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**Prospects for a Multilateral Framework on Investment
The Indian Bolt**

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ABSTRACT

The potential inclusion of a multilateral framework for investment at the WTO aims to coordinate the global regulation on trade and investment. In addition to the difficulties arising during these negotiations, one major concern is the fact that certain countries like India do not have an interest to go for a full-scale Capital Account Convertibility. As a part of the G4, India is currently a major player in the trade-related international regulatory framework. It is argued here that the question of a multilateral framework for investment cannot be solved without taking into account the Indian reluctance to a freer investment regime. There is a historical reluctance of developing countries to establish freer investment regimes. The project on a New International Economic Order already put as a preeminent point the sovereignty of States and their necessary control of the private sector notably of foreign capital. But that political approach is reinforced by objective arguments analysed here. First we briefly discuss the debate on having a freer investment framework and foreign investment regime in India. India's submissions to the WTO on this front are reviewed next. Finally in order to evaluate the legitimacy of India's concerns, through an empirical model the potential impact of a destabilizing shock on her capital account is analysed. Finally based on the findings, the policy lessons are drawn.

KEY WORDS

Investment, WTO, RTAs, Doha Round, India

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1. Introduction

Since the liberalization of its economy in 1991, India has undergone major economic reforms, which have caused deep changes in its economy and consequently in its influence at the global level. These reforms consisted of opening up the economy to more foreign trade and investment, and the dismantling of the industrial licensing system. Over the last decade, India's growth rate has picked up, foreign exchange reserves have increased considerably, and the information technology sector has taken-off, making India a major economic player in the global setting. These developments have led to a worldwide interest in the Indian economy, not previously witnessed since the time of India's independence. However, despite this growing association with the global flow of goods and investment, India has always held a reluctant view to engage in negotiations on a multilateral framework for investment.

It is widely held by some scholars that in recent times trade and investment are complementary,¹ and achieving one is impossible in the absence of the other. However, the inclusion of the relationship between Trade and Investment (henceforth TI) in the World Trade Organisation (WTO) forum for negotiation with the establishment of a Working Group on Trade and Investment (WGTI), one of the four Singapore Issues,² has been subject to fiery debates right from the beginning.³ Moreover, investment had been the subject matter at the origin of the derailing of the WTO's Cancún meeting.⁴ Indeed too important differences of opinion made negotiations impossible and contributed, in part, to the breakdown of the Cancun Ministerial meeting. In the summer of 2004, WTO Members

¹ Egger, Peter, Mario Larch and Michael Pfaffermayr (2004), "Multilateral trade and investment liberalization: effects on welfare and GDP per capita convergence", *Economic Letters*, Vol. 84, No. 1, pp. 133-140.

² Alongside trade and competition, trade facilitation and transparency in government procurement.

³ See: Sauvé Pierre (2006): "Multilateral rules on investment: is forward movement possible?", *Journal of International Economic Law* 9(2), pp. 325-355.

⁴ Baldwin, Robert E. (undated), "Failure of the WTO Ministerial Conference at Cancun: Reasons and Remedies", available at <http://www.ssc.wisc.edu/~rbaldwin/cancun.pdf>

conceded that “no work towards negotiations on [investment] will take place within the WTO during the Doha Round.”

The conflict of interest between the two groups of countries plays a key role in resulting the current scenario. In general the developed countries believe that the inclusion of TI under the negotiating agenda of the WTO would be a major step for ensuring the WTO objectives of freer trade and a liberal investment regime, leading to increased Foreign Direct Investment (FDI) to members with freer investment regimes. In this perspective, Japan and the European Union (EU) pushed forcefully for the commencement of negotiations on investment while the United States (US) was not supporting strongly this initiative.⁵ The ‘Flying Geese model’ experienced by Asian tigers has always been a case in their point.⁶ However, a number of developing countries remained averse to that idea, mostly owing to the potential risk involved with capital flight and the development consequences observed in the post South East Asian currency crisis, which led even the International Monetary Fund (IMF) and the World Bank to acknowledge the importance of maintaining a strict investment regime in developing countries.⁷ In this connection, the idea of making capital mobility conditional with the access obtained in labour mobility of the South as a bargaining tool has surfaced at times.⁸ Nonetheless, the effectiveness of such a policy has been questioned.⁹

The International Investment framework currently is materialized by thousands of individual agreements without any formal coordination. In the absence of global investment rules, States have no other choice but to continue concluding bilateral or regional agreements. As an immediate consequence this move further accentuates the diversity and fragmentation

⁵ Jürgen Kurtz, “A General Investment Agreement in the WTO? - Lessons from Chapter 11 of NAFTA and the OECD Multilateral Agreement on Investment”, NYU School of Law, Jean Monnet Working Paper No. 6/02, p. 58. Deblock C., (2005), “Nouveau Régionalisme ou Régionalisme à l’américaine ? Le cas de l’investissement”, Cahiers du Centre Études internationales et Mondialisation, Institut d’études internationales de Montréal (32 p.).

⁶ de Mello, L. (1997), “Foreign Direct Investment in Developing Countries and Growth: A Selective Survey”, *Journal of Development Studies*, Vol. 34, pp. 1-34.

⁷ RBI (2004) notes that while Global Economic Prospects (World Bank, 1999) called adopting a cautious approach towards capital accounts liberalization, World Economic Outlook (IMF, 2001) held that capital controls in the short run paves a strong platform for more fundamental reforms in the future. Reserve Bank of India (2004), “Approach to Capital Account Convertibility”, Chapter VIII in “Report on Currency and Finance: 2002-03”, pp. 218-252, Mumbai.

⁸ Hoekman, B. and K. Saggi (2001), “From TRIMS to a WTO Agreement on Investment?” in B. Hoekman and W. Martin (Eds) *Developing Countries and the WTO: A Pro-Active Agenda*, pp. 201-214, Oxford: Blackwell.

⁹ Das, S. P., (2003), “An Indian Perspective on WTO Rules on Foreign Direct Investment”, in Aaditya Mattoo and Robert M. Stern eds, *India and the WTO*, pp. 141-168, Washington D C, The World Bank and Oxford University Press.

of the International Investment Agreement universe. This scenario has justified and given rise to the current project, intending to create an effective multilateral framework for investment.

Of course, investment provisions are already embraced in several international agreements (NAFTA, GATS, TRIMs etc.) and further negotiations on investment would not to that extent represent a major progress. However, the coverage under these agreements deals only with limited investment provisions. Indeed, these investment provisions do not comprehensively address the key investment concerns like legal security, policy coherence or the transparency of government commitments etc. Undoubtedly, addressing these issues in greater details would considerably improve the global business environment and facilitate investment. In short, the current state of affairs challenges all countries and their economic policies to commit themselves to ongoing efforts towards the improvement and further liberalization of investment regimes.

Here is the thesis of this contribution: the potential inclusion of a multilateral framework for investment at the WTO aims to coordinate the global regulation on trade and investment. In addition to the difficulties arising during these negotiations,¹⁰ one major concern is the fact that certain countries like India do not have an interest to go for a full-scale Capital Account Convertibility (CAC). As a part of the G4,¹¹ India is currently a major player in the trade-related international regulatory framework. It is argued here that the question of a multilateral framework for investment cannot be solved without taking into account the Indian reluctance to a freer investment regime. There is a historical reluctance of developing countries to establish freer investment regimes. The project on a New International Economic Order (NIEO) already put as a preeminent point the sovereignty of

¹⁰ Concerned namely with the breadth of the definition of “investment” and “investors”; the extent of transparency obligations, notably in respect of prior notification requirements; the degree and form of technical assistance required to help developing countries overcome a widely-perceived analytical deficit in this area; the operational modalities of development provisions governing the trade and investment interface in a possible WTO investment framework; the desirability of replicating a GATS-like approach to scheduling liberalization commitments, notably in respect of pre-establishment rights, as well as the links between FDI and technology transfer. See, Sauvé Pierre (2003), “Investment and the Doha Development Agenda: a look at the issues”, in *The Doha Development Agenda, Perspectives from the ESCAP Region*, New York: United Nations, 2003, pp. 69-98.

¹¹ G4 consists of the United States of America, the European Union, India and Brazil acting as representatives of major industrialized and emerging economies.

States and their necessary control of the private sector notably of foreign capital. But that political approach is reinforced by objective arguments analysed here.

The current paper is organized along the following lines. First we briefly discuss the debate on having a freer investment framework and foreign investment regime in India. India's submissions to the WTO on this front are reviewed next. Finally in order to evaluate the legitimacy of India's concerns, through an empirical model the potential impact of a destabilizing shock on her capital account is analysed. Finally based on the findings, the policy lessons are drawn.

2. Foreign Investment and Financial Mobility Regime in India

Before going into the WTO negotiations on TI, the theoretical perspective behind the developing country concerns needs to be reviewed. According to open economy macroeconomics, large capital inflow into a country causes the relative prices of the goods to change (the speed of which depends on the exchange rate regime), and makes exports relatively dearer (and imports relatively cheaper). This causes a worsening of the current account balance and vice versa. To complicate the situation, a Balance of Payments (BOP) crisis may occur from the dynamics of short-term debt, when speculators try to get rid of the domestic currency in exchange for the central bank's foreign exchange reserves in crisis situations, resulting in the collapse of the exchange rate.¹² The long adjustment period required in the aftermath of the crisis mainly influences the developing countries to be hesitant about freer investment regimes. However, it has been argued that Capital Account Convertibility (CAC) is neither necessary nor sufficient for a foreign exchange crisis.¹³

Up to the early nineties, India maintained a controlled exchange rate regime and various components of capital accounts transactions (e.g. FDI, portfolio equity investment,

¹² Rao, Manohar M J (1997), "Macro-Economics of Capital Account Convertibility", *Economic and Political Weekly*, pp. 3261-3267, December 20.

¹³ Agarwal, Manmohan (1998), "Capital Account Convertibility: Fact and Frenzy", in M. Agarwal, A. Barua, S.K. Das and M. Pant eds, *Indian Economy in Transition: Environmental and Development Issues*, New Delhi: Har-Anand Pvt. Ltd.

external commercial borrowing, non-resident deposits, short-term credit and outward investment) were subject to restrictions.¹⁴

The situation improved after the BOP crisis in July 1991, when India applied for IMF loans and hence had to follow a liberalized framework in return. Subsequently in January 1994, India joined the Multilateral Investment Guarantee Agency (MIGA), which protected the inward investment against a probable event of expropriation or nationalization.¹⁵ Later in August 1994, the Indian rupee was made fully convertible on current account (as per IMF Article VIII). In order to explore the possibility of having CAC, the Tarapore Committee was set up in the subsequent period, which in May 1997 recommended the introduction of CAC by 1999-2000 in a phased manner.¹⁶

However, the recommendation was subject to criticism after the South East Asian experience,¹⁷ and India preferred to follow a cautious approach on that front. The debate on the preparedness of the country for CAC has been revisited from time to time, and it is held that provided the preconditions suggested by the Tarapore Committee are met and the process is implemented with relevant considerations,¹⁸ a movement towards full convertibility is possible to achieve.¹⁹ However, the preparedness of the country for going towards full CAC is still doubted by scholars.²⁰

A gradual reform of foreign investment and financial flow regulations took place in India in the following period. It was realised that the draconian Foreign Exchange

¹⁴ The proportion of market determined components in capital account increased since the early eighties. Virmani, Arvind (2001), "India's BOP Crisis and External Reforms: Myths and Paradoxes", ICRIER, December 2001. p. 24.

¹⁵ For further details on MIGA, see: Wenhua Shan: [EU Enlargement and the Legal Framework of EU-China Investment Relations](#), Journal of World Trade and Investment 2005, Vol. 6, No. 2, pp. 237-262.

¹⁶ The Committee identified fiscal consolidation, a mandated inflation target and strengthened financial sector as the three most crucial preconditions to be fulfilled before achieving CAC.

¹⁷ EPW Research Foundation (1997), "Mapping a Risky Path: Capital Account Convertibility Report", Economic and Political Weekly, June 7, pp. 1300-1303, Mumbai.

¹⁸ Jadhav, Narendra (2003), "Capital Account Liberalization: The Indian Experience", paper presented at conference by IMF and NCAER on "A Tale of Two giants: India's and China's Experience with Reform and Growth", New Delhi, November 2003; RBI (2004).

¹⁹ It needs to be mentioned that a significant proportion of the recommendations made by the Tarapore Committee have already been fulfilled. See Annex VIII.1 in RBI (2004) for details.

²⁰ Gupta, Desh and Milind Sathye (2004), "Financial Developments in India: Should India introduce capital account convertibility?", Paper presented at an international conference to Mark 10 Years of ASARC (Australia South Asia Research Centre), University House, Australian National University, Canberra, 27 & 28 April 2004, available at http://rspas.anu.edu.au/papers/asarc/2004_07.pdf.

Regulation Act (FERA), enacted in 1973 during the severe shortage of foreign exchange in the country has outlived its utility, and a new Foreign Exchange Management Act (FEMA) was introduced in June 2000. In 2003 the overseas investment norms for corporate houses were eased by allowing the prepayment of foreign loans over US\$100 million. In a recent period the limit to overseas investment under the automatic route was increased from 100 percent of the net worth of the Indian entity to 200 percent in April 2005 and remittance limits have also been substantially relaxed.²¹

3. India's regime for Foreign Direct Investment

The current Indian FDI regime is incorporated in the Foreign Exchange Management Regulations, 2000.²² Since 1991, the investment regime in India has been considerably simplified and liberalized, and is now open to foreign investment with the exception of certain specific areas (e.g. railways, print media, retail and agriculture).

At the international level, India has been very active and negotiated several Bilateral Agreements on Investment. Since 2002, it has signed 16 bilateral investment agreements, of which 8 are yet to be ratified.²³ Of the agreements signed before 1 January 2002, 10 have entered into force since 1 January 2002.²⁴ That shows the willingness of the Indian government(s) to attract FDI in the country. As a result, these gradual reforms have resulted in continued growth in annual FDI inflows. Indeed, annual FDI inflows into India grew from

²¹ Reserve Bank of India (2006), "Chronology of Major Policy Announcements: April 2005 – July 2006", Annex IV in 'RBI Annual Report', Mumbai, pp. 250-266.

²² Foreign Exchange Management (Transfer or issue of security by a person resident outside India), Regulations, 2000, Notification No. FEMA 20 /2000-RB dated 3rd May 2000. http://www.rbi.org.in/Scripts/BS_FemaNotifications.aspx?Id=174

²³ Trade Policy Review Body - Trade Policy Review - Report by the Secretariat – India, WT/TPR/S/182, 18/04/2007, para 45.

²⁴ Argentina (12.08.2002), Belarus (23.11.2003), Chinese Taipei (25.02.2005), Croatia (19.01.2002), Cyprus (12.01.2004), Finland (09.04.2003), Hungary (02.01.2006), Indonesia (22.01.2004), Kuwait (28.06.2003), Lao PDR (05.01.2003), Mongolia (29.04.2002), Portugal (19.07.2002), Tajikistan (14.11.2003), Turkmenistan (27.02.2006), Ukraine (12.08.2003), and Yemen (10.02.2004) (Ministry of Finance online information. Viewed at: http://www.finmin.nic.in/the_ministry/dept_eco_affairs/investment_div/invest_index.htm#Background_and_salient_features [8 June 2006]).

US\$3.13 billion in 2002-03 to US\$5.6 billion in 2005-06.²⁵ However, it could never match the inward success story of other Asian neighbours like China due to various reasons: “A May 2002 report on reforming the investment approval and implementation procedures concluded that, despite economic liberalization, FDI had not entered India to the degree expected; and this was due to several constraints, including in the complexity of procedural requirements of several laws and regulations, as well as transparency in the approval procedures”.²⁶

The impacts of the investment related disputes involving India as a respondent and the unilateral reform measures undertaken by it are worth mentioning here. It had to amend its policies to bring them into line with the WTO investment regime after losing a case against the US²⁷ and the EU²⁸ on TRIMs²⁹. In 2001, the *India - Measures Affecting the Automotive Sector* case involved a TRIM requiring « trade balancing ». In May 1999 the US government lodged a complaint against the Indian government for the auto industry measures it introduced in November 1997. Under the 1997 law, the Indian government required all new foreign auto manufacturing investments to sign a standard MOU with the government establishing:

- a minimum US\$50 million investment in joint ventures with majority foreign ownership;
- a waiver of import licenses if local content exceeds 50 per cent;

²⁵ Trade Policy Review Body - Trade Policy Review - Report by the Secretariat – India, WT/TPR/S/182, 18/04/2007, para 37.

²⁶ Trade Policy Review Body - Trade Policy Review - Report by the Secretariat – India, WT/TPR/S/182, 18/04/2007, para 39.

²⁷ DS 175 - Measures related to Trade and Investment in the Motor Vehicles Sector - request for consultation on 2 June 1999.

²⁸ DS 146 – on the same issue as in DS 175 – request for consultation on 6 October 1998.

²⁹ The TRIMs Agreement has constituted a significant net step forward in the investment area at the multilateral level. It addressed investment measures that were trade related and which violated Article III (National Treatment) or Article XI (general elimination of quantitative restrictions). Basically it prohibited member countries making the approval of investment conditional on compliance with laws, policies or administrative regulations that favoured domestic products. The TRIMs agreement adds value to the GATT/WTO system by describing types of trade-related investment measures (para. 2.1) that are considered to be inconsistent with GATT Article III or XI. See further, Gugler, Philippe and Chaisse, Julien (2008), « Investment Issues and WTO Law – Dealing with Fragmentation », in : Chaisse , Julien and Balmelli, Tiziano (Eds.), *Essays on the Future of the WTO*, EDIS, Geneva.

- and the obligation to export within 3 years, with possible restrictions on imports for CKD and SKD if export requirements are not met.

According to the Panel, as of the date of the establishment of the trade balancing condition, « there would necessarily have been a practical threshold to the amount of exports that each manufacturer could expect to make, which in turn would determine the amount of imports that could be made. This amounts to an import restriction. The degree of effective restriction which would result from this condition may vary from signatory to signatory depending on its own projections, its output, or specific market conditions, but a manufacturer is in no instance free to import, without commercial constraint, as many kits and components as it wishes without regard to its export opportunities and obligations »³⁰.

Article XI of the GATT 1994 stipulates the general elimination of quantitative restrictions. Article XI of the GATT 1994 prohibits any measure other than duties, taxes or other charges “or other measures having equivalent effect”. Therefore, it is not the legal form of the measure but its effect on trade which is important³¹. In that case, the Panel found that “the trade balancing condition contained in Public Notice No. 60 and in the MOUs signed thereunder, by limiting the amount of imports through linking them to an export commitment, acts as a restriction on importation, contrary to the terms of Article XI:1”³². After finding that the trade balancing requirements violate GATT Article XI:1, the India - Measures Affecting the Automotive Sector panel invoked the principle of judicial economy and concluded that it was not necessary to analyse the measures under the TRIMs Agreement³³.

³⁰ India - Measures Affecting the Automotive Sector - Report of the Panel, WT/DS146/R, WT/DS175/R, 21 December 2001, para. 7.277.

³¹ The Illustrative List annexed to the TRIMs Agreement sets out three categories of « TRIMs that are inconsistent with the obligation of general elimination of quantitative restrictions provided for in [Article XI:1 of the GATT] » (Annex, para. 2). TRIMs that are inconsistent with Article XI:1 include TRIMs that are : mandatory or enforceable under domestic law or under administrative rulings, or compliance with which is necessary to obtain an advantage, and which restrict « the importation by an enterprise of products used in or related to its local production, generally or to an amount related to the volume or value of local production that it exports; (b) the importation by an enterprise of products used in or related to its local production by restricting its access to foreign exchange to an amount related to the foreign exchange inflows attributable to the enterprise; or (c) the exportation or sale for export by an enterprise of products ».

³² India - Measures Affecting the Automotive Sector - Report of the Panel, WT/DS146/R, WT/DS175/R, 21 December 2001, para. 7.278.

³³ India - Measures Affecting the Automotive Sector - Report of the Panel, WT/DS146/R, WT/DS175/R, 21 December 2001, para. 7.323-7.324.

Among other reform measures with implications on smoothening capital flows – the gradual deregulation of financial services, and liberalization of the procedure concerning FDI in the banking, insurance and infrastructure sectors, increased coverage of FDI inflow under the automatic route and the relaxation of procedures relating to external commercial borrowings (ECBs) need to be mentioned. However, developed countries are still unhappy about the remaining restrictions on foreign equities in India.

For instance, the US government underlined in 2004 that, “the rules vary from industry to industry and are frequently changed, most often in the direction of further deregulation. The process is not always transparent and the restrictions on combined FDI and portfolio investment are inconsistent across industries... The automatic approval route is not available to foreign investors who wish to set up new ventures in India or who wish to enter into new technical collaborations or trademark agreements in India, if such foreign investors have or have previously had any joint venture, technology transfer or trademark agreement in the same or allied field in India... Such foreign investors would have to obtain an approval from the Indian government; .. In its application, such foreign investor would have to give reasons for which it finds it necessary to set up a new venture or enter into a technical collaboration or trademark agreement. The onus is on the investor to provide adequate justification to the satisfaction of the Indian government that its new proposal would not jeopardize the interests of the existing venture or the stakeholders thereof. The government may, at its discretion, approve or reject the application giving reasons for such rejection”.³⁴

Despite the attempts by India to ease the procedure, the trade partners remained skeptic to the changes, as re-stressed by the US in 2007, “Foreign purchaser attempts to acquire 100 percent ownership of a locally traded company, permissible in principle, faces regulatory hurdles that render 100 percent ownership unobtainable under current practice... Press Note 18, promulgated in 1998 by the Ministry of Industry, poses major impediments to investment in India by requiring prior approval of the Indian party to a joint venture before

³⁴ USTR (2004), p. 224.

the foreign partner can pursue other investment opportunities in India. This provision was widely abused, holding foreign partners hostage, even for failed joint ventures".³⁵

India is still trying to clarify and improve its domestic regulation of FDI and a number of steps have been undertaken in this regard: "In the latest move to rationalize policy further, in February 2006 equity restrictions were lifted in several activities, including brewing and distillation of alcohol; manufacturing activities in products subject to industrial licensing within 25 km of large cities; and in sensitive sectors such as the manufacture of explosives and hazardous chemicals, and "greenfield" airports, where investment has been permitted under the automatic route subject to sectoral regulations and, where applicable, an industrial licence under the Industries (Development and Regulation) Act".³⁶ After the changes made to the FDI policies during 2006, the revised investment procedures for various sectors in India and the foreign equity limits can be observed from **Annex 1**.

The country's gradually changing perspective on investment could be captured through a comparison of India's Conditional Initial Offer³⁷ and the Revised Offer³⁸ to the Council for Trade in Services. While the initial offer tabled in 2004 had imposed a foreign investment upper limit on a number of sectors, that condition has been removed for several categories (e.g. – Computer and related services, technical testing and analysis services etc.) (in) the revised offer to be submitted to the WTO next year. The revised offer generally requires that the establishment should be through incorporation and subject to Foreign Investment Promotion Board (FIPB) / Reserve Bank of India (RBI) approval. Also the foreign equity participation limit has been revised upwards for several categories (e.g. – telecommunication services). A detailed analysis of India's revised offer may be observed from **Annex 2**. Given the recent revisions incorporated in 2006, it could be expected that the subsequent offers would be more liberal on FDI procedures and equity limits.

³⁵ USTR (2007), p. 283.

³⁶ Trade Policy Review Body - Trade Policy Review - Report by the Secretariat – India, WT/TPR/S/182, 18/04/2007, para 39.

³⁷ India's submission to WTO, 'Conditional Initial Offer', TN/S/O/IND, 12 January 2004.

³⁸ India's submission to WTO, 'Revised Offer', TN/S/O/IND/Rev.1, 24 August 2005.

4. Investment Issues and other concerns under WTO: An Indian Perspective

Under the WTO, while TRIMs refers to provisions related to trade in goods; GATS deals with investment measures in the services category.

GATS deals mostly with investment issues of all the existing WTO obligations. The investment implications of GATS are largely derived from the key definition of Article I.2, which identifies modes by which services can be supplied. Several of these imply a significant presence (referred to as a “commercial presence” in the legal texts) in the country where the service is provided, and provide the basic protections of GATS to the investments that are an integral part of this presence. The supply of trade in services through “commercial presence”, which is in essence an investment activity, is covered by Mode 3.

Nevertheless, GATS Mode 4 also tackles investment issues because it deals with the temporary entry of managerial and other key personnel. Or in less opaque language, the admission of foreign nationals to another country to provide services there which is of high interest for India³⁹.

GATS uses in large part the selective liberalization approach to provide access to foreign service suppliers, i.e., to foreign investors in the field of services. However, it also contains elements of both the national and most favoured national treatment principles and it relies on the use of both positive lists of commitments and negative lists of exemptions for different purposes.⁴⁰

The Agreement on Trade Related Investment Measures (TRIMS) bans a limited number of performance requirements in so far as they are inconsistent with GATT provisions on national treatment and quantitative restrictions. All Members are required to notify and phase out contravening measures, although developing and least developed

³⁹ The visiting persons involved may be employees of a foreign service supplier, or may be providing services as independent individuals. Mode 4 can be then combined with Mode 3.

⁴⁰ For further details, see: Gugler, Philippe and Chaisse, Julien (2008), « Investment Issues and WTO Law – Dealing with Fragmentation », in : Chaisse, Julien and Balmelli, Tiziano (Eds.), Essays on the Future of the WTO, EDIS, Geneva.

countries were granted generous transitive periods. The Agreement has considerably enhanced the transparency of investment policies in the world. Nevertheless, the Agreement is limited to measures affecting only trade in goods.

Three further agreements – the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), the Government Procurement Agreement (GPA), and the Agreement on Subsidies and Countervailing Measures (ASCM) – have only indirect effects on investment. Hence we do not consider them in the current analysis⁴¹.

In order to strengthen the provisions of the GATS and TRIMs agreements, the Singapore Ministerial (1996) introduced the relationship between Trade and Investment for future discussion at WTO forums. Technically, TRIMs could be expanded by adding more examples to the Illustrative List. This adds to the uncertainty about which aspects of a national industrial policy can or will be challenged in the WTO, either through a loose interpretation of TRIMs or additions to the Illustrative List. But negotiations on that point did not succeed.

A working group was constituted to look into the relevant concerns, which submitted its report in December 1998, recommending further studies on FDI related issues.⁴² Furthermore, the study put the evaluation of the relationship between the mobility of capital and the mobility of labour among other issues on the future checklist.

In the initial period of the discussion during the late nineties, India interestingly considered the question of linking capital and labour mobility for some time, as observed from its submission to the Working Group on Trade and Investment:⁴³

“It is important for the Working Group on the Relationship between Trade and Investment to hold discussions to explore the nature and extent of issues in labour resources faced by different sectors. The Working Group can consider ways to overcome the labour crunch and improve productivity of capital by improving the mobility of labour... Even if the Working Group considers ways for the mobility of capital, there is little or no guarantee that appropriate labour inputs would become

⁴¹ For further details, see: Gugler Philippe, Tomsik Vladimir, A Comparison of the Provisions Affecting Investment in the Existing WTO Obligations, World Trade Institute Working Paper No.15, 2006, pp. 5-6.

⁴² Document No. WT/WGTI/2, Dated 8 December 1998.

⁴³ India's submission to WTO - WT/WGTI/W/39, 4 June 1998.

available for utilization of that capital. Hence, the Working Group can help align grassroots realities and suggest easy mobility of selected categories of labour apart from the higher categories of personnel for which most Member countries of the WTO have already undertaken commitments under the GATS. For complementing immediate production purposes, the Working Group can suggest ways for selected labour to move from surplus regions to deficit regions.”

The outlook continued in the subsequent period as reflected from India’s submission to the WTO in the following period:⁴⁴

“The extensive debate on free mobility of capital may have to be supplemented by an equally extensive study on free mobility of labour. If cheap labour is an important determinant of investment decisions, and results in higher profitability for investors which can be ploughed back into the home country economy, it may be, at the least, equitable to augment host country economies by returns from a mobile labour working in the investors’ home country... mobility of labour should be inextricably linked with the discussions on trade-investment linkage if the WTO is to go beyond looking at delivery systems to look at production systems.”

Even after the failure of the Seattle Ministerial (1999), as reflected through its submissions to the WTO, India did not abandon the idea of linking labour and capital mobility. For instance, during the Seattle-to-Doha Period, it focused on a number of questions involving the optimality of barrier-free FDI inflow into developing countries,⁴⁵ foreign investors’ obligations, issues pertaining to investment incentives, the costs of adjustment and impact on social gains in developing countries and the comparative flexibility with bilateral investment agreements etc. It maintained that there is a need to check the following to ensure the above-mentioned issues:

“Whether mobility of labour should also not be meaningfully addressed when movements relating to the other three factors of production namely, goods, services and capital are being taken up in one form or the other.”

⁴⁴ India’s submission to WTO - WT/WGTI/W/72, 13 April 1999.

⁴⁵ India’s submission to WTO - WT/WGTI/W/86, 22 June 2000.

However, in the subsequent period, India started slowly moving away from this position, probably in the light of the East Asian Experience. Before the Doha Round, India expressed dissatisfaction over the progress of technology transfer into developing countries, and cited the following argument as an obvious reason for regulating FDI inflow or investment:⁴⁶

“One major reason why FDI is sought by countries, especially developing countries, is that FDI generally brings with it the much needed state-of-the-art technology that developing countries lack. However, available facts and figures do not vindicate this expectation of developing countries... more striking, particularly for the developing countries, is the fact that while their share of FDI inflows has gone up, their share in global technology transfers has come down. ... the inevitable conclusion that developing countries should preserve their right and ability to influence foreign direct investment flows into their territories with a view to ensuring that it is accompanied by appropriate technology..”

This motive, along with the volatility concern, has been one of the key factors behind India’s decision to oppose the initiation of discussion on TI both at the Doha and Cancun Ministerials of the WTO. As observed from **Table 1**, India’s share in world FDI inflow has increased since 2001, but that has not been commensurate with its expectations. However, in general all of the countries cited in the table experienced a fluctuating trend in terms of proportional FDI inflow. Perhaps the intention of maintaining a smooth growth curve, in light of the volatility associated with FDI-led growth elsewhere, was instrumental behind India’s decision to adopt a cautious approach.

Table 1: The Global FDI inflow Scenario as a proportion of World flows (%)

Country	1992-97*	1998	2000	2001	2002	2004	2005
Brazil	2.13	4.18	2.36	2.75	2.44	2.55	1.64
Chile	0.94	0.67	0.35	0.51	0.28	1.01	0.73
China, PR	10.54	6.58	2.94	5.73	7.77	8.53	7.90

⁴⁶ India’s submission to WTO - WT/WGTI/W/105, 26 June 2001.

India	0.54	0.38	0.17	0.42	0.51	0.77	0.72
Malaysia	1.87	0.39	0.27	0.07	0.47	0.65	0.43
Mexico	3.09	1.78	1.20	3.28	2.17	2.63	1.97
Singapore	2.67	1.11	1.24	1.84	0.84	2.09	2.19
Thailand	0.73	1.08	0.24	0.47	0.16	0.20	0.40

* - (Annual average)

World Investment Report (2006)

At the Doha Ministerial (2001), India decided against discussion on any of the Singapore issues, until and unless the level of market access promised to the developing countries at the Uruguay Round is realized.⁴⁷ It is interesting to note that apart from developed countries, a number of developing countries like Chile, Costa Rica, South Korea, Morocco, Czech Republic and Hungary were not averse to the idea of discussing TI at the ministerial meeting.⁴⁸ Finally in line with India's argument the ministerial declaration, i.e., 'Doha Development Agenda' announced that the negotiations on TI would take place after the Fifth Session of the Ministerial Conference (paragraph 20-22). The ministerial declaration promised that in future "Any framework should reflect in a balanced manner the interests of home and host countries, and take due account of the development policies and objectives of host governments as well as their right to regulate in the public interest. The special development, trade and financial needs of developing and least-developed countries should be taken into account as an integral part of any framework, which should enable members to undertake obligations and commitments commensurate with their individual needs and circumstances".

⁴⁷ "... negotiations (on Singapore Issues) can be launched in these areas only if there is explicit consensus. As far as the proposal to negotiate rules on foreign direct investment in concerned, I would at the outset like to request everybody not to mix up two different issues namely, willingness of a country of receive foreign direct investment and willingness of a country to accept binding multilateral rules on foreign direct investment in the WTO. I would also like to point out that India has a fairly open and liberal foreign investment regime but does not believe that there is need for negotiating rules on this subject in the WTO. In our assessment, the only purpose of such an exercise would be to protect the interests of foreign investors and to take away the policy flexibility available to the developing countries." Statement by Mr. Prabir Sengupta, Commerce Secretary, Government of India, at the informal General Council Meeting of the WTO held in Geneva on 25 June, 2001. *India and the WTO*, June-July 2001, p. 6.

⁴⁸ Singh, Yashika (2001), India at the Fourth Ministerial Meeting in Doha: Déjà vu – again?, RGICS Working Paper No. 32, New Delhi.

It is argued that developing countries are more prone to enter into Bilateral Investment Treaties (BITs) if there is competition for attracting investments with their counterparts.⁴⁹ When we look at the historic steps, it must be underlined that between 1995 and 2001, India entered into Bilateral Investment Treaties (BITs) with 41 countries,⁵⁰ and that development got reflected in its submissions to the WTO stressing their advantages during the subsequent period:

“Developing countries need to retain the ability to screen and channel FDI in tune with their domestic interests and priorities. Bilateral investment treaties have been favoured the world over for precisely the flexibility they provide to the host country while at the same time extending necessary protection to foreign investors.”⁵¹

This trend to go through bilateral negotiations is still relevant. As mentioned above between 2002 and 2006, India entered into several negotiations and concluded 16 BITs, 10 of which have already entered into force.⁵²

Before the Cancun Ministerial, India focused on a wide range of issues spanning from the extent of constitutional powers available to the authorities to make rules and regulations related to foreign investment, to the disclosure and accounting procedures, effects of technology transfer, restrictive business practices etc.⁵³ It further noted that the developed countries favouring a multilateral agreement on investment should keep the special characteristic of capital in mind and must learn from the past experiences at other forums (e.g. – OECD):

“.. the question of non-discrimination in capital flows becomes more complex. There is no clear buyer-seller linkage, as is the case of goods and services, and no certainty regarding the source of funds. There is also no certainty regarding the manner in which funds will be retained in the host country and at what point in time, in what

⁴⁹ Elkins, Zachary, Andrew T. Guzman, and Beth A. Simmons, “Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000”, International Organization, Vol. 60, No. 4, pp. 811–46, 2006.

⁵⁰ Das (2003), *op cit.*

⁵¹ India’s submission to WTO - WT/WGTI/W/150, 7 October 2002.

⁵² Trade Policy Review Body - Trade Policy Review - Report by the Secretariat – India, WT/TPR/S/182, 18/04/2007, para 45.

⁵³ WT/WGTI/W/152, Dated 19 November 2002.

manner, and to what extent funds will flow out... A certain degree of discrimination between different kinds of investment is unavoidable... A case in point is the OECD Code for the Liberalization of Capital Movements in which right of establishment was introduced in 1984. Another instance is that of the APEC non-binding investment principle. A multilateral Agreement on Investment under the auspices of the economically well-off countries of the OECD, which envisaged in the draft agreement binding national treatment obligations, did not find favour with many of these countries, and had to be abandoned. How then can an agreement of this nature, envisaging national treatment and MFN provision of a binding nature, be considered in a much more heterogeneous group like WTO?"

In the subsequent period, the argument of the worsening BOP situation in case of a potential currency crisis was also brought to the forefront for the first time by India in 2002, as is evident from its submission to the WTO:⁵⁴

"Any movement of capital that would cause serious damage to the domestic industry, particularly small and medium-sized enterprises and have adverse effects on employment would need to be carefully regulated. Developing countries need to retain the ability to screen and channel foreign investment in accordance with their domestic interests and priorities. Another point to which attention needs to be drawn is the possible damaging effect of capital outflows on balance-of-payments.... there is also a strong case for performance requirements such as export obligations and foreign exchange neutrality to moderate the adverse effects of capital outflows."

At the Cancun Ministerial (2003) India was upset with the fact that despite the promise made at Doha to have future discussions on Singapore Issues only after arriving at consensus, several developed countries attempted to include TI in the negotiating agenda.⁵⁵ India in association with other developing countries rejected the 'Derbez Draft' and the negotiation process was stalled for almost a year. It was decided in the July 2004 declaration

⁵⁴ India's submission to WTO - WT/WGTI/W/148, 7 October 2002.

⁵⁵ "... in relation to the Singapore issues, the 13th September draft was even more curious.... The Agenda of Doha was very clear on this ... negotiations on modalities for the Singapore Issues would commence only after explicit consensus is reached in the next Ministerial Conference. Explicit Consensus means 146 members – now 148 members – have to explicitly say yes, and only then, modalities could begin... India was the first to speak against the Singapore issues – the 13th September draft, if we had taken the head count of the countries opposing, it should well have been in three figures ... If such a large part of the WTO membership does not agree, how is the 13th September draft produced, which says that modalities will now very shortly commence on investment, and immediately commence on trade facilitation and transparency in Government Procurement..." Text of keynote address by Mr. Arun Jaitley at FICCI-UNCTAD Seminar on "Reflections on post-Cancun Agenda: The way ahead" - 22 October 2003, New Delhi, India and the WTO Newsletter (October-November 2003).

of the WTO that no negotiation on TI would take place within the WTO during the Doha Round.

After the Doha Ministerial, buoyed by the upsurge in outward movement (both short-term and long-term) of professionals from the country, India stopped linking the movement of labour with capital and attempted to convince the developed countries about the gains they could experience by allowing free movement of labour from their developed counterparts:⁵⁶

“There is a much greater convergence of interests in Mode 4 between the developed and the developing countries in the current negotiations as compared to Uruguay Round. A strong impetus to such movement is the large gap between the projected needs and the local availability of certain categories of personnel in developed countries, further accentuated by their increasingly aging populations. Welfare gains from freer movement of natural persons would, therefore, accrue to both groups of countries as has been documented in recent studies... Some Members have not introduced any improvement to the existing commitments, others have introduced some minor changes aimed at clarifying and in some cases expanding the scope of commitments... The problem (in administrative procedures) seems to be the inability to clearly separate the temporary movement of service suppliers from permanent immigration and the application of the normal immigration rules and procedures to even temporary movement under GATS...”

It was furthermore pointed out by India in the following period⁵⁷ that the WTO negotiation process has largely failed to meet the expectation of the developing countries. It also stressed the importance of de-linking Mode 4 from other categories of services, given their importance to the developing countries, in no uncertain terms:

“After analysing the initial offers presented by developed Members, in our assessment, most of these offers do not show any real improvement to the existing commitments in Mode 4. Some Members have not introduced any improvement to the

⁵⁶ India’s submission to WTO - TN/S/W/14, 3 July 2003.

⁵⁷ India’s submission to WTO - TN/S/W/19, 31 March 2004.

existing commitments; others have only introduced some minor changes aimed at clarifying and only in a few cases expanding the scope of commitments. Basically commitments continue to be limited to categories of personnel related to commercial presence despite the expressed interest of developing Members for commitments in categories de-linked from commercial presence as well... Developing Members in general have comparative advantages only in a narrow range of services activities. The primary mode for most of these relates to Mode 4. The liberalisation of this mode of supply would, therefore, provide effective market access to service providers from developing Members and contribute significantly to the implementation of Article IV of the GATS.”

India also pointed out in the following period⁵⁸ the ineffectiveness of the existing GATS rules in improving the transparency of the regulatory procedures on Mode 4 and concluded that there exist enormous opportunities for improving it. From this point, the link between mobility of capital and labour has not been stressed by India any more. With this background, the current paper analyses India’s potential ability to utilize CAC as a policy tool to extract benefits from other areas (e.g. – mobility of labour) from the developed countries and comments on its reluctance to go for the CAC or a freer investment regime.

One key reason behind the lack of interest on India’s part towards TI negotiation may evolve from its recent Regional Trade Agreements (RTA) strategy. Before the Cancun Ministerial, India depended heavily on multilateralism and did not join any vibrant trade bloc. However, since 2003 India has entered into a number of RTA negotiations with countries located in Asia, Africa and Latin America initially. In a recent period preliminary discussions with Canada and the EU on the preferential trade and investment agreement have just started. India’s interest in the Free Trade Agreements (FTA) with Association of Southeast Asian Nations (ASEAN) can be explained by its willingness to be a part of the broader trade and investment network developed between the ASEAN members. Similarly the interest in entering into the FTAs with the capital-rich economies of the region (e.g. – Japan, Korea) is obvious. The recent discussions indicate that India would prefer to enter into a Bilateral Investment Promotion and Protection Agreement (BIPA) with China rather

⁵⁸ India’s Informal paper submission to WTO - JOB(04)/142, 29 September 2004.

than a simple FTA in goods. For boosting investment inflow, the Comprehensive Economic Cooperation Agreement (CECA) with Singapore includes an investment cooperation agreement as well as a Double Taxation Avoidance Agreement (DTAA). Investment cooperation is also incorporated in Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), which links the South Asian Association for Regional Cooperation (SAARC) countries (minus Pakistan) with regionally closer ASEAN countries (Myanmar, Thailand) and in the Trade and Economic Framework Agreement with Australia. Perhaps these forums to a certain extent dilute the incentives for supporting TI.

5. The Empirical Analysis⁵⁹

The current analysis attempts to estimate the potential destabilizing effects of capital and current account balances (KAB and CAB respectively) on each other using the Indian data in order to analyse the potential threat to the country. The quarterly data on CAB and KAB are obtained from various issues of RBI Bulletins and the Handbook of Statistics on Indian Economy. The first quarter of 1979 to the second quarter of 2005 is taken as the sample period for our analysis. The following underlying relationship is tested here following Wong and Carranza (1999):⁶⁰

$$\text{CAB} = f(\text{KAB}, \text{€}) \text{ ceteris paribus.}$$

where € stands for any other determinants of the CAB.

⁵⁹ The analysis draws from Chakraborty, Debashis and Guha, Arup (2007), "Should India opt for Full Capital Account Convertibility? Some Exploratory Results", *Foreign Trade Review*, 42(1), pp. 1-27.

⁶⁰ Wong, Chong-Huey and Luis Carranza (1999), "Policy Responses to External Imbalances in Emerging Market Economies: Further Empirical Results", *IMF Staff Papers*, Vol. 46, No. 2, pp. 225-237.

5.1. Stationarity Test

The Augmented Dicky-Fuller (ADF) test reported in **Table 2** shows that the CAB and the KAB series are stationary and non-stationary respectively. Hence for further analysis we consider the first difference of the series (DKAB), which is stationary.

Table 2: Augmented Dicky-Fuller Test Results

Series	ADF Test Statistics	5% Critical Values
CAB	-3.86245	-3.4543
KAB	0.380583	-3.4543
DKAB	-5.996884	-3.4548

5.2. Chow Breakpoint Test

To identify the nature of the changing dynamics in the capital inflow, reflected through the capital account balance series, the Chow test is undertaken. In January and August 1994 India accepted MIGA membership and adopted current account convertibility respectively, and given our interest in the interaction between CAB and KAB, it is assumed that substantial liberalization occurred during the third quarter of 1994. In order to test whether the policy change is reflected in the data or not, the aforesaid period is put to "Chow Forecast test", which uses the estimated model for a subsample comprised of the pre-break observations to generate predicted values of the dependent variable in the remaining data points. A large difference between the actual and predicted values casts doubt on the stability of the estimated relationship between the two sub samples. This difference, if statistically significant, establishes the postulated breakpoint as a structural break. The Chow forecast test statistic reported in **Table 3** confirms the third quarter of 1994 to be a structural break of the first difference of the KAB data series. Hence we consider the period before the

second quarter of 1994 and the period after as the pre-liberalization and post-liberalization time period respectively.

Table 3: The Chow Forecast Test to the DKAB Series

Chow Forecast Test: 1994:3			
F-statistic	23.59900	Probability	0.000000
Log likelihood ratio	310.8631	Probability	0.000000

5.3. Granger Causality Tests

Using these two stationary series, we next test for Granger Causality. For selecting the best fit, a bivariate VAR model is estimated with both the pre-liberalization and post-liberalization periods as defined by us separately, and optimum lag lengths are determined in each case by looking at the Akaike Information Criteria (AIC). The results are reported in **Table 4:**

Table 4: The Granger Causality Results

Null Hypotheses	Pre-Liberalization 1979: 1 – 1994: 2 (4 lags)	Post-Liberalization 1994: 3 – 2005: 2 (3 lags)
CAB does not Granger Cause DKAB	Rejected (0.00389)	Rejected (0.00001)
DKAB does not Granger Cause CAB	Accepted (0.18381)	Accepted (0.18048)

The results indicate that while in the case of the pre-liberalization as well as in the post-liberalisation periods, CAB influences changes in DKAB, the relationship does not hold the other way round. However, the determined lag length is found to be longer during the

pre-liberalization period. One probable explanation for the absence of causality by DKAB on CAB is perhaps that the movements in the current account are influenced more by excluded factors.⁶¹ Second, the number of observations in the post-liberalization period perhaps puts a limitation on the finding.

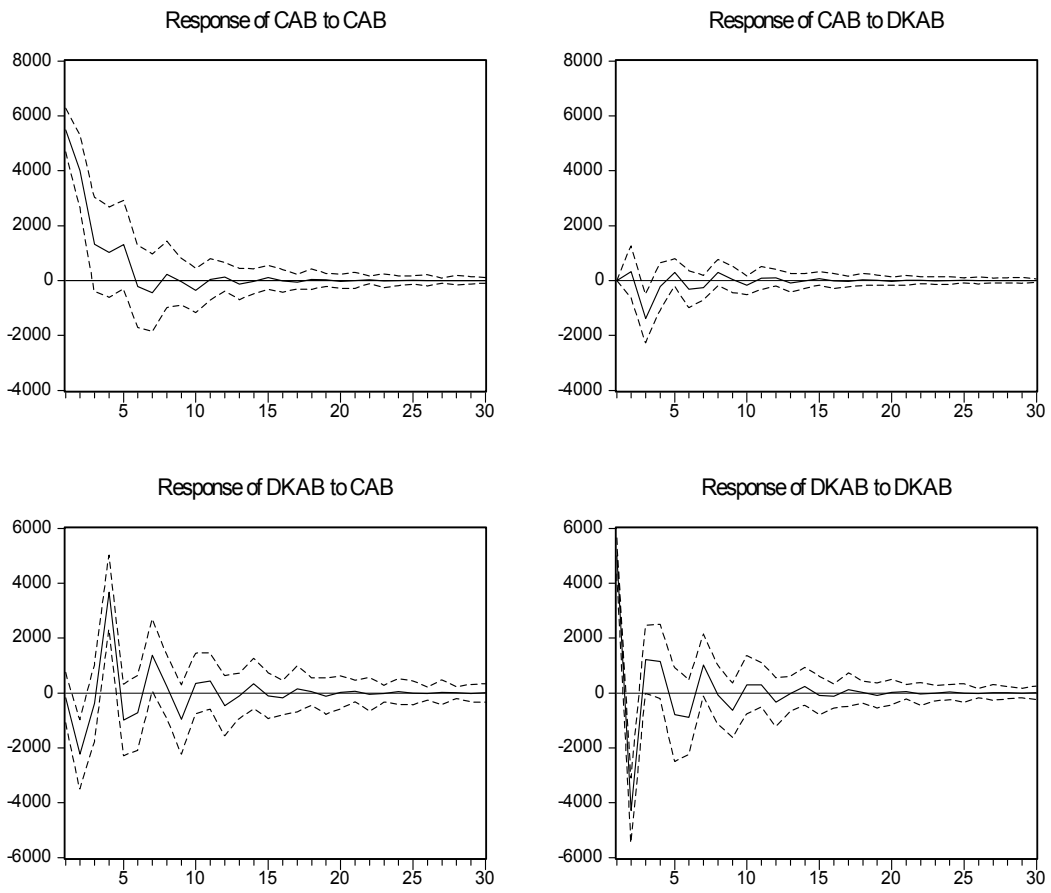
5.4. Current Account and Capital Responses to Capital inflows

A further analysis of Impulse Response Functions enables us to trace the effect of a once-and-for-all unanticipated shock (i.e., a crisis) in capital account on the current account balance. The results are reported in **Diagram 1**. The CAB and the KAB series take around 20 and 30 quarters respectively to get back to equilibrium in the aftermath of a shock and the fluctuations are both negative and positive beginning with an initial huge fall in the series causing the crisis. The lower time taken by the CAB series to converge may be explained by the absence of direct causality between the two series. The indirect effects through the working of other macro variables perhaps also play a key role here.

⁶¹ The findings of Chakraborty and Guha (2007) indicate that variance in capital inflow into India can be explained by innovations to interest rate differentials and budget deficits.

Diagrams 1: Responses of CAB and DKAB to an unanticipated shock

Response to One S.D. Innovations ± 2 S.E.



6. Conclusion

Conflict over the interpretation of the TRIMs reflects the fact that it was a compromise agreement in the first place. Differences between trade officials from developing and developed countries could not be resolved during the Uruguay Round of GATT talks, and this is reflected in the vague wording of the TRIMs Agreement. Concerning inconsistencies with TRIMs agreement, the domestic automobile development policies of India, Indonesia, Brazil, and the Philippines as well have been brought forward or made subject to consultation for dispute settlement. Also, developing countries were not easily able to attain extensions of the period for removing measures that do not comply with the agreement. In response to these incidents, developing countries remain concerned that adoption of a new agreement would impede their freedom to implement policies with national development priorities⁶².

The paper initially raised two arguments favouring a freer investment regime in India, namely, facilitating more FDI inflow and the option of ensuring freer mobility of labour in partner countries.

The FDI regime in India has been considerably simplified and liberalized, and is now open to foreign investment with a few exceptions. That liberalization results from a unilateral process. By refusing to go into multilateral negotiations on investment India has been able to gradually facilitate foreign investments. That approach can be understood in the light of the Asian crisis. But it is not the only argument.

The scope for a multilateral agreement on investment at the WTO depends on other negotiations. It was not in the interest of India to abandon bluntly the control on FDI. At the same time India expected (and still expects) some gains from the ongoing negotiations on

⁶² Conflict over the interpretation of the TRIMs reflects the fact that it was a compromise agreement in the first place. Differences between trade officials from developing and developed countries could not be resolved during the Uruguay Round of GATT talks, and this is reflected in the vague wording of the TRIMs Agreement. If the EC, US and Japanese governments had succeeded, then TRIMs would have been a comprehensive agreement on investment similar to Chapter 11 of NAFTA or the MAI. See, Gugler, Philippe and Chaisse, Julien (2008), « Investment Issues and WTO Law – Dealing with Fragmentation », in : Chaisse, Julien and Balmelli, Tiziano (Eds.), *Essays on the Future of the WTO*, EDIS, Geneva.

GATS and its exports under mode 4. It seems to us that establishing a link between trade and investment is a strategy to obtain major concessions regarding Mode 4.

Given the absence of causality between KAB and CAB established from the empirical analysis, it may be argued that India is ready for full-scale CAC. However, in light of the potential imbalances caused by an imaginary unanticipated shock in our analysis, India's decision to cautiously open up the domestic economy to FDI inflow and foreign equity holding seems to some extent justifiable. Moreover, it needs to be borne in mind that apart from the potential foreign exchange crisis, the adoption of CAC significantly affects fiscal policy, which is least effective under free mobility of capital. Perhaps these concerns collectively leads India to adopt a less enthusiastic approach at the WTO forums on TI.

Given the abundance of 'cheap' skilled professionals in the Indian labour market, the concern over the lower volume of FDI inflow, in comparison with China and other East Asian countries, should better be addressed through targeted policy actions (e.g. – creation of better infrastructure). Linking Mode 4 with Investment might have its own limitations. In addition, although the dream of achieving free mobility of labour is not coming true soon, the internal conflicts of interest in the developed countries over the H1-B visa often gets visible. A few years back, Bill Gates, one of the major employer of software professionals from India demanded to the US policymakers that the H1-B visa cap on the number of foreign tech workers should be abolished.⁶³ It is probably not entirely coincidental that a week later the US had granted an additional 20,000 H1-B visas for fiscal year 2005.⁶⁴ The concern for India still exists, as Gates in early 2007 once again had to criticise the US decision to lower the number of the H1-B visas from over 200,000 in the 1990s to the current level of about 65,000. He pleaded for an increase in skilled worker visas by indicating that the allotments of 65,000 H1B visas in 2007 were exhausted some four months before the year began.⁶⁵

⁶³ "The whole idea behind the H1-B thing is, 'Don't let too many smart people come into the country'. The thing basically doesn't make sense. That's just wondering ourselves in this global competition," Gates told policy makers on Capitol Hill on Wednesday." The Hindustan Times, Friday, April 29, 2005.

⁶⁴ The Hindustan Times, Friday, May 6, 2005.

⁶⁵ "Bill Gates Slams US Visa Policy: More H1-B?", March 8 2007, available at <http://onlybombay.blogspot.com/2007/03/bill-gates-slams-us-visa-policy-more-h1.html>

The lesson from these events is that as long as the competitiveness of India's 'products', i.e., the expertise of the professional service providers exists, it would be able to achieve its goal slowly, the barriers notwithstanding. Any attempt to facilitate this move by linking it with a freer investment regime is uncertain, and therefore in the light of these findings, India's current negotiating stance on TI seems reasonably justifiable.

Any project of multilateral agreement on investment should take into account these legitimate expectations. Perhaps the Indian approach shows that an investment agreement could only follow a "GATS-type" positive list approach in the "pre-establishment" phase, meaning that countries could "pick and choose" which commitments they wanted to take. The positive list approach would probably permit a more gradual liberalization, which some countries may be more comfortable with. It is common knowledge that in GATS, no Member of the WTO is a priori forced to make any commitments in any given sector. Perhaps the stream of negotiations on TI issues over the last decade calls for a similar arrangement here as well.

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Annex 1: Current FDI Scenario in India

Area	New Policy
Change of route	FDI has been allowed up to 100 per cent under the automatic route for distillation and brewing of potable alcohol; manufacture of industrial explosives; manufacture of hazardous chemicals; manufacturing activities located within 25 km of the Standard Urban Area limits requiring industrial license under the IDR (Act), 1951; setting up of Greenfield airport projects; laying of natural gas/LNG pipelines, market study & formulation and investment financing in the petroleum sector; and cash & carry wholesale trading and export trading.
Increase in equity caps	FDI caps have been increased to 100 per cent and automatic route extended to coal & lignite mining for captive consumption, setting up infrastructure relating to marketing in Petroleum & Natural Gas sector, and exploration and mining of diamonds and precious stones.
FDI in new activities	FDI has been allowed up to 100 per cent on the automatic route in power trading, and processing and warehousing of coffee and rubber. FDI has been allowed up to 51 per cent for 'single brand' product retailing, which requires prior Government approval. Specific guidelines have been issued for governing FDI for 'single brand' product retailing.
Removal of restrictive conditions	Mandatory divestment condition for B2B e-commerce has been dispensed with..
Procedural simplification	The transfer of shares by residents to non-residents including acquisition of shares in an existing company has been placed on the automatic route subject to sectoral policy on FDI.
Equity caps on FDI inflow are presently imposed only in select sectors as mentioned in the following:	
Upto 20%	FM Radio Broadcasting.
Upto 26%	Insurance, Defence production, Petroleum refining in the PSUs; Print and Electronic media covering News & current affairs.
Upto 49%	Air Transport Services; Asset Reconstruction Companies; Cable network; DTH; Hardware for uplinking, HUB etc
Upto 51%	Single Brand Retailing of products.
Upto 74%	Atomic Minerals; Private Sector Banking; Telecom services; Establishment & operation of Satellites.

Source: Quoted from the Annual Report,
Department of Industrial Policy and Promotion, Government of India (2006-07)

Annex 2: India's Sectoral Revised Offer for Trade in Services – Select Sectors

Sector	Limitations on Market Access
Architectural services	None except that the establishment would be only through incorporation as partnership firm constituted by Architects and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Integrated Engineering services	None except that the establishment would be only through incorporation and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Urban planning and Landscape Architectural services	None except that the establishment would be only through incorporation as partnership firm constituted by Architects and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Medical and Dental services	Only through incorporation with a foreign equity ceiling of 74 per cent subject to the condition that the latest technology for treatment will be brought in and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Veterinary services	None except that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Services provided by Midwives, Nurses, Physiotherapists and para-medical personnel	Only through incorporation with a foreign equity ceiling of 74 per cent subject to the condition that the latest technology for treatment will be brought in and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Computer and Related Services	None except that the establishment would be only through incorporation.
R&D services on the .. natural sciences only	None except that the establishment would be only through incorporation and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Real Estate Services	None for Consultancy Services, subject to FIPB approval and also subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Rental/Leasing Services without	None subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval

operators)	would be required.
Other Business Services	None subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Telecommunication Services	The service will be permitted to be provided only after the operator gets a licence from the Designated Authority. In the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required. Number of licenses, may, however, be limited due to scarce resources such as right of way and spectrum availability, subject to a minimum of two licences in each service area. The private operator should be a company registered in India in which total foreign equity must not exceed 49 per cent.
Motion picture or video distribution services	<ul style="list-style-type: none"> • Only through representative offices which will be allowed to function as branches of companies incorporated outside India. • Import of titles restricted to 100 per year.
General Construction work for civil engineering	None except that the establishment would be only through incorporation and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Commission agents' services covering sales on a fee or contract .. :	None, subject to approval of RBI/FIPB and conformity with FEMA regulations, as applicable and also subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Wholesale trade services	None, subject to approval of RBI/FIPB and conformity with FEMA regulations, as applicable and also subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Higher Education Services	<ul style="list-style-type: none"> • None subject to the condition that service providers would be subject to regulations, as applicable to domestic providers in the country of origin. • None subject to the condition that fees to be charged can be fixed by an appropriate authority and that such fees do not lead to charging capitation fees or to profiteering. Subject further to such regulations, already in place or to be prescribed by the appropriate regulatory authority. In the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Refuse Disposal Services Sanitation and Similar Services	None subject to incorporation and the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Life Insurance	None, except establishment would be through incorporation with foreign equity not exceeding 26 per cent and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Non-life insurance	<ul style="list-style-type: none"> • Unbound except in the case of insurance of freight, where there is

	<p>no requirement that goods in transit to and from India should be insured with Indian insurance companies only. Insurance is taken by the buyer or seller in accordance with the terms of the contract. This position will be maintained. Once under a contract the Indian importer or exporter agrees to assume the responsibility for insurance such as in the case of f.o.b. contracts for imports into India or c.i.f. contracts for exports from India, insurance has to be taken only with an Indian insurance company.</p> <ul style="list-style-type: none"> • None except establishment would be through incorporation with foreign equity not exceeding 26 per cent and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Services auxiliary to insurance, such as consultancy, actuarial, risk assessment	<p>None subject to the conditions that foreign companies can be established through incorporation with foreign equity not exceeding 51 per cent and further subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required. In the case of Actuarial and Advisory Services, formal certification by Actuarial Society of India would be required.</p>
Banking and other financial services	<ul style="list-style-type: none"> • .. through branch operations and as a wholly owned subsidiary of a foreign bank licensed and supervised as a bank in its home country and subject to regulations of the Reserve Bank of India. • A limit of twelve twenty licences per year both for new entrants and existing banks. • Banks are allowed to install ATMs at branches and at other places identified by them. Installation of ATM at a place other than in licensed branches is treated as a new place of business and requires a licence. Licences issued for ATMs installed by foreign banks will not be included in the ceiling of twenty licences referred to in item .. above. • .. foreign banks are permitted to invest in private sector banks through the FDI route subject to foreign equity ceiling of 49 per cent and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Financial leasing	<p>Allowed for foreign financial services companies (including banks) through incorporation and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.</p>
Asset Management, confined to such as cash or portfolio management, all forms of collective investment management, pension fund management,	<p>None except establishment would be through incorporation with foreign equity not exceeding 26 per cent and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.</p>

custodial, depository and trust services	
Financial consultancy services, i.e. financial advisory services provided by financial advisers, etc. to customers on financial matters, investment and portfolio research and advice, advice on acquisitions and on corporate restructuring and strategy	<ul style="list-style-type: none"> • Allowed for foreign financial services companies (including banks) through incorporation. • And subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Hospital Services	<ul style="list-style-type: none"> • None for provision of services on provider to provider basis such that the transaction is between two established medical institutions, covering the area as of second opinion to help in diagnosis of cases or in the field of research. • Only through incorporation with a foreign equity ceiling of 74 per cent and subject to the condition that the latest technology for treatment will be brought in and further subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required. Publicly funded services may be available only to Indian citizens or may be supplied at differential prices to persons other than Indian citizens.
Hotels and other lodging services	Only through incorporation and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Travel Agency Tour Operator Services	Only through incorporation in and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Tourist Guides Services	<ul style="list-style-type: none"> • Only through incorporation and subject to total ceiling of 500 tourist guides conversant in Chinese, Spanish, Portuguese, French and Japanese and in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required. • None for tourist guides conversant in Chinese, Spanish, Portuguese, French and Japanese languages subject to a total ceiling of 500. For others: Unbound except as in horizontal Commitments.
Entertainment Services (including	None and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.

Theatre, Live bands and circus services	
Maritime Transport Services International Transport	<ul style="list-style-type: none"> • At least 40 per cent of cargo carried by liner shipping companies must be reserved for Indian Flag ships. • Preference will be given to Indian Flag vessels for government cargoes; and Government owned/ controlled cargo. • Government policy on FOB/ FAS imports and export will hold good. • Indian flag vessels will have the first right of refusal for carrying such cargo and only thereafter can foreign flag ships be allowed to be in-chartered/ taken on international rental basis.
Maritime Cargo Handling services	None, except as indicated in Horizontal commitment/ Head Note to this Schedule and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Storage and Warehousing services in Ports	Do
Maritime Agency Services	Do
Maritime Freight Forwarding Services	Do
International rental/charter of vessels with crew or on bareboat basis (excluding cabotage and offshore transport)	None except obtaining permission from Director General (Shipping) for chartering a foreign flag vessel in the absence of availability of a suitable Indian vessel.
Maintenance and repairs of sea going vessels	None, except as indicated in Horizontal commitment/ head Note to this Schedule and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Ship Broking Service	None, except as indicated in the Head Note and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.
Maintenance and repair of aircraft	None and subject to the condition that in the case of foreign investors having prior collaboration in that specific service sector in India, FIPB approval would be required.

Source: Constructed from India's revised Offer (TN/S/O/IND/Rev.1, 24 August 2005)