestic economy. The UAE and other Gulf countries are also significant producers of aluminium, involving energy intensive smelting, that need careful scheduling. Duty reductions and their phasing will have to keep in view India's own Aatmanirbhar Bharat programme.

Equally important will be to ensure that the rules of origin and its certification mechanisms are on the one hand trade friendly, but are also tightly monitored so that re-export goods do not enter into the CEPA stream. While the UAE may in future use the CEPA to market itself to third countries as a gateway to the Indian market, the administration of the rules of origin should ensure there is substantial transformation in that country. It would also be very important for the agreement to have strong provisions on customs cooperation and transparency, to enable verification in case of transactions of dubious value or veracity.

Trade in Services and other issues

While there will be substantial interest among both the sides to have an ambitious services chapter in the CEPA, following a positive list in scheduling of commitments may be easier. In the GCC-Singapore FTA as well as in the GCC-EFTA FTA, such a positive list is followed[13]. An important aspect for India both in respect of services and investment will also be the scope of coverage of persons/entities in the commitments made. Will it extend only to Emirati natural persons and Emirati majority companies, or will the coverage be also extended to all juridical entities registered in the country and include foreign nationals who may be permanent residents of the UAE who are considered natural persons[14]? It will be in India's interest to restrict coverage to the former, particularly considering the range of expatriate nationalities in the UAE. This is

[12] See Table 3.3 presenting India's tariff structure in page 47 of the WTO Secretariat's report for India's trade policy review 2021 that can be accessed at https://www.wto.org/english/tratop_e/tpr_e/s403_e.pdf

[13] In both these FTAs only services were covered. Investment and intellectual property were left for later negotiations.

[14] UAE which had a conservative approach in extending such permanent residence is seen as being more liberal now. See also https://www.business-standard.com/article/pti-stories/uae-announces-plan-to-invest-in-economy-liberalize-laws-121090500815_1.html

important since it is seen that in both the GCC-Singapore and the GCC-EFTA FTAs, the latter approach has been followed. Another issue here is whether it should extend to Indian majority companies incorporated in the UAE wanting to trade in services or invest in India. While allowing this could encourage round tripping, not doing so it could curtail even beneficial exchanges. A balanced view will need to be taken. Further, the concerns expressed in this para will also be relevant in case disciplines are sought to be added on digital trade/e-commerce in the agreement

Considering the scale of movement of professionals, it will be important to have a strong chapter on this subject in the agreement. News reports suggest that India will be pushing for long term visas in the CEPA[15]. It would further be pertinent for India to look at whether there should be a chapter on the Indian worker's welfare in the CEPA. While the two countries have a separate MOU on the subject, considering its importance it may be a good opportunity to bilaterally assess progress in its implementation. This issue receives the Parliament's attention in India from time to time[16].

It is not clear whether the CEPA with the UAE will have provisions on IPRs, considering that this was not addressed in the GCC FTAs with Singapore and EFTA. But it would be in India's interest to have strong IPR enforcement provisions against pirating of movies and other videos, which continue to persist despite governmental actions[17]. Another aspect that India could focus on is getting a good set of provisions included on geographical indications, with specific items of interest recognised. It could also serve as a template for India's future FTAs.

Some overall aspects

The foregoing lists a few challenges that could confront negotiators in concluding a balanced CEPA. There could be others. It is important that they are all dealt with carefully and the negotiations are not fast tracked to meet unrealistic time frames. This writer would also not recommend going in for early harvest provisions unless these are very carefully considered and balanced. India's past experience in this regard has not been very successful[18].

[15] https://www.arabianbusiness.com/politics-economics/467886-india-may-push-for-long-term-visas-in-proposed-fta-with-uae
[16] https://www.mea.gov.in/rajya-sabha.htm?dtl/28177/question+no+1621+indian+workers+going+to+uae
[17] See https://gulfnews.com/uae/firms-step-in-to-stem-video-piracy-1.348678
[18] See the DPG policy brief by the author on "India-Australia FTA Talks: A Quick Harvest Should Not Become the Sole Harvest "

That said, the CEPA with the UAE could still turn out to be the first among the FTAs to be signed by India after a gap of over ten years (The CEPA with Mauritius signed earlier this year is a limited preferential trade agreement). It could also be a forerunner to more FTAs for which negotiations are underway. While each FTA will need crafting based on the partner in question, it is nevertheless useful for the country's trade policy administration if the FTAs are designed with a degree of coherence in terms of rules and commitments entered into. While the negotiation team for each FTA is headed by the Joint Secretary of the respective territorial division in the Ministry of Commerce, close coordination is crucial to ensure coherence. An understanding of the negotiation histories of India's earlier FTAs would provide useful pointers in this regard.

Some experts have also expressed a legitimate concern[19] that by rushing into a CEPA with the UAE, India could be prematurely ruling out such an arrangement with countries like the Kingdom of Saudi Arabia, which has a much larger economy as well as its own ambitious plans for expanding trade and industry. Indian diplomacy has its task cut out in this regard. The move should be projected as not ruling out another prospective partner, while prodding others also to come forward. After all, India's earlier plans for an FTA with the GCC did not proceed beyond a few negotiating rounds. FTA dynamics have shown that a compelling reason for a country to seek an FTA arrangement with a third country is because it does not want to get left behind in relation to a neighbour.

Concluding note

This brief outlines certain challenges in negotiating a bilateral CEPA that meets the aspirations and ambitious development plans of both India and the UAE. With substantial economic complementarities and due to the likely absence of non-trade issues, the task should be less difficult. It is to be welcomed that all concerned stakeholders in India are being consulted[20]. Beyond such sectoral responses and suggestions, it would be important to study the possible linkages between market access liberalisation, investment flows and prevailing taxation regimes in the specific context of the two countries. Its findings can provide useful inputs to Indian negotiators, particularly for phasing of tariff reductions and for defining the scope of beneficiary entities/persons in the services and

[19] See https://economictimes.indiatimes.com/news/india/view-india-uae-cepa-negotiations-is-a-case-for-making-haste-slowly/articleshow/87285009.cms
[20] See for example https://chemexcil.in/circulars/stakeholder-consultations-on-india-uae-cepa-negotiations-on-chemicals-and-petrochemicals--tariff-lines/5528/90da6cfebb0901fd82b4e8cbc85a7d9c.html. and https://dpiit.gov.in/sites/default/files/Stakeholder_Consultation_UAE_01October2021.pdf

investment chapters. A good agreement with the UAE can eventually also serve as a suitable template for India's possible negotiations with other GCC countries.

Annex 1: India-UAE bilateral trade for select years, in US$ billion

	2005-06	2010-11	2012-13	2013-14	2017-18	2018-19	2019-20	2020-21
India's exports to the UAE	8.59	33.82	36.32	30.52	28.15	30.13	28.85	16.68
India's imports from the UAE	4.35	32.75	39.14	29.02	21.74	29.78	30.26	26.62
Total bilateral trade	12.95	66.58	75.46	59.54	49.89	59.91	59.11	43.3
Trade balance for India	4.24	1.07	-2.82	1.5	6.41	0.34	-1.41	-9.94
Exports to UAE as % of India's total exports	8.33	13.54	12.1	9.71	9.27	9.13	9.21	5.72
Imports from UAE as % of India's total imports	2.92	8.86	7.98	6.45	4.67	5.79	6.37	6.75
India's exports of Petro products to UAE	1.39	4.02	6.17	4.18	4.48	2.85	5.59	2.71
India's imports of Petro products from UAE	0.213	9.39	14.97	13.25	9.06	13.33	15.97	11.72
India's exports of non-petro products to UAE	7.2	27.8	30.15	26.34	23.67	27.28	23.27	13.97
India's imports of non-petro products from UAE	4.14	23.36	24.16	15.77	12.67	16.45	14.29	14.1

Source: DGCIS

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