

A REPORT OF THE CSIS  
WADHWANI CHAIR IN U.S.-INDIA  
POLICY STUDIES

# BIT and Beyond

ADVANCING THE U.S.-INDIA ECONOMIC RELATIONSHIP

*Principal Author*

Matthew Stokes

*Contributing Author*

Niraj Patel

*Foreword*

Karl F. Inderfurth



November 2012



50  
YEARS

| CHARTING  
OUR FUTURE

CSIS

| CENTER FOR STRATEGIC &  
INTERNATIONAL STUDIES



A REPORT OF THE CSIS  
WADHWANI CHAIR IN U.S.-INDIA  
POLICY STUDIES

# BIT and Beyond

ADVANCING THE U.S.-INDIA ECONOMIC RELATIONSHIP

*Principal Author*

Matthew Stokes

*Contributing Author*

Niraj Patel

*Foreword*

Karl F. Inderfurth

November 2012



50  
YEARS

| CHARTING  
OUR FUTURE

CSIS

| CENTER FOR STRATEGIC &  
INTERNATIONAL STUDIES

## About CSIS—50th Anniversary Year

For 50 years, the Center for Strategic and International Studies (CSIS) has developed practical solutions to the world's greatest challenges. As we celebrate this milestone, CSIS scholars continue to provide strategic insights and bipartisan policy solutions to help decisionmakers chart a course toward a better world.

CSIS is a bipartisan, nonprofit organization headquartered in Washington, D.C. The Center's 220 full-time staff and large network of affiliated scholars conduct research and analysis and develop policy initiatives that look into the future and anticipate change.

Since 1962, CSIS has been dedicated to finding ways to sustain American prominence and prosperity as a force for good in the world. After 50 years, CSIS has become one of the world's pre-eminent international policy institutions focused on defense and security; regional stability; and transnational challenges ranging from energy and climate to global development and economic integration.

Former U.S. senator Sam Nunn has chaired the CSIS Board of Trustees since 1999. John J. Hamre became the Center's president and chief executive officer in 2000. CSIS was founded by David M. Abshire and Admiral Arleigh Burke.

CSIS does not take specific policy positions; accordingly, all views expressed herein should be understood to be solely those of the author(s).

Cover photos: *Top*, U.S. secretary of state Hillary Rodham Clinton and Indian minister of external affairs S.M. Krishna shake hands following the signing of a U.S.-India bilateral science and technology endowment agreement in New Delhi, India, July 20, 2009; photo by State Department, <http://www.flickr.com/photos/statephotos/3742846752/>. *Left bottom*, a pile of money (\$100 dollar bills), photo by Philip Taylor PT, <http://www.flickr.com/photos/9731367@N02/7643873724/>. *Right bottom*, photo of rupees by jon smith, <http://www.flickr.com/photos/unanoslucror/4798661931/>.

© 2012 by the Center for Strategic and International Studies. All rights reserved.

ISBN 978-0-89206-756-5

Disclaimer: Matthew Stokes is a visiting fellow at the Center for Strategic and International Studies on temporary detail from the U.S. Department of State. The views presented in this report are those of the authors and do not necessarily represent the views of the U.S. Department of State or the U.S. government.

Center for Strategic and International Studies  
1800 K Street, NW, Washington, DC 20006  
Tel: (202) 887-0200  
Fax: (202) 775-3199  
Web: [www.csis.org](http://www.csis.org)



# CONTENTS

Foreword v

Acknowledgments vii

Executive Summary and Recommendations viii

**1 Introduction 1**

**2 Why Prioritize Trade with India? 4**

U.S.-India Economic Relations: Recent Bumps in the Road 5

U.S.-India Trade and Investment: Growing but Not Keeping Pace 8

**3 Background on BITs 15**

What Is a BIT? 15

Does Increased Investment Follow a BIT? 16

**4 The Case for a BIT 18**

How the United States Would Benefit from a BIT with India 18

The View from India 19

**5 Issues for Negotiation 22**

Changes to the U.S. Model BIT 22

Potential Sticking Points 23

**6 From Negotiation to Implementation 27**

The U.S. Senate: Support Is Strong—for Now 27

The Indian Government: Supportive but Shaky 28

The Indian Business Community: Still on the Fence 28

The Indian-American Community: Huge Potential for Support 29

Realistic Timelines and Quick “Wins” 30

Restarting the Trade Policy Forum 30

Pushing Ahead with State-to-State Engagement 31

Making a Public Affairs Push on Economic Issues 32

<b>7 The Long Term: Thinking Beyond the BIT</b>	<b>33</b>
An FTA Would Benefit Both Sides but Would Be Overly Ambitious for Now	33
An Agreement on IT Trade: A Realistic Option for Continued Progress	34
<b>8 Conclusion</b>	<b>36</b>
<b>Appendixes:</b>	
<b>A: List of U.S. and Indian Bilateral Investment Treaties</b>	<b>37</b>
<b>B: Senate India Caucus Letter to President Regarding the BIT</b>	<b>39</b>
<b>C: Further Reading</b>	<b>41</b>
<b>About the Authors</b>	<b>43</b>



## FOREWORD

What do American and Indian officials see as their top priority for moving the bilateral relationship forward? Both the U.S. ambassador to India, Nancy Powell, and India's ambassador to the United States, Nirupama Rao, have addressed this question—and have provided virtually identical responses.

Said Powell in New Delhi: “My top objectives as ambassador for this partnership are going to be: Bolstering bilateral trade and investment and expanding business opportunities.” Said Rao in Washington: “Let me highlight some priority areas: Firstly, the strengthening of the economic partnership.”

An opportunity now presents itself that will allow the United States and India to do precisely what the two ambassadors propose.

After a three-year interagency review, the Office of the U.S. Trade Representative (USTR) and the U.S. State Department announced in April that they had finalized a “Model BIT”—that is, bilateral investment treaty—which the United States uses as the foundation for its agreements on investor protection and to promote two-way economic partnerships with other countries. At the June U.S.-India Strategic Dialogue in Washington, Secretary of State Hillary Clinton and her counterpart, External Affairs Minister S. M. Krishna, highlighted their commitment to move forward on a high-standard BIT, calling for an “expeditious conclusion” to negotiations.

The timing is certainly right for reframing the United States’ trade and investment relations with India. Several factors are converging to push a BIT with India higher on the U.S. economic agenda.

First, India holds great promise as a potential economic partner for the United States. However, this potential is far from realized. Despite being on track to become the world’s 3rd-largest economy, India is only America’s 13th-largest trade partner. Secretary Clinton acknowledged this during her visit to India in May: “There is much more potential to unleash. We should be working toward having one of the world’s largest trading relationships, and we need to continue to reduce barriers and open our markets to greater trade and investment.”

Second, even as the volume of U.S.-India trade continues to grow—it is expected to surpass \$100 billion for the first time in 2012—the share of Indian trade that involves the United States is dropping, from almost 11 percent in 2005 to just over 7 percent in 2010. Meanwhile, the U.S. share of total foreign direct investment (FDI) in India is declining even more dramatically, from 21 percent in 2005 to just 6 percent in 2011.

Third, other countries are pushing ahead with their trade and investment ties with India. Today, India has investment agreements with 80 countries, including all the major European nations, the 10 members of the Association of Southeast Asian Nations (ASEAN), Japan, and South Korea.

The European Union is working to finalize a free trade agreement (FTA) with India in 2012. If the United States does not take concrete steps to solidify its economic partnership with India, India's focus could shift to its other trading partners.

For their part, Indian leaders agree that the time is right for a U.S.-India BIT, but many suggest that the two countries should begin to envision something even more ambitious. India's foreign secretary, Ranjan Mathai, articulated this view earlier this year in an address at CSIS: "While we should expeditiously conclude a Bilateral Investment Treaty, we must look beyond it, too. The United States is the only advanced economy in the world with which India has not concluded or is pursuing a Comprehensive Economic Partnership Agreement."

Foreign Secretary Mathai's "BIT and Beyond" diplomatic challenge resonated with the Wadhvani Chair at CSIS. Soon after his remarks, and in collaboration with the CSIS Scholl Chair in International Business, a six-month project was commenced, directed by Wadhvani Chair visiting fellow Matthew Stokes. Its purpose was to examine in detail the case for a U.S.-India BIT, the issues for negotiation, how to proceed from negotiation to implementation, and what might Mathai's "beyond" entail for the two countries.

The mission of the CSIS Wadhvani Chair is to "unlock the full potential of the U.S.-India relationship." I believe that this report, *BIT and Beyond: Advancing the U.S.-India Economic Relationship*, makes an important contribution in furtherance of that objective.

Karl F. Inderfurth  
Wadhvani Chair in U.S.-India Policy Studies, CSIS





## ACKNOWLEDGMENTS

In preparing this report, I received invaluable assistance and support from many colleagues and friends in both Washington and India who deserve recognition. First and foremost, at CSIS I thank Ambassador Karl F. Inderfurth for his enthusiastic support of the initial proposal and his insight and guidance for its execution. At CSIS, Meredith Broadbent, the Scholl Chair in International Business, and her colleague, Robbins Pancake, have been instrumental throughout the process. Matthew Goodman, the CSIS Simon Chair in Political Economy, provided valuable insights in formulating the project and reviewing this report. I would also like to thank the Economic Studies Program of the State Department's Foreign Service Institute and Alyssa Ayres and Tom Palaia in the State Department's South and Central Asia Bureau for their efforts in making this fellowship possible.

Most of this report resulted from a series of off-the-record roundtable sessions and countless individual interviews with experts in the field in both Washington and Delhi. My heartfelt thanks go to everyone who gave very generously of their time to participate in these sessions and to those who took the extra time to review initial drafts of the final report. I particularly thank Ambassador H. K. Singh and Tincy Solomon at the Indian Council for Research on International Economic Relations for their support and hospitality in hosting a roundtable event in New Delhi.

This report was a team effort, and all the staff of the Wadhwani Chair in U.S.-India Studies contributed to its completion. Particular thanks go to Niraj Patel, whose contributions as a researcher, analyst, writer, and editor were all invaluable. Nick Lombardo provided exceptional support throughout the process. Persis Khambatta and Amer Latif offered important assistance on both substance and procedures. Sameer Punyani, Jesse Sedler, and Ritika Bhasker each provided able support during their internships. Finally, I would like to thank the Wadhwani Foundation for its support of this project and its continuing dedication to advancing the U.S.-India relationship.

Matthew Stokes

*Visiting Fellow*

*Wadhwani Chair in U.S.-India Policy Studies, CSIS*



## EXECUTIVE SUMMARY AND RECOMMENDATIONS

In the U.S.-India relationship, economic engagement remains at the top of the agenda for both sides. Economic cooperation has been the primary engine of closer relations, as Indian reforms have allowed a rapid expansion of U.S.-India trade and investment flows in both directions over the last 20 years. The progress made on economic ties has set the stage for successes in other phases of the relationship, such as military cooperation. However, now that cooperation in defense, education, and strategic issues is growing stronger, some troubling trends have emerged in the economic partnership. A series of recent policy decisions in India have observers on both sides worried, and the economic foundation that was once the strength of the relationship, though still expanding, is now showing signs of weakening. Both governments recognize the key role that trade and investment play in this partnership, and the Indian government has made a promising return to its internal economic reform agenda. Both governments should now act with vision and determination to capitalize on this momentum and propel the U.S.-India economic partnership forward.

A Bilateral Investment Treaty (BIT) is the most frequently discussed option to make a significant and positive change in the U.S.-India economic relationship and at the same time to regain a larger sense of forward movement. A BIT would yield clear benefits for both sides by reassuring each country's private sector with more certainty in entering the other country's market, providing India with much-needed FDI, creating jobs on both sides, and building stronger ties between the two strategic partners. In recognition of this potential, the Joint Statement from the 2012 U.S.-India Strategic Dialogue, which was chaired by Secretary of State Clinton and External Affairs Minister Krishna, calls for the "expeditious conclusion" of a BIT. In 2013, between the U.S. elections and Indian elections, there will be a window of opportunity to conclude a treaty. The leadership in both countries will need to continue to prioritize completion of the BIT to avoid unnecessarily drawn-out negotiations that would miss this opportunity.

The BIT is a promising next step, but it cannot be the ultimate goal. Both nations should also look beyond the BIT and begin laying out a more comprehensive vision of economic cooperation. While an FTA would surely yield significant gains for both sides, negotiating a full FTA is too ambitious a step to take immediately. A series of smaller, sector-specific trade agreements is a more feasible and prudent way to continue advancing the economic relationship even though such a piecemeal approach is uncommon for the United States. Trade in IT goods and services is a sector with clear potential for gains on both sides; preliminary discussions on such an agreement should begin now.

This report, the result of a series of roundtable discussions and interviews in Washington and New Delhi, argues for the need to pursue a BIT aggressively, primarily from the U.S. perspective,

and provides recommendations for ensuring success of this effort.<sup>1</sup> In thinking about a BIT as a key part of this agenda, a number of steps should be taken beforehand, other actions taken in direct pursuit of a BIT, and plans should be made for next steps after its completion.

## Before a BIT

In the short term, there is a concern that simmering frustration with the U.S.-India relationship may weaken the current level of strong support for India in the United States. Some immediate actions are needed to stem this trend:

- *A BIT is not a short-term initiative, but negotiation itself is a positive sign.* Trade negotiations require patience, and the BIT should not be unduly rushed in order to get a “win” to change momentum. Both governments should strive to complete negotiations in 2013. While rigid deadlines are not appropriate for this kind of undertaking, setting a time frame for completion of the BIT will underscore the determination of both parties to accomplish this task in an “expeditious” manner.
- *Reinvigorate the Trade Policy Forum.* One source of frustration has been the cancellation of the Trade Policy Forum (TPF) this year and the difficulty of setting a schedule for the next meeting. Both sides are looking to regain momentum in the economic relationship, and thus they should use the TPF as it was designed, to find opportunities to work together on the trade agenda. Both governments should focus on placing a TPF meeting on the agenda, and on reaching immediate deliverable, even if modest, results. However, even without deliverables, restarting the TPF process can build trust and familiarity, furthering BIT negotiations.
- *Look to U.S. and Indian states for short-term “wins.”* There are substantive trade issues that need to be resolved through the TPF or through longer-term negotiated agreements. However, part of the current difficulty is the negative impressions caused by a series of disappointments that are important but limited in scope. The significant issues for negotiation do not lend themselves to quick solutions, but it may only take a modest positive accomplishment to move the discussion forward and provide a stepping stone for larger efforts. In this regard, some Indian states have been enthusiastic in seeking out these opportunities, and the United States should push a more aggressive agenda of state-to-state trade missions, which can produce positive results as well as serve as a stepping stone to national-level agreements. The creation of a special representative for global intergovernmental affairs at the State Department has been helpful in ensuring top-level attention and working-level prioritization of state-to-state relations. This momentum should be institutionalized in the South and Central Asia Bureau’s operations. The State Department should continue with convening or even matchmaking efforts targeted at state-level officials in both countries.

---

1. The Wadhvani Chair in India-U.S. Policy Studies at the Indian Council for Research on International Economic Relations will publish a forthcoming companion report focusing on the Indian perspective on the BIT.

## Concluding a BIT

It is critical that having set a course for a BIT, the United States does not allow negotiations to founder or drag on for an extended period, or result in an agreement that does not advance the interests of the private sector in both countries. Instead, it needs to:

- *Insist on high standards—but remain flexible.* The United States uses a Model BIT, and historically it has negotiated with smaller countries that will accept U.S. terms with only modest revisions. But the United States has never concluded a BIT with a country as large, or a democracy as dynamic, as India. While U.S. negotiators must insist on high standards, they also must be willing to treat the Model BIT as a starting point that can be modified, based on each country's objectives. A negotiating position in which the United States declares the issues India most cares about to be off the table is destined to drag on and end in a stalemate. India should also remain flexible, given that the U.S. Model BIT is seen around the world as a gold standard for such agreements, and an agreement would hold value as a signal of security to potential investors regardless of their location.
- *Use the past as a precedent to speed conclusion.* While a rushed, low-standard deal is not desirable, both countries should seek to work as quickly as possible. Eighteen months may be an ambitious time frame for concluding a BIT, but it would allow for completion of negotiations before the Indian elections in 2014. Most technical issues in the BIT's main text should be surmountable if negotiators are creative. The issues most likely to require special attention can be broken into two categories, based both on previous agreements and what is known about these negotiations to date:

—*Foundational issues: investor–state arbitration and visas.* These two issues are potential disagreements at the heart of what a BIT should cover. India will need to decide whether it can accept investor–state arbitration in a new BIT. India should recognize that a BIT without a credible enforcement mechanism will deliver no benefits, and a treaty without investor–state arbitration fails this test. The United States should engage on this issue because the Indian government may set policy against investor–state arbitration that negotiators will be hard-pressed to overcome. Whether temporary entry of business personnel is an issue appropriate for a treaty negotiation is another divide, discussed in more detail below.

—*Technical issues: preestablishment treatment, performance requirements, labor and environmental standards.* Previous treaties by both countries show that a middle ground was taken on most issues. These issues will still take hard work and creativity to resolve, but negotiators can look to recent U.S. FTAs and Indian comprehensive economic partnership agreements (CEPAs) with Japan and South Korea for approaches that have been successful in the past.

- *Engage on the issue of temporary business visas (a.k.a. General Agreement on Trade in Services Mode 4).* India's competitive advantage is in service delivery. But Indians cannot invest in service delivery in the United States if their service providers cannot get visas. The U.S. position in recent FTAs has been that it does not discuss visas in trade negotiations. Both nations should work to find a statement of principle—not unlike the labor and environmental chapters—that does not bind the United States to politically impossible promises but instead offers continued collaboration on visas.

- *Build a coalition to ensure implementation.* Previous reforms and proposed market openings—such as early attempts to allow FDI in multibrand retail—have been stymied in late stages due to political opposition. Building a coalition in support of a BIT on the Indian side will help prevent this problem. To date, Indian businesses have not been sufficiently engaged on the issue and industry groups are only beginning to develop their positions. American businesses and both the U.S. and Indian governments should engage in education and public diplomacy efforts to spread information on the benefits of a high-standard BIT for Indian consumers, Indian businesses, and the Indian economy. Waiting for negotiations to conclude before trying to win support may well be too late.
- *Engage the diaspora community on BIT specifically.* The Indian-American community was a driving force behind the U.S.-India civil nuclear agreement. A similar effort would be of great use on the BIT (and any future trade liberalization efforts). Because a BIT would benefit both countries and improve ties, there will likely be broad support in the community. Further, there is a strong presence of Indian-Americans in technology businesses and other sectors that could benefit from freer trade and investment with India. The BIT would personally benefit these individuals, or others who themselves desire to invest in India in some form.

## Beyond the BIT

In building a more strategic vision of the U.S.-India relationship, neither side should wait for the conclusion of a BIT to decide what comes next. A BIT should be viewed as one part of a process moving toward stronger ties and greater economic cooperation, not the ultimate goal. Next steps beyond the BIT should include:

- *Make trade liberalization an explicit objective.* The further both sides liberalize trade, the greater the potential job creation. The BIT contributes to meeting that objective, but both sides should think big and agree on ambitious trade and investment goals, even if they are not ready to negotiate them all immediately.
- *Consider alternatives to the FTA model.* The model for U.S. FTA negotiations should be a useful tool but not a strict limitation on the kinds of trade agreements that the United States discusses. Negotiating with India can be used as an opportunity to rethink the U.S. FTA model. The USTR must work within the limits of what Congress will approve, but it should also think creatively about negotiating agreements that can make incremental progress on opening important markets. India, as a critical strategic partner and a major economy, is worth the effort of adjusting its thinking.
- *Build toward the long-term goal through a series of smaller agreements.* Based on a common understanding of objectives, India and the United States can begin discussing sectoral agreements—what might have been portions of a comprehensive FTA—to capitalize on areas of clear mutual interest and maintain forward progress. After a BIT, negotiations should continue on expanding the range of goods covered by the World Trade Organization's (WTO's) Information Technology Agreement (ITA) model, and then expanding it to IT services, a field in which the two countries have a strong trade relationship. Subsequent sector-specific trade agreements (chemicals is another sector with strong potential) can build on previous work, thereby building the momentum and slowly evolving into a deep and comprehensive free trade system over time.

The United States and India both have thriving private sectors that are eager to seek out opportunities for investment and partnership. The key to moving forward is working together with common strategic interests in mind, resisting protectionist tendencies, and letting private-sector efforts thrive. With some modest steps to regain a positive tone, a successful effort to complete a BIT, and a clear direction for future engagement, the United States and India can continue building on the significant achievements of the last 20 years. It is undisputed that there is huge potential for the U.S.-India economic relationship. Governments on both sides should establish the conditions that will allow the economic dimension of the bilateral relationship to continue to be the driving force in unlocking this potential.

# 1

## INTRODUCTION

The United States and India are often described as natural partners due to the vast and fundamental similarities between them. The world's two largest democracies share basic commitments to personal freedoms and market economies. They share both the benefits and the challenges associated with highly diverse populations. Common interests in counterterrorism have drawn the two even closer. Security cooperation is stronger than ever, with joint military exercises taking place regularly. Efforts are under way to work together on key regional security issues, such as stability in Afghanistan. Underlying these factors is a strong and growing trade and investment relationship. Since the end of the Cold War, a relationship once rife with mistrust has come a long way in a short time. It is tempting to look at this trend and assume that a deep, purposeful partnership will naturally blossom. However, such relationships are not declared; they are built. It will take continued effort on both sides to unlock the full potential of this relationship.

Of late, however, prospects for a continuing upward trajectory for the U.S.-India economic relationship have encountered some difficulties and setbacks. India's economic growth has slowed, and discussions of serious structural problems are once again prominent.<sup>1</sup> External forces outside India's control are partially to blame for this economic slow-down, but some of the negative reports about India that have dominated business coverage have been self-inflicted. While international investors have surely been chastened by India's slowing economic growth, it is the unpredictable regulatory environment that really sets them on edge. This has had the twin effects of causing investors to be more cautious and casting a shadow on the economic partnership emerging with the United States. It should be noted that India's United Progressive Alliance government—led by Prime Minister Manmohan Singh, newly appointed Finance Minister Palaniappan Chidambaram, and Commerce and Industry Minister Anand Sharma—recently announced a set of “big bang” reforms that have been welcomed by investors and indicate a renewed focus by India's leaders to address its deteriorating economic condition. However, it is still too soon to tell whether the United Progressive Alliance and India's leaders can withstand opposition forces, proceed with implementation on the state level, and continue to build the momentum needed for additional reforms.

The U.S.-India relationship can continue making progress in areas other than trade and investment, but the commercial relationship is under close scrutiny, and is often considered the most immediate indicator that the United States is “getting something back” for its significant investment in India's rise as a major global player. However, in order to ensure a renewal of positive momentum, the United States cannot simply rely on India continuing ahead with domestic economic

---

1. GDP growth is expected to be more than 6 percent annually in coming years—still impressive, but less than what some had hoped for. Projection from “South Asia Region,” Global Economic Prospects, June 2012, South Asia Annex, World Bank, June 2012, [http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1322593305595/8287139-1339427993716/GEP12bSAR\\_RegionalAnnex.pdf](http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1322593305595/8287139-1339427993716/GEP12bSAR_RegionalAnnex.pdf).

reforms. Instead, the United States and India need to make a concerted push, together, to address their bilateral commercial relationship.

The assumption that the United States and India are “natural partners” is premised on the correct assessment of common strategic interests. However, assuming that these common interests will lead to agreement on policy issues or marquee commercial gains ignores the areas where the two nations’ values differ, which are particularly prominent in the economic sector. The United States, in its business culture and echoed in its policymaking, places a priority on innovation and an acceptance of risk. The U.S. government will, in many cases, let the market try something new rather than first demanding government examination. This can be seen in cases ranging from hydraulic fracturing in search of energy sources to financial innovation. Conversely, India, in addition to a historical desire for autonomy, places a relatively higher value on certainty and caution. This leads to attempts to regulate the foreseeable outcomes of any industrial endeavor before permitting it to proceed. This difference in government approaches means that it will require political will to reach any trade and investment agreement.

Given this situation, what are the policy options? Although a number of smaller issues can and should receive attention, in terms of a broad strategy, the menu of bilateral economic policy options can be boiled down to roughly these six:

1. Do nothing, allowing the market to sort things out under present conditions.
2. Conclude a BIT.
3. Conclude a sector-specific FTA, perhaps in IT goods and/or services.
4. Conclude a comprehensive FTA or CEPA.<sup>2</sup>
5. Continue work on the Transpacific Partnership agreement, bringing India into this framework either during initial negotiations or after their completion.
6. Work directly with India’s state governments to boost trade and investment.

It would be possible to pursue several of these options concurrently, but it would be wise to decide which set of these options is realistic and desirable in the short, medium, and long terms. For the purposes of this report, the growing consensus that the Doha Round of WTO negotiations is at best at an impasse, and at worst dead, is accepted.<sup>3</sup> When thinking specifically about India, the United States needs to think bilaterally and regionally.

Much of the focus in recent discussions of India has been about the short-term need for a so-called win to regain momentum. Some have looked to the possibility of a BIT as a possible next step that could be concluded quickly. Indeed, moving to conclude a high-standard BIT is a criti-

---

2. India has entered into CEPAs, comprehensive economic cooperation agreements, and similar agreements with several Asian partners. These agreements are like recent U.S. FTAs in that they involve chapters on trade in goods, trade in services, investment, and other related issues. They have typically been less robust than U.S. FTAs, but the term “CEPA” does not necessarily indicate a higher or lower level of rigor in the agreement.

3. “A Conversation with Six Former USTRs: Taking Stock and Assessing Priorities for the 2012 Trade Agenda,” Center for Strategic and International Studies, April 6, 2012, [http://csis.org/files/attachments/120406\\_ustr\\_transcript.pdf](http://csis.org/files/attachments/120406_ustr_transcript.pdf); Office of the U.S. Trade Representative, “Remarks by USTR Ron Kirk on the Doha Development Agenda,” December 2011, <http://www.ustr.gov/about-us/press-office/speeches/transcripts/2011/december/remarks-us-trade-representative-ron-kirk-do>.



cal step to build a stronger economic relationship, assuming that it is done correctly. However, the United States should also look elsewhere for immediate wins.

In the Joint Statement from the June 2012 Strategic Dialogue, Secretary Clinton and Minister Krishna called for the expeditious conclusion of a BIT. “Expeditious” in this case should be taken seriously, but understood realistically. Top-level leadership should continue to press for rapid negotiations, with an eye toward completion by the end of 2013.

Looking beyond the BIT, there are observers who wish to see announcement of a more ambitious project between the two countries—some calling for full-fledged FTA negotiations. Working toward an FTA is a worthy goal, but announcing an ambitious agenda and falling short threatens to energize opposition and engender disappointment in the end. Instead, both sides should build toward an FTA by identifying sectors on which they can negotiate now.

In the *short term*, the primary goal should be to capitalize on the momentum generated by the recent economic reforms that ended a stretch of economic inaction that were seen as setbacks. This can be achieved by promoting and conducting state-to-state trade missions and by renewing the TPF in order to generate positive movement in the economic realm.

In the *medium term*, a BIT is a realistic and significant goal and should be a priority. The difference between U.S. and Indian starting positions is significant, but the outstanding issues are surmountable. However, despite the time and effort needed to conclude a BIT, its passage will not carry the weight of the relationship on its own; longer-term objectives are also necessary.

In the *long term*, the United States should be laying out the vision of a U.S.-India economic partnership with minimal barriers to trade and investment. As Secretary Clinton said, “There is much more potential to unleash. We should be working toward having one of the world’s largest trading relationships, and we need to continue to reduce barriers and open our markets to greater trade and investment.” But because few expect to be able to move from an investment treaty to a comprehensive package in one leap, the United States should also begin laying the groundwork for a more modest next step, following up the BIT with an agreement specific to the IT sector.

To conclude, while the idea of a BIT may be agreed in broad principle, it is far from being a fait accompli. This report examines the differences in position between the two countries that the negotiators will need to work through. It further presents the argument that negotiating through these differences and difficulties is mutually advantageous, with an eye to the equally important hurdle of gaining the political acceptance needed to make the implementation of a BIT successful. Finally, this report briefly presents the case for moving beyond the BIT with an incremental approach to trade liberalization. These recommendations are the result of a series of roundtable discussions and interviews, in Washington and New Delhi, with experts in trade, investment, and international relations from both the Indian and U.S. governments, private industry, and academia.

# 2

## WHY PRIORITIZE TRADE WITH INDIA?

While debate continues, most observers agree that the Doha Round of WTO talks is for all practical purposes dead. Many countries, in recognition of the increasingly dim prospects of immediate gains through multilateral forums, have placed a renewed emphasis on bilateral or regional agreements. In the formal U.S. trade agenda for 2012, the vision for India remains decidedly modest.<sup>1</sup> The U.S. trade agenda balances a number of competing priorities, but India merits greater emphasis.

The major forward-looking trade initiative on the agenda is the Transpacific Partnership (TPP). The TPP is an important initiative, and one that could expand someday to include far more than the current 11 participants. However, pursuit of the TPP should not come at the expense of efforts to cultivate closer economic ties with the world's largest potential markets, such as India.

India is just the kind of trading partner that should be a priority. A major study by the Council on Foreign Relations on U.S. trade and investment policy noted a need for ambitious trade and investment negotiations with the biggest and fastest-growing markets.<sup>2</sup> India is the world's 2nd-most-populous country, among the top 10 largest economies (ranked 10th by the World Bank,<sup>3</sup> or 3rd, if ranked at purchasing power parity<sup>4</sup>), and it has growth rates that will see it moving up in the rankings. Among the emerging markets in the world, many present rich potential for U.S. businesses, but with roughly 1 billion people each, India and China are in a league of their own, four times larger than any other potential U.S. trade partner. Under the status quo, American firms are at a disadvantage compared with foreign competitors that enjoy treaty protections for investment or lower tariffs through FTAs. This sacrifices opportunities that would create jobs in both India and the United States.<sup>5</sup>

Efforts to boost trade and investment with India are not purely about the gains from trade. Strategic concerns also play a role. U.S. foreign and strategic policy is shifting to recognize both the importance of "economic statecraft" and the rising importance of Asia. Many countries in Asia are becoming global players on the strength of robust economic growth. A wise rebalancing of American economic efforts toward the Asia-Pacific region must include not just Pacific nations

---

1. Office of the U.S. Trade Representative, "President's 2012 Trade Policy Agenda," March 2012, <http://www.ustr.gov/sites/default/files/FULL%20REPORT%20-%20PRINTED%20VERSION.pdf>.

2. Andrew H. Card, Thomas A. Daschle, Edward Alden, and Matthew J. Slaughter, "U.S. Trade and Investment Policy," Council on Foreign Relations Independent Task Force, September 2011, <http://www.cfr.org/trade/us-trade-investment-policy/p25737>.

3. World Bank, World Data Bank, World Development Indicators database, "Gross Domestic Product 2011," July 9, 2012, <http://databank.worldbank.org/databank/download/GDP.pdf>.

4. Devika Banerji and Rishi Shah, "India Overtakes Japan to Become Third-Largest Economy in Purchasing Power Parity," *Economic Times*, April 19, 2012, [http://articles.economictimes.indiatimes.com/2012-04-19/news/31367838\\_1\\_ppp-terms-india-s-gdp-power-parity](http://articles.economictimes.indiatimes.com/2012-04-19/news/31367838_1_ppp-terms-india-s-gdp-power-parity).

5. David Dollar and Aart Kraay, "Trade, Growth, and Poverty," *Finance and Development*, September 2001, <http://users.nber.org/~wei/data/FinGlobal-F&D.pdf#page=78>.

but also India, as part of a broader Indo-Pacific region. A strong and prosperous India is in the U.S. national interest. The United States has already made a “strategic bet” on India—to borrow one of Secretary Clinton’s phrases—hoping for a partner to support democracy, pluralism, and economic freedom in Asia.<sup>6</sup> For India’s part, working with the United States as a partner to ensure stability in Asia makes sense, given that stability will aid India’s continued development over the coming years and decades.

Political calculations in each of the two countries have made it difficult to make the largely positive relationship more concrete. India prioritizes its continued strategic autonomy, while the United States is subject to protectionist streaks, sometimes based on labor or environmental concerns and exacerbated by electoral campaigns.<sup>7</sup> However, both countries are generally probusiness, and to some extent rely on their business communities as diplomatic front lines. Given these tendencies, one obvious way to build a stronger economic relationship is to get governments out of the way and let the private sector build bridges between the two countries. Both sides see value in these efforts, but India has concerns about maintaining its ability to regulate economic activity. As a result, the two governments will need to focus their efforts on finding ways to work through these differences in approach.

## U.S.-India Economic Relations: Recent Bumps in the Road

Since the end of the Cold War, India has grown greatly in its stature on the world stage. A series of economic reforms beginning in 1991 helped usher in India’s rise. Opening the Indian economy to investment set off a huge wave of growth, with gross domestic product (GDP) increasing 6.8 percent annually for the following 20 years and even more quickly in the last decade.<sup>8</sup> These reforms made clear that the Indian economy held a reservoir of huge potential that had been restrained by the “License Raj” and its aggressive regulatory system. However, more recently, difficult relationships in the governing coalition and strong populist pressure on the parties have hindered the reform agenda. The list of recent problems is substantial: the Government of India’s policy reversals, declining FDI in India, civil nuclear liability issues, and the TPF’s cancellation. It is useful to briefly examine each.

### The Government of India’s Policy Reversals

The drumbeat of reports of the Government of India changing policy on previous decisions has led to a growing impression that India is an unpredictable—and perhaps even “unfriendly”—environment for foreign investors. For example, in February, the Indian Supreme Court canceled 122 licenses for spectrum rights, including many purchased by foreign companies.<sup>9</sup> In another

---

6. Hillary Clinton, “America’s Pacific Century,” *Foreign Policy*, November 2011, [http://www.foreignpolicy.com/articles/2011/10/11/americas\\_pacific\\_century](http://www.foreignpolicy.com/articles/2011/10/11/americas_pacific_century).

7. Sunil Khilnani, Rajiv Kumar, Pratap Bhanu Mehta, Lieutenant General (Retired) Prakash Menon, Nandan Nilekani, Srinath Raghavan, Shyam Saran, and Siddharth Varadarajan, “Nonalignment 2.0,” Centre for Policy Research, January 30, 2012, [http://www.cprindia.org/sites/default/files/NonAlignment%202.0\\_1.pdf](http://www.cprindia.org/sites/default/files/NonAlignment%202.0_1.pdf).

8. World Bank, World Data Bank, July 9, 2012, <http://databank.worldbank.org/ddp/home.do?Step=1&id=4>.

9. Jason Overdorf, “India 2G Spectrum Case: Supreme Court Revokes 122 Telecom Licenses,” *Global Post*, February 2, 2012, <http://www.globalpost.com/dispatches/globalpost-blogs/india/>

example, on November 24, 2011,<sup>10</sup> the government announced a plan to allow FDI in multibrand retail.<sup>11</sup> It then retracted that announcement a few days later after one party threatened to leave the coalition if the reform proceeded, which would have brought down the government. Recently, in attempts to buoy rapidly deteriorating macroeconomic conditions, the central government announced “big bang” reforms that once again allowed FDI in multibrand retail.<sup>12</sup> While this is a welcome sign and a step in the right direction, the reforms have not yet been implemented. On March 16, 2012,<sup>13</sup> the government announced a new budget that attempted to shrink the fiscal deficit through a number of measures, including one to retroactively tax overseas deals that involved assets in India.<sup>14</sup> Under this proposal, the Vodafone group would have to pay capital gains tax of \$2.2 billion for its 2007 acquisition of Hutchison Essar. Foreign investors are still living under the fear of additional retrospective impositions of taxes.<sup>15</sup>

## Declining FDI in India

Whether related to these policies or not, according to Government of India figures, inflows of FDI peaked in 2008 after a decade of consistent increases, and have dropped for the subsequent two years.<sup>16</sup> While this trend may be related to global trends as investors flee risk, the Government of India appears to be serious about examining what it can do to stem it. The Indian Department of Industrial Policy and Promotion circulated a discussion paper seeking input on whether current limitations on FDI should be discontinued.<sup>17</sup> Prime Minister Singh announced a decision to permit states to ease some of these limitations, allowing up to 49 percent foreign ownership in Indian private airlines, increasing FDI limits in broadcast-carriage services to 74 percent, permitting up to 49 percent foreign investment in power trading exchanges, and up to 51 percent FDI in multibrand retail.<sup>18</sup> These steps will help to slow diminishing FDI inflows to India, however many uncertainties remain, such as whether these reforms could be retracted (as has happened before) or if the states will even choose to ease the limitations.

---

india-2g-spectrum-revokes-licenses.

10. Sujay Mehdudia, “Business Chambers Welcome 51 Per Cent FDI in Multi-Brand Retail,” *The Hindu*, November 25, 2011, <http://www.thehindu.com/business/Economy/article2658262.ece>.

11. Indian regulation distinguishes between “single-brand retail” enterprises that sell only products they manufacture—e.g., Apple Stores or clothes retailers like the Gap—and “multibrand retail,” which sells products bought from a number of suppliers, such as grocery stores or Walmart.

12. “FDI: ‘Big Bang’ Reforms, Says Corporate America,” *Hindu Business Line*, September 15, 2012, [http://www.thehindubusinessline.com/industry-and-economy/economy/article3900474.ece?homepage=true&ref=wl\\_home](http://www.thehindubusinessline.com/industry-and-economy/economy/article3900474.ece?homepage=true&ref=wl_home).

13. Vikas Bajaj, “India Proposes Higher Taxes and Slower Spending,” *New York Times*, March 16, 2012, [http://www.nytimes.com/2012/03/17/business/global/india-to-tackle-deficit-but-no-fix-offered-for-slowng-economy.html?\\_r=2](http://www.nytimes.com/2012/03/17/business/global/india-to-tackle-deficit-but-no-fix-offered-for-slowng-economy.html?_r=2).

14. Neha Thirani and Malavika Vyawahre, “Hidden Bombs in India’s Budget for Foreign Investors,” *New York Times: India Ink Blog*, March 20, 2012, <http://india.blogs.nytimes.com/2012/03/20/hidden-bombs-in-indias-budget-for-foreign-investors/>.

15. Rajas Kelkar, “The Indian Telecom Saga: Dream Turned Sour,” *NDTV*, July 20, 2012, <http://profit.ndtv.com/News/Article/the-indian-telecom-saga-dream-turned-sour-308142>.

16. Department of Industrial Policy and Promotion, Indian Government, “FDI Policy-Rationale and Relevance of Caps,” [http://dipp.nic.in/english/Discuss\\_paper/DiscussionPaper\\_relevance\\_23June2011.pdf](http://dipp.nic.in/english/Discuss_paper/DiscussionPaper_relevance_23June2011.pdf).

17. Ibid.

18. “FDI: ‘Big Bang’ Reforms.”

## Civil Nuclear Liability Issues

A major breakthrough in U.S.-India relations was the announcement of a deal on civilian nuclear power, initiated in July 2005 and finalized in 2008.<sup>19</sup> India separated its military and civilian nuclear programs, and the United States worked to grant India a waiver from the Nuclear Suppliers Group to allow full engagement in nuclear materials trade, despite the fact that India is not a signatory to the Nuclear Non-Proliferation Treaty. This was a major concession on the American side. However, as of today, India has still not limited the liability of foreign companies working in the field, essentially preventing American firms from entering the market.<sup>20</sup> Thus, what had seemed like a milestone in U.S.-India relations has become a source of frustration and disappointment for American policymakers and businesses.

## The TPF's Cancellation

The U.S.-India TPF is intended to be the primary mechanism for working through trade-related issues. It is chaired by the U.S. Trade Representative and the Indian Minister of Commerce, and includes working groups on agriculture, innovation, investment, services, and tariffs / nontariff barriers to trade. The TPF meeting scheduled for early 2012 was canceled.<sup>21</sup> As of the writing of this report, it has not been rescheduled, and some are questioning if it will start up again. It is not clear that the TPF was delivering as much as it could have when it was in progress—but canceling it entirely certainly does not contribute to a positive environment for future collaboration.

The two governments need to act to regain positive momentum. One thing both governments agree on, at least in their public statements, is the potential for a BIT. Negotiations began well before the current slowdown, during the Bush administration. When President Obama took office, he announced an internal review of the Model BIT, the language U.S. negotiators use as a starting point for negotiations. The review lasted three years, during which time U.S.-India negotiations slowed substantially. In April 2012, the administration announced the new Model BIT language, which included important changes, most of which will place the United States' starting point for negotiations further away from India's Model BIT.<sup>22</sup>

Despite the certainty of challenging negotiations, India and the United States have committed to a serious attempt at concluding a BIT. The most prominent demonstration was in June 2012, when the U.S.-India Strategic Dialogue took place in Washington. As mentioned above, the culminating Joint Declaration from the Strategic Dialogue called for the “expeditious conclusion” of a BIT.<sup>23</sup> President Obama has reinforced this commitment, noting that “with some 1.5 billion consumers between us, there's so much more we can build as partners. So we continue to work

---

19. U.S. Department of State, “U.S.-India: Civil Nuclear Cooperation,” <http://www.state.gov/p/sca/c17361.htm>.

20. Geoffrey Pyatt, “Taking Stock of the U.S.-India Nuclear Deal,” U.S. Department of State, Mumbai, September 20, 2011, <http://www.state.gov/p/sca/rls/rmks/2011/174883.htm>.

21. Office of the U.S. Trade Representative, “Postponement of U.S.-India Trade Policy Forum (TPF),” January 2012. <http://www.ustr.gov/about-us/press-office/press-releases/2012/january/postponement-us-india-trade-policy-forum-tpf>.

22. U.S. Department of State, “2012 U.S. Model Bilateral Investment Treaty,” <http://www.state.gov/documents/organization/188371.pdf>.

23. U.S. Department of State and Indian Ministry of External Affairs, “Joint Statement on the Third U.S.-India Strategic Dialogue,” June 13, 2012, <http://www.state.gov/r/pa/prs/ps/2012/06/192267.htm>.

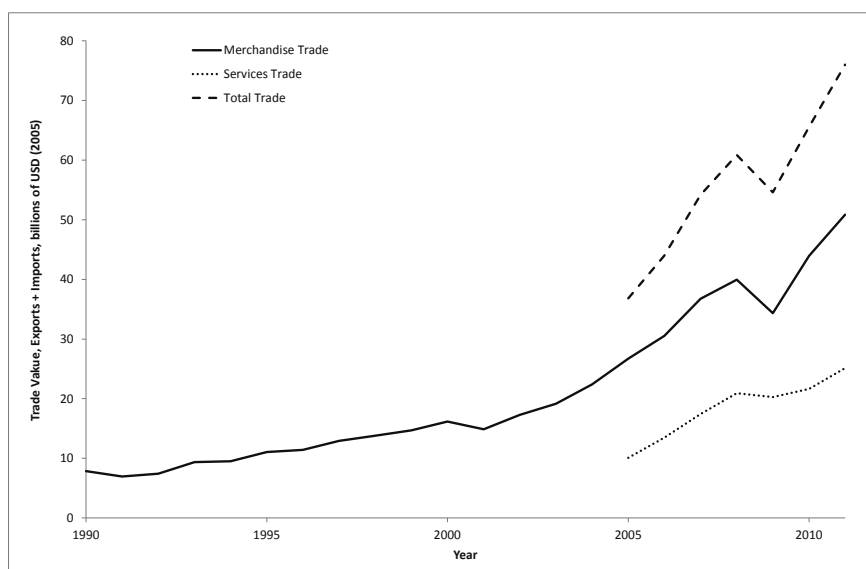
to make it easier for our companies to do business together, including working toward a bilateral investment treaty.”<sup>24</sup>

## U.S.-India Trade and Investment: Growing but Not Keeping Pace

### U.S.-India Trade

Bilateral trade between the United States and India has grown considerably since India’s economic reforms of the early 1990s. Total bilateral trade is expected to exceed \$100 billion in 2012. This is true for trade in both goods and in services, as highlighted by figure 1, which shows growth in bilateral trade in constant 2005 dollars. In 1990 the two nations exchanged approximately \$7.9 billion in goods, growing to \$50.9 billion by 2011. Similarly, total trade in services was valued at \$2.5 billion in 1994, growing to \$25.1 billion in 2011.<sup>25</sup> This trade has not been balanced; the United States has run a trade deficit with India, which topped \$12.9 billion in 2011 (figure 2). Over the last two decades, bilateral trade in both goods and services has grown not just in absolute terms but also as a share of GDP in both countries.

**Figure 1. U.S.-India Trade Value Is Expanding**

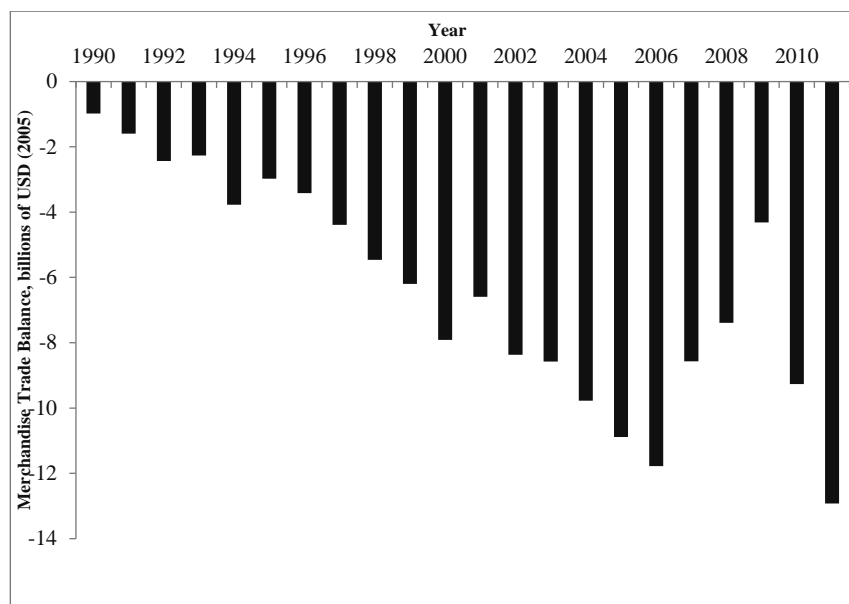


Sources: Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable>; Office of the USTR, <http://www.ustr.gov/countries-regions/south-central-asia/india>.

24. Lalit K. Jha, interview with President Barack Obama, “We Believe in the Promise of India,” *Outlook India*, July 30, 2012.

25. Data on trade in services are notoriously difficult. Despite some problems with these data, including possibly significant underreporting, they are likely to show general trends accurately.

**Figure 2. The United States Runs a Trade Deficit with India**

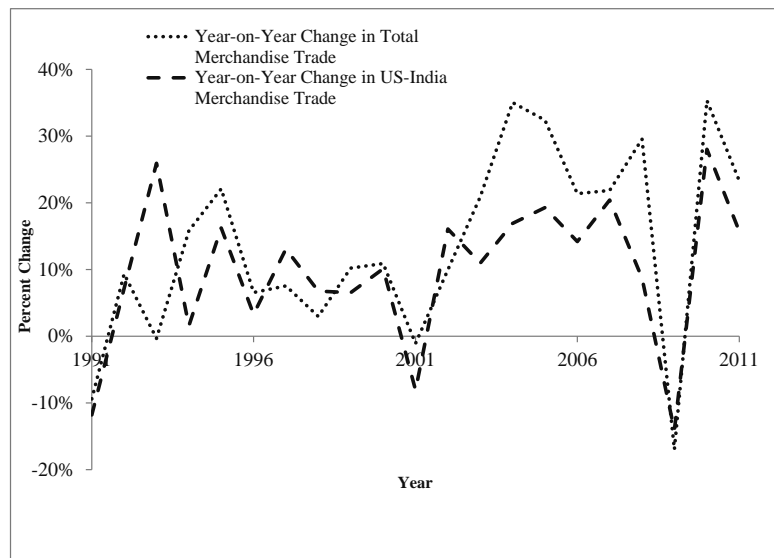


Source: Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable>.

On the surface, brisk growth in U.S.-India trade as a share of each country's GDP would suggest a deepening of trade ties. This is true in absolute terms, but when looking at the extent to which India considers the United States an important trading partner, relative terms may be more important—and in relative terms, the United States is losing ground. Since 1994, India's total two-way trade has grown from \$82.5 billion to \$906 billion in 2011, or roughly 15.1 percent annual growth. However, during the same period, total trade between the United States and India grew at only 11.5 percent. In other words, India's growth in total trade with the world is outpacing the growth in U.S.-India trade. From 1991 to 2011, there were only five years where the rate of growth in U.S.-India trade surpassed India's overall growth in trade.

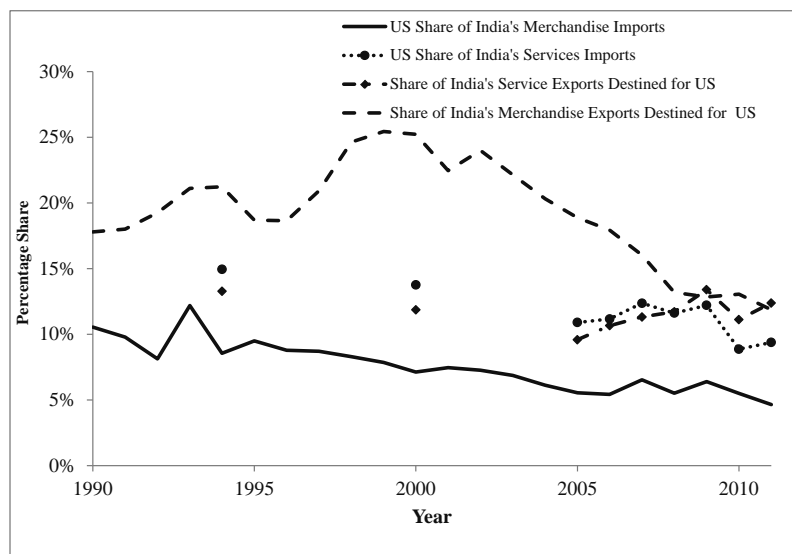
The U.S. share of global trade with India is falling, as India is increasingly diversifying its trade partner portfolio. In 1990, American merchandise made up 10.5 percent of all Indian imports. In 2011, this number had fallen to 4.7 percent (figure 4). Similarly, in services, in 1994, 14.9 percent of all Indian service imports were American. By 2011, this figure had fallen to 9.4 percent. Downward trends are also evident in the share of Indian merchandise exports destined for the United States. Only India's share of service exports destined for the United States has remained constant, at about 12 percent.

**Figure 3: India's Trade Growth**



Sources: World Trade Organization, Statistics Database, <http://stat.wto.org/Home/WSDBHome.aspx?Language=E>, analysis by CSIS; Office of the USTR, <http://www.ustr.gov/countries-regions/south-central-asia/india>; Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable>.

**Figure 4. The U.S. Share of India's Trade**

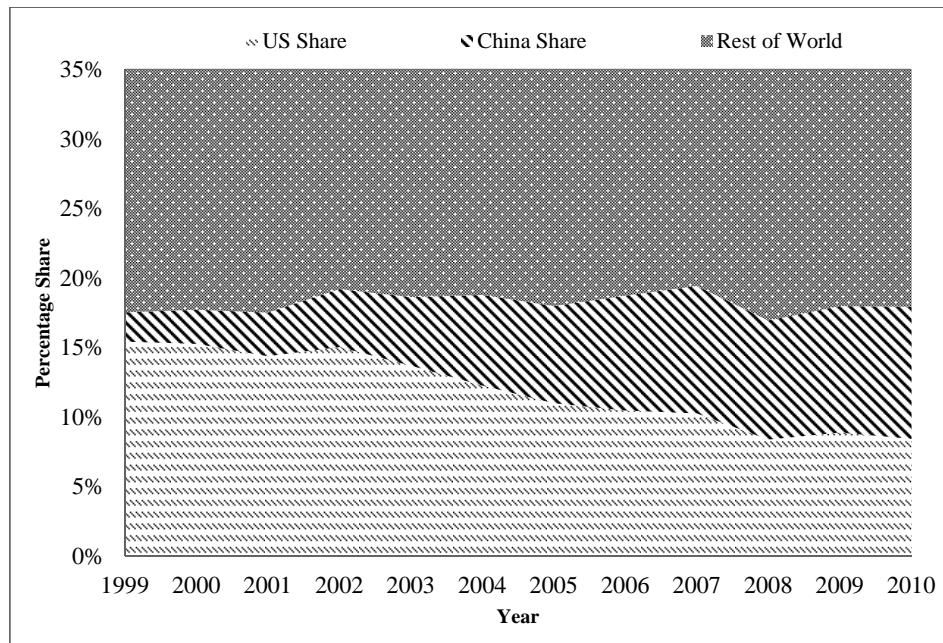


Sources: WTO, Statistics Database, <http://stat.wto.org/Home/WSDBHome.aspx?Language=E>, analysis by CSIS; Office of the USTR, <http://www.ustr.gov/countries-regions/south-central-asia/india>; Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable>.



In this relativistic analysis, if the United States is losing share, another country must be gaining. It should not come as a surprise that China is the primary gainer. In fact, China's gains in the share of Indian foreign trade have roughly equaled the United States' loss in share over the last 20 years (figure 5). By 2010, China's share of total merchandise trade with India was roughly equal to that of the United States. Just over a decade earlier, the U.S. share was seven times larger.

**Figure 5. China's Share of Indian Trade Grows as the U.S. Share Falls**



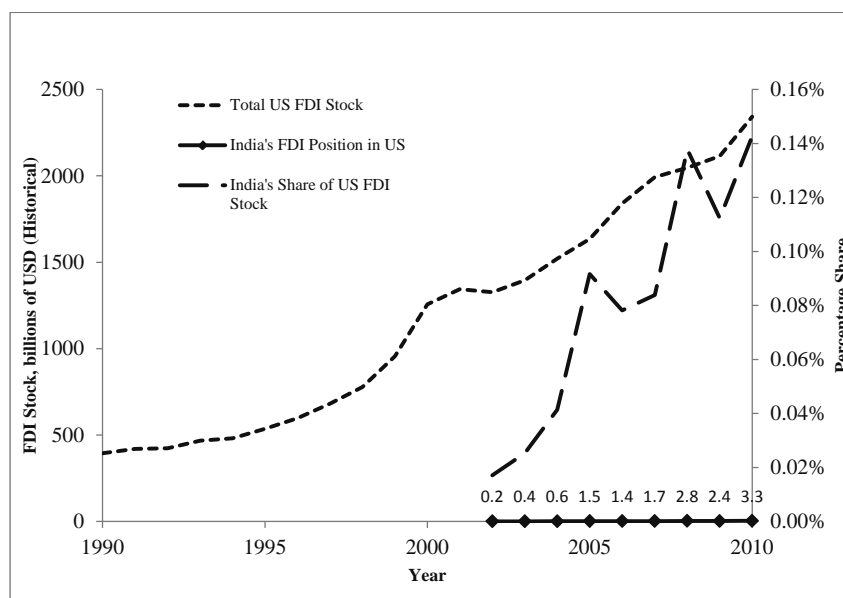
Sources: WTO, Statistics Database, <http://stat.wto.org/Home/WSDBHome.aspx?Language=E>, analysis by CSIS; Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable/>; Ministry of Commerce and Industry, Government of India, Export-Import Databank 6.0, <http://commerce.nic.in/eidb/Default.asp> analysis by CSIS.

Overall, we see India becoming much more open to the global economy, with trade growing as a share of GDP. The United States is clearly gaining from this increased trade. But whereas the United States was once a major component of a small trade relationship, it now has a shrinking slice of a rapidly expanding pie. Given global trends, it is not surprising that India is also trading with other neighbors. Because trade is not a zero-sum game, the gains of rapidly expanding economies like China are not necessarily a negative for the United States. That said, with ambitious goals for boosting exports, the United States should have a clearly defined trade strategy for a country as large and dynamic as India. Furthermore, to the extent that the United States hopes to use economic ties as an anchor for a broader bilateral relationship, it is falling behind.

## Foreign Direct Investment

The United States and India have both experienced increases in their stock of FDI since 1990. In 1990, the United States had a total of \$395 billion in FDI. By 2010, this figure had grown—roughly, linearly through three business cycles—to \$2.3 trillion. Similarly, India experienced growth in its investment position. In 1990, its total FDI amounted to \$1.7 billion, and then stagnated for a few years and thereafter quickly accelerated after 1996 as economic liberalizations took root, ultimately growing to a total FDI stock of \$205 billion in 2010 (figures 6 and 7).

**Figure 6. India Is a Small but Growing Source of U.S. FDI**



Source: Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable/>; analysis by CSIS.

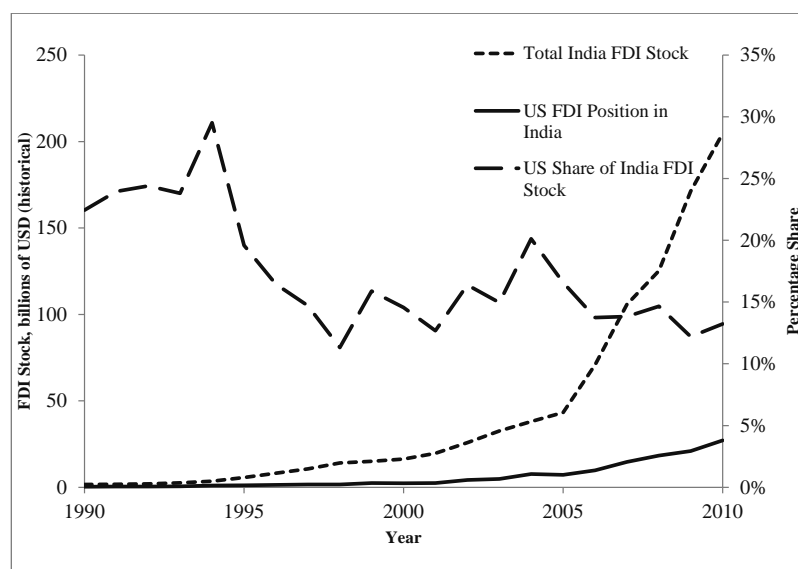
Looking at the share of FDI stock belonging to the partner country (figures 6 and 7), we see opposing trends in shares of one another's FDI stock. The United States' share of FDI in India has shrunk from 22.5 percent in 1990, peaking shortly after the 1991 liberalization reforms, to 29.5 percent in 1994, and dropping to 12 percent by 2010. In comparison, in 2010, the U.S. FDI position abroad amounted to 14.8 percent of total global FDI stock.<sup>26</sup> Relative to the rest of the world, the United States is underinvested in India.

India's share of FDI stock in the United States grew from 0.02 percent in 2002 to 0.14 percent in 2010. While India's FDI share in the United States is small, the proportion of Indian ownership of U.S. FDI stock has grown sevenfold in approximately eight years. The total stock of Indian

26. United Nations Conference on Trade and Development, UNCTADSTAT Database, "Foreign Direct Investment," <http://unctad.org/en/pages/Statistics.aspx>.

investment in the United States has grown from \$230 million to \$3.3 billion.<sup>27</sup> During this time, Indian technology companies have created 280,000 direct and indirect jobs in the United States.<sup>28</sup>

**Figure 7. The U.S. Share of Indian FDI Is Shrinking**



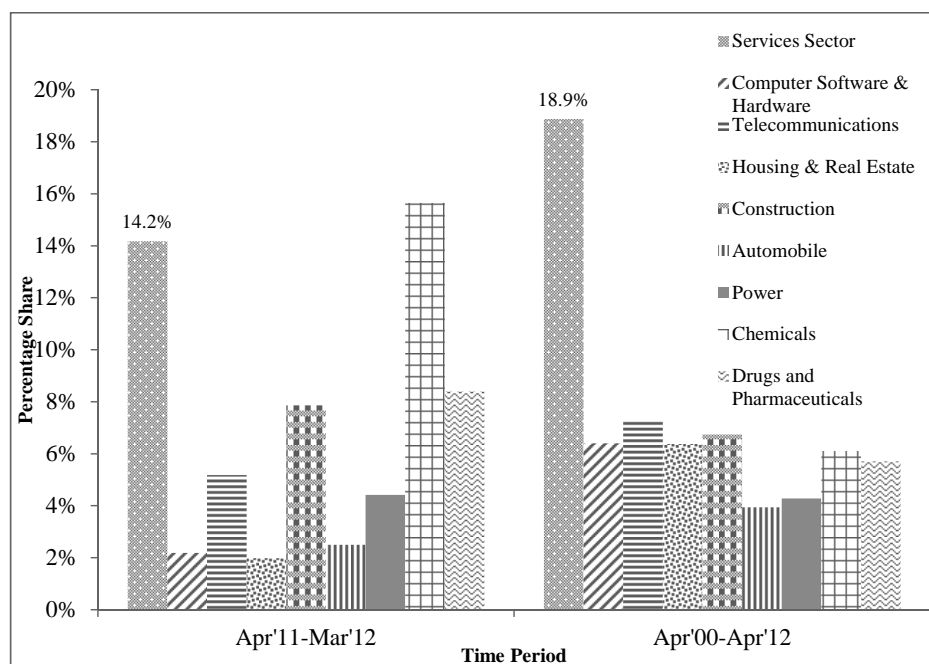
Sources: Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable/>, analysis by CSIS; United Nations, UNCTADStat, [http://unctadstat.unctad.org/ReportFolders/reportFolders.aspx?sCS\\_referer=&sCS\\_ChosenLang=en](http://unctadstat.unctad.org/ReportFolders/reportFolders.aspx?sCS_referer=&sCS_ChosenLang=en), analysis by CSIS.

The service sector in India is the largest recipient of FDI within the Indian economy (figure 8). Cumulatively, since April 2000 the service sector possesses 18.9 percent of all the FDI stock in India. This is followed by telecommunications, at 7.3 percent. Correspondingly, the composition of total U.S.-India bilateral trade is gradually shifting away from goods and toward services (figure 9). In 1994, services accounted for 20.8 percent of total trade (imports and exports) between the United States and India. By 2009, this composition had shifted to 37.1 percent services. Since 2009, this trend has reversed. This divergence back toward a goods-heavy composition could be related to the decrease in the services sector's share of FDI in India (figure 8). In 2008, 23.2 percent of FDI in India could be found in the services sector, dropping to 14.2 percent in 2011. Securing a BIT could help to reenergize U.S. FDI flows into the Indian service sector, thereby helping to grow the sector in India (providing positive domestic economic benefit for India) as well as help to create a more balanced bilateral trade composition with the United States that is not as reliant on merchandise trade.

27. Bureau of Economic Analysis, U.S. Department of Commerce, "International Data: Direct Investment and MNC," <http://www.bea.gov/itable/itable.cfm?ReqID=2&step=1>.

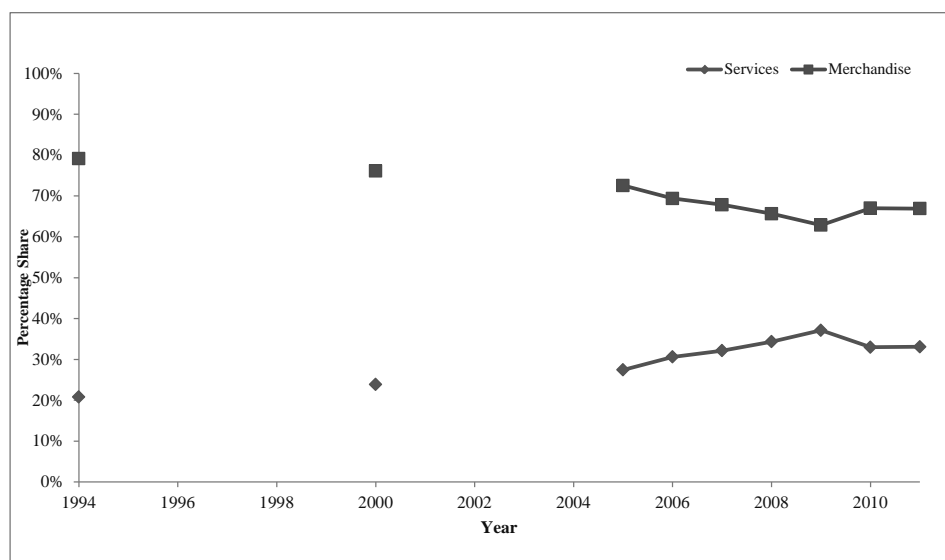
28. NASSCOM, "Indias Tech Industry in the U.S.," March 2012, <http://www.nasscom.org/india%E2%80%99s-tech-industry-us>.

**Figure 8. Services Is the Biggest Sector for FDI in India**



Source: Government of India, Department of Industrial Policy and Promotion, [http://dipp.nic.in/English/Publications/FDI\\_Statistics/FDI\\_Statistics.aspx](http://dipp.nic.in/English/Publications/FDI_Statistics/FDI_Statistics.aspx), May 2012 Report, analysis by CSIS.

**Figure 9. Trade Is Shifting from Goods to Services**



Sources: WTO, Statistics Database, <http://stat.wto.org/Home/WSDBHome.aspx?Language=E>, analysis by CSIS; Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable/>, analysis by CSIS.

# 3

## BACKGROUND ON BITS

### What Is a BIT?

Bilateral investment treaties have proliferated greatly since the first BIT was signed in 1959 between Germany and Pakistan. Unlike global trade and monetary systems, there are no multinational institutions that meaningfully govern the flow of FDI between countries, so governments have relied on BITs. These treaties establish the norms, terms, and conditions for private investment by nationals and firms of one country in the jurisdiction of another country. India often uses the term “Bilateral Investment Promotion and Protection Agreement,” but the provisions are essentially the same. The core provisions are:

1. Treatment equal to that given to home-country investors (“national treatment”) or other countries’ investors (“MFN [most-favored-nation] treatment”).
2. Treatment meeting minimum international standards (“fair and equitable treatment”).
3. Limits on expropriation.
4. Binding international arbitration between investors and states.
5. Market-rate transfers of funds in and out of the country.
6. Choice of top management, regardless of nationality.

This set of guarantees is intended to increase the flow of investment, and particularly FDI, by mitigating some of the risks of operating outside one’s home country. Because these risks are greatest in countries where existing institutions are least robust, most BITs have been between one mature economy and one emerging market or developing economy.

India has signed 82 BITs, of which 72 are in force.<sup>1</sup> India already has a BIT (or an investment protection chapter in a more comprehensive agreement) with most industrial nations and nearly all its major trading partners (see appendix A for a list of BITs that have been signed). The only significant trading partners with which India does not have a BIT are China and the United States. Mauritius and Singapore have become major sources of investment, as investors from larger industrial countries funnel investments through these two countries for tax advantages—and in the case of the United States, to be able to claim BIT protections.<sup>2</sup> In addition to stand-alone BITs, India has or is negotiating FTAs or CEPAs with most of its major trading partners. These include completed CEPAs with Japan, South Korea, and ASEAN, and ongoing negotiations about an FTA with the EU.

---

1. Ministry of Finance, Government of India, “Bilateral Investment Promotion and Protection Agreements (BIPA),” July 2012, [http://finmin.nic.in/bipa/bipa\\_index.asp](http://finmin.nic.in/bipa/bipa_index.asp).

2. Ashwath Rau and Pallabi Ghosal. “Entering the Tiger’s Den: Foreign Investment in India through Mauritius or Singapore,” *Law Gazette*, February 2012, <http://www.lawgazette.com.sg/2012-02/330.htm>.

The United States has never been at the vanguard of concluding BITs. The United States waited well after many European competitors to start working on investment treaties, and since that time, America has signed only 46 BITs, mostly with relatively small countries. In comparison, Germany has signed 139 BITs, and China has signed 131.<sup>3</sup> The United States has signed only two BITs in the last decade despite the international resurgence of bilateral treaties.

The United States has concluded a relatively low number of BITs in part because it rightly insists on high standards for all its investment treaties. Recent BITs signed by the United States include a number of provisions absent in many other countries' treaties, notably provisions on labor and environmental protections, and elimination of performance requirements such as local content requirements or export quotas. By demanding a more complete level of investment protection, the United States eliminates a number of potential treaty partners whose strategy is to get something on paper with minimal legal protection for investment.

## Does Increased Investment Follow a BIT?

In essence, a BIT is intended to give host governments an edge in attracting foreign capital given that it ensures foreign investors that the host government has promised to treat FDI "fairly" and within the rules prescribed in the treaty, offering a level playing field for foreign and domestic firms. Through these signals, the end goal of a BIT is to increase bilateral FDI flows.<sup>4</sup> In theory, a BIT may function as a substitute for high-quality domestic institutions, thereby raising confidence. Some studies even suggest that BITs can help to strengthen weak domestic institutions, including the protection of property rights.<sup>5</sup>

Does the half century's worth of experience with BITs verify these benefits? Yes, but with qualifiers. The evidence is strong that countries with a wide network of BITs generally experience increases in flow of FDI with partner countries. Looking at the period 1960–2000, a positive correlation is evident between the total BITs in effect and the average inflow of FDI to developing countries as a percentage of GDP.<sup>6</sup> In 2011, the Institute of European Studies found that EU member country FDI outflows increased by 35 percent to developing partner countries after the signing of a BIT. The study also concludes that the BITs between developing countries and the member countries of both the Organization for Economic Cooperation and Development and the EU have a statistically significant positive impact on FDI outflow.<sup>7</sup> However, the total stock of BITs is subject to diminishing returns. With every additional BIT in effect in the global market, the returns to one additional BIT measured in FDI flow decreases.<sup>8</sup>

---

3. "Country-Specific Lists of Bilateral Investment Treaties," United Nations Conference on Trade and Development, June 1, 2012, <http://unctad.org/en/Pages/DIAE/International%20Investment%20Agreements%20%28IIA%29/Country-specific-Lists-of-BITs.aspx?Do=1,50>.

4. Zachary Elkins, Andrew T. Guzman, and Beth Simmons, "Competing for Capital: The Diffusion of BITs, 1960–2000," *International Organization* 60, no. 4 (October 2006): 811–846.

5. Eric Neumayer and Laura Spess, "Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?" *World Development* 33, no. 10 (October 2005): 1567–1585.

6. Elkins, Guzman, and Simmons, "Competing for Capital."

7. Selen Sarisoy Guerin, "Do Bilateral Investment Treaties Encourage FDI Outflows?" Institute of European Studies, February 2011.

8. Chang Hoon Oh and Michele U. Fratianni, "Do Additional Bilateral Investment Treaties Boost Foreign Direct Investments?" Money and Finance Research Group, Università Politecnica Marche, May 2010.

It is important to note that the ratification of a BIT, not the signing, is the key milestone. Simply signing a BIT can signal to financial actors reduced costs for investment in a host developing country; however, empirical analysis has found that the effect on FDI is positive but not statistically significant. The actual ratification (hence implementation) of a BIT is what exerts a strong, positive, and statistically significant effect, increasing FDI stocks from 15 to 30 percent.<sup>9</sup>

Evidence is mixed regarding the effect of a BIT on a host developing country's institutional quality and protection of property rights. At its core, a BIT serves as an assurance to investors that their property rights will be protected and that credible dispute settlement mechanisms will be in place if their rights are violated. However, a 2003 study by the World Bank indicates that BITs instead serve more as complements for good institutional quality and local property rights rather than as substitutes. If a developing country has little history of established institutions and a poor record of protecting property rights, then the signing of a BIT will not magically address these deficiencies. Admittedly, other options for affecting this kind of change are limited, but a host country must meet a "minimum" for a BIT to truly take root, positively affect institutions, and, most important, promote FDI inflows.<sup>10</sup>

Taking this thinking to its logical conclusion, some argue that BITs have little or no impact on the perception that foreign companies and nationals have of a host country's investment climate, and therefore a minimal effect on FDI inflows. For a BIT to be effective, policymakers in both countries must take into consideration the economic, geographic, and institutional characteristics of their respective countries.<sup>11</sup> If a BIT is narrow, applying to only small sectors, and has lax rules regarding dispute settlement, then it will have little effect on investors' perceptions and FDI inflows.<sup>12</sup>

In summary, the literature would support the call for a U.S.-India BIT. Both countries fulfill the necessary prerequisites for a successful and effective BIT. Both nations have established institutions with a clear track record of protecting property rights (notwithstanding that India's recent actions have shaken this confidence somewhat). India has many challenges, such as corruption and an overburdened court system, that a BIT will not fix, but the basic institutions are in place. FDI between the two countries is generally increasing in both directions, indicating that economic fundamentals are in line, and treaty protections could provide a boost.

---

9. Peter Egger and Michael Pfaffermayr, "The Impact of Bilateral Investment Treaties on Foreign Direct Investment," *Journal of Comparative Economics* 32, no. 4 (December 2004): 788–804.

10. Mary Hallward-Driemeier, "Do Bilateral Investment Treaties Attract FDI? Only a Bit . . . and They Could Bite," World Bank Policy Research Working Paper 3121 (Washington, D.C.: World Bank, 2003).

11. Oh and Fratianni, "Do Additional Bilateral Investment Treaties Boost Foreign Direct Investments?"

12. Jason Yackee, "Do Bilateral Investment Treaties Promote Foreign Direct Investment? Some Hints from Alternative Evidence," University of Wisconsin Legal Studies, Research Paper 1114, March 2010.

# 4

## THE CASE FOR A BIT

### How the United States Would Benefit from a BIT with India

The United States is missing out on opportunities in India. Most competitors already have investment treaties, and thus American businesses are at a relative disadvantage and the United States loses out on the jobs that those business ventures could create at home. That does not mean American companies will not invest, but in a competitive business world any edge can have some impact on who will gain footholds early in the growing Indian market.

Getting in now is important for American firms because of early mover advantages. While others are already ahead of the United States, there is still time to establish a market position as the Indian middle class expands. Much FDI in India at this point is based on a desire to sell consumer goods, provide services to Indians, or to invest in infrastructure projects gaining a return from future Indian economic activity. Building connections and consumption patterns early, and participating in standards setting for these industries, will be critical for future success. It is true that some portion of investment in India involves outsourcing job functions that once took place in the United States. However, international trade is becoming increasingly intracompany—for example, shipping components of a product from one phase of production in one country to the next phase in a different country. As this process happens, free trade becomes increasingly likely to create jobs in both countries, rather than simply moving them from one country to another.<sup>1</sup>

Three sectors in particular stand out as potential winners:

- *Infrastructure*, broadly defined. To great notice, India has declared a need for \$1 trillion of investment in infrastructure over five years, of which half would need to come from the private sector.<sup>2</sup> The recent massive power blackouts across northern and eastern India were not a surprise to those already familiar with India's infrastructure challenges, and highlighted to the world India's infrastructure needs. Models for public-private partnerships will still need to be smoothed out, but a BIT will provide additional incentives for firms considering major investments in India and to work with the Indian government on other challenges in the sector.
- *Business services*. While the greatest government desire is for investment in infrastructure, the sector that currently attracts the most FDI in India is services. American firms are world leaders in these industries, many of them already have a strong presence in India, and the protections of a BIT should only strengthen these ties.

---

1. Scott Thurm, "U.S. Firms Add Jobs, but Mostly Overseas," *Wall Street Journal*, April 27, 2012.

2. Mukesh Jagota and Anant Vijay Kala, "India's PM Unveils Infrastructure Investment Plan Source," *Wall Street Journal*, June 6, 2012.



- *Retail.* Assuming a treaty that includes national treatment during the preestablishment phase of investment (still a point of contention), retailers that have been faced with uncertainty regarding limits on FDI in the retail sector could suddenly be freed to enter the market. While the recently announced reform to FDI limits is a welcome step, a treaty prohibition on such limits would be a much stronger guarantee of protection. This would be a winner for American multibrand retailers, and for the Indian farmers who would gain access to the sophisticated cold storage and supply chain advances that a Walmart could offer. Concerns that allowing Walmart (or Tesco or Carrefour) into India would put small shopkeepers out of business should not be dismissed out of hand, but the net gain for Indian consumers and farmers would be great, and associated investments in cold storage would drastically reduce the amount of food lost to spoilage within India.<sup>3</sup> That said, if India makes the political calculation that it must protect small shopkeepers by excluding multibrand retail from the deal, that ought not be a deal breaker for the United States in pursuing a BIT.

Perhaps of equal value is the process of negotiation itself. BIT negotiations should be directed and purposeful, providing a common goal for the two countries to work toward together. Demonstrating the ability of the two countries to agree on something controversial will provide momentum for future efforts in any number of fields. Each project where the two countries successfully collaborate—from the TPF to BIT negotiations and beyond—can be a step forward in trust.

## The View from India

From the Indian perspective, the basic protections of a BIT will also be valuable. Indian FDI in the United States is growing quickly. While the United States has a more open regulatory environment and a strong court system, binding legal protection for Indian investments still has value—particularly with respect to U.S. state government actions, which have been the subject of a number of arbitration cases under previous American FTAs.<sup>4</sup>

In addition, India needs to take steps to improve its investment climate and attract FDI. India faces both a serious budget deficit and a serious current account deficit, which it must continue to finance through inflows of capital. However, statistics maintained by India's Department of Industrial Policy and Promotion show FDI inflows falling from their 2008 peak (figure 10).<sup>5</sup>

While it may be early to declare a crisis based on two years' decline, the government is considering a number of measures to bolster investor confidence—such as easing caps on FDI in some sectors, or revisiting decisions that have led to investors filing claims under other BITs. Each of these would be positive, though narrow. Furthermore, the infrastructure needs that India faces are insurmountable without foreign investment. Finally, the kinds of industries in which U.S. firms would invest if given stronger protections would likely be more advanced, with higher-end jobs than the average current FDI investment. Boosting investment in services, for example, would

---

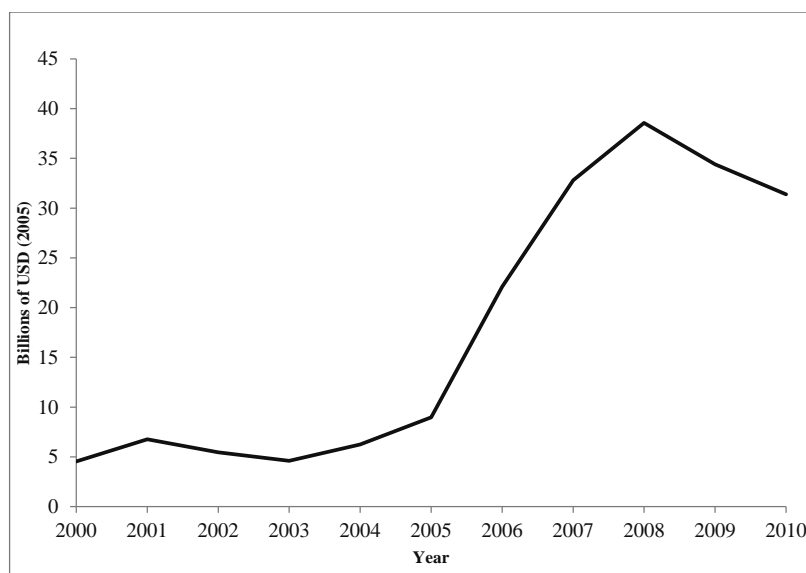
3. Associated Press, "Fruit and vegetables rot as hunger stalks India," *Dawn.com World*, August 30, 2011, <http://dawn.com/2011/08/30/fruit-and-vegetables-rot-as-hunger-stalks-india/>.

4. Public Citizen, "Table of Foreign Investor-State Cases and Claims under NAFTA, CAFTA, and Peru FTA," October 2011, [http://www.citizen.org/documents/Ch11cases\\_chart.pdf](http://www.citizen.org/documents/Ch11cases_chart.pdf).

5. Statistics from the DIPP are based on figures from the Reserve Bank of India. Because of differences in reporting periods and definitions, it is difficult to reconcile these figures with data from the World Bank or the International Monetary Fund.

bring high-end jobs and significant spillover effects in technology that would help lift the overall Indian economy.

**Figure 10. Indian FDI Inflows Have Fallen from Their 2008 Peak**



Sources: Department of Industrial Policy & Promotion, Government of India, [http://dipp.nic.in/English/Publications/FDI\\_Statistics/FDI\\_Statistics.aspx](http://dipp.nic.in/English/Publications/FDI_Statistics/FDI_Statistics.aspx), analysis by CSIS; Bureau of Economic Analysis, U.S. Department of Labor, <http://www.bea.gov/itable/> (date accessed, July 31, 2012), analysis by CSIS.

The signaling value of the treaty also offers an advantage for India. A BIT with the United States would provide a more robust and long-term sense of certainty in the Indian investment climate for American businesses, but also make India more attractive for other investors. Because the United States is well known for negotiating tough terms in its BITs, they can be seen as a “gold standard” of the form. Other countries’ investors can have confidence that India will meet the strong standards set by the U.S. treaty, and while they may not be able to file claims themselves, they can ride on the coattails of any reforms inspired by the U.S. treaty.

Although India is quickly developing, it is still home to hundreds of millions living in poverty. Given trends toward greater trade and investment rather than direct assistance, a BIT could be beneficial in poverty reduction, as well.<sup>6</sup>

The case for a BIT with the United States is strong, but in India doubts remain. India maintains a historic dedication to its strategic autonomy, avoiding becoming too entangled with any one foreign partner. That said, it values the partnership of the United States and recognizes that

---

6. Meredith Broadbent and Robbins Pancake, *Reinvigorating the U.S. Bilateral Investment Treaty Program: A Tool to Promote Trade and Economic Development* (Washington, D.C.: Center for Strategic and International Studies, 2012), <http://csis.org/publication/reinvigorating-us-bilateral-investment-treaty-program>.

both nations share common strategic interests. The Indian government is well stocked with technocrats who fully understand and appreciate the importance of FDI and how such investment can be encouraged via a BIT. However, India's democracy is as complex and unwieldy as that of the United States. Original attempts to reform FDI limitations in multibrand retail failed as a result of one state party's populist stance against foreign capital—a pattern that could be repeated in the context of a BIT. Business groups that would benefit most directly have not been aggressive in support of the treaty. Overall, there is still a lot of work to be done to convince a broader segment of India that a BIT is a good idea.

# 5

## ISSUES FOR NEGOTIATION

### Changes to the U.S. Model BIT

The 2012 Model BIT differs from the 2004 Model in several important ways, but none of them should present major obstacles to negotiations with India.<sup>1</sup> The Model BIT is the language that the United States presents as a starting point for any negotiation. In the past, the final agreements that the United States has signed have not wavered too far from the original model language.

Drastic changes from the 2004 to 2012 models that added to the list of demands from partner countries could have spelled doom for a BIT with India. However, the 2012 Model reveals only modest and incremental changes, and strengthens the model without introducing any provision that should preclude a deal.

The most widely discussed issue in the Model BIT review was regarding language on labor and environmental protections. Environmentalists and unions are concerned that BITs facilitate a “race to the bottom,” helping companies move their operations to the location with the weakest environmental and labor regulations. They pushed for stronger language to avoid this problem.<sup>2</sup> The 2012 Model BIT thus recognizes these concerns and strengthens the chapters on labor and environment, including a pledge not to derogate from labor and environmental laws in order to attract investment, and to effectively enforce existing laws. The changes do not go so far as to make these commitments enforceable by arbitration. India still considers any provision on labor or environment to be an unusual and problematic addition to a BIT, so labor and environment provisions will continue to be controversial. However, the new language should not be significantly more challenging to work with than the old.

Other changes in the model regarding transparency and state-owned enterprises are significant, but have received less attention. India is likely to see some of the new language in the latter sections as burdensome, but again, not something that cannot be negotiated. Stronger requirements for public notice and comment periods or consultations on improving transparency will be an additional burden for the Indians, and state-owned enterprises are significant players in India, but the changes are modest in relation to the 2004 model.

By introducing relatively modest changes, the 2012 Model BIT will only slightly increase the complexity of what was already destined to be a challenging negotiation. Overall, the new Model

---

1. Most information in this section results from CSIS review of the U.S. and India Model BIT language and recently concluded agreements and from roundtable discussions with government officials and industry leaders.

2. Dany Khayat, Timothy J. Keeler, William H. Knull III, and Duane W. Layton, “Worldwide: U.S. Bilateral Investment Treaties: Recent Developments,” Mayer Brown, June 11, 2012, <http://www.mondaq.com/unitedstates/x/181826/International+Trade/US+Bilateral+Investment+Treaties+Recent+Developments>.

BIT language will make it more difficult to conclude a deal with India. However, it will not make it impossible, which was a risk some observers saw going into the review.

## Potential Sticking Points

Why have the United States and India not yet arrived at an agreement? There are still significant issues that will need to be negotiated. The following are five notable disagreements on the body of the BIT text between the Indian Model BIT and the new U.S. 2012 Model BIT. It is worth noting that India is now considering its own internal review and some potential complications could arise from its decisions, particularly on investor-state arbitration.

- *Investor-state arbitration.* India has recently faced a series of arbitration cases under previously signed BITs. The most recent cases involve foreign telecommunications firms worried about the cancellation by the Supreme Court of previous agreements and retroactive taxation. Perhaps the most notable case was brought by White Industries, in which the Australian firm claimed that the promise of MFN treatment in the Australia-India BIT meant that they were entitled to the protections offered in other countries' BITs with India (or they would not be the "most favored"). They successfully used an unusually investor-friendly Kuwait-India BIT to win their claim, raising concerns that each treaty involving an MFN clause was actually more expansive than had been realized.<sup>3</sup>

India has thus been reminded that the guarantees offered in its BITs are real and serious, and at times place a significant limitation on its regulatory options. As a result, the Indian government is considering its own internal review of the Indian Model BIT language, and there is an active discussion as to whether India should agree to investor-state arbitration in future BITs (not to mention renegotiating previously agreed-to BITs).<sup>4</sup>

To the United States, a treaty without a core provision such as the recourse to investor-state arbitration is no longer a BIT, and would not be worth it. The literature demonstrates that credible enforcement is crucial to gaining any advantage in investment after a BIT. Many Indian observers believe that their government understands this point, and they argue for internal review but caution that refusing investor-state arbitration would be throwing out the baby with the bathwater. Nonetheless, it should be recognized that the government of India may decide they cannot accept further exposure to arbitration cases, which would essentially end negotiations before they start. The United States should actively engage Indian interlocutors to make

---

3. Prabhash Ranjan, "The White Industries Arbitration: Implications for India's Investment Treaty Program," International Institute for Sustainable Development, Investment Treaty News, April 13, 2012, <http://www.iisd.org/itn/2012/04/13/the-white-industries-arbitration-implications-for-indias-investment-treaty-program/>.

4. One additional concern about exposure to arbitration issues has raised some amount of attention in India: In the wake of the Arab Spring, some multinationals have filed cases under BITs signed by Libya, e.g., for failure to protect their investments. In essence, a state struggling to emerge from a major disturbance could potentially be saddled with massive obligations for failing to protect foreign investments, as promised in the BIT. This concern reflects a small risk, and it is not yet established whether any arbitrator would take such a claim seriously. However, some international nongovernmental organizations are raising the issue, and are gaining attention in India. For more on this argument see the Transnational Institute assessment of the issue at [http://www.tni.org/sites/www.tni.org/files/download/legalised\\_profiteering-web.pdf](http://www.tni.org/sites/www.tni.org/files/download/legalised_profiteering-web.pdf).

sure this point is widely understood—waiting to deal with this during scheduled negotiations would be too late.

- *Preestablishment treatment of investment and market access.* One of the major issues facing U.S. firms hoping to invest in India is the sector-by-sector limitation on foreign ownership. In the most restrictive cases, no foreign ownership is allowed at all.<sup>5</sup> In other industries, caps ranging from 26 to 74 percent ownership limit the stake that a foreign investor can hold.<sup>6</sup> For many potential investors, the existence of the cap is a deterrent to any level of investment.

At question is whether these limitations will be forbidden under an investment treaty. India argues that FDI limitations are not an issue of unfair treatment of investments—if prohibitions on foreign capital prevent an investment from being made in the first place, there is no way to then discriminate against it. The United States will argue that rules regarding market access and establishment of investment (including FDI caps) concern a vital part of the investment cycle and should also be subject to national treatment protection.

This is a significant hurdle, but one that India has given ground on before. In comprehensive economic partnership agreements with Japan, and South Korea (but not stand-alone BITs), India has agreed to include preestablishment treatment of investments in the treaty by including it in the definition of “investment.”<sup>7</sup>

- *Performance requirements.* In its laudable efforts toward “inclusive growth” that ensures the benefits of economic expansion are shared across society, India uses a number of tools that have the unintended consequence of discouraging investment. One clear example is the continued use of local content requirements. Foreign investors in single-brand retail are obliged to draw 30 percent of the products they sell from small Indian providers. This has delayed or prevented investment from foreign firms such as the Swedish home furnishings giant IKEA. Most major manufacturers have complex international supply chains that are difficult to adjust for one market, even one with the potential of India.<sup>8</sup>

The U.S. Model BIT would proscribe rules like these that limit the ability of investors to conduct their business as they desire. Export requirements and technology transfer obligations are other notable approaches ruled out by the U.S. Model BIT. Again, while the Indian Model BIT fails to address performance requirements, the investment chapter of the Japan-India CEPA includes language on the issue. Detailed negotiation on a negative list of exclusions will not be easy, but the philosophical difference between the sides is not vast.

---

5. “Nitish Also Says No FDI in Multi-Brand Retail,” *Indian Express*, July 30, 2012, <http://www.indianexpress.com/news/nitish-also-says-no-fdi-in-multibrand-retail/981493/0>.

6. “Discussion Paper: FDI Policy Rationale and Relevance of Caps,” Department of Industrial Policy and Promotion, Government of India, June 2011, [http://dipp.nic.in/english/Discuss\\_paper/DiscussionPaper\\_relevance\\_23June2011.pdf](http://dipp.nic.in/english/Discuss_paper/DiscussionPaper_relevance_23June2011.pdf).

7. For Japan, see Ministry of Commerce and Industry, Government of India, “Comprehensive Economic Partnership Agreement between the Republic of India and Japan,” [http://commerce.nic.in/trade/ijcepa\\_basic\\_agreement.pdf](http://commerce.nic.in/trade/ijcepa_basic_agreement.pdf). For South Korea, see Ministry of Commerce and Industry, Government of India, “Comprehensive Economic Partnership Agreement between the Republic of India and Korea,” <http://commerce.nic.in/trade/india%20korea%20cepa%202009.pdf>.

8. IKEA has since asked for a delayed window to bring its local sourcing up to Indian standard, and the Indian government appears willing to discuss it. See <http://in.reuters.com/article/2012/07/06/india-retail-ikea-idINDEE86509R20120706>.

- *Labor and the environment.* The new U.S. Model BIT's articles on these issues will not make negotiations easier, but do not pose as large a hurdle as advocates of BITs had feared. Both sections call for the treaty parties to refrain from derogating from existing labor and environmental protections in order to attract investment, but they do not provide any binding arbitration mechanism for alleged breaches. Opening up these kinds of regulations to arbitration would have been unacceptable to India. The current model remains collaborative and respectful of India's regulatory prerogatives, leaving room for a deal. The India-Japan CEPA does include an environmental (but not a labor) clause along similar lines.
- *Visas.* One area in which India's Model BIT and CEPA investment chapters have been more demanding than the U.S. Model BIT's text is the availability of temporary visas for business travelers, also known as General Agreement on Trade in Services Mode 4.<sup>9</sup> India considers an article on "entry and sojourn of personnel" as a key to any treaty. The argument is that India's most competitive international industry is the business services sector. However, an investment in the provision of services is different from investing in the production of goods in that the application of skilled labor *is* the product. Mode 4—the provision of services by natural persons physically present at the point of delivery—is critical for many Indian businesses. A barrier to movement of the employees who would deliver services in the target country is tantamount to a limitation on investment in services. Given the U.S. demands for market access, it is hard to argue that this kind of provision has no place in an investment treaty.

However, this is the line that the United States is predisposed to take. U.S. visa law is inextricably linked to both concerns regarding losing jobs to cheaper foreign labor and national security. After including language on "temporary movement of business personnel" in the North American Free Trade Agreement and the Chile and Singapore FTAs, some members of the Senate have demanded that such issues never again be included in a trade and investment agreement.<sup>10</sup> While trade in services is clearly related to visas, the Senate's desire for a comprehensive visa policy rather than a patchwork of bilateral visa agreements is no less reasonable. If an agreement to allow free entry and exit of service personnel were part of a BIT with India, support in the Senate would quickly diminish.

While the BIT is clearly beneficial for India in that it will improve the Indian investment climate, many Indians feel that they would be required to yield more in terms of regulatory space than the United States. In other words, the burden of reform and implementation work involved with a BIT will fall disproportionately on the Indian side. As a result, it may be necessary for the United States to offer something tangible to India. Visa issues are not easy for U.S. policymakers, but perhaps easier than adjustments to how Indian workers in America are repaid for payments into the Social Security system (i.e., a totalization agreement, India's other primary request in discussions with the United States) or agreements on processes of the Committee on Foreign Investment in the United States, which is chaired by the U.S. Treasury Department. A concession on visas would not be unprecedented, but careful consultation with

---

9. The WTO defines four "modes" in which services can be delivered across borders. At issue in this case is mode four, delivery of services by a natural person who is physically in the country buying the service. Find more on the modes of trade in services at [http://www.wto.int/english/tratop\\_e/serv\\_e/cbt\\_course\\_e/c1s3p1\\_e.htm](http://www.wto.int/english/tratop_e/serv_e/cbt_course_e/c1s3p1_e.htm).

10. U.S. Senate, "United States–Chile Free Trade Agreement Implementation Act," 108th Cong., 1st sess., July 21, 2003, 41–45.

Congress would be necessary in order to ensure support. The language in Indian CEPAs asks for consideration of visa issues without requiring any set numbers or promising free entry. Not unlike the labor and environmental provisions, a section could pledge both sides to properly enforce their own laws. This kind of pledge, without a binding cap but with the promise of consultations and careful application of existing law, could present a compromise position on the issue.

Overall, there appears to be clear common ground on most issues and the prospects for overcoming them seem bright. Two issues appear more challenging: investor–state arbitration and visas, both of which could become deal breakers based on each country’s fundamental approach to the issues, rather than negotiators’ efforts. Negotiators will still need to hammer out the details of each remaining item of contention, and engagement from higher-level political leaders on both sides may be needed to reach solutions. These issues in the BIT’s main text represent only the first part of a multiphase process of completing a BIT. The second half of the negotiation of a BIT will be the negotiation of nonconforming measures, or industries granted exceptions to the main text, which can be a difficult process in its own right. Once that is done, the challenge will be ensuring final agreement and implementation on both sides.



# 6

## FROM NEGOTIATION TO IMPLEMENTATION

After the negotiators have reached a deal, both countries will need to approve and implement the treaty. Recent agreements with India have run into trouble after it seemed that a deal had been reached. Looking ahead now will help prevent similar disappointments. There are several key groups that will need to support the BIT to ensure its successful implementation: The U.S. Senate must ratify it; the Indian Cabinet must approve the treaty; and the U.S. and Indian business communities and Indian state governments will need to provide active support as well. Finally, the Indian-American community represents a potentially valuable ally in advancing the U.S.-India trade and investment agenda.

### The U.S. Senate: Support Is Strong—for Now

For the U.S. side, there appears to be strong support for a BIT in the Senate, as currently constituted. Broadly speaking, the Senate understands the need for engagement with India and the key role that economic ties play in U.S. efforts across Asia. The bipartisan India Caucus, led by senators Mark Warner and John Cornyn, is the largest in the Senate.<sup>1</sup> A bipartisan group of 10 senators wrote to President Obama urging a U.S.-India BIT (this letter is included below as appendix B). In addition, in a speech at CSIS, Senator John McCain singled out bilateral treaties with India (and Taiwan) as a top trade negotiation priority.<sup>2</sup>

However, a perpetually crowded Senate calendar and rules allowing a single senator to hold up any bill mean that Senate support cannot be taken for granted. Labor and environmental groups will continue to oppose any liberalization of international investment or trade, and they can be expected to make a significant push against a U.S.-India BIT. The recently concluded BIT with Rwanda took almost four years from signature to ratification,<sup>3</sup> and Rwanda is almost certainly a less controversial treaty partner than India.<sup>4</sup> India suffers a reputation as a destination for the outsourcing of American jobs, making the visa issue particularly sensitive. Negotiators will need

---

1. Sunita Sohrabji, “Warner Seeks Direction for Senate India Caucus,” *Times of India*, November 7, 2011, [http://articles.timesofindia.indiatimes.com/2011-11-07/us-canada-news/30369117\\_1\\_warner-senate-india-caucus-tri-valley-university](http://articles.timesofindia.indiatimes.com/2011-11-07/us-canada-news/30369117_1_warner-senate-india-caucus-tri-valley-university).

2. John McCain, “Defining American Interests in Asia,” speech at the Center on Strategic and International Studies, May 14, 2012, <http://csis.org/event/senator-john-mccain-r-az-defining-american-interests-asia>.

3. Office of the U.S. Trade Representative, “United States, Rwanda Ratify Bilateral Investment Treaty,” December 2011, <http://www.ustr.gov/about-us/press-office/press-releases/2011/december/united-states-rwanda-ratify-bilateral-investment>.

4. “Treaty between the Government of the United States and the Government of the Republic of Rwanda Concerning the Encouragement and Reciprocal Protection of Investment,” February 19, 2008, [http://tcc.export.gov/Trade\\_Agreements/All\\_Trade\\_Agreements/RwandaBIT.asp](http://tcc.export.gov/Trade_Agreements/All_Trade_Agreements/RwandaBIT.asp).

to consult particularly closely with the Congress while engaging on the visa issue to find a solution that the Indians regard as significant but the Senate regards as sufficiently flexible.

In the absence of any action, growing frustration with India will tend to undermine the support that a treaty now enjoys in the Senate. In part, that is why the United States needs a “quick win” on the public relations front, but also a part of why BIT negotiators should have an ambitious target for the completion of negotiations.

## The Indian Government: Supportive but Shaky

Gaining support in India will be more challenging. The treaty could be accepted on the Indian side through a decision of the Cabinet, without a vote in the full Parliament. The political leadership in India almost certainly supports the BIT. Its members understand the depth of their need for foreign investment, generally want to move forward with reforms, and value a strong relationship with America.

However, there are still ways the project could fail due to lack of support in India. First, the government could be persuaded to declare a moratorium on treaties that include investor-state arbitration, as discussed above. Second, if negotiators reach a high-standard agreement, the government could lack the political support it needs to approve and implement it. The current coalition is tenuous, with minor parties able to hold the government hostage with threats to pull out of the coalition and bring down the government, as they did in putting a stop to initial efforts to open multibrand retail to FDI in November 2011. Alternatively, implementation could be held up due to other political imperatives in India, similar to the liability issue preventing U.S. firms from taking advantage of the civil nuclear agreement. The possible worst-case scenario for both sides would be a serious negotiation held in good faith, requiring investment of political capital and difficult concessions on both sides, which was then blocked by insufficient political support or key political opponents. This would simply cement the unfortunate perception that the U.S.-India relationship is not yielding benefits for both sides.

American firms and both the U.S. and Indian governments should start laying the groundwork for a coalition in support of the treaty, including state-level officials and business leaders. The immediate task is to spread understanding that without investor-state arbitration in Indian BITs, India's firms will have less protection abroad, and India would lose out on the power of the treaty to attract FDI. The second task is to ensure broad support for the U.S.-India BIT when it comes time for Cabinet approval and implementation.

## The Indian Business Community: Still on the Fence

India, at least so far, lacks a coalition that will push for a high-standard BIT. Opposition will come in the form of habitually anti-American or anticapitalist forces, or, more important, in small businesses that fear American competition more than they support American assistance in spurring growth. In the United States, industry is at the forefront of pushing for a BIT. It will take active effort to build sufficient support in India to ensure success. Industry groups are of mixed opinions:

- Some, based on a general support for economic reform, support a U.S.-India BIT.

- Other large companies—particularly in the service sector—look at the treaty and ask, “What’s in it for us?” They already enjoy a generally welcoming investment environment in the United States, and they see limited value in the protections offered by the treaty. Most important, for services, they see the restrictive visa policy as a severe limitation on their ability to do business here. With services dominating Indian investment in the United States, a treaty that does not address visa issues will lose a significant part of the internal constituency it could need to move forward. Even without an agreement on visas, there is a clear case to persuade these companies: Services are an industry likely to gain from greater U.S. investment in India, at the least from spillover effects of U.S. technology, and from opportunities to form partnerships with U.S. firms in joint ventures.
- There remains a significant portion of businesses, both large and small, that have no knowledge of the issue. Despite analysis of the BIT regime on Indian editorial pages and debate in think tanks, the U.S.-India BIT is still not a topic of much discussion. In the interviews done for this report, some industry groups mentioned that the government had not called them to inquire about it, and thus they have not formed an opinion on BITs. This means that they cannot yet be part of a coalition in support of the BIT but, of particular importance, it also means they are still open to persuasion in either direction.

The Indian business community has not established a position on the issue, meaning that the time is ripe to present information that argues for a BIT, and its likelihood to increase employment and growth in both countries. This should not be a high-profile campaign, but rather needs to be a dispersed effort by economic agencies, public diplomacy sections at the embassy and consulates, and, most important, the leaders of U.S. industry working with their partners and colleagues in India. The members of each of these groups should take advantage of regular contacts to inform and persuade Indian industry, state governments, and any other interested parties to express their support for the U.S.-India BIT. To solidify support, the United States should put forth a good faith effort to find some acceptable language on visas and thereby garner support from critical business constituencies in India.

## The Indian-American Community: Huge Potential for Support

The State Department has been active in engaging the members of diaspora groups who have come to the United States from countries around the world.<sup>5</sup> The Indian-American community can be a particularly good ally in the pursuit of stronger economic ties with India. This group demonstrated its power with a positive, coordinated effort to push through the U.S.-India civil nuclear deal in 2008.<sup>6</sup> A similar effort would be of great use on the BIT (and any future trade liberalization efforts). Because a BIT would benefit both countries and improve ties, there will likely be broad support in the community. Further, there is a strong presence of Indian-Americans in technology businesses and other sectors that could benefit from freer trade and investment with India.

---

5. “Clinton Encourages Diaspora Communities to Assist Back Home,” Voice of America, July 25, 2012, [http://www.voanews.com/content/clinton\\_encourages\\_diaspora\\_communities\\_to\\_assist\\_back\\_home/1446671.html](http://www.voanews.com/content/clinton_encourages_diaspora_communities_to_assist_back_home/1446671.html).

6. Aditi Bhaduri and Swadesh Chatterjee, “India Gave Us Our Lives and the U.S. Our Livelihood,” *Times of India*, Opinion Section, July 1, 2011, [http://articles.timesofindia.indiatimes.com/2011-07-01/interviews/29725634\\_1\\_atomic-energy-act-global-advisory-council-nuclear-deal](http://articles.timesofindia.indiatimes.com/2011-07-01/interviews/29725634_1_atomic-energy-act-global-advisory-council-nuclear-deal).

The BIT would personally benefit these individuals, or others who themselves desire to invest in India in some form.

The members of the Indian-American community have growing influence. They represent a significant and growing voting bloc in some U.S. congressional districts, and many of the particularly successful individuals retain influence with business leaders and/or government officials back in India. They do not have a generations-old tradition of political advocacy in the United States, as do some other diaspora groups, so it may take conscious effort by those interested in the U.S.-India relationship to ignite the community's interest in trade and investment issues. However, the effort undertaken is likely to pay significant dividends—perhaps most important in the role that they could play in public education in India on the benefits of trade and investment ties for both sides.

## Realistic Timelines and Quick “Wins”

Some enthusiastic supporters of the U.S.-India relationship are hoping for a lightning-fast conclusion to the BIT. Their view is that a “win” is needed soon, and a BIT is attainable. This is an admirable goal, but pushing for a victory at the expense of a robust set of protections for American capital in the treaty would be shortsighted. Bringing positive momentum back to the relationship is important, but if the United States were to sign a substandard BIT for the sake of expediency, a price would be paid for the life of the treaty in India, and such a BIT would set a new, lower bar for all future negotiations—such as those ongoing with China.

But that is not to say that the United States should not be concerned about a timeline. Past BIT negotiations can be instructive: Negotiations on a BIT between India and Canada lasted 14 rounds and were first signed five years ago before being reopened at India's request in 2009.<sup>7</sup> That discussion is still ongoing, and there is still no agreement in force. Some kind of target date is needed to keep negotiations moving, and completing negotiations in 2013 is an achievable target. Political leadership at both the State Department and the USTR should continue to emphasize the importance of this effort in the overall U.S.-India relationship, and push to meet this timeline.

The BIT is a valuable medium-term goal. Working out an agreement over the next year will be a valuable process, but it leaves a pressing need for a “win” to regain positive momentum in the U.S.-India economic relationship. Although many substantive trade issues will need time to be worked out, there are a few options the United States can undertake in the short term to accomplish this objective: restarting the Trade Policy Forum, pushing ahead with state-to-state engagement, or making a public affairs push on economic issues.

## Restarting the Trade Policy Forum

The TPF was proving to be long on process and short on deliverables. However, its abrupt cancellation has contributed to the impression that the United States and India cannot get anything done. While nobody was expecting major breakthroughs, many have expressed disappointment

---

7. Foreign Affairs and International Trade Canada, Government of Canada, “Canada-India Foreign Investment Promotion and Protection Agreement (FIPA) Negotiations,” April 4, 2012, <http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/india-inde.asp?lang=eng&view=d>.

or surprise that the TPF has been put on hold. Providing a forum and a regular schedule for trade discussions remains a solid idea, as it was when the TPF was conceived. The United States should prioritize restarting the TPF process while keeping expectations modest.

Both sides, recognizing the importance of maintaining strong trade ties, should regard the TPF as a tool for constructive dialogue and problem solving at the staff level before TPF meetings. The process is necessary, but process itself cannot be the goal. The goals for the TPF should remain modest, reaching for small steps forward and building momentum for bigger issues like a BIT or a resolution to India's concerns on temporary business visas. Modest initiatives on protections of intellectual property rights (both countries have thriving film industries) or customs transparency present opportunities for progress, and could be stepping stones to the bigger issues that each country has on its national agenda.

## Pushing Ahead with State-to-State Engagement

Trade missions and partnerships with the states hold potential to generate positive economic results that can help lift the mood around the U.S.-India relationship even without major breakthroughs. Indian states have proven dynamic and aggressive in facilitating foreign investment. The federal government has an important matchmaking and convening role in this process, and the U.S. Embassy in New Delhi and the four U.S. consulates are moving ahead to engage actively with the states. The U.S. government should encourage this and back the effort with resources such as personnel dedicated to facilitating state-to-state relations. Ambassador Nancy Powell has highlighted the importance of this effort. In a speech this year to the American Chamber of Commerce in India, she said, "I, too, want to continue to look beyond our usual capital city contacts to progressive Chief Ministers for opportunities to develop strong business ties. . . . This facet of our cooperation holds enormous potential as we seek to leverage the innovative work and broadened connections across financial, technology, and human capital at the state, city, and local levels."<sup>8</sup> Trade missions led by Maryland governor Martin O'Malley and Virginia governor Robert McDonnell have already taken place, and more should follow.

At the State Department, the special representative for global intergovernmental affairs (SRGIA) has provided a valuable service in ensuring that the bureaucracy focuses on this effort. Because special representatives' offices are highly dependent on how a given secretary of state chooses to structure his or her staff, it is unclear whether the next administration will maintain a dedicated SRGIA. The role of drawing attention to state-to-state engagement does not necessarily need a special representative, but if the office is eliminated, the role of prioritizing and facilitating state-level interactions in India must be absorbed by the State Department's South and Central Asia Bureau at a sufficiently senior level to ensure that it is not lost in the shuffle of other priorities. State Department institutions are more accustomed to dealing with national governments, and national-level issues naturally attract more time and resources if there is not a concerted effort to engage with the states.

---

8. Nancy Powell, speech at the American Chamber of Commerce 20th Annual General Meeting, April 27, 2012, <http://newdelhi.usembassy.gov/sr270413.html>.

## Making a Public Affairs Push on Economic Issues

The majority of effort in working with the Indian public to ensure support for economic reform must be done by the Indian government. However, U.S. industry and the U.S. government can play a supporting role. Indian public opinion is already strongly pro-United States.<sup>9</sup> Americans in both industry and government should be highlighting the potential benefits of expanded trade and investment ties with the United States, and not just to the Indian government but also to the Indian business community. Through a mix of economic officers broadly engaging public affairs officers on economic issues, and working with the local U.S.-India Business Council and American Chamber of Commerce, the U.S. Embassy in New Delhi can help build up an understanding of these issues. This will lay the groundwork for a broader base of support for the day when a window of political opportunity opens.

---

9. Dhruva Jaishankar and Daniel M. Kliman, “U.S., India Share Long-Term Interests,” *Politico Opinion*, June 12, 2012, [http://www.politico.com/news/stories/0612/77337\\_Page2.html](http://www.politico.com/news/stories/0612/77337_Page2.html).

## 7

## THE LONG TERM THINKING BEYOND THE BIT

A BIT is a necessary but not sufficient step toward greater economic engagement with India. It can have real and positive effects, but its symbolic power is also of significant value. Precisely because its success is not guaranteed, completing a BIT could go a long way to dispelling the idea that India and the United States cannot cooperate on matters of significance. Completing one negotiation can surely build momentum and serve as a springboard for further collaboration.

Each step in the U.S.-India relationship—whether individual transactions, a BIT, or something bigger—will be made easier if there is a sense of purpose and direction to the discussions. If this truly is a strategic partnership—let alone what President Obama has called “one of the defining partnerships of the 21st century”—then the two nations should arrive at an agreed-on vision for the future, beyond the next deal on the table.<sup>1</sup> Advocates of making a full FTA the centerpiece of this vision are on the right track, but an incremental approach to trade liberalization would provide a vision for the future while holding a better chance of success.

### An FTA Would Benefit Both Sides but Would Be Overly Ambitious for Now

Support for FTAs has been modest in recent years in the United States. The current administration has not aggressively pursued new bilateral FTAs beyond seeking ratification of agreements with Colombia, Panama, and South Korea. Efforts have been more focused on the Transpacific Partnership (TPP) and on normalizing trade relations with Russia. Meanwhile, India has been active in negotiating FTAs or similar arrangements. It has concluded CEPAs with Japan, South Korea, and ASEAN, and it is negotiating an FTA with the European Union. As with investment agreements, the United States is losing ground on trade agreements by standing still.

There are two schools of thought on how to proceed with trade liberalization: Either the United States should start talking up an FTA now in the form of feasibility studies or formation of a committee for preliminary technical discussion, or it should try to build incrementally to the eventual result of a de facto FTA through the cumulative effect of smaller agreements. The next administration should consider prioritizing trade liberalization with India using this incremental approach. The advocates of an FTA are correct on the economics, but the political climate does not support an ambitious attempt at a full FTA immediately.

From an economic perspective, the case is clear: Free trade would be beneficial for both sides. Two large market-driven economies, with many complementary industries, would realize significant gains from expanded trade. Ernest Preeg’s 2010 study of the issue for the Manufactur-

---

1. Lydia Polgreen, “Friendship Parallels a Strategic Partnership,” *New York Times*, November 8, 2010, <http://www.nytimes.com/2010/11/09/world/asia/09india.html>.

ers' Alliance for Productivity and Innovation presents the case for an FTA in full, and while some trends have shifted since then, the facts have not changed in any way that would ultimately affect the argument.<sup>2</sup>

Many outside observers and think tanks are using these economic arguments to urge the government to pursue a full FTA, but as with most free trade arguments, it is the political calculus of the situation, not the economic logic, that prevents further liberalization. The vast majority of U.S. government officials with extensive experience working with India caution against pursuing a full FTA immediately. Some argue that India is not ready to discuss an FTA, or that differences are too great and the result would only be disappointment. Both U.S. and Indian officials note the low staffing levels on the Indian side as a limitation on the scale of initiatives that the two countries can hope to tackle together. A truly comprehensive FTA would run into problems that have vexed high-level talks at the WTO, such as agriculture (both U.S. subsidies and Indian protection of its huge and inefficient agricultural sector), Mode 4 trade in services, and others.

Proponents of immediate FTA discussions argue that other countries, like Japan and South Korea, have managed to achieve trade agreements with India. If these countries can get a comprehensive deal done with India, why cannot the United States? However, it is important to note that an FTA along the lines of previous American FTAs would exceed the standards set by most competitors. Indian CEPAs with Asian countries allow more exceptions and lighter restrictions than a United States–negotiated FTA would permit. In addition, the EU has been “close” to completing an FTA with India for some time now, and negotiators are not positive about prospects to cross the finish line soon. For the United States, this is a cautionary tale—remaining on the doorstep of a deal without breaking through is perhaps worse than never making any progress at all.

The other argument in favor of pursuing an FTA as a next step is to establish an ambitious vision and political support for it, making smaller agreements easier. FTA proponents argue that high-level political agreement on pursuit of an FTA would signal the mutual importance of the relationship and provide top cover for Indian bureaucrats to work productively on any number of smaller issues now. Unfortunately, this argument has not proven true in practice. India already is negotiating an FTA with the EU, but it is not clear that European firms are seeing any advantages of an ambitious trade agenda in resolving smaller disputes (e.g., IKEA, Zara, Vodafone).

Given those limitations, a full-blown FTA along the lines of what the United States has recently concluded with other countries is overly ambitious. However, this does not mean that a longer-term pursuit of an FTA is beyond reach. Traditionally, the USTR has been limited to mechanisms like the TPF, a model for a BIT, and the outline for an FTA. The United States should look beyond these tools and push for incremental reforms, one chapter of an FTA at a time. This would be a new mode of operation, but one worth pursuing.

## An Agreement on IT Trade: A Realistic Option for Continued Progress

India presents an important opportunity to start thinking beyond the limited options of TPF (or a trade and investment framework agreement), BIT, and FTA. The administration has shown a

---

2. Ernest Preeg, “Economic Report: The Growing U.S. Interest in a Free Trade Agreement with India (PR-159),” MAPI Manufacturers Alliance, May 2011.



willingness to forge new approaches with the Transpacific Partnership.<sup>3</sup> The United States should show the same willingness to think about new trade models in bilateral settings. Concerns about congressional approval have been a barrier to the USTR's ability to seek new kinds of trade deals, but given support for the U.S.-India relationship, this is a perfect case to work with Congress on something new. The case for working together is not just an economic imperative but also a strategic imperative that enjoys broad bipartisan support on Capitol Hill and across administrations.

The United States should take advantage of this opportunity to craft a long-term vision of deep economic integration, a series of intermediate steps that can reach that goal over the course of a decade, and a plan to lay the groundwork for the first few steps in that process. To some extent this will involve responding to opportunities as they arise, identifying Indian policy priorities to which the United States can usefully contribute, and adjusting course as necessary.

The United States should be planning its next steps now. After completion of a BIT, the next promising candidate would be an agreement on trade in IT-related goods and services. The model for this kind of agreement exists in the WTO's ITA.<sup>4</sup> Given the rapid pace of change in this sector, even an agreement that is 16 years old could benefit from an update. There is also a plurilateral effort in the WTO to do this. Nonetheless, modernizing the goods agreement on a bilateral basis, and updating to include services, would ensure that both sides would gain in a sector that is one of their strongest in the bilateral relationship. This agreement could also be tailored to more completely address high-technology companies' concerns about indigenous innovation and technology transfer.

With a more limited scope of negotiations, clear benefits for both sides, and support from experts and business groups on both sides, an agreement focused on the IT sector would be a significant next step after a BIT. This approach has been proposed elsewhere—most notably by the Private Sector Advisory Group. The President's Trade Agenda for 2012 notes the intention to make more use of this group's recommendations, and an IT-sector agreement would be an ideal place to start. It should not be the last step, but the next phase in a long-term agenda of economic cooperation. The biggest obstacle may be moving beyond the concept that only a comprehensive agreement is worth the time to negotiate.

Subsequent agreements could then build on this framework, moving stepwise to an increasingly comprehensive free trade regime. As the next biggest source of FDI in India, the chemical sector presents another opportunity with industry leaders in the United States looking for open markets and positive technological spillover effects for India. As India works to provide services to its growing population, the health care industry could be another sector worth exploring.

---

3. It is possible that the United States could seek to bring India into the TPP process, or conclude a deal on the TPP with an "open architecture" that allows other countries to join, accepting all the terms of the TPP as a take-it-or-leave-it offer. However, attempting to add more countries—and especially a significant player like India—to the current group of negotiators would surely add untold complexity and years to the negotiations. Hoping to bring India in after conclusion of a deal is also not a good option. Given a large and unwieldy group of current participants, the timeline for completion is unknown, during which time there would be essentially no engagement with India. Completing the deal first and then investing an unknown amount of time to bring a large country like India into the framework would essentially mean accepting very little advancement of the U.S.-India relationship for many years. This would be unacceptable for both sides.

4. See [http://www.wto.org/english/tratop\\_e/inftec\\_e/inftec\\_e.htm](http://www.wto.org/english/tratop_e/inftec_e/inftec_e.htm).

# 8

## CONCLUSION

It is worth repeating that the United States and India have a strong economic partnership that serves as a solid foundation for their overall relationship, and continues to grow. Both bilateral trade and investment are increasing. However, other countries' economic ties with India are growing even more quickly, and the United States is losing ground as a result.

For what President Obama calls one of the “defining partnerships of the 21st century,” letting the economic side of things drift is unacceptable. It is possible that if governments do nothing, the private sector will find a way to continue to build strong economic ties. However, strong leadership in government can set conditions in which business ties are more likely to be a force driving positive change. Political leaders on both sides will need to push for an expansive vision of the possible cooperation between the two countries, and will need to leverage the ability of business leaders to make it happen. In the short term, some small economic “wins” and patience will keep the attitude positive and keep things on the right track and restore the needed momentum to the economic partnership.

Concluding a bilateral investment treaty is the most significant step that the United States and India can take that can be completed in relatively short order—ideally, before the next Indian elections in 2014. There are differences between initial bargaining positions, but few show any philosophical difference that cannot be overcome. The exception is the risk of India turning away from investor–state arbitration, a move that would degrade the enforcement mechanism of the treaty to the point that it would not yield any of its potential benefits. Finding a middle ground on visa issues will increase the likelihood of strong support within India and successful implementation. Both in the early phases of discussions and as implementation approaches, it will be important to build broader support for the treaty—and perhaps for U.S. investment overall. The Indian business community, state-level governments, and members of the American-Indian diaspora can all play important roles in this effort.

Whether the BIT comes to pass sooner or later, building an economic relationship will require government effort and a vision for what 21st-century economic cooperation ought to look like. Now is an excellent opportunity to think beyond historical structures and push for an agreement of a kind into which the United States and India have not entered in the past. By midcentury, the United States and India are forecast to be the second- and third-largest economies in the world. Now is the time for these two economic giants to prioritize their bilateral economic relationship in order to rise to this occasion.

## APPENDIX A

# LIST OF U.S. AND INDIAN BILATERAL INVESTMENT TREATIES

U.S. BITs that have been signed and are being enforced:<sup>1</sup>

- |                                      |                |                         |
|--------------------------------------|----------------|-------------------------|
| 1. Albania                           | 15. Egypt      | 29. Panama              |
| 2. Argentina                         | 16. Estonia    | 30. Poland              |
| 3. Armenia                           | 17. Georgia    | 31. Romania             |
| 4. Azerbaijan                        | 18. Grenada    | 32. Rwanda              |
| 5. Bahrain                           | 19. Honduras   | 33. Senegal             |
| 6. Bangladesh                        | 20. Jamaica    | 34. Slovakia            |
| 7. Bolivia                           | 21. Jordan     | 35. Sri Lanka           |
| 8. Bulgaria                          | 22. Kazakhstan | 36. Trinidad and Tobago |
| 9. Cameroon                          | 23. Kyrgyzstan | 37. Tunisia             |
| 10. Democratic Republic of the Congo | 24. Latvia     | 38. Turkey              |
| 11. Republic of the Congo            | 25. Lithuania  | 39. Ukraine             |
| 12. Croatia                          | 26. Moldova    | 40. Uruguay             |
| 13. Czech Republic                   | 27. Morocco    |                         |
| 14. Ecuador                          | 28. Mozambique |                         |

U.S. BITS that have been signed but are not yet being enforced:<sup>2</sup>

- |                |              |               |
|----------------|--------------|---------------|
| 1. Belarus     | 3. Haiti     | 5. Russia     |
| 2. El Salvador | 4. Nicaragua | 6. Uzbekistan |

1. See [http://tcc.export.gov/Trade\\_Agreements/Bilateral\\_Investment\\_Treaties/index.asp](http://tcc.export.gov/Trade_Agreements/Bilateral_Investment_Treaties/index.asp).

2. See <http://www.state.gov/e/eb/ifd/bit/117402.htm>.

Indian BITS that have been signed and are being enforced:<sup>3</sup>

- |                           |                 |                         |
|---------------------------|-----------------|-------------------------|
| 1. Argentina              | 25. Israel      | 49. Romania             |
| 2. Armenia                | 26. Italy       | 50. Russian Federation  |
| 3. Australia              | 27. Jordan      | 51. Saudi Arabia        |
| 4. Austria                | 28. Kazakhstan  | 52. Senegal             |
| 5. Bahrain                | 29. Kuwait      | 53. Serbia              |
| 6. Bangladesh             | 30. Kyrgyzstan  | 54. Slovak Republic     |
| 7. Belarus                | 31. Laos        | 55. South Korea         |
| 8. Belgium                | 32. Latvia      | 56. Spain               |
| 9. Bosnia and Herzegovina | 33. Libya       | 57. Sri Lanka           |
| 10. Brunei                | 34. Lithuania   | 58. Sudan               |
| 11. Bulgaria              | 35. Macedonia   | 59. Sweden              |
| 12. China                 | 36. Malaysia    | 60. Switzerland         |
| 13. Croatia               | 37. Mauritius   | 61. Syria               |
| 14. Cyprus                | 38. Mexico      | 62. Taiwan              |
| 15. Czech Republic        | 39. Mongolia    | 63. Tajikistan          |
| 16. Denmark               | 40. Morocco     | 64. Thailand            |
| 17. Egypt                 | 41. Mozambique  | 65. Trinidad and Tobago |
| 18. Finland               | 42. Myanmar     | 66. Turkey              |
| 19. France                | 43. Netherlands | 67. Turkmenistan        |
| 20. Germany               | 44. Oman        | 68. Ukraine             |
| 21. Greece                | 45. Philippines | 69. United Kingdom      |
| 22. Hungary               | 46. Poland      | 70. Uzbekistan          |
| 23. Iceland               | 47. Portugal    | 71. Vietnam             |
| 24. Indonesia             | 48. Qatar       | 72. Yemen               |

Indian BITS that have been signed but are not yet being enforced:

- |                                     |               |              |
|-------------------------------------|---------------|--------------|
| 1. Colombia                         | 5. Ghana      | 9. Uruguay   |
| 2. Democratic Republic of the Congo | 6. Nepal      | 10. Zimbabwe |
| 3. Djibouti                         | 7. Seychelles |              |
| 4. Ethiopia                         | 8. Slovenia   |              |

---

3. See [http://www.fnmin.nic.in/bipa/bipa\\_index.asp?pageid=1](http://www.fnmin.nic.in/bipa/bipa_index.asp?pageid=1).

## APPENDIX B

# SENATE INDIA CAUCUS LETTER TO PRESIDENT REGARDING THE BIT

United States Senate  
WASHINGTON, DC 20510

December 19, 2011

President Barack Obama  
The White House  
1600 Pennsylvania Avenue NW  
Washington, D.C. 20500

Dear Mr. President,

We commend you on resuming negotiations regarding a Bilateral Investment Treaty (BIT) with India. As members of the Senate India Caucus, we urge you to expedite the ongoing discussions about the treaty as part of a proactive engagement strategy that will produce tremendous benefits for American companies and investors, as well as for their Indian counterparts.

An investment treaty between India and the U.S. would provide important protections to U.S. investors from arbitrary, discriminatory or confiscatory measures, and would be enforceable by independent international arbitration. Such a treaty could also help facilitate additional investment in infrastructure and other priorities in India where investment is badly needed. It would further provide protections to Indian companies as they expand investments in the U.S.

As the world's largest free-market democracy, India has become one of the United States' most critical strategic partnerships. The country's resilient economy, fast-growing middle class, and entrepreneurial spirit have deservedly made it an attractive destination for American investment. Protecting this existing and future investment through a high-standard BIT should be a top priority as the United States seeks to revitalize economic opportunities for American firms and strengthen our bilateral economic relationship with an important partner.

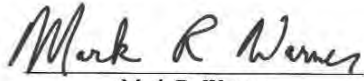
Many countries have already recognized and acted upon the incredible economic opportunities India represents. India has completed investment agreements with 80 countries including all major European nations, ASEAN, Japan, and South Korea. In order to overcome the competitive disadvantage already facing American companies in the Indian marketplace, it is imperative that the United States move forward quickly to negotiate and conclude this treaty. A high-standard U.S.-India BIT would better protect our businesses and create new sales and economic opportunities, and would further solidify U.S.-India economic relations.

The tremendous potential of a BIT with India to protect and promote growth-producing American investments abroad, attract Indian investment into the United States, put our companies on equal footing with international counterparts in India and strengthen ties with a strategic partner is too significant to ignore. We urge you and your Administration to move quickly on concluding a high-standard and comprehensive BIT as soon as possible, and stand ready to assist you in this endeavor.

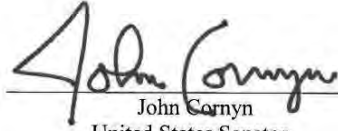
*(Letter continues on the next page.)*

Letter (continued)


Sincerely,



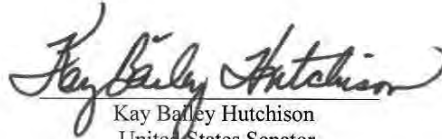
Mark R. Warner  
United States Senator



John Cornyn  
United States Senator



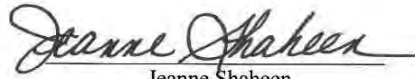
Joseph L. Lieberman  
United States Senator



Kay Bailey Hutchison  
United States Senator



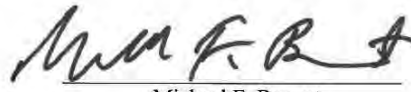
Robert Menendez  
United States Senator




Jeanne Shaheen  
United States Senator




Mark Begich  
United States Senator



Michael F. Bennet  
United States Senator



Christopher A. Coons  
United States Senator



Mark Kirk  
United States Senator



## APPENDIX C

# FURTHER READING

- Armitage, Richard, and R. Nicholas Burns. "Natural Allies: A Blueprint for the Future of U.S.-India Relations." Center for a New American Security, Washington, D.C., October 2010.
- Blackwill, Robert D., and Naresh Chandra. *The United States and India: A Shared Strategic Future*. Joint Study Group Report. New York: Council on Foreign Relations and Aspen Institute, 2011.
- Broadbent, Meredith, and Robbins Pancake. "Reinvigorating the U.S. Bilateral Investment Treaty Program: A Tool to Promote Trade and Economic Development." Center for Strategic and International Studies, Washington, D.C., June 2012. <http://csis.org/publication/reinvigorating-us-bilateral-investment-treaty-program>.
- Card, Andrew H., and Thomas A. Daschle. *U.S. Trade and Investment Policy*. Independent Task Force Report 67. New York: Council on Foreign Relations, 2011.
- Clinton, Hillary. "America's Pacific Century." *Foreign Policy*, November 2011. [http://www.foreignpolicy.com/articles/2011/10/11/americas\\_pacific\\_century](http://www.foreignpolicy.com/articles/2011/10/11/americas_pacific_century).
- Department of Industrial Policy and Promotion, Government of India. "Discussion Paper: FDI Policy Rationale and Relevance of Caps." June 2011. [http://dipp.nic.in/english/Discuss\\_paper/DiscussionPaper\\_relevance\\_23June2011.pdf](http://dipp.nic.in/english/Discuss_paper/DiscussionPaper_relevance_23June2011.pdf).
- Jain, Kamlesh, and Vinod K Jain. *How America Benefits from Economic Engagement with India*. Washington, D.C.: India-U.S. World Affairs Institute, 2010.
- Office of the U.S. Trade Representative. "President's 2012 Trade Policy Agenda." <http://www.ustr.gov/sites/default/files/FULL%20REPORT%20-%20PRINTED%20VERSION.pdf>.
- Perkovich, George. *Toward Realistic U.S.-India Relations*. Washington, D.C.: Carnegie Endowment for International Peace, 2010.
- Preeg, Ernest. "Economic Report: The Growing U.S. Interest in a Free Trade Agreement with India (PR-159)." MAPI Manufacturers Alliance, May 2011.
- "Report of the Private Sector Advisory Group to the India-U.S. Trade Policy Forum." January 2011, [http://uscsi.org/images/stories/PSAG\\_Report\\_Feb\\_9\\_2011.pdf](http://uscsi.org/images/stories/PSAG_Report_Feb_9_2011.pdf).
- Schwab, Susan C. "After Doha." *Foreign Affairs*, May-June 2011.
- U.S. Department of State. "2012 U.S. Model Bilateral Investment Treaty." <http://www.state.gov/documents/organization/188371.pdf>.
- Vickery, Ray. *The Eagle and the Elephant*. Baltimore: Johns Hopkins University Press, 2011.







## ABOUT THE AUTHORS

**Matthew Stokes** is a visiting fellow at the Wadhwani Chair in U.S.-India Policy Studies at CSIS. He has been detailed to CSIS from the U.S. Department of State, where he is a Foreign Service officer. Previous to joining CSIS, he served as a provincial affairs officer at the U.S. Embassy in Kabul, where he oversaw grants programs for Provincial Reconstruction Teams conducting development and governance programs outside of the capital and served as adviser to the ambassador on developments in the eastern provinces of Nangarhar, Kunar, Laghman, and Nuristan. He has served as an economic officer in Riga, working with the U.S. Department of the Treasury and the International Monetary Fund to provide technical assistance during the Latvian bailout program. He has also served in Washington and as a consular officer in Guatemala City. Before joining the Foreign Service, he was a professional staff member for the U.S. Senate Committee on Finance, focusing on taxation and legislation to reform tax laws to promote job creation and economic growth. He has also worked as a research assistant at the University of California, Berkeley, Program on Housing and Urban Development. In the private sector, he worked as a project manager at ImaginEngine, a San Francisco-based software developer, and as a research assistant at Abt Associates, a public policy research and evaluation firm. He holds a master's in public policy from the University of California, Berkeley, and a bachelor of arts from the University of Colorado, Boulder, where he graduated summa cum laude with a major in economics. The views presented in this report are those of the authors and do not necessarily represent the views of the U.S. Department of State or the U.S. government.

**Niraj Patel** is an intern scholar with the Wadhwani Chair in U.S.-India Policy Studies at CSIS. Before coming to CSIS, he worked at the Brookings Institution in the Metropolitan Policy Program performing research and analysis on manufacturing-sector wages, employment, and productivity in the United States. He was formerly an aerospace design engineer and performed innovative work on major defense and commercial programs such as the F-35 Joint Strike Fighter at Northrop Grumman and the 787 Dreamliner at Boeing. He received an M.A. in international relations and international economics from the Paul H. Nitze School of Advanced International Studies at Johns Hopkins University with a concentration in U.S. foreign policy and U.S.-South Asian relations. He graduated with highest honors from the University of Illinois at Urbana-Champaign, receiving a B.S. in aerospace engineering and a minor in analytical mathematics.







1800 K Street, NW | Washington, DC 20006  
Tel: (202) 887-0200 | Fax: (202) 775-3199  
E-mail: [books@csis.org](mailto:books@csis.org) | Web: [www.csis.org](http://www.csis.org)

