Why India forwent RCEP? Analyzing Trade Diversion Effects of Indian FTAs

Madhuri Kumari
Ayesha Fatma
Nalin Bharti
nalinbharti@iitp.ac.in

Abstract: *India was a dialogue partner in RCEP negotiations since the dialogue process formally launched in 2012. However, India backed out of the negotiations in November 2019. This has led to an intense debate over the gain vs. loss for India, and, whether India's decision to exit was a rational one. This study investigates this decision by examining how the existing Indian FTAs with countries that are also RCEP members, have served India till now. We also investigate how existing FTAs among the other ASEAN plus one FTA partners, have performed. The central focus of the study is on assessing the impact of these FTAs on the domestic market of India, through the inclusion of internal trade data. For the empirical analysis, the study follows an extended version of the Structural Gravity model, using panel data estimation, covering the time period 1962-2019. The results point towards overall strong domestic trade diversion effects with some variations from agreement to agreement. These findings indicate that India's decision to forego RCEP can be seen as the decision to protect its domestic market.*

Keywords: *Trade diversion, Internal trade, Structural gravity model, RCEP, ASEAN, IKCEPA, IJCEPA*

1. Introduction

Background

RCEP is one of the World's largest trading bloc and it aspires to strengthen the economic partnership that would create new jobs, enhance living standards and raise the welfare of the people within the region. The rationale behind the formation of the RCEP was to unite the ASEAN members and plus one members under a common agreement. The Joint Leader's Statement on RCEP in 2019, mentions that "Completion of the RCEP negotiations will demonstrate our collective commitment to an open trade and investment environment across the region". India was a part of the RCEP negotiations until November 2019. The country, however opted to quit the negotiations over significant issues, discussed in subsequent section. RCEP was eventually concluded by ASEAN and five countries with which they have Free Trade Agreements (FTAs) except India i.e. Australia, China, Japan, South Korea and New Zealand. However, the ministers reiterated at the 4th summit held in 2020 that India can join the agreement anytime as it was a part of the negotiation since launched in 2012. Also, they recognized India's potential in contributing to the overall prosperity in the region.

Reasons for India Exiting

India already shares trade agreements with ASEAN and two other ASEAN plus one FTA partners- Japan and South Korea. Wang and Sharma, (2021) explored that the major reasons for India to back out from RCEP are India's unbalanced economic relations with RCEP members,

China's rising hegemony in the region and India's push towards self-reliance. Deb (2020) points out that the decision is likely to protect the Indian domestic market from China's invasive dumping. India's decision also stems from the fear of being flooded with cheap imports from RCEP countries if it joins the agreement. Other reason to quit RCEP may be the expected welfare loss of India after joining RCEP due to the formation of new trade relations with new trade partners: China, New Zealand and Australia. Figure 1 and Figure 2 show India's export to, and import from the RCEP countries. It can be observed in Figure 1 that Indian export is highest to ASEAN. However, Figure 2 reveals that import to India is highest from China. This means that China as an RTA partner have could widened more the existing trade deficit gap of India with China (Table 1 and Figure 3), and also affecting the domestic producers by decreasing demands of domestic production. Moreover, New Zealand is the world's largest dairy exporter. India's yes to the agreement could have hurt the emerging dairy industry of the country (Mint, Nov 2019).

The condition of the existing Indian FTAs, especially the FTAs with ASEAN, Japan and South Korea also plays an equal important role in this decision. Indian FTAs have also recently come under the scanner of the Indian Government. The Government has in fact taken an interest in reviewing certain trade agreements, owing to doubts about their efficacy, as well as potential harm to the Indian economy due to these agreements. The members of these three FTAs are also the member of RCEP. Therefore, it is necessary to analyze the extent of trade creation or diversion in these FTAs.

Figure 1: India's Export to RCEP Countries
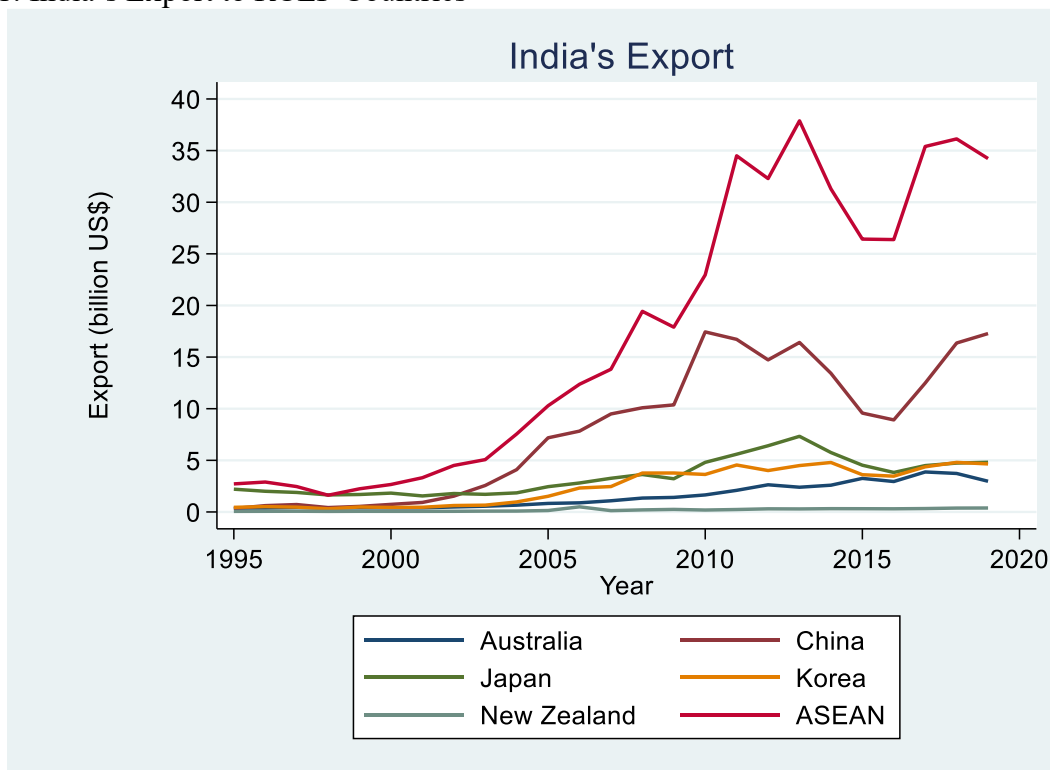
Source: UN Comtrade

Figure 2: India's import from RCEP countries
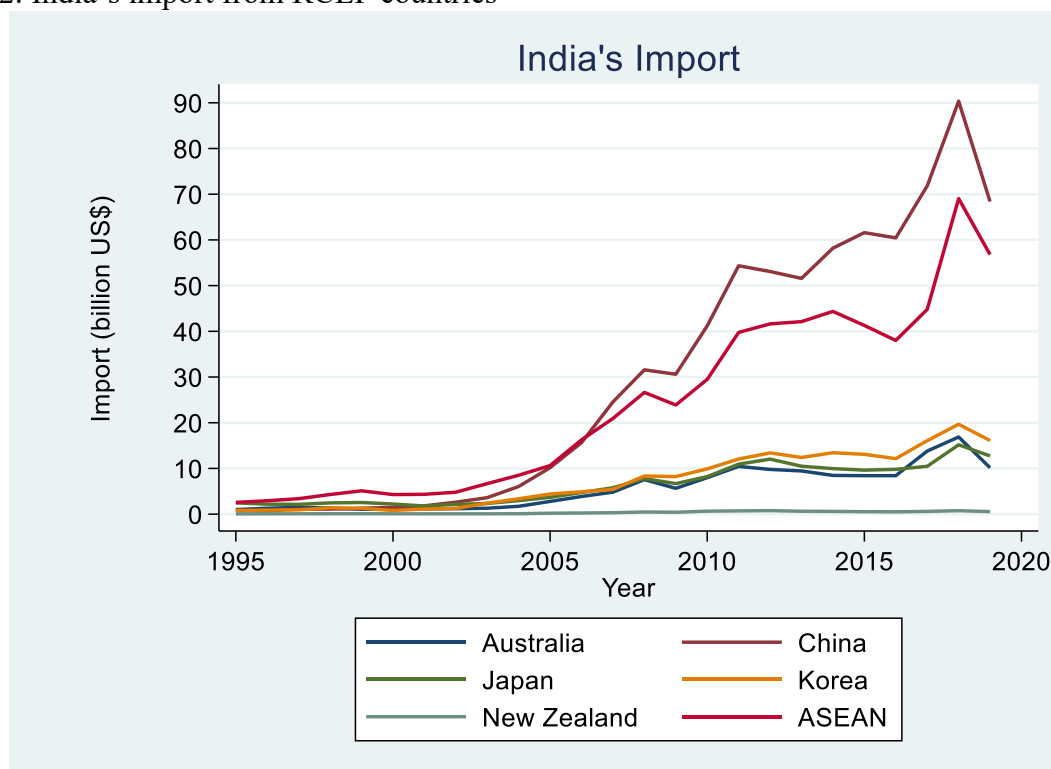
Source: UN Comtrade

Table 1: India's Trade deficit with RCEP members

Year	Australia	China	Japan	Korea	New Zealand	ASEAN
1995	-632714.39	-475290.368	-253069.49	-366399.814	-1762.096	144711.458
2000	-652413.53	-742692.262	-390868.56	-375268.361	-24773.675	-1632528
2005	-1955876.6	-2980399.68	-1225946.4	-2884091.53	-64745.257	-338570.94
2010	-6331410	-23744963.2	-3406377.8	-6270561.38	-462609.12	-6518775
2015	-5170311.1	-52013854.5	-5093609.1	-9478019.78	-235944.85	-14860902
2016	-5469651.6	-51532461.6	-5978406.9	-8677598.63	-199847.74	-11624281
2017	-9930079.1	-59334455.4	-5972326.7	-11703712.9	-282491.19	-9393555.9
2018	-13151593	-73994029.5	-10437811	-14870016.9	-371628.03	-32911880
2019	-7177642.6	-51123259.9	-7928787	-11457254.2	-174453.34	-22566941

Source: UN Comtrade

Figure 3: India's trade deficit with RCEP members

Madhuri Kumari
Ayesha Fatma
Nalin Bharti
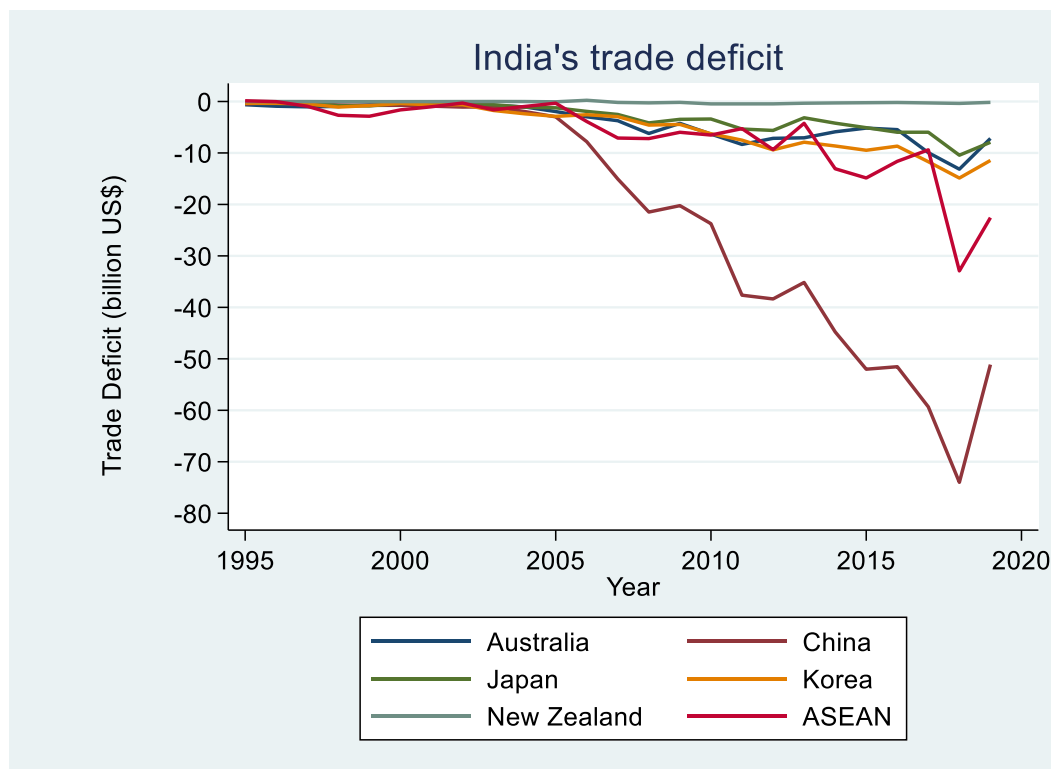
Source: UN Comtrade

Objective of the study

This study examines the impact of the Indian FTAs and ASEAN FTAs on trade flow. However, the study specially emphasizes the Indian FTAs with ASEAN, Japan and South Korea, since these three FTAs are members of the RCEP. This study investigates the trade creation and diversion effects of the FTAs. Further, another major highlight of the paper is the inclusion of internal trade data, because the study would be partial without considering the impact of internal trade, as internal trade represents the domestic market of the economy, and therefore it is a major determinant of the international trade creation and diversion. We have also estimated the impact of FTAs on internal trade, separately. Our analyses help us understand the impact of existing FTAs of India and ASEAN in two separate models, which allows us to assess how useful these agreements have been for the participant countries. The results from our study provide a thorough empirical assessment of the impact of existing trade agreements among RCEP members. This provides us with evidence-based reasoning behind India's exit from RCEP, as it considers the role of existing agreements in contributing towards India's decision to exit RCEP.

The paper is organized as the follows. Section 2 presents a brief Literature Review, followed by Section 3 explaining Data and Methodology. Subsequently, Section 4 presents the Results and Discussions of our findings, followed by the Conclusion on Section 5.

2. Literature Review

An RTA is supposed to assist trade and investment among the members. However, the RTA may have different effects on member countries and non-member countries. It may have trade creation effects if the RTA liberalization leads to substitution of high-cost products in the domestic market by low-cost products by the RTA member. On the other hand, it may have trade diversion effects for the non-member countries due to high tariffs faced by them. RTAs may not only divert trade away from non-partner countries but also from internal trade in partner countries (Dai et al., 2014).

Evidence on existing FTAs of RCEP members

Gopalakrishnan (2020) explored that AFTA has no any pure trade creation nor any pure trade diversion effects. However, ASEAN's exports to the world is significant and positive, that is, there is export trade creation. Sattayanuwat and Tangvitoontham (2017) analyzed the effects of ASEAN PTAs. The study revealed that RCEP including India has an intra-block trade creation effects for ACFTA, AJCEP and AIFTA. However, results show that there is export trade diversion in AKFTA and AANZFTA.

Most of the existing body of literatures suggest that negotiating countries will get benefit from RCEP while non-negotiating countries will lose relatively (Cheong & Tongzon, 2013; Kawasaki, 2015; Li et al., 2016; Rahman & Ara, 2015). Petri et.al (2017) found that the agreement would create global GDP gains worth US$ 286 billion. Kawasaki (2015) reveals that developing countries will have more GDP gains than the developed countries of the agreement.

India and RCEP

a) Overview

Li et al. (2016) forecast a large welfare gain as a percentage of GDP for India and Korea i.e. 1.79% and 2.77%, respectively. However, Sharma (2018) called RCEP a sort conventional trade agreement focused around tariff cuts and debars other major cooperation issues. Further, Kumar (2019) called RCEP a "lose-lose-lose" proposition for India. Most of the subjects of the agreement seemed to be unfavorable for India, particularly the prerequisite to lower tariffs with MFN treatment, no address of NTB's issues, and inadequate commitment for trade in services and inability of the economy to safeguard strict rules of origin against import surge.

Among the six ASEAN plus one FTAs, India-ASEAN FTA has resulted in the least liberalization indicating RCEP tariff concessions to be far exceeding than this FTA (Oba, 2016). However, lowering of tariffs by developing countries can attract more investment from other RCEP countries further enhancing the global value chains (Flento and Ponte, 2017). India could gain with the liberalization of the service sector gaining an opportunity to employ its skilled professionals (Raghavan and Haidar, 2018). RCEP may reduce the risk of the 'spaghetti bowl' of overlapping Asian FTAs (Wignaraja, 2014). However, it could have been detangled to a greater extent with inclusion of India, since India is partner of various bilateral and multilateral FTAs with other Asian countries.

b) India and RCEP: Evidence from ex-ante general equilibrium analysis

Narayanan et.al (2019) analyzed welfare effects for India hypothesizing a full tariff liberalization for the RCEP negotiations and further focused on automobile sector applying CGE (Computable General Equilibrium) simulation utilizing 2015 baseline data. The findings suggest an overall welfare gain, but a negative impact on automobile sector unless it grows with at least 2.5% of annual productivity. India is not in a stage to consider full tariff liberalization. Therefore, India needs to focus on manufacturing sector and improve domestic productivity while negotiating any future RTAs that considers a phased tariff liberalization.

Mahadevan and Nugroho (2019), applying a dynamic CGE model analyzed the effect of RCEP if India back outs. The results reveal that the economy's GDP growth will fall marginally if it does not join compared to slight increase after it joins. However, the study further reveals that if India joins the agreement, India' s welfare loss as percentage of GDP would be larger compared to if it backs out. India's withdrawal have only a little impact on the agreement members, particularly the small economies of the RCEP.

Research Gap

The existing studies focus more or less on the ASEAN plus one FTAs to draw the conclusion if India should have joined RCEP. There is scanty literature focusing on the state of existing Indian FTAs that also play a crucial role in India's decision-making regarding approval for a new FTA, especially since India already has FTAs with several RCEP members. Further, the is lack of empirical studies on India's and ASEAN's FTAs, that accounts for the importance of internal trade in influencing the decision. As our study employs the Structural Gravity model, the inclusion on internal trade data also makes the model more theoretically consistent.

3. Data and Methodology

The study uses secondary trade data extracted from CEPII gravity model database for a total of 247 trading partners, covering the time period of 1962-2019. The recent advancement in the gravity model i.e. the structural gravity model by Anderson and Wincoop (2003) has been applied in the study. The baseline model follows Baier and Bergstand (2007) by using bilateral fixed effects considering the endogeneity of the FTAs. The model has been estimated by adopting PPML estimator proposed by Santos Silva and Tenreyro (2006). Further, the study focuses on internal trade following the novel approach by Dai et al. (2014). We have produced two sets of models to figure out the possible reasons for India cutting out of RCEP negotiation. The first set of models explains the impact of existing Indian FTAs on the trade. Whereas, the second set of models unfolds the effect of ASEAN plus one FTAs on trade. All the estimates have been obtained after accounting for the full set of fixed effects- importer-time fixed effect, exporter-time fixed effect and country pair fixed effects. Further, standard errors reported are robust and have been obtained by clustering country pairs.

The models for the study:

1. Indian FTAs model

(a) Baseline econometric specification
$$X_{ij,t} = \exp\left[\pi_{i,t} + \chi_{j,t} + \eta_{ij} + \sum_k \beta_k FTAI_{ij,t}\right] \times \varepsilon_{ij,t}$$

(b) Augmented model for diversion effects of FTA
$$X_{ij,t} = \exp\left[\pi_{i,t} + \chi_{j,t} + \eta_{ij} + \sum_k \beta_k FTAI_{ij,t} + \sum_l \beta_l FTAI_{i,-j,t} + \sum_m \beta_m FTAI_{-i,j,t}\right] \times \varepsilon_{ij,t}$$

Here the independent variable X denotes export value from country "i" to country "j" at time "t", the dependent variable π is time varying exporter fixed effect, χ is time varying importer fixed effect, η is set of country pair fixed effects and ε is the error term. The inclusion of π, χ and η in the model controls for the multilateral resistances for the trade. The term $"\sum_k \beta_k FTAI_{ij,t}"$ denotes the set of FTAs signed by India. These are the India's FTAs with Afghanistan, Bhutan, Chile, Japan, South Korea, Sri Lanka, Malaysia, Nepal, Singapore, Thailand, ASEAN, APTA, MERCOSUR, SAFTA and SAFTA. $FTA_{ij,t}$ is a dummy variable capturing the presence of a free trade agreement between partners i and j at time t. It takes value 1 if both exporter and importer countries are the member of FTA. Model (b) is the extended version of model (a) to capture diversion effects. $FTAI_{i,-j,t}$ is an indicator that takes value 1 if exporter i has signed an FTA with any trade partner other than j (i.e., with an outsider) and it takes value zero otherwise. Similarly, $FTAI_{-i,j,t}$ equals one if importer j has signed an FTA with any outside trade partners.

2. ASEAN plus one FTAs model

(a) Baseline econometric specification
$$T_{ij,t} = \exp\left[\theta_{i,t} + \gamma_{j,t} + \Omega_{ij} + \sum_p \lambda_p FTAA_{ij,t}\right] \times \omega_{ij,t}$$

(b) Augmented model for diversion effect of FTAs
$$T_{ij,t} = \exp\left[\theta_{i,t} + \gamma_{j,t} + \Omega_{ij} + \sum_p \lambda_p FTAA_{ij,t} + \sum_q \lambda_q FTAA_{i,-j,t} + \sum_r \lambda_r FTAA_{-i,j,t}\right] \times \omega_{ij,t}$$

As the previous model, the independent variable T here denotes export value from country "i" to country "j" at time "t", the dependent variable θ is time varying exporter fixed effect, γ is time varying importer fixed effect, λ is set of country pair fixed effects and ω is the error term. The term $"\sum_p \lambda_p FTAA_{ij,t}"$ denotes the set of ASEAN plus one agreements. These are the FTAs with Australia-New Zealand, China, Japan and South Korea. $FTAA_{i,-j,t}$ and $FTAA_{-i,j,t}$ extends the model to explain creation and diversion effects. Further elucidation for model (b) goes same as the previous model.

4. Results and Discussion

The PPML estimator has been used to analyze both sets of specifications. Table 1 and Table 2 shows the analysis results. Table 1 reports results for model specifications 1a and 1b i.e., the impact of Indian FTAs on trade flow and Table 2 reports results for model specifications 2a and 2b i.e., the impact of ASEAN plus one FTAs on trade flow. In both the tables, Column (1) and Column (2)

report results for our baseline model i.e., model specification (a). Column (3) and Column (4) report results for model specification (b) which augments baseline model by adding export and import diversion effects.

The coefficients in Column (1), shows the estimates of FTAs on international trade only, whereas Column (2) also accounts for the impact of internal trade of the countries. We account for internal trade by supplementing the dataset with additional observations that includes data on internal trade as well. Column (3) augments the specification of Column (2) by also reporting results for the export and import creation/diversion effects of the FTAs. In Column (4) we further include a separate variable for internal trade, which takes the value 1 when the observations depict internal trade, after the country joins an FTA at time t. This helps us show the domestic trade creation/diversion effect of an FTA.

In Column (3), the positive magnitudes of the subscripts "ij,t", "i,-j,t", "-i,j,t" shows an overall increase in trade between the members, trade creation due to export and trade creation due to import, respectively. When these coefficients take a negative value, it shows a decrease in trade between the FTA members, export diversion and import diversion in same order. In Column (4) the positive magnitude for the additional subscript "ii,t" indicates internal trade creation, while the negative sign shows the opposite i.e. internal trade diversion.

Table 1: Indian FTAs

VARIABLES	(1) PPML without IT	(2) PPML with IT	(3) PPML TE	(4) PPML TE with IT
AFGINDij,t	-0.910**	-0.447	-3.588***	-3.558***
	(0.400)	(0.400)	-0.442	(0.360)
AFGIND$i,-j,t$			5.259***	3.436***
			(1.215)	(1.137)
AFGIND$-i,j,t$			-1.488	-2.230**
			(1.353)	(1.127)
AFGINDii,t				0.997***
				(0.221)
BTNINDij,t	0.579	0.614*	0.595*	0.550
	(0.534)	(0.343)	(0.353)	(0.542)
BTNIND$i,-j,t$			-2.572***	-1.970***
			(0.588)	(0.620)
BTNIND$-i,j,t$			0.481	1.451*
			(1.088)	(0.842)
BTNINDii,t				0.360
				(0.835)
CHLINDij,t	0.557***	2.058***	1.145***	0.157
	(0.151)	(0.165)	(0.102)	(0.127)

CHLINDi,-j,t			0.880***	0.318*
			(0.220)	(0.174)
CHLIND-i,j,t			1.266***	0.645***
			(0.217)	(0.184)
CHLINDii,t				-1.365***
				(0.181)
IJCEPAij,t	-0.076	0.542***	-1.568***	-0.972***
	(0.171)	(0.170)	(0.158)	(0.150)
IJCEPAi,-j,t			-0.012	-0.039
			(0.170)	(0.171)
IJCEPA-i,j,t			0.160	0.062
			(0.124)	(0.105)
IJCEPAii,t				-0.145*
				(0.087)
IKCEPAij,t	0.194**	1.318***	0.429***	-0.035
	(0.085)	(0.135)	(0.097)	(0.093)
IKCEPAi,-j,t			0.123	-0.260
			(0.247)	(0.229)
IKCEPA-i,j,t			-0.143	-0.642***
			(0.254)	(0.233)
IKCEPAii,t				-0.907***
				(0.085)
LKAINDij,t	0.662***	0.913***	0.678***	0.397***
	(0.172)	(0.179)	(0.160)	(0.133)
LKAINDi,-j,t			-0.958*	-1.175***
			(0.506)	(0.446)
LKAIND-i,j,t			-0.761***	-0.935***
			(0.281)	(0.289)
LKAINDii,t				-0.829***
				(0.256)
MYSINDij,t	-0.000	-0.011	-0.037	-0.059
	(0.110)	(0.173)	(0.150)	(0.088)
MYSINDi,-j,t			0.331	0.509**
			(0.253)	(0.226)
MYSIND-i,j,t			0.058	0.163
			(0.326)	(0.296)
MYSINDii,t				0.334***
				(0.110)
NPLINDij,t	0.503**	0.395**	0.023	0.552**
	(0.199)	(0.162)	(0.190)	(0.229)
NPLINDi,-j,t			-1.608***	0.221
			(0.509)	(0.485)
NPLIND-i,j,t			-1.345***	-0.227
			(0.383)	(0.338)
NPLINDii,t				2.303***
				(0.187)

SGPINDij,t	-0.081	-0.064	-0.042	-0.248
	(0.193)	(0.269)	(0.239)	(0.181)
SGPINDi,-j,t			-0.001	0.339*
			(0.194)	(0.188)
SGPIND-i,j,t			-0.639***	-0.303
			(0.197)	(0.191)
SGPINDii,t				0.747
				(0.854)
THAINDij,t	0.116	1.183***	0.841***	-0.245
	(0.316)	(0.351)	(0.258)	(0.265)
THAINDi,-j,t			0.610**	0.320
			(0.308)	(0.266)
THAIND-i,j,t			0.552**	0.040
			(0.258)	(0.195)
THAINDii,t				-1.185***
				(0.141)
AFTAINDij,t	0.109	0.910***	0.057	-0.025
	(0.134)	(0.240)	(0.199)	(0.095)
AFTAINDi,-j,t			0.281*	0.014
			(0.166)	(0.163)
AFTAIND-i,j,t			0.690***	0.400***
			(0.148)	(0.146)
AFTAINDii,t				-0.759***
				(0.086)
APTAij,t	0.168***	0.299***	0.036	0.160***
	(0.049)	(0.054)	(0.062)	(0.050)
APTAi,-j,t			0.407*	0.449**
			(0.215)	(0.214)
APTA-i,j,t			0.781***	0.810***
			(0.209)	(0.206)
APTAINDii,t				-3.052***
				(0.243)
MERCOSURINDij,t	0.274***	1.553***	-0.074	-0.070
	(0.088)	(0.140)	(0.111)	(0.102)
MERCOSURINDi,-j,t			-1.448***	-1.214***
			(0.095)	(0.121)
MERCOSURIND-i,j,t			1.402***	1.379***
			(0.233)	(0.225)
MERCOSURINDii,t				-
SAFTAij,t	-0.059	0.622***	0.146	-0.274**
	(0.175)	(0.120)	(0.124)	(0.135)

	(1)	(2)	(3)	(4)
SAFTAi,-j,t			-1.999	-0.451
			(1.465)	(1.288)
SAFTA-i,j,t			3.267**	4.246***
			(1.498)	(1.281)
SAFTAii,t				-0.851***
				(0.098)
SAPTAij,t	0.068	0.796***	0.638**	-0.070
	(0.190)	(0.241)	(0.304)	(0.261)
SAPTAi,-j,t			1.861	-0.209
			(1.612)	(1.431)
SAPTA-i,j,t			-2.602*	-4.026***
			(1.531)	(1.315)
SAPTAii,t				-0.510***
				(0.113)

Robust standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

Table 2: AFTA plus one FTAs

VARIABLES	(1) PPML	(2) PPML with IT	(3) PPML DE	(4) PPML DE with IT
AFTAINDij,t	0.101	1.097***	0.974***	0.207
	(0.120)	(0.152)	(0.142)	(0.143)
AFTAINDi,-j,t			-0.073	-0.026
			(0.260)	(0.209)
AFTAIND-i,j,t			0.033	0.077
			(0.325)	(0.251)
AFTAINDii,t				-0.553**
				(0.215)
AFTACHNij,t	0.116*	1.225***	-0.050	-0.543***
	(0.070)	(0.127)	(0.164)	(0.147)
AFTACHNi,-j,t			0.430*	-0.168
			(0.220)	(0.141)
AFTACHN-i,j,t			0.627***	-0.028
			(0.212)	(0.131)
AFTACHNii,t				-1.773***
				(0.117)
AFTAJPNij,t	0.122*	0.421***	-0.214*	-0.603***
	(0.070)	(0.115)	(0.126)	(0.161)
AFTAJPNi,-j,t			0.027	0.004
			(0.184)	(0.162)
AFTAJPN-i,j,t			-0.040	-0.075
			(0.152)	(0.132)

Madhuri Kumari
Ayesha Fatma
Nalin Bharti

	(1)	(2)	(3)	(4)
AFTAJPNii,t				0.036
				(0.124)
AFTAKORij,t	0.133*	0.730***	0.642***	0.076
	(0.070)	(0.111)	(0.104)	(0.156)
AFTAKORi,-j,t			0.462***	0.490***
			(0.132)	(0.130)
AFTAKOR-i,j,t			0.318**	0.321*
			(0.146)	(0.167)
AFTAKORii,t				-0.006
				(0.195)
AFTAAUSNZLij,t	-0.067	0.446***	0.233***	-0.581***
	(0.069)	(0.094)	(0.077)	(0.109)
AFTAAUSNZLi,-j,t			-0.093	0.202
			(0.147)	(0.129)
AFTAAUSNZL-i,j,t			-0.123	0.113
			(0.276)	(0.181)
AFTA_AUS_NZLii,t				0.018
				(0.247)

Robust standard errors in parentheses
*** $p<0.01$, ** $p<0.05$, * $p<0.1$

The FTA estimates in both our models, without internal trade (as reported in Column 1), as well as with internal trade (Column 2) have positive and statistically significant coefficients. This shows a trade creation effect of the FTAs among the FTA members. The coefficients in Column (2) for all FTAs are greater than Column (1), Nepal-India FTA being an exception. This shows that accounting for internal trade has resulted in increasing the magnitude of the trade creation effects of the FTAs.

Internal Trade Creation and Diversion Effects

Column (4) of Table 1 and Table 2 reports results for the internal trade creation and diversion effects of Indian FTAs and ASEAN plus one FTAs respectively. In Table 1, we can see that the coefficients for almost all Indian FTAs are negative and significant. This shows that there is a clear internal trade diversion affecting the domestic trade for the members of the particular FTAs. However, in Table 2, only estimates for ASEAN-India and ASEAN-China internal trade turn to be significant.

a) Indian FTAs

We focus on three particular Indian FTAs: India-ASEAN, IJCEPA and IKCEPA, as these countries were supposed to be RCEP members. Drawing the results from Table 1 which includes all other Indian FTAs, the inclusion of internal trade makes its estimate significant and positive that shows an overall increase in trade among the trade partners. However, as seen in Column (3),

including the trade effects separately, for export and import, show both significant export creation and import creation effects for FTA members. In Column (4), again we see that the internal trade effects coefficients are all significant except India-ASEAN. The India-ASEAN FTA shows a slightly negative but insignificant impact on trade flow, a small export creation effect also insignificant. The import creation effect, however is significant and comparatively larger in magnitude. We also see significant internal trade diversion effects of the agreement.

Similar to the India-ASEAN case, the inclusion of internal trade in IJCEPA, as seen in Column (2), Table, makes it significant and positive, indicating increase in trade. However, in Column (3) we see that the inclusion of export and import effects keeps the coefficients significant but turns it negative. However, the export and import effects themselves remain insignificant. In Column (4), the internal trade effect is significant and negative, which confirms internal trade diversion. This indicates that the agreement has had a negative impact on overall trade between India and Japan when the effect on internal trade is accounted for. This shows that exclusion of domestic effects can give an incomplete picture of an agreement's impact.

For IKCEPA, the results show a significant increase in trade due to the FTA both without internal trade (Column 1) and with, the inclusion of internal trade (Column 2). However, the results are insignificant for export and import effects as seen in Column (3). The inclusion of separate internal trade effects in Column (4), shows a significant import diversion effects, and a greater diversion in internal trade than that of IJCEPA.

Our results show that IJCEPA and India-ASEAN agreements' positive impact is observable only when we account for internal trade. For IKCEPA, the impact is positive for both cases. Accounting for internal trade separately however, shows clear internal trade diversion effects of all three agreements. The picture is more mixed for the India-ASEAN agreement but even in that case, the internal trade diversion effects can be observed. This shows us an emerging pattern of adverse domestic effects of Indian FTAs. These findings show India's FTA with RCEP members, have not achieved their desired objectives and hence helps explain India's hesitancy in entering into a large agreement like the RCEP with these countries. India is also in-fact keen on reviewing both IJCEPA and IKCEPA (Mint, 2019; Sen, 2021)

b) ASEAN plus one FTAs

Table 2 shows significant and positive estimates for all ASEAN plus one FTAs upon when including internal trade, as seen in Column (2). However, Column (3) shows, these results vary after the inclusion of separate import effects and export effects. India, Korea, Australia and New Zealand see a positive and significant impact of FTAs with ASEAN, whereas Japan sees a negative and significant impact. China sees an insignificant impact. The results for ASEAN FTAs with India, Japan, Australia and New Zealand are insignificant for export and import effects, and significant and positive for China and Korea. Column (4) shows significant negative impact of ASEAN FTAs with China, Japan and Australia-New Zealand. ASEAN FTAs with India and South Korea, on the other hand, turn insignificant. Only South Korea has a significant trade creation through both export and import. For ASEAN-South Korea, the internal trade diversion effect is negative but magnitude is very low, near to zero. For ASEAN-Japan and ASEAN-Australia and New Zealand, the internal trade diversion effect is positive. However, they all are insignificant.

Madhuri Kumari
Ayesha Fatma
Nalin Bharti

Our results, once again, show that internal trade plays a crucial role in depicting the whole picture. It also shows that the benefits of the ASEAN agreement are uneven among members. For instance, India and China overall appears to be negatively impacted by its FTA with ASEAN whereas other members are not significantly impacted. For both India and China, export and import effects are insignificant, so it is the significant negative internal trade effects that is the driving factor behind the overall negative impact of the agreement for these countries.

5. Conclusion

To make decision whether to join a new RTA, it is necessary for a country to analyze whether its existing FTAs/ RTAs serve their stated purpose. It is also essential to assess the impact of trade relations with the new RTA partners. Our study assesses this impact for existing Indian FTAs, and also ASEAN plus one FTAs, to investigate the potential usefulness of RCEP membership. Based on how efficient how these already existing FTAs have been, this can be an important indicator of whether another agreement in form of RCEP is a good idea or not.

Our results show that for most of the Indian FTAs as well as ASEAN plus one FTAs, the role of internal trade is crucial. For instance, when our study focusses on India's existing agreements with RCEP members, Japan, Korea and ASEAN, after accounting for internal trade separately we see clear diversion effects of all three agreements. As far as the ASEAN plus one agreement is concerned, for India as well as China, we again see internal trade effects to be the driving factor behind the overall negative impact of the agreement for these countries.

Given the adverse impacts of these agreements on internal trade, India's decision to quit RCEP can be seen as the decision to protect its domestic market. To be able to get gains from trade agreements in the form of trade creation effects, especially via exports, the only long-time viable path for India, is to improve its competitiveness and produce cost effective and quality products so that it does not lose out the opportunity to enter new markets. India can gain from such agreements only when it is in the position to move beyond simply being a market for other countries' goods (Verma, 2020). The floor to join RCEP is still open for India. The economy must prepare itself to stand with the global market and take advantage of the vast market offered by RCEP.

References

Anderson, James E., van Wincoop, Eric, 2003. Gravity with gravitas. Amer. Econ. Rev. 93 (1), 170–192.

Aiyar, S. S. A. (2020). India Should Join Asia's New Free- Trade Area. *Cato Institute Economic Development Bulletin*, (32).

Baier, Scott L., Bergstrand, Jeffrey H., 2007. Do free trade agreements actually increase members' international trade? J. Int. Econ. 71 (1), 72–95.

Cheong, I., & Tongzon, J. (2013). Comparing the economic impact of the trans-Pacific partnership and the regional comprehensive economic partnership. *Asian Economic Papers*, *12*(2), 144-164.

Dai, M., Yotov, Y. V., & Zylkin, T. (2014). On the trade-diversion effects of free trade agreements. *Economics Letters*, *122*(2), 321-325.

Deb, R. (2020). Is RCEP a Panacea for India?. *The Indian Economic Journal*, *68*(4), 659-666.

Flentø, D., & Ponte, S. (2017). Least-developed countries in a world of global value chains: Are WTO trade negotiations helping? World Development, 94, 366–374

Gopalakrishnan, N. (2020). Trade Creation or Diversion? An ASEAN Perspective.

Joint Leader's Statement on the Regional Comprehensive Economic Partnership (RCEP). 4 November 2019, Bangkok, Thailand. https://rcepsec.org/wp-content/uploads/2019/11/FINAL-RCEP-Joint-Leaders-Statement-for-3rd-RCEP-Summit.pdf

Kawasaki, K. (2015). The relative significance of EPAs in Asia-Pacific. Journal of Asian Economics, 39, 19–30.

Kumar,M. (2019). Rejecting RCEP was an easy part. Hindustan Times. https://www.hindustantimes.com/analysis/rejecting-rcep-was-the-easy-part-ht-analysis/story-oM0QORymKE5CGUZo9GEAPP.html

Li, C., Wang, J., Whalley, J. (2016). Impact of mega trade deals on China: A computational general equilibrium model. Economic Modelling, 57, 13–25.

Mahadevan, R., & Nugroho, A. (2019). Can the Regional Comprehensive Economic Partnership minimise the harm from the United States–China trade war?. *The World Economy*, *42*(11), 3148-3167.

Mint. (5 November, 2019). As India says no to RCEP, dairy farmers heave a sigh of relief. https://www.livemint.com/news/india/as-india-says-no-to-rcep-dairy-farmers-heave-a-sigh-of-relief-11572955122690.html

Mint. (30 Decemeber, 2019). Govt to review free trade agreements, says Piyush Goyal. https://www.livemint.com/news/india/govt-to-review-free-trade-agreements-says-piyush-goyal-11577717183056.html

Narayanan, B. G., Sen, R., & Srivastava, S. (2019). *Tariff liberalization in the RCEP trade agreement and impact on India's automobile industry: An applied general equilibrium analysis* (No. 183). ARTNeT Working Paper Series.

Oba, M. (2016). TPP, RCEP, and FTAPP: Multilayered Regional Economic Integration and International Relations. Asia Pacific Review, 23, 100–114

Petri, P., Plummer, M., Urata, S., & Fan, Z. (2017). Going it alone in the Asia-Pacific: Regional trade agreements without the United States (Working Paper 17–10, October 2017). Peterson Institute for International Economics, Massachusetts.

Raghavan, S., & Haidar, S. (2018) ASEAN member countries of RCEP offer India concession. The Hindu 8 November 2018. Retrieved from https://www.thehindu.com/business/Economy/asean-member-countries-of-rcep-offer-indiaconcession/article25439321.ece

Rahman, M., & Ara, L. (2015). TPP, TTIP and RCEP: Implications for South Asian economies. South Asia Economic Journal, 16, 1–19.

Santos Silva, J.M.C., Silvana, Tenreyro, 2006. The log of gravity. Rev. Econ. Stat. 88 (4), 641–658

Sattayanuwat, W., & Tangvitoontham, N. (2017). Trade creation and trade diversion of ASEAN's preferential trade agreements'. *IAFOR Journal of the Social Sciences*, *3*(1), 5-1

Sen, A. (2021). CEPA Review: India wants pact revision; Japan proposes corrections within existing framework. The Hindu Business Line. https://www.bilaterals.org/?cepa-review-india-wants-pact

Sharma, M. (2018). India can't keep dodging trade deals. Bloomberg Opinion 16 November 2018. Retrieved from https ://www.bloomberg.com/opinion/articles/2018-11-15/india-and-china-can-t-let-rcep-trade-talks-fail

Madhuri Kumari
Ayesha Fatma
Nalin Bharti

Verma, R. (2020). The regional comprehensive economic partnership and India: A test case of Narendra Modi's statesmanship. *Australian Journal of International Affairs*, *74*(5), 479-485.

Wang, C., & Sharma, V. (2021). India's RCEP Dilemma with China: Beyond the Legal Texts. *Pacific Focus*, *36*(1), 40-62.

Wignaraja, G. (2014). The regional comprehensive economic partnership. An initial assessment. In P. Petri & T. Guoqiang (Eds.), New directions in Asia-Pacific economic integration. Honolulu, HI: East-West Center