India's Free Trade Agreements and Micro, Small and Medium Enterprises

A Case Study of the Food Processing Industry

I. Introduction

In recent years, India's international trade policy has been increasingly moving away from WTO's multilateral framework towards **Free Trade Agreements (FTAs)**. While the WTO's multilateral trade framework obliges its member countries to reduce border duties and adhere to higher labour and environmental standards, FTAs aim at total elimination of all tariffs and contain many items that are not part of the rules of the WTO (See Box 1). Since FTAs have such wide coverage they can create a significant impact on domestic production system. As a result, FTAs may severely impact the growth prospects of certain key sectors of the economy including the **Micro, Small and Medium Enterprises (MSME)** sector.

> **Box 1: What do FTAs Cover?**
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> **FTAs are trade (and investment) agreements between two countries (or blocs) which aim to give each other access to each others' markets.**
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> - ✓ **FTAs can cover trade in goods (such as agricultural or industrial products) or trade in services (such as banking, construction, trading etc) by;**
> - ✓ **Lowering or removing border protection measures such as border taxes on exports and imports, on goods trade;**
> - ✓ **Changing/ creating other barriers such as standards and processes, rules of origin, trade facilitation and dispute settlement.**
> - ✓ **FTAs can also cover other areas such as intellectual property rights (IPRs), investment, government procurement and competition policy.**

India's MSME sector in general and certain industries in particular play an important role in its economic and social arena. India's Food Processing (FP) industry is one of the largest industries in the country mainly on the account of its strong agricultural base. The FP industry occupies fifth rank in terms of production, consumption, export and expected growth. The size of the Indian FP industry is estimated at Rs 280,000, and it contributes more than 14% of the manufacturing GDP and over 6% of India's over all GDP. The FP Industry in India is also a big employer of people from the unorganised sector. It employs about 13 million directly and about 35 million people indirectly. The unorganised sector contributes more than 70% of production in volume terms and about 50% in the value terms (All figures are from Annual Report, 2010-11, MOFPI, GOI). The share of India's export of processed food in global trade is 1.5%. Given the size and growth prospect of this sector, India's trade policy has an important role to play in shaping its future. How we liberalise processed food markets now will determine how and in which segments it can continue to grow.

II. Why is the Food Processing Industry Important?

India's food processing (FP) sector covers activities such as agriculture, horticulture, plantation, animal husbandry and fisheries. It also includes other industries that use agriculture inputs for manufacturing of edible products. Table 1 gives the major segments of the FP industry in India along with their major products. Even though the Indian FP sector is a large one, it is still at a nascent stage. The processing level of food produce is very low in India compared to other countries of the world. Only about 2% of the total food produce in the country is processed. While the level of processing is higher in dairy (about 35%) and marine products (26%), it is very low in fruits and vegetables (2.2%) (See Table 2) compared to countries like USA (65%), Philippines (78%), and China (23%).

Table 1: Segmentation of Different Sectors in Food Processing Industry

Sectors	Products
Dairy	Whole Milk Powder, Skimmed milk powder, Condensed milk, Ice cream, Butter and Ghee, Cheese
Fruits & Vegetables	Beverages, Juices, Concentrates, Pulps, Slices, Frozen & Dehydrated products, Potato Wafers/Chips, etc
Grains & Cereals	Flour, Bakeries, Starch Glucose, Cornflakes, Malted Foods, Vermicelli, Beer and Malt extracts, Grain based Alcohol
Fisheries	Frozen & Canned products mainly in fresh form
Meat & Poultry	Frozen and packed - mainly in fresh form, Egg Powder
Consumer Foods	Snack food, Namkeens, Biscuits, Ready to eat food, Alcoholic and Non-alcoholic beverages

Source: Ministry of Food Processing, GOI, Annual Report, 2004

Sub Sector Analysis

Dairy: India is on the verge of assuming an important position in the global dairy industry. The branded butter market, the cheese market and ice cream are registering impressive growth and show growth prospects especially in the urban areas. Some of the big corporate players, including MNCs, such as Nestle, Britannia and ITC are now focusing on this market. The dairy sector has also attracted huge foreign investment in the recent past which indicates that there are enormous business opportunities in this segment of the food processing industry.

Fruit and Vegetable Processing: There is enormous scope for improving the level of processing in this sector. Over the last few years, the installed capacity has improved and the industry has seen a positive growth in ready-to-serve beverages, fruit juices and pulps, dehydrated and frozen fruits and vegetable products, pickles, processed mushrooms and curried vegetables. According to government estimates, processing in this sector will grow up to 25% by 2025.

Grains: Every year, India produces more than 200 million tonnes of different food grains such as rice, wheat, maize, barley and millets like jowar (great millet), bajra (pearl millet) and ragi (finger millet). Primary milling of rice, wheat and pulses is the most important activity in food grains processing. Led by Basmati Rice, branded rice is becoming popular in both the domestic as well as the export market. Indian Basmati rice commands a premium in the international market. This segment thus offers opportunities in marketing of branded grains, as well as grains processing.

Meat and Poultry: There is a large potential for setting up modern slaughter facilities and development of cold chains in the meat and poultry processing sector. In the case of poultry, export from India is mostly to Maldives and Oman. Other markets such as Japan, Malaysia, Indonesia and Singapore are being explored. The growing number of fast food outlets in the country has had a significant impact on the meat processing industry in India. Most of the production of meat and meat products continues to be in the unorganised sector. Some branded products like Venky's and Godrej's Real Chicken are, however, becoming popular in the domestic market.

Table 2: Level of Processing in Food Processing Sector

Item	Organised Sector (%)	Unorganised Sector (%)	Total (%)
Fruits & Vegetables	1.20	0.50	1.80
Dairy Products	15	22	37
Meat	21	--	21
Poultry	6	--	6
Marine Fisheries	1.70	9	10.70
Shrimps	0.40	1	1.40

Source: Ministry of Food Processing, GOI, Annual Report, 2004

Fish Processing: India is the third largest fish producer in the world and is second in inland fish production. The fisheries sector contributes US$ 4.4 billion to the national income, which is about 1.4% of the total GDP. With its over 8,000 km of coastline, 3 million hectares of reservoirs, 1.4 million hectares of brackish water, 50,600 sq km of continental shelf area and 2.2 million sq km of exclusive economic zone, India is endowed with rich fishery resources, both inland and marine. Processing of fish into canned and frozen forms is carried out almost entirely for the export market. It is widely felt that India's substantial fishery resources are under-utilised and there is tremendous potential to increase the output of this sector.

Consumer Foods or Packaged Foods: Consumer food industry includes packaged foods, aerated soft drinks, packaged drinking water and alcoholic beverages. This segment comprises bakery products, ready-to-eat snacks, chips, namkeens (salted snacks and savouries) and other processed /snack foods. The confectioneries sector is growing at the rate of 5.7% per annum. Biscuits too have a huge market both in urban and rural India, and the segment is growing at 7.5 %per annum. India is the second largest producer of biscuits in the world after USA. Other products like bread, chocolates are also growing at a significant rate. There is a demand for Indian snack food (Ready-to-eat) in overseas markets. The exports market is growing at around 20 %annually.

Aerated Soft Drinks: The aerated soft drinks industry in India comprises over 100 plants across all States. It provides direct and indirect employment to over 125,000 employees. It has attracted one of the highest FDI in the country. Two of the biggest global brands in this segment are well established in India. Soft drinks constitute the third largest packaged foods segment, after packed tea and packed biscuits. Total export earnings of the industry are over US$ 156 million per annum. Penetration levels of aerated soft drinks in India are quite low compared to other developing and developed markets, an indication of further potential for rapid growth.

Alcoholic Beverages: India is the third largest market for alcoholic beverages in the world. The demand for spirits and beer is estimated to be around 400 million cases per annum. The market is estimated to grow at a healthy rate of around 25 per cent per annum in the next five years, indicating attractive investment potential.

III. Gender Issues in the Food Processing Sector

The food processing (FP) sector is important for its gender sensitivity as well. Limited by unequal access to financial as well as capacity and skill building resources, women proliferate more in the primary and linked sectors. The agriculture and plantation sector are well known for being a mainstay for women in India. Agriculture (including plantations) is a highly gender sensitive sector and engaged 101,729 female workers or 74.41% (2001 Census) of all women workers. Women occupy the largest segment of the plantation (production) workforce in tea (58%) and coffee (57%). This sector contributes about 6.86% of women's employment in the agriculture and allied sector. The fishing sector provided about 232,000 jobs to women and contributed about 0.17% of women's total employment in India. However, trade liberalisation in some segments especially in plantation products has resulted in a loss in women's jobs. Women are also engaged on lower wages, as temporary workers, and are not entitled to healthcare benefits, or sometimes not even maternity leave.

The difference between the food processing industry and other industries is that it is intrinsically linked to basic crop cultivation, animal husbandry, plantation and fishing activities. It is natural, therefore, that women find employment in the processing sector. Women have significant involvement in products like tea, coffee, spices, fruits and nuts, dairy and marine products. About 1353,000 women were employed in the manufacture of food products and beverages in 2004, contributing about 0.99% of total women's employment in India. Of this 608,000 jobs were in urban India, accounting for 2.8% of women's jobs in urban areas. The sector still remains largely informal. A study[1] of cashew processing, horticulture, dairying and chilli processing has indicated that women constitute 95.23% of workers in the cashew nut shelling, processing and packaging sector. In the processing and preservation of fruits and vegetables, about 40% of direct employees are women but this is not uniform across regions. Women, where employed, are preferred to men in the processing activity while men are generally employed in administration and management. Dairying activity in India is predominantly in the informal sector, and overall women constitute as high as 93% of the total employment in dairy production according to FAO estimates. The Annual Reports 2005–06, Department of Animal Husbandry and Dairying (DAHD) reports 75 million women workers as against 15 million men. Women have also been at the forefront of the dairy cooperative movement in India.

But like in agriculture, plantations, and fisheries, trade liberalisation is already impacting women's jobs in food processing. A Study (NPC, 2009) finds that due to the entry of large domestic companies and multinationals in the FP industry, small units in the unorganised sector "which dominated the country's food processing is in danger of being increasingly marginalized. This is already affecting employment avenues and opportunities for women".

For example in the cashew sector, processors/exporters from the developing countries are pitted against the corporate concentration and retailer market power of the developed countries. This trend forces the processors who get only 5% of the value of the final product to suppress wages, casualise labour and reduce costs. The pressure is borne by women workers. In the dairy sector, increased mechanisation and shift towards capital-intensive techniques and the competition posed by higher imports and lower import duties has led to a fall in women's job shares. Also, women's control over the resources and output is negligible with only 25% of dairy cooperative memberships being held by women. Women from small-farm households have poor access to finances for short-term investments into their dairy enterprises. They also lack training in the areas of dairy, cooperative management and marketing.

IV. Policy Framework in the Food Processing Industry

Indian food industry has witnessed significant growth and changes over the last one decade, brought about largely by the changing trend in urbanisation, income and life styles. Unless India has a developed food processing sector, benefits of productivity gains in agriculture will not get transferred to the farmer. In view of the significant backward and forward linkages that the food processing industry has with agriculture, manufacturing and services sectors of the Indian economy, the Government of India has accorded high importance to the growth and development to the food processing industries in India. According to the *Vision Statement 2015* by the Ministry of Food Processing, Government of India, Indian food industry expects to increase its level of food processing from 2% in 2005 to 20% by 2015.The industry seeks to enhance its value addition from its current level of around 20% to 35% by 2015. More so, the food processing industry aims to double its share of foreign trade from present 1.5% to 3%. The industry is estimated to be growing at around 10% during the Eleven Plan period. The government has been developing agri-zones and the concept of mega food parks to promote food processing industry in India.

[1] National Productivity Council (NPC), 'Impact of Trade and Globalisation on Gender in India'. 2009.

In order to promote investment in the food processing sector, several policy initiatives have been taken during recent years. The liberalised overall policy regime, with specific incentives for the high priority food processing sectors, includes the following: i) allowing full repatriation of profits and capital; ii) automatic approvals for foreign investment up to 100 per cent, except for alcohol, beer and reserved items; iii) zero duty import of capital goods and raw material for 100 per cent export-oriented units; iv) allowing sales of up to 50 per cent in domestic tariff area for agro-based, 100 per cent export oriented units; v) government grants given for setting up common facilities in Agro Food Park; and vi) full duty exemption on all imports for units in export processing zones.

Most of the processed food items have been exempted from the purview of **licensing** except items reserved for small-scale sector and alcoholic beverages. Since 1999, the food processing industries have been included in the list of **priority sector for bank lending**. In the budget of 2001-02, **excise duties** on processed fruits and vegetables were brought down to zero. Later in the budget for the year 2004-05, **income tax holiday** including a few other concessions were announced for certain categories of food processing industry. In the budget for the year 2006-07, excise duty waivers were given to some more products such as condensed milk, ice-cream, preparations of meat, fish and poultry, pectin, pasta nod yeast. Excise duties were also halved from 16 to 8% in the year 2007-08 (For aerated drinks, from 24% to 16%) and were further completely waived off in the following year on certain items. Exemption limit of excise duty for small-scale industry has been raised from Rs 1 crore to 1.5 crore. To help with **capital goods supply**, Customs duty on refrigerated motor vehicles has been waived off while custom duty on food processing machinery is reduced from 7.5% to 5%. Recent policy initiatives have attempted to strengthen the supply chain, improve infrastructure, cold storage facility, upgrade and modernise technology. In this regard, concessional import duty of 5% for setting up of mechanised handling system, pallet racking system in mandis and warehouses for food grain and sugar and full exemption from service tax for the installation and commission of such equipments have also been provided.

In addition to the general policies, there are sub-sector specific policies. The first of these lay down: ***a) sub-sector specific FDI norms***, and conditions thereof. For example, in the fruits and vegetables segment and in packaged foods, setting-up 100% export-oriented units require specific government approvals and automatic approval of foreign technology agreement and up to 51% foreign equity participation is allowed. Fish processing projects with a minimum of 20% value addition can be set up as 100% export-oriented units. Foreign equity participation up to 51% is automatically allowed in milk products except in malted foods.

b) There are sub-sector specific rules also vis-à-vis exports. Export of fruit & vegetable products, marine fish products (except silver pomfrets of weight less than 300 gms), are freely allowed. Export of meat is subjected to pre-shipment inspection and a certificate is required from State Animal Husbandry Department/Directorate of Marketing and Inspection and export of beef is prohibited. Exports of some milk-based products are freely allowed provided these units comply with the compulsory inspection requirements of concerned agencies.

c) The third set of regulation is related to licensing requirements and reservation policies via food related Acts. For example, fruit and vegetable products sub-sector is regulated by the Fruit Products Order, 1955 (FPO), issued under the Essential Commodities Act and all processing units are required to obtain a license under this order. Some items like pickles & chutneys, tapioca sago and tapioca flour are reserved for exclusive manufacture in the small-scale sector. Since liberalisation, there is no license requirement for setting up or capacity expansion of roller flour mills. Under dairy products, ice cream was earlier reserved for manufacturing in the small-scale sector, but has now been de-reserved. No license is required for setting up of large-scale production facilities for ice cream.

The various Acts governing the food processing industry are now brought under the Food Standards and Safety Act (2006). The older laws that are superseded are: The Prevention of Food Adulteration Act, 1954; The Fruit Products Order, 1955; The Meat Food Products Order, 1973; The Vegetable Oil Products (Control) Order, 1947; The Edible Oils Packaging (Regulation) Order, 1998; The Solvent Extracted Oil, De oiled Meal, and Edible Flour (Control) Order, 1967; The Milk and Milk Products Order, 1992; and the Essential Commodities Act, 1955. The Act is to "regulate and monitor the manufacture, processing, storage, distribution, sale and import of food so as to ensure the availability of safe and wholesome food for human consumption…all food imports will therefore be subject to the provisions of the Act and any rules and regulations made under the Act" (Ministry of Food Processing, GOI).

V. What are the Key Chapters and Provisions in the FTAs?

Under FTAs, the key trade issues can be classified into two categories: **Goods Trade Issues and Non-Goods Trade Issues**. Under **Goods Trade issues**, the important agreements pertain to agreements on mainly six issues: (I) Import duties; (II) Export measures; (III) Non-tariff measures; (IV) Rules of Origin; (V) Anti-concentration clause; and

(VI) Sectorals (Zero for Zero reduction). Under the **Non-Goods Trade issues**, there are four key issues: (I) Intellectual Property Rights policy; (II) Investment policy; (III) Public Procurement policy; and (IV) Competition policy. Trade facilitation and dispute settlement are also included under FTAs.

***Note*: For more details on FTA Provisions and Key Features, see Part I and Part II of this series.**

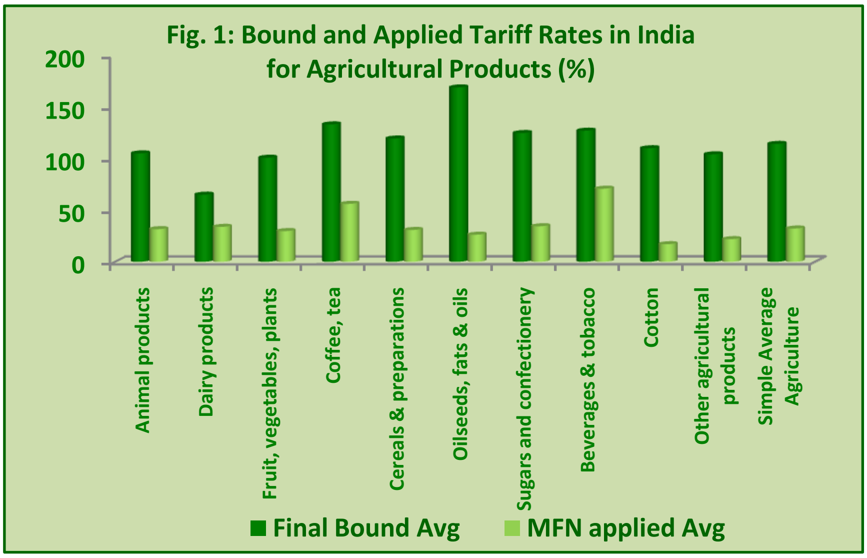
VI. Trade Pattern in the Food Processing Industry: World and FTA Partners

Table 03: HS Codes / Chapters of Processed Food Products (at 2 digit level)

HS Code/ Chapter 02: Meat and edible meat offal (including poultry)	HS Code/ Chapter 03: Fish and crustaceans, molluscs and other aquatic invertebrates	HS Code/Chapter 04: Dairy produce; birds' eggs; natural honey; edible products of animal origin, not elsewhere specified or included	HS Code/ chapter 07: Edible vegetables and certain roots and tubers
HS Code/ chapter 08: Edible fruit and nuts; peel of citrus fruit or melons	HS Code/Chapter 09: Coffee, Tea, Mate and Spices	HS Code/Chapter 11: Products of the milling industry; malt; starches; insulin; wheat gluten	HS Code/Chapter 15: Animal or vegetable fats and oils and their cleavage products; prepared edible fats; animal or vegetable waxes
HS Code/Chapter 16: Preparations of meat, of fish or of crustaceans, molluscs or other aquatic invertebrates	HS Code/Chapter 17: Sugars and sugar confectionery	HS Code/Chapter 18: Cocoa and cocoa preparations	HS Code/Chapter 19: Preparations of cereals, flour, starch or milk; pastry cooks' products
HS Code/Chapter 20: Preparations of vegetables, fruit, nuts or other parts of plants	HS Code/Chapter 21: Miscellaneous edible preparations	HS Code/Chapter 22: Beverages, spirits and vinegar	

Note: Chapter 10 (cereals) is not included as these include largely primary and not processed agricultural products.
Chapters 2, 3, 7, 8 and 9 deal only partially with processed products.
For full list of processed food products at 4-8 digits, go to **http://www.dgciskol.nic.in/itchs2007/itc(hs).htm**

The food processing industry in India is spread over several chapters under the harmonised system of product (tariff line) classification. The processed food products are broadly classified under HS chapters given below (Table 3). For a producer who wants to find out any trade related information on his/her product, for example, current duties, duties in other countries, export or import figures, he or she must first find out the relevant HS code. The chapters give the broad categories and have two digit numbers. But individual products are classified up to eight digits which fall under these chapters. Product groups under chapters are classified as heading (4 digits), sub heading (six digits).



Source: WTO Tariff Profile (2009)

***Note*: How to assess your HS code? Check the list given at** http://www.dgciskol.nic.in/itchs2007/itc(hs).htm **for the 4-8 digit code of your product.**

Duty Structure: India has about 700 agricultural products which include both basic agricultural crops as well as processed food products. It has relatively high maximum (called bound) and applied duties on most of its agricultural products as it has a general policy of protecting agricultural products from international competition. Bound duties on agricultural products are 114.2% and the average 2009-10 applied duty was 32.2% (see Fig.1). The highest applied duties are on beverages and tobacco, coffee and tea. In oilseeds, fats and oils, India has the highest bound rate but one of the lowest applied duties. India also uses tariff rate quotas, i.e. certain quantity of imports are allowed at certain tariff rates. The banded structure offers scope to exporters to export certain limited volumes at relatively low tariffs to India.

Trade Pattern: India's current agricultural trade (primary and processed products) is very low. Exports contributed Rs 89,522.59 crore amounting to only 10.59% of total exports in 2009-10. Imports, at Rs 59,367.62 crore, was 4.38% of total imports. This is because at a global level, agricultural trade is low compared to industrial trade and agricultural duties are generally higher. But this is also because of India's high protection levels. Exports remain low also because the Indian FP industry is not so developed yet and cannot often meet standard barriers, especially in developed country markets. India's food processing sector is still in a nascent stage, and many segments need significant protection if future growth potential is to be retained. India, in spite of being major producers of oilseeds, does not have the processing capacity and imports huge quantities of vegetable oil to meet domestic needs. This import has also destroyed the growth of India's own processing capacity. With the increasing number of FTAs that India is signing or is about to sign, agricultural trade will become much more open.

Recent trends reveal India's weakness in food processing. Exports of many major chapters of food products showed a decline or very moderate increase between 2009-10 and 2008-9. On the other hand, imports increased in all segments with high growth in many segments. Import growth ranged between 3.68% in cereal products (Chapter 19) to a massive 720.51% in sugar and confectionary (Chapter 17). India's biggest trade is in vegetable oil (under Chapter 15) and import under this chapter was valued at a massive Rs 2669.73 crore and showed a trade deficit of Rs 2404.96 crore in 2009-10.

Dairy products (Chapter 04) exports stood at Rs 91470 lakh in 2009-10, showing a massive decline of about 40% from 2008-09. But imports increased sharply by 179.48%. Exports fell also of coffee, tea, spices (Chapter 09) by 8.76%, of sugar products by 89.8%, and of cereal preparations by 7.71%. Exports of animal or vegetable fats and oils (Chapter 15), meat and edible offal (Chapter 02), fish (03) increased by 0.71%, 0.73% and 1.01% while preparations of vegetables, fruits and nuts exports (Chapter 20) grew by 3.67%. However, exports of the milling industry (Chapter 11), meat and fish preparations (Chapter 16) showed growths 26.52% and 14.77%, respectively. Miscellaneous preparations such as coffee and tea essences and concentrates, mixed sauces and seasonings, and ice creams (under Chapter 21) showed high export growth and wine and beverages (Chapter 22) exports grew by a significant 9.33%.

On the import front, apart from vegetable and animal fats and oils (Chapter 15), which grew by 66% between 2008-09 and 2009-10, edible vegetables grew by 62.5%, meat and offal grew by 44.3%, coffee, tea and mate grew by 33.47%, products of the milling industry by 49.48%, cocoa and preparations by 54.63%, and beverages, spirits and vinegar by 56.13%.

Table 4: Key Processed Food Segments and Top 5 Countries from/to which we Import and Export (Country shares in brackets)

HS Code/Chapter 04: Dairy produce; birds' eggs; natural honey; edible products of animal origin, not elsewhere specified or included		HS Code/Chapter 09: Coffee, Tea, Mate and Spices		HS Code/Chapter 15: Animal or vegetable fats and oils and their cleavage products; prepared edible fats; animal or vegetable waxes	
Export	Import	Export	Import	Export	Import
AFGHANISTAN (12.13)	NEW ZEALAND (56.31)	U S A (8.87)	VIETNAM SOC REP (25.32)	CHINA P RP (31.20)	INDONESIA (60.52)
U S A (11.67)	IRELAND (9.56)	UNITED ARAB EMTS (8.1)	SRI LANKA (16.91)	NETHERLAND (14.29)	MALAYSIA (13.95)
BANGLADESH (9.35)	AUSTRALIA (7.40)	U K (6.98)	INDONESIA (13.15)	U S A (9.96)	ARGENTINA (9.54)
UNITED ARAB EMTS (8.12)	DENMARK (4.57)	RUSSIA (6.43)	NEPAL (10.71)	FRANCE (8.43)	UKRAINE (6.91)
GERMANY (4.64)	U S A (4.06)	MALAYSIA (6.28)	CHINA P RP (7.84)	JAPAN (7.08)	U S A (3.51)
HS Code/Chapter 16: Preparations of meat, of fish or of crustaceans, molluscs or other aquatic invertebrates		**HS Code/Chapter 19: Preparations of cereals, flour, starch or milk; pastry cooks' products**		**HS Code/Chapter 22: Beverages, spirits and vinegar**	
Export	Import	Export	Import	Export	Import
JAPAN (10.60)	SRI LANKA (47.84)	U S A (17.86)	NEPAL (24.33)	UNITED ARAB EMTS (31.49)	BRAZIL (54.74)
ITALY (7.98)	CHINA P RP (12.12)	U K (12.82)	U S A (11.91)	ANGOLA (13.28)	U K (18.18)
FRANCE (7.28)	NETHERLAND (8.79)	UNITED ARAB EMTS (7.52)	ITALY (9.45)	NETHERLAND (7.84)	NEPAL (7.36)
U S A (6.84)	NEW ZEALAND (6.61)	NEPAL (7.51)	KOREA RP (7.26)	SINGAPORE (7.18)	FRANCE (2.83)
CHINA P RP (6.32)	THAILAND (6.26)	BANGLADESH (4.03)	THAILAND (6.30)	GHANA (3.60)	AUSTRIA (2.75)
	FTAs Signed		FTAs being negotiated		PTAs Signed

Source: Based on Data from Ministry of Commerce.

India has a trade surplus in dairy products; meat and offal; fish; coffee, tea, mate and spices; products of milling industry; and in preparations of meat, fish, cereal, vegetable and miscellaneous edible preparations. However, India has a huge deficit in vegetable oils. In addition, India has a trade deficit in edible vegetables, edible fruits, and sugar and cocoa products. Wine and beverages is one area where India is trying to grow its potential but still has a deficit of Rs 79,392.23 lakh.

A country-wise break up of India's trade in key processed food products reveals the importance of FTAs (see Table 4). Out of the top five export destinations and import sources, most are either FTA or PTA partners or countries/blocs with which India is seriously negotiating an agreement. For coffee, tea, mate and spices, India's major partners are the South Asian and ASEAN countries, with which India already has agreements. In vegetable oil imports, Indonesia, Malaysia (palm oil), and Argentina are important suppliers. While the first two are part of the ASEAN bloc, India has a Preferential Trade Agreement (PTA) with Mercosur, of which Argentina is a member. Another thing to note is that though India exports almost all the products listed in Table 4 to USA, it sells to very few European countries though the EU is a major trade partner in industrial products. Indian food products are often blocked off by high European food standards (see section below on NTBs).

***Note*: If you are a processed food products producer, do you sell to or buy from any of the FTA partners? Check list of FTAs from Part I of this series.**

VII. FTAs and Key Issues for the Food Processing Industry

a) Tariff Rates and Market Access

India has offered up to 90% of products for zero/near zero duty in the currently signed FTAs. Depending on the sensitivity of the product, duties can be cut over a longer period of time or not cut fully to zero (*for more information see Part I and II of this series*). The rest of the products (called tariff lines) can be kept in the exemption/exclusion/negative list where duties can stay at current applied levels and does not have to be reduced at all.

Trade in agricultural and food products often do not work in the same way as industrial goods. Most countries want to maintain basic food security and develop subsistence food supply. As Section II showed, this sector is also a large employment generating sector and the largest MSME sector in the country. India has more defensive (import protection) rather than offensive (export oriented) interest in this segment. In agricultural and processed food products, duty cuts in the past have often led to large imports into the country. Apart from vegetable oil and palm oil where duty cuts led to large inflow from countries such as Indonesia and Malaysia, the most glaring example remains the **dairy sector** where duty cuts in milk powder has already led to large increases in imports (See Box 2).

Table 5: India's Exclusion List in India-ASEAN FTA in Key Food Processing Sectors
02 Poultry not cut and cut fresh, chilled, frozen; poultry liver fresh or chilled
03 Flours, meals and pellets of fish and crustaceans; fish fillets, dried, salted or in brine
04 Milk and cream, concentrated or not concentrated, or containing or not containing added sugar or other sweetening matter (including Milk Powder), whey, butter and other fats, birds egg fresh, preserved or cooked
07 Fresh or chilled potatoes, tomatoes, onion, shallot, garlic, cauliflower, carrots, cucumber, peas and beans; frozen potatoes, beans, sweet corn, terragon; Dried vegetables e.g. onion, garlic, potatoes, peas etc
09 (plantation products) Almost all lines are special product, sensitive product or are in the exclusion list.
11 cereal flour, groats and pellets; cereal grains worked; dried leguminous vegetables
15 Soyabean, groundnut, sunflower seed, saffola, coconut, palm, rapeseed, colza, mustard, sesame, linseed, castor oil products, vegetable fats and oils,
16 sausages, homogenised preparationsof other meat, Hams & shoulder cuts, prepared or preserved tuna, caviar, shrimps, prawns, lobsters
20 prepared or preserved without vinegar tomatoes, mushroom, truffles, potatoes; with vinegar potatoes, peas, beans, sweet corn, bamboo shoots; vegetables, fruits and nuts preserved with or without with sugar; frozen juices, grapefruit, tomato juice
21 Extracts, essenvces, concentrates; Food preparations not elsewhere specified or included.
22 Beer, wine of fresh grapes, vermouth and other wine; fermented beverages; Undenatured ethyl alcohol; Undenatured ethyl alcohol of an alcoholic strength by volume of less than 80 % vol; spirits, liqueurs and other spirituous beverages.

Note: Chapters 8, 17, 18 and 19 are not included as fewer excluded products are there

Box 2: Impact of Import Duty Reduction in the Dairy Sector

- *Import and export of dairy products were restricted through quantitative restrictions (QRs) and canalisation of trade, but these had to be converted to tariffs under the WTO rules. Imports tariffs ranged between 0 (skimmed milk powder or SMP) to 100-150% (milk and cream, butter milk, yoghurt and whey).*
- *India re-negotiated and established tariff rate quota (TRQ) for SMP from June 2000. A quota of 10,000 tonnes at a 15% duty, and an over-quota tariff of 60% were imposed.*
- *India experienced high surge in imports of dairy products in 1999-2000 following dairy trade liberalization under the WTO and primarily an importer of milk powder and butter oil/ghee, which account for over 70% of total dairy imports.*
- *According to projections for the EU-India FTA, India will get hurt in the dairy where many small holders, particularly women are engaged. The EU and member states maintain substantial amount of subsidies both as domestic support as well as export subsidy in respect of dairy sector, which makes EU's products competitive and these practices are trade distorting and restrictive.*

***Source*:** Vijay Paul Mehta, 'India-EU Free Trade Agreement: Likely Implications for the Indian Dairy Sector', Draft Paper, April 2011

In its FTAs, India has used its negative list quite extensively until now. For example, in the ASEAN India FTA, India has kept many products in its negative list (see Table 5). In its FTAs with Japan, India has kept many agricultural items on the sensitive/negative list. Japan, in turn, has kept edible oil, dairy products and sugar on its negative list. India is expected to get additional market access in basmati rice, mangoes, and eggs in its FTA with Malaysia while Malaysia is to get access in fruits, cocoa and palm oil.

Driven by high income growth and changing tastes, especially in urban high income areas, the demand within India for processed food products is growing rapidly. It has been estimated that the size of the middle to upper classes will increase at more than 300% between 2005 and 2015. During the same period the youth population (age group 15 –25) in India is expected to grow by 11%. This will lead to an increasing demand for food products to meet demands of convenience, variety, health and a changing palate" (IBEF, Advantage India: Food Processing, 2010). Developed countries such as the European Union, with whom India is currently negotiating a FTA, want access to this growing market. The EU and many other developed countries are much more advanced in the production of food products. Many products also receive considerable subsidy in the EU. According to reports, the EU wants access to dairy, poultry, fisheries, other processed food products and the wine, spirits market in India. Though production facilities in India cannot yet cater to the growing demand, opening up these segments also run the risk of destroying the growth potential in these segments. On the other hand, Indian products face non-tariff barriers in developed country markets, especially in the EU. For an example of poultry products, see Box. 4.

***Note*: Check what the tariff for your product is in India and which countries produce similar food products.**

b) Export Measures

India uses *temporary export bans and quantitative restrictions (quotas)* to control the domestic supply of cereals, vegetables and other food products. The measures restricting export of food products, for example export cess and quotas on some agricultural goods, are already being gradually eased. Even then, India has effectively used temporary export bans from time to time (see Box 3 for some of the bans India has used). Apart from those listed in Box 3, India also used bans on edible oil and milk powder. This is important as it ensures both basic food supply as well as raw material for the food processing industry and is necessary for a country with a large poor population and a large Public Distribution System. From an industry perspective, export measures on raw material are important for the food industry to grow.

However, some countries, especially developed countries, notably the EU, want export measures to be completely removed in partner countries under FTAs. Though removal of export taxes is their major demand, lifting of export bans may also be on the cards. Not only will this jeopardise the food security of the country especially in times of food crisis, this will also reduce supply and raise prices of essential raw material for the industry. The cereal and pulse based industries, and confectionary manufacturers will be affected.

***Note*: Check whether you use any product as raw material on which India imposes temporary bans.**

Box 3: India's Export Bans on Agricultural Products

Onions

2010, December–2011, September: India banned onion exports as prices peaked (70-80 Rs/kg) from time to time, lowered floor prices to $225 per tonne though minimum export price of Bangalore Rose and Krishnapuram (two premium varieties) has been fixed at $600 per tonne. In September 2011, India has allowed export of onions.

Pulses

2006, June - India banned export of pulses and exempted them from customs duty to check spiralling prices. The ban has stayed in place since, though it has been reviewed from time to time, along with allowing the import of pulses at zero duty. In **2011, March** - India extended the ban till March 31, 2012. Export of Kabuli chana and organic pulses is allowed, with a ceiling of 10,000 tonnes.

Rice

2007, October - India imposed a ban on non-basmati rice exports but lifted it following protests from exporters.

2008, April 1 - Indian banned the export of non-basmati rice to try and control soaring domestic food costs. The price for exports of aromatic basmati rice has also been raised to $1,200 per tonne to discourage exports. In **2011, February 9**, India eased the three-year ban on rice exports, allowing export of three varieties of non-basmati rice (Ponni Samba, Rosematta and Sona Masuri) at $850 a tonne, up to 1.50 lakh tonnes. As of March 11, **2011** India is unlikely to lift ban on export of non-basmati rice in the wake of high food inflation and food security concerns.

Sugar

2006, June 22 – India banned sugar exports to keep domestic supplies and prices under check and introduced export quota of 500,000 tonnes under open licences in 2010, December.

Wheat

India had suspended wheat exports in early 2007 and is still unlikely to lift the ban in February 2011, in the wake of high food inflation and food security concerns.

Source: Susana Barria, India's Export Measures, 2011

c) Non Tariff Measures (NTMs)

Non Tariff Measures (NTMs) are all measures other than normal tariffs that can restrict trade, namely; trade related procedures, regulations, standards, licencing systems and even trade defence measures such as anti-dumping duties, etc. which have the effect of restricting trade between nations. *For more on NTMs and NTBs see Part I of this series.* Standards form an important part of NTMs and can in effect be used as trade barriers (those that cannot be justified are called NTBs) especially when tariffs are low. Since food is clearly connected to basic health issues, every country lays down food safety standards for its own consumers. The WTO recognises that every member country has the right to use its own standards and even allows export prohibitions or restrictions necessary to the application of standards or international trade regulations. The standards in international trade agreements are known as the Sanitary and Phyto Sanitary Measures (SPSMs) and the WTOs SPS Agreement lays down the international rule in this regard. However, some rules may be seen as unfair NTBs. The process requirements for trading which act as barriers are called technical barriers to trade (TBTs). Table 6 shows some of the NTBs faced by Indian food products listed by the Ministry of Commerce.

Table 6: Some NTBs Faced by India in Food Products

HS Code	Name of Product	Type	Country	Description
20700	Poultry Products	Import Restriction	Bangladesh	Ban despite India regaining avian influenza free status.
20700	Poultry Meat	Import Restriction	EC	India not in approved list for export of Poultry Meat products (2005/696/EC)
40000	Milk products	Standards	EC	EIC has implemented the RMP for Milk & Milk Products, approved by EIA and the list of approved establishments has been sent to the EC.
40800	Sprayed dried egg yolk powder & whole egg powder	Standards	Australia	High food safety standards and bio-security issue
40800	Egg products	Standards	EC	Non harmonized egg products standards amongsts EU members. Individual approval of production units required.
4081100	Egg Powder	Standards	EC	New MRL limits without time for adaptation
70000 00	Vegetables	Subsidy	Korea	Direct export subsidies to lower marketing costs
90100 00	Coffee	Subsidy	Colombia	Export subsidies
110100 00	Wheat flour	Minimum Import Price	Chile	Price band with floor and ceiling prices to be adjusted downwards by 2% per year from 2008 to 2014 and then reviewed by President
160000 00	Fish - Prepared/ Preserved	Minimum Import Price	Argentina	If price below Minimum Import Price (MIP), importer to validate invoice from Customs in origin country and submit full set of original documents
220300 & 220400	Beer & Wines	Customs	Chile	Additional ad-valorem tax of 15%
220800	Spirits	Customs	Chile	Additional ad-valorem tax of 27%

Source: Ministry of Commerce, GOI

India has own its domestic standards for food products. As discussed under Section IV, the government has introduced the new Food Safety and Standards Act, 2006 (34 of 2006) that overrides all other food laws. There are fears that this has already adversely affected smaller producers and food vendors in India. The government does not provide standard testing laboratory and other infrastructure that will help the smaller producers comply with current standards.

However, Indian food standards are much lower compared to those in developed countries. The European Union, for one, is well known for its high food safety standards (see Box 4). Indian products often get rejected on health and sanitary grounds in European countries and exports are often limited to developing countries, apart from the USA. Countries like Australia and New Zealand impose ban on import of Indian mangoes and other fruits due to presence of fruit flies and weevil. Indian MSME producers find it even more difficult to meet these standards as they cannot even meet domestic standards. The government infrastructure needs to be significantly strengthened if smaller producers are to meet domestic and international standards.

Box 4: Food Standards in the EU and How it can Impact Indian Exports: The Example of the Poultry Sector

NTBS on Poultry Products

- ***Lack of harmonization of egg products standards in EU member countries resulting into requirement of approval of production units by individual member countries.***
- ***MRL limits on egg powder.***

If EU and India remove tariffs on egg and egg products and there is no mutual recognition agreement on standards (or removal of Non-Tariff Barriers by EU and India, in general), FTA will be give market access to EU and not to India.

- ***Import Restrictions on Indian Poultry Meat***

In the area of poultry meat, India does not process much. Demand for breast is high in EU whereas demand for legs is high in India. Therefore India can theoretically sell breasts to EU and EU can sell legs to India. However again if the FTA reduces high Indian tariffs (30-100%) but does not reduce standards or gets MRAs, India will lose in the bargain.

Other EU NTBs

- ***Different MRLs by the member countries for pesticides, drugs and other contaminants***
- ***Definition of Whiskies – CN Code***
- ***Complex Procedures for Sampling/Product Testing***
- ***Equivalence Agreement on Organic Products***

NTBs in India's FTAs

Most FTAs have a chapter on NTBs, but most agree to abide by WTO's SPS and TBT Agreements, such as the India-ASEAN and India-Malaysia Agreements. But some FTAs, often by developed countries, target to lay down higher and stricter standards in their FTAs which may be difficult for developing countries to meet. *Standards by themselves are hardly ever lowered under FTAs. Therefore, even if tariffs are reduced under FTAs, these will continue to be a barrier in key countries. For example, poultry standards are high in the EU and will continue to face standard barrier even if India signs an FTA with the EU (see Box 4).*

However, FTAs can lay down additional mechanisms to simply TBTs through Mutual Recognition Agreements (MRAs) that involves mutual recognition of each others' standards and certifying processes and agencies. For example, in the India-Japan FTA, a Sub-Committee on Technical Regulations, Standards and Conformity Assessment Procedures, and SPS Measures have been set up to discuss having MRAs. This may ease some of the food-related technical barriers if MRAs can finally be reached. However, Japan is very cautious about its food and health standards. It is also unlikely that India will get MRAs in food products with the EU. India is negotiating FTAs with other developed countries such as Australia, Canada and New Zealand. Therefore, Indian producers may get blocked off by high standards and TBTs in FTA markets, while foreign products can easily come into India unless protected by tariffs/exclusion lists.

***Note*: Check whether you can meet current standards and process requirements on exports to FTA partners and whether these are eased in the signed FTAs.**

d) Intellectual Property Rights(IPRs)

India's food processing industry, like other industries is lagging behind in registering IPRs such as Patents, Trademarks, Collective Marks and Geographical Indications (GIs). *For definition of and discussion on IPRS and these instruments see Part I and Part II of this series.* Registering IPR instruments require large financial and human resources to gather knowledge on processes, access information on what to do, and do detailed documentation (for example in the case of GIs). In FTAs, developed countries such as the EU, USA, Japan and Switzerland want to impose on India such IPR commitments that go beyond WTO's TRIPS commitments. The EU has been quite insistent on this. This affects agriculture and food-related issues significantly. For example, ratifying UPOV 1991 according to the EU's demands will prevent Indian farmers from saving, using and freely exchanging seeds. This will prevent cultivation at low cost and may reduce supply while raising prices of raw material for the food processing industry.

The EU also wants its 190 GIs, most of them relating to agriculture and food products (highly relevant to wines and spirits), to be recognised in India (Business Standard, August 2, 2011). A GI is the official stamp of protection for products originating from a particular region, with a special quality and reputation that go back several decades or centuries. At the WTO, the EU is pushing for the multilateral recognition system of GIs but that refers mainly to wines and spirits. GI applications from the EU member-countries in India that can get recognised through the FTA goes much further and are mostly in the category of beverages such as beer and wine brands, processed meat and milk products, and various bakery items, including biscuits and pastries. This can be a major problem for India's producers, especially MSME producers, because India's underdeveloped IP system in agriculture and FP cannot compete with the EU's well-advanced system of IP recognition. The EU is apparently also attempting to get procedures simplified for easy registration of these GIs in India (Business Standard, August 2, 2011).

***Note*: Do you know of any other country having GIs in a product similar to the one you produce? Have registered any intellectual property instrument (e.g., Geographical Indications, Patents, Trademark, Collective Mark, etc)?**

e) Investment

Some FTAs include chapters on investment that can allow foreign investment up to 100% in every sector unless otherwise specified. The FTAs with Japan, South Korea, Malaysia and Singapore contain investment chapters. Even the ASEAN agreement is to include an investment chapter at a later stage. As a reciprocal, Indian producers will also be able to invest in partner countries. As discussed under Section IV, the government is trying to encourage foreign investment in the sector. FDI is allowed up to 100% under the automatic route in agro products, milk and milk products, and marine and meat products. But FDI in some sectors such as agricultural farming and plantation activities is banned. In addition, there are restrictions on investments in the MSME sector with a cap of 24% on foreign equity. Performance Requirements (PRs) exist, especially in the MSME sector. Countries usually impose PRs on foreign investment such as limits on ownership, board membership, and specified requirement of exports, compulsory local content, compulsory transfer of technology, etc. These requirements can be used to improve opportunities for MSMEs. Currently, there are PRs on the sectors that are mentioned in Box 5 (See bullet point 2).

In its FTAs, India may have to give access to 100% FDI in sectors which were closed until now and remove PRs. India, in its current FTAs, has retained some existing caps especially on MSME sector FDI and not given national treatment to foreign investors. It has also retained PRs subject to domestic laws. Indian producers will also look forward to investing in FTA partner countries. Obviously, as the FTA with South Korea show, partner countries can in turn impose restrictions on investment liberalisation (see Box 5).

Box 5: Investment Provisions in Food Processing Sector in India's FTAs with Japan and South Korea

- ***In the India-Japan and India-South Korea FTAs***, India has retained exceptions for the MSME sector (<24% foreign equity) and current MSME FDI norms will continue. This means prior approval will be needed for Japanese and Korean investors to invest more than 24% in the MSME sector and they are subject to performance requirements.
- ***In the India-Japan FTA* and India-South Korea FTA**, India has retained the right to adopt or maintain any measure to impose performance requirements vis-à-vis certain sub sectors under the food processing sectors: Fisheries, Dairy Products; Canning and Preservation of Fruits and Vegetables; Crustacean and Similar Foods; Bakery Products; Hydrogenated Oils, Vanaspati, Ghee, etc. and Vegetable Oils; Distilling, Rectifying and Blending of Spirits, Ethyl Alcohol Production from Fermented Materials and Manufacture of Wines.
- ***In the India-South Korea FTA,*** South Korea has withheld National Treatment (Article 10.3), Performance Requirements (Article 10.5) and Senior Management and Boards of Directors (Article 10.6) in case of Agriculture, Hunting, Forestry, Fishing and related service activities (including rice and barley polishing, and activities related to a rice processing complex) and on fisheries.

***Note*: Assess whether you benefit from FDI or whether you will have to compete with fully owned foreign companies/multinationals?**

VIII: Conclusion

The food processing industry in India offers huge potential for growth and income and employment generation. It is the largest segment of the MSME sector. Its potential and significance in terms of creation of jobs, household oriented business opportunities (*griha udyog*), as well as providing a wide range of processed food at relatively cheaper prices to India's population is undeniable. It is also a gender-sensitive sector as there are segments with high women's participation in work force as well as in entrepreneurship. Some segments require small capital so women-based household enterprises can flourish. But for this sector to realise its maximum potential, it needs support from the government in terms of infrastructure, markets, credit as well as a suitable policy environment. Its involvement with international trade has been low until now and its consumers remain largely confined to other developing countries. Current import duties range mainly between 30 and 100% and this offers some protection to the domestic producers. However, even in the past, in spite of having a good base of raw material, India's policy of allowing imports to cater to domestic demand have often hampered the growth of the domestic processing industry and affected employment especially in the small-scale sector. Vegetable oil is a case in point. Even imports of close substitutes (such as palm oil), of products made in India (e.g. coconut oil) has affected the food processing industry.

In its FTAs, India is cutting import duties on more than 90% of products. This means that even if agricultural products get more protection (on the sensitive or negative list) compared to industrial products, duties in many processed food products will have to be cut ultimately. Large blocs like the EU wants products like wine and spirits removed from India's negative list and access to markets in fish products, dairy, poultry and meat products. However, Indian standards are not very high, and Indian food products will still get blocked off by high standards and other NTBs in developed country markets even if they are FTA partners. Therefore, India will end up reducing its main protection of import duties, but will not get access in developed country markets because of NTBs which will not get reduced under FTAs. MRAs are hardly ever possible in FTAs with developed countries. If India is forced to remove export bans on essential food items, not only can domestic food supply be threatened, the Indian processed food industry could be facing high raw material costs and shortage of supply. Indian small producers will also have to compete with IPR protections that developed country products already enjoy, but will not have either the financial resources or the know to use these instruments.

Therefore, though there is untapped demand in India for processed food products, the government still has to calibrate its trade liberalisation so that it leaves enough space for its own food processing industry to grow. Since food is not just another commodity but is essential for human survival, self-sufficiency is something that every developing country must aim for. Finally, given the high growth in India's income and food demand, the domestic industry needs to use every opportunity to capture this market and maximise the gains from it. They need to assess their own situation regarding FTAs and lobby with the government to ensure that their interests are protected not only in the short run, but in the long run as well.

IX: How and Whom to Influence in the Government to Make Your Voices Heard?

- Get your MSME associations interested and build strong alliance of the MSMEs on the issue
- Based on the information and analyses, articulate your argument and do collective submission to the following:

Name of Office Bearer/ Organisation	Contact Information
Prime Minister, Prime Minister's Office, GOI	Fax: 011-23016857/9545, Tel: 011 2301 8939
Minister, Ministry of Commerce and Industry (MOCI), GOI	cim@nic.in Fax: 011-23062947
Minister of State, Ministry of Commerce and Industry, GOI	Fax: 011-23062321
Secretary, Department of Commerce, MOCI	csoffice@nic.in, Fax: 011-23061796
Secretary, Department of Industrial Policy and Promotion, MOCI	rp-singh@nic.in, Fax: 011-23061598
Minister, Ministry of Food Processing, GOI	Tel: 011-2649-3889/90, Fax : 26493298
Joint Secretary, Ministry of Food Processing, GOI	venkateswarlu86@nic.in, Tel: 011-2649 4032.

X. How to Access More Information on FTAs and Assess the Impact on Your Enterprise?

You need to track the trade-related developments in the food processing sector in order to be able to assess your situation so that you can prepare your business and make suitable recommendations to the relevant authorities through your associations.

Access to Information about FTAs and MSMEs

Source and Types of Information on FTAs	Web links
FTA Documents, Min. of Commerce and Industry, GOI	http://commerce.nic.in/trade/international_ta.asp?id=2&trade=i
WTO Cell of Indian Institute of Foreign Trade	http://wtocentre.iift.ac.in
Information on Non-Tariff Measures(NTMs)	http://commerce.nic.in/trade/international_ntm.asp?id=4&trade=i
Information on IPRs	http://dipp.nic.in/intellectual_property_dipp.htm
For Data on India's trade	http://commerce.nic.in/tradestats/indiatrade.asp
Where can you access more information about the food processing sector?	
For Food safety standards	http://www.fssai.gov.in/
A Market Survey Report on Food Processing	http://www.cci.in/pdf/surveys_reports/food-processing-india.pdf
For information on food industry	http://www.indianfoodindustry.net/
For information and training for SMEs in food processing	http://www.smeiift.com/sme/prog/smefood.pdf
For data and information related to exports	http://www.apeda.gov.in/apedawebsite/index.asp
Ministry of Food Processing, Government of India	http://mofpi.nic.in/

How Can You Assess the Impact on Your Enterprise?

Having known the source of information on FTAs, now you can assess the situation and analyse the impact FTAs may have on your enterprise. Seek answers to these questions given in **Part I and II of this Series.**

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