

EAEU-India Free Trade Area: Potential Tariff Liberalization Effects for Russia¹

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Abstract. In 2017 negotiations on the free trade area between India and the EAEU countries entered an active phase. The negotiations covered such issues as import tariff liberalization and the elimination of non-tariff restrictions. The present study aims to quantify the potential impact of mutual tariff liberalization on the dynamics of bilateral trade between Russia and India, in order to develop key principles for Russia's negotiating position (as part of the EAEU), taking its strategic priorities into account. The research methodology is based on the SMART partial equilibrium model and a qualitative analysis of modern trends in import demand and the degree of India's trade protectionism towards imports from the EAEU countries. The study found that symmetric bilateral tariff liberalization may result in a higher potential increase in Russian exports to India than imports, which will increase the bilateral trade surplus. This is in the interests of Russia, but it hardly meets the strategic interests of India due to its chronic trade deficit. The free trade area may lead to diversification of the commodity component of Russian exports due to the growing export supplies of Russian coal, and, to a lesser extent metals (aluminum, copper and articles thereof). However, the opportunities to increase the share of hi-tech products in the structure of Russian exports remain limited. The free trade area can become an important tool for strengthening Russian exporters of fertilizers, as well as certain categories of agricultural products. In turn, Indian exporters can strengthen their positions on the Russian medicines market, an increase the share of textile products, jewellery, and certain categories of agricultural products. The results can help develop Russia's positions (as an EAEU member) in multilateral negotiations.

Keywords: EAEU; Russia; India; free trade area; SMART model; econometric analysis; tariffs.

The St. Petersburg Economic Forum 2017 officially launched the negotiation process for a free trade zone between the Eurasian Economic Union (EAEU) and India. In 2017, a joint report on the feasibility of the integration scenario was published.

¹ English translation from the Russian text: Arapova E. 2021. Zona svobodnoi trgovli EAES-India paramentry i potentsial. *Mezhdunarodnyye protsessy [International trends]*. 19(4). P. 68-88. <https://doi.org/10.17994/IT.2021.19.4.67>.

The free trade zone could unite countries with a total GDP of nearly USD 4.5 trillion (at current prices) and a population of more than 1.5 billion people, becoming a vital tool for boosting mutual trade. According to Eurasian Economic Commission estimates, the “mutual liberalization of the trade regime will lead to the GDP increase in all the EAEU countries and India already in the short term. In addition, according to expert estimates, when moving to a free trade regime, the turnover could grow by 30-40% in comparison with the current level depending on the depth of tariff liberalization to be achieved as a result of the negotiations.”²

The consequences of the new integration regime will be directly determined by the agreements reached by the parties, primarily with regard to the schedule for reducing customs duty rates.

This article aims to quantify the likely trade effects for Russia based on the SMART model in case of a one-percent reciprocal linear reduction in customs duty rates by India and EAEU countries to identify the elasticity of trade flows with regard to customs duty rates, draw conclusions about the impact of tariff liberalization on the dynamics and sectoral structure of mutual trade between Russia and India, and offer recommendations regarding Russia's stance in the negotiations (as part of the EAEU), bearing in mind the mutual trade dynamics, trends in import demand and the degree of trade protectionism adopted by the Indian government.

Effects of Tariff Liberalization: Impact on Foreign Trade

The question of the impact of tariff liberalization on foreign trade intensity has been the subject of fierce debate among various theoretical schools over recent decades, with the protectionist doctrine being opposed to the free trade doctrine. Those in favour of the latter support the idea that liberalization, including tariffs, has a positive impact on the volume and growth rate of foreign trade flows, including both imports and exports (Trefler 1993; Learner, Levinsohn 1995; Wang 2001; Helpman 2011; Sequeira 2016) and, accordingly, that stronger tariff protectionism has the opposite effect due to higher prices for imported products and poorer price competitiveness (Feenstra 1995).

At the same time, a number of experts have empirically proved the absence or ambiguity of the impact of tariff liberalization on the intensity of foreign trade (Cline et al. 1978; Baldwin, Lewis and Richardson 1980; Bhagwati 1988; Ostry 1991). They are especially sceptical about the possibility of increasing exports through tariff liberalization (Ostry 1991; Greenaway, Sapsford 1994; Rose 2002).

² EAEU and India Began Formal Negotiations on a Free Trade Agreement. Eurasian Economic Commission. URL: <http://www.eurasiancommission.org/ru/nae/news/Pages/3-06-2017.aspx> (accessed: 08.12.2020).

Most researchers recognize significant differences in the intensity of the impact of tariff regulation, depending on the starting conditions of trading countries and the level of competitiveness of individual industries. In particular, Anne Krueger proved that import flows respond significantly faster to a reduction in customs duty rates, although the effect on exports in the longer term is also positive (Krueger 1998).

Michael Porter's theory of national competitiveness concluded that the effects of foreign trade policy are largely determined by the degree of competitiveness (at the level of individual industries and the economy as a whole), the nature of competition and government measures to enhance competitiveness (Porter 1985). The effects of tariff liberalization are also determined by the degree of market monopolization (Krugman 1979; Feenstra 1995) and the complementarity of domestic and imported goods (Houthakker, Magee 1969; Goldstein, Kahn 1978).

It has been empirically proven that the effect of tariff liberalization is stronger when a country is more deeply involved in international trade, or when it trades more actively with regional partners, as customs duties are typically reduced in such cases (within the framework of integration associations) (Nenci 2011; Feenstra 2003; Peters 2002; Salvatore 2013).

The nature and intensity of foreign trade with lower customs duties also depends on the consistency of the country's foreign trade policy (Francois, Martin 2004). If the reduction in customs duties is due to the countries' commitments under WTO treaties or regional trade agreements, then the positive effect of tariff liberalization may be greater than if such commitments to maintain the course of liberalization were not in place.

The example of a potential EAEU–India free trade zone is interesting in terms of finding new empirical arguments for the development of the academic discussion on the factors that predetermine the magnitude of trade effects. The countries have high sectoral complementarity of foreign trade flows, while the volume of India's mutual trade with its largest trade partner in the EAEU – Russia – is low. At the same time, India's foreign trade policy is characterized by instability, high differences in customs duty rates depending on the degree to which goods are processed, and a focus on protectionist policies. Comparing the starting conditions of liberalization with the results obtained in this specific case study will help better understand the effects of tariff liberalization.

Scientific Discourse in the Field of Bilateral Trade and Economic Cooperation between Russia and India

Issues related to trade ties between India and the EAEU countries remain high on the agenda for both Russian and foreign researchers.

The academic discourse centres on the potential of expanding the economic partnership between Russia and India and the factors that predetermine the possibilities and intensity of its implementation. India is characterized by unpredictable trade policies, contradictory multilateral diplomacy, and a somewhat paradoxical combination of the desire to maintain multilateral contacts amid high trade protectionism and an

ambiguous, “cyclical” attitude towards globalization. Accession to the WTO and reforms to speed up infrastructure development in the electricity, telecommunications, and textile industries (Malyarov 2007; Sinha 2019; Zakharov 2020) have helped expand the country’s export potential, open up the domestic market and ensure greater involvement in global trade. The Modi government’s focus on attracting foreign investment as a key driver of economic growth is paradoxically combined with a high level of trade protectionism, both tariff and non-tariff (Bragina 2015; Zakharov 2020). Political factors also have a noticeable impact on trade cooperation with Russia: India’s concern about improving Russia–China and Russia–Pakistan ties (Zakharov 2018), relations with the United States, and the sanctions policy (Zakharov 2019; Lunev 2020; Denisov, Safranchuk, Bochkon 2020; Galishcheva, Nebolsina 2021).

Experts point to the high potential of cooperation between Russia and India in the energy sector (Shikin, Bhandari 2017) and in information technology (Pant 2017), as well as the prospect of boosting trade in pharmaceutical, chemical and agricultural products. Technological cooperation in defence, the space and energy sectors, information technology, and cybersecurity issues could become new drivers of bilateral cooperation (Zakharov 2017; Konovalova 2017; Valueva, Konovalova 2018). According to Indian researchers, trade integration between India and the EAEU will help increase the volume of mutual trade and investment, expanding access for India’s industry to the markets of the EAEU member states (India EAEU FTA Survey Report 2016). Tariff liberalization within the framework of the FTA can have a positive effect on the dynamics of multilateral trade, especially in industrial and agricultural products. At the same time, experts emphasize the need to consider the difference in the level of development of individual industries in India and the EAEU member states (Singh, Sharma 2017).

Most previous studies were based on a qualitative analysis of trends in mutual trade and foreign trade contracts, as well as on the results of surveys conducted among those involved in foreign economic activity in India and the EAEU member states. This is a new area of research and, as such, the assessment of the effects of EAEU integration with India, based on the results of econometric analysis, remains underdeveloped in the scientific literature (Likhacheva, Kalachigin 2018). This article seeks to fill the existing gap, quantify the potential effects of tariff liberalization and the extent of its impact on the nature of bilateral trade, and compare the resulting estimates with the initial conditions of mutual trade and the specific features of the foreign trade policy of the countries involved.

Mutual Trade Patterns and Strategic Priorities

Relations between Russia and India are seen as privileged and go back a long way. The Soviet Union was the first nation to announce a diplomatic mission to India, doing so before India gained independence in 1947. Preferential loans and raw materials provided by the Soviet Union on a barter basis were used to implement industrialization programmes and finance the development of the military space sector and the nuclear power industry. Some state-owned Indian companies with a strong global standing,

such as Bharat Heavy Electricals Limited (BHEL), Oil and Natural Gas Corporation (ONGC) and Hindustan Aeronautics Limited (HAL), as well as the entire steel industry, were established in cooperation with the Soviet Union (Nivedita Das Kundu 2016).

Today the share of mutual trade in the foreign trade turnover of both countries is small: Russia accounts for a tiny 0.54% of India's foreign trade, while India accounts for just 0.61% of Russia's trade turnover. Russia–India trade saw its fastest growth in 2017 and 2018 (by 21.4% and 17.3%, respectively), reaching USD 11.23 billion in trade in goods and USD 1.34 billion in trade in services in 2019 (see Table 1).

Russia's trade with India has traditionally been in surplus. However, the surplus in merchandise trade decreased due to faster import growth in 2019 and a relatively smaller decline compared to the volume of Russian exports during the pandemic, while the bilateral surplus in services trade was steadily on the rise.

The top place in the structure of domestic exports is occupied by mineral products, with their share growing steadily before the outbreak of the COVID-19 pandemic, while the share of machinery and equipment shrank from 39.2% in 2009 to 20.8% in 2019 (Table 2). It has not been possible to diversify the raw materials component of exports: Russian metal producers lag far behind suppliers from China, Japan, South Korea and the United States, and the share of metals in the structure of Russian exports is shrinking gradually.

Table 1. Trends in mutual trade in goods and services between Russia and India, 2009–2020

| | 2009 | 2012 | 2014 | 2017 | 2018 | 2019 | 2020 |
|---|-----------|------------|-----------|-----------|------------|------------|-----------|
| Trade in goods | | | | | | | |
| Russia's exports to India, USD m | 5937 | 7,566.693 | 4,395.697 | 6,455.535 | 7,752.309 | 7,308.101 | 5,798.193 |
| Russia's imports from India, USD m | 1,524.455 | 3,041.318 | 3,170.707 | 2,902.422 | 3,224.629 | 3,921.794 | 3,457.947 |
| Total turnover, USD m | 7,461.455 | 10,608.011 | 7,566.404 | 9,357.957 | 10,976.938 | 11,229.895 | 9,256.14 |
| Russia's trade balance, USD m | 4,412.545 | 4,525.375 | 1,224.99 | 3,553.113 | 4,527.68 | 3,386.307 | 2,340.246 |
| Russia's trade balance, % to exports | 74.32 | 59.81 | 27.87 | 55.04 | 58.40 | 46.34 | 40.36 |
| Russia's share in India's trade turnover, % | 0.34 | 0.39 | 0.41 | 0.39 | 0.39 | 0.49 | 0.54 |
| India's share in Russia's trade turnover, % | 0.32 | 0.36 | 0.4 | 0.5 | 0.47 | 0.59 | 0.61 |
| Trade in services | | | | | | | |
| Russia's exports to India, USD m | 422.8 | 865.6 | 643.5 | 663.3 | 593.9 | 924.914 | 752.894 |
| Russia's imports from India, USD m | 217.9 | 335.1 | 437.7 | 432.1 | 407.546 | 416.276 | 220.751 |
| Total turnover of services, USD m | 640.7 | 1,200.7 | 1,081.2 | 1,095.4 | 1,001.446 | 1,341.19 | 973.645 |
| Balance of services of Russia, USD m | 204.9 | 530.5 | 205.8 | 231.2 | 186.354 | 508.638 | 532.143 |
| Balance of services of Russia, % to exports | 48.46 | 61.29 | 31.98 | 34.86 | 31.38 | 54.99 | 70.68 |

Source: Trade Map. International Trade Centre Database. URL: <https://www.trademap.org/> (accessed: 19.07.2021)

Table 2. Sectoral breakdown of Russia's commodity exports to India, 2009–2020, %

| | 2009 | 2012 | 2014 | 2017 | 2018 | 2019 | 2020 |
|---|-------|-------|-------|-------|-------|-------|-------|
| Food products (01–24) | 0.83 | 1.86 | 1.45 | 2.44 | 0.86 | 3.19 | 6.86 |
| Mineral products (25–27) | 7.46 | 4.06 | 7.86 | 24.71 | 24.81 | 31.27 | 19.45 |
| Chemical products (28–38) | 15.02 | 16.98 | 13.86 | 7.49 | 7.53 | 7.63 | 13.30 |
| Plastics and articles thereof (39–40) | 0.98 | 0.98 | 2.98 | 3.75 | 4.06 | 4.04 | 4.05 |
| Raw hides, leather and furs (41–43) | 0.01 | 0.00 | 0.10 | 0.18 | 0.12 | 0.11 | 0.06 |
| Wood and articles of wood (44–49) | 2.45 | 2.69 | 5.75 | 5.95 | 5.12 | 6.10 | 4.21 |
| Textiles and textile articles (50–63) | 0.22 | 0.21 | 0.50 | 0.26 | 0.28 | 0.21 | 0.09 |
| Pearls, precious and semi-precious stones, silver ...(71) | 2.17 | 9.91 | 25.34 | 16.01 | 13.88 | 10.48 | 15.14 |
| Base metals and articles of base metal (72–83) | 11.04 | 9.66 | 7.34 | 4.41 | 4.08 | 4.14 | 6.09 |
| Machinery and equipment (84–90) | 39.22 | 45.98 | 34.34 | 18.69 | 24.29 | 20.81 | 19.10 |
| Other goods | 20.6 | 7.67 | 0.5 | 16.10 | 14.97 | 12.02 | 11.66 |

Source: Author's calculations based on Trade Map. International Trade Centre Database. URL: <https://www.trademap.org/> (accessed: 19.07.2021)

Table 3. Sectoral breakdown of Russia's commodity imports from India, 2009–2020, %

| | 2009 | 2012 | 2014 | 2017 | 2018 | 2019 | 2020 |
|---|-------|-------|-------|-------|-------|-------|-------|
| Food products (01–24) | 23.65 | 18.61 | 21.03 | 23.02 | 21.50 | 18.28 | 18.20 |
| Mineral products (25–27) | 0.44 | 0.60 | 0.61 | 0.39 | 0.36 | 0.59 | 0.50 |
| Chemical products (28–38) | 36.33 | 31.13 | 27.77 | 31.06 | 27.37 | 27.56 | 30.01 |
| Plastics and articles thereof (39–40) | 2.41 | 3.15 | 2.90 | 3.10 | 3.27 | 2.98 | 3.29 |
| Raw hides, leather and furs (41–43) | 1.01 | 1.24 | 1.39 | 1.65 | 1.82 | 1.55 | 1.40 |
| Wood and articles of wood (44–49) | 0.39 | 0.21 | 0.29 | 0.15 | 0.18 | 0.35 | 0.36 |
| Textiles and textile articles (50–63) | 10.31 | 8.91 | 12.07 | 10.63 | 9.22 | 6.80 | 6.54 |
| Footware (64) | 0.82 | 1.47 | 1.67 | 2.38 | 1.95 | 1.63 | 1.51 |
| Pearls, precious and semi-precious stones, silver ...(71) | 0.66 | 0.91 | 4.75 | 0.49 | 0.94 | 1.15 | 1.10 |
| Base metals and articles of base metal (72–83) | 4.21 | 8.02 | 6.60 | 6.20 | 5.88 | 5.77 | 6.96 |
| Machinery and equipment (84–90) | 17.59 | 23.92 | 18.77 | 18.20 | 25.26 | 31.51 | 27.48 |
| Other goods | 0.49 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |

Source: the author's calculations based on Trade Map. International Trade Centre Database. URL: <https://www.trademap.org/> (accessed: 19.07.2021)

Russia's imports from India are dominated by chemicals, which account for more than 30% of the total flow of goods. Second is machinery, equipment and vehicles, accounting for 27.5% in 2020 (a record 31.5% was recorded in 2019), followed by food products and agricultural raw materials (see Table 3). India accounts for a large share of Russian imports of leather goods, tea, tobacco, semi-precious stones, diamonds, pharmaceuticals, and organic chemicals (up to 70% for some items).

Bilateral trade between Russia and India is characterized by relatively high complementarity. India has traditionally been a major supplier of pearls, precious and semi-precious stones and metals, raw materials, and chemical products (pharmaceuticals and organic chemical compounds), and depends on supplies of primary sector goods – coal and crude oil, along with strategically important defence and power en-

gineering products. For its part, Russia is more than 60% dependent on the export of mineral fuel, while at the same time being a major supplier of weapons and actively pursuing projects to build nuclear reactors abroad.

The attractiveness of the Indian market is determined by its high capacity, combined with its large population, high economic growth rates, and a rapidly expanding middle class (Arapova 2018).

As part of the strategic and privileged nature of the bilateral partnership, Russia is increasing its supplies of mineral fuel (coal, oil and natural gas) to India, and seeks to diversify the raw materials component of its exports through a potential increase in the supply of ferrous metals, copper and aluminum. Cooperation is expanding in nuclear power, exports of weapons, space and power engineering products are growing, and there is potential for greater cooperation in shipbuilding.

Russian exports are dominated by minerals. At the same time, India's demand for mineral fuels is increasing, despite the negative growth rates of the global supply. Russia supplies liquefied natural gas to India as part of the Sakhalin-1 and Sakhalin-2 projects. Plans are being studied to extend the Power of Siberia gas pipeline from Russia via China to South Asia. And Russia's RosGeo and Sevmorneftegeofizika (SMNG) are conducting marine seismic surveys on the Indian continental shelf together with India's Oil and Natural Gas Corporation (ONGC).

India is focused on accelerated industrialization and the development of hi-tech industries: doubling the growth rate of the industrial sector by 2022 and introducing advanced Industry 4.0 technologies (Strategy for New India 2018), which requires a significant increase in fuel and metals supplies.

India has overtaken Russia, the United States and Japan in terms of ferrous metals production, climbing to second place behind China. However, the lack of investment and relatively low labour productivity are forcing an increase in metal imports in order to meet the skyrocketing demand. Similar problems, combined with a lack of technology and relatively poor infrastructure, result in higher costs and longer times for steel production, which can make imported purchases much more profitable.

Another challenge for India's industrial development is the shortage of coal, which has become a key import item. Although India is the world's second-largest coal producer, high consumption made it the second largest coal importer after Japan by 2019. Despite the sharp decline in coal consumption and imports on the back of the pandemic and high hydropower generation, India still remains in the top three in terms of imports, second only to Japan and China (IEA 2020). The main suppliers include Australia, Indonesia and South Africa, but with a more liberal trade regime, Russia has a good chance to ramp up its coal exports to India and expand its investment partnership in this area.

Russia and India are actively cooperating on nuclear energy. In 2014, the parties signed a roadmap Strategic Vision for Strengthening Cooperation in Peaceful Uses of Atomic Energy between India and Russia. This document served as the basis for the

project to build the Kudankulam Nuclear Power Plant, which began construction of Unit 5 in June 2021. In an effort to reduce its reliance on fossil fuels, India plans to triple its nuclear capacity by 2024.

The defence industry remains a key driver of Russian exports to India. According to the Stockholm International Peace Research Institute, India accounts for 23% of Russian exports of arms and military equipment, or 49% of India's total arms imports. That notwithstanding, this figure has decreased in recent years (from 70%), due to a drop in purchases, while the imports of weapons from Israel, Germany and the United States have continued to grow steadily (SIPRI 2021). 2015 proved to be a record year for the supply of Russian arms to India, with India purchasing arms to the tune of USD 4 billion from Russia (accounting for just under 25% of Russia's total arms exports) and signing contracts for the delivery of Mi-18 helicopters, BMP-2K armoured personnel carriers and other military equipment.³ In 2018, contracts were signed for the supply of S-400 systems, Project 11356 frigates and a batch of munitions worth an estimated USD 14.5 billion; negotiations are underway for the supply of MiG-29 and Su-30MKI fighters.

In recent years, however, trade relations between the two countries have deteriorated amid sanctions pressure from the United States. After Russia's flagship arms trading company, Rosoboronexport, came under OFAC sanctions, Indian banks froze credit lines to Russian defence companies and all deals were suspended as a result (this affected payments under arms supply agreements between the two countries worth USD 2 billion).

Nevertheless, the mutual interest in expanding trade ties prompts the parties to look for ways to minimize risks and ensure that the contracts that have already been concluded are honoured. The governments are negotiating with banks that are ready to carry out transactions under foreign trade contracts (with Indian Bank and Vijaya Bank as potential counterparties from the Indian side, and Sberbank from the Russian side).

In 2018, Russia and India signed the first and largest rouble-denominated contract for the S-400 Triumf surface-to-air missile (SAM) system, worth approximately USD 5 billion, or more than 330 billion roubles. Rosoboronexport also signed a series of contracts on military and technical cooperation at the Aero India 2019 international aerospace and defence exhibition. India's order portfolio for Russian military hardware stands at USD 10 billion.

The strategic priorities of India's industrial development agenda and Russia's interest in increasing the surplus of the bilateral balance and building up technological exports could drive the negotiation process to establish a free trade zone between the

3 "Joint Russian-Indian statement on the Results of the Official Visit to the Russian Federation by Narendra Modi, Prime Minister of the Republic of India, 'Through trusting relations to new horizons of cooperation,' President of Russia, December 24 2015, <http://kremlin.ru/supplement/5050>.

EAEU and India. However, the potential terms of the agreement are largely determined by the likely effects of tariff liberalization. With its chronically negative trade balance, India, like Russia, has a keen interest in stepping up its exports, so the country will focus on expanding its own export opportunities while keeping the entry barriers to its market in place, as much as is feasible, while implementing an integration scenario.

Tariff Protectionism in India

Among developing Asian countries, India has one of the highest levels of tariff protectionism, which it continues to increase steadily. The average level of most favoured nation (MFN) customs duty rates reached 17.6% by 2019, up from 13.4% in 2016 (see Chart 1).

The highest rates of customs duties apply to agricultural products: beverages (including tea and coffee), sugar and cereals, vegetable oils and dairy products (see Table 4). The average level of customs duties is over 100% for food, around 33% for vegetables, and 30% for livestock products. These are the commodity categories that have the greatest elasticity of Indian imports in terms of customs duty rates.

2018 and 2019 were marked by a sharp increase in import duties for vehicles and components, as well as minerals and metals, including petroleum products, which are a key item of Russia's exports to India. In 2020, India slightly lowered its customs duties, but this is more of a short-term move aimed at stimulating foreign trade in the face of the COVID-19 pandemic rather than a measure consolidating the overall course towards foreign trade liberalization.

In the context of growing tariff protectionism, concluding a free trade agreement could become an important lever to encourage exports to India from the EAEU countries, primarily from Russia, and increase the presence of Russian exporters in the Indian market, including by forcing out competitors, which will be subject to the MFN trade regime.

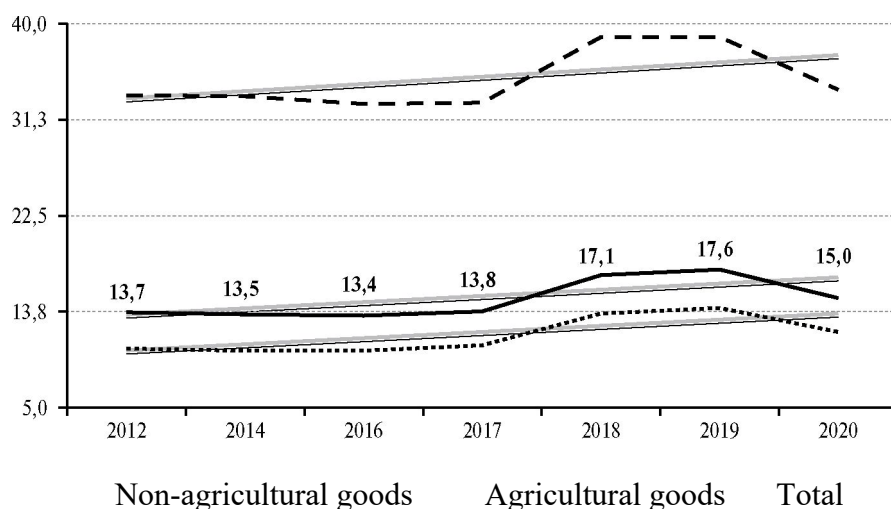


Chart 1. Tariff protection trends in India, 2012–2020, %

Source: WTO World Tariff Profiles 2013–2021.

Table 4. Evolution of the average level of India's customs duty rates under the MFN regime, broken down by commodity, %

| | 2012 | 2014 | 2016 | 2018 | 2019 | 2020 |
|-------------------------------------|------|------|------|------|------|------|
| Animal products | 31.1 | 31.1 | 31.1 | 32.5 | 32.5 | 30.8 |
| Dairy products | 33.5 | 33.5 | 33.5 | 34.8 | 35.7 | 35.7 |
| Fruits and vegetables | 31 | 30.8 | 29.4 | 32.4 | 33.2 | 30.2 |
| Tea, coffee | 56.3 | 56.3 | 56.3 | 56.3 | 56.3 | 56.3 |
| Grains | 31.3 | 31.3 | 31.3 | 37.1 | 37.1 | 32.9 |
| Fats and oils | 37.4 | 37 | 35.1 | 54.1 | 52 | 33.9 |
| Sugar | 35.9 | 35.9 | 35.9 | 51.5 | 51.5 | 50.9 |
| Drinks and tobacco | 69.1 | 69.1 | 68.6 | 74.7 | 74.7 | 75.8 |
| Cotton | 6 | 6 | 6 | 26 | 26 | 6.0 |
| Other agricultural products | 22.5 | 22.4 | 22.3 | 29 | 29 | 22.8 |
| Fish and seafood | 29.9 | 29.9 | 29.9 | | 30 | 29.9 |
| Mineral products and metals | 7.6 | 7.6 | 8.2 | 11 | 11.2 | 8.9 |
| Oil | 4.9 | 4.9 | 4.2 | 9.2 | 9.2 | 3.7 |
| Chemical products | 7.8 | 7.9 | 7.9 | 10.1 | 10.2 | 8.1 |
| Lumber | 9 | 9 | 9 | 10 | 10 | 10.2 |
| Textiles | 13.5 | 12 | 11.7 | 20.7 | 22.3 | 13.9 |
| Clothing | 14.1 | 12.5 | 12.3 | 20.5 | 23.9 | 21.5 |
| Footwear and leather | 10.2 | 10.1 | 10.1 | 12.1 | 13.1 | 13.7 |
| Non-electrical engineering products | 7.3 | 7.1 | 7.1 | 7.8 | 8.1 | 7.8 |
| Electric products | 7.3 | 7.3 | 7.3 | 8.8 | 9.1 | 9.3 |
| Vehicles | 21.2 | 21.7 | 19.3 | 31.1 | 31.2 | 25.3 |
| Industrial goods | 8.8 | 8.8 | 8.8 | 11.1 | 11.1 | 11.4 |

Source: Compiled by the author on the basis of WTO World Tariff Profiles 2013–2021.

Research Methodology and Data

This study is based on SMART partial equilibrium modeling tool, which was developed back in the 1980s by experts at UNCTAD and the World Bank to quantify the effectiveness of the General Agreement on Tariffs and Trade (GATT).

This model makes it possible to quantify changes in import flows in response to trade policy shocks through the effect on the commodity price index and the relative prices of substitute goods (Plummer, Cheong, Hamanaka 2010). The partial equilibrium model identifies direct effects of a trade shock in one market and indirect effects in other markets, and side effects are ignored. However, to assess the effects of tariff liberalization within integration blocs, especially in Asia and Africa, the SMART model is widely used by experts at the WTO (Piermartini, Teh 2005), the Asian Development Bank (Cheong 2010), the UN Economic Commission for Africa (ECA) (Lang 2006)

and national research centres, in particular the Centre for WTO Studies at the Indian Institute of Foreign Trade (Choudhry, Kallummal, Varma 2013) and the African Trade Policy Centre (Karingi, Oulmane, Lang 2005).

The advantage of the model is the availability of the data set required for the calculation (trade flows, import duty rates, import demand elasticity and elasticity of substitution) and the results are obtained at a high disaggregated level (Plummer, Cheong, Hamanaka 2010). In addition, the SMART model, being part of the World Integrated Trade Solution, allows the calculation of two types of trade effects of tariff liberalization in accordance with the generally accepted classification of the effects by the World Bank and UNCTAD (Amjadi et al. 2011), based on the terminology introduced by Jacob Viner (Viner 1961):

trade creation effect – increased demand for imports from the partner country due to lower tariff rates;

trade diversion effect – redirection of import flows from traditional trading partners in favour of countries with lower customs duties.

The model allows us to estimate not only the effects in those countries that are subject to tariff liberalization, but also in third states, as well as to predict possible changes in the market structure and the potential benefits and costs of all participants in international trade.

The basic assumptions of the WITS-SMART model are as follows:

The Armington assumption (Armington 1969) about the optimization by consumers of their own demand and the substitution of domestic goods for imported ones under conditions of changes in their quality and price.

The elasticity of export supply is assumed to be 99 (i.e., the sensitivity of export supply to changes in the export price is at a maximum).

The elasticity of import substitution is assumed to be 1.5, implying that similar goods from different countries are imperfect substitutes.

The base year (the starting point for calculating the effects of tariff liberalization) is 2019.

The effect of trade creation is calculated using the formula:

$$TCE_{ijn} = \frac{M_{ijn} * \pi * \Delta T_{ijn}}{((1 + T_{ijn}) * (\pi/\omega))}$$

where TCE_{ijn} is the effect of trade creation with respect to product n imported by country i from country j ; M_{ijn} is the volume of imports of product n of country i from country j ; π is the elasticity of import substitution in the importing country; T_{ijn} is the value of the import tariff for product n levied by country i on imports from country j ; ω is the elasticity of exports.

The trade diversion effect for countries that are not affected by a trade shock (change in tariff policy) is calculated according to the formula:

$$TDE_{ikn} = \frac{M_j * M_{row} \left(\left(\frac{1 + T_{new}}{1 + T_{base}} \right) - 1 \right) * \lambda}{M_j + M_{row} + M_{row} \left(\left(\frac{1 + T_{new}}{1 + T_{base}} \right) - 1 \right) * \lambda}$$

where TDE_{ikn} is the effect of trade diversion for product n imported by country i from country k ; M_j is the volume of imports from integration partner country j ; M_{row} is total imports from other countries; T_{new} is a new level of customs duty rates; T_{base} is the basic level of customs duty rates; λ is the elasticity of substitution. The total trade effect of the integration scenario is the sum of the effects of trade creation and diversion.

Based on calculations using the SMART model, this study estimates the potential increase in bilateral trade flows in the case of a one percent reciprocal linear reduction in customs duty rates by Russia (as part of the EAEU) and India. In contrast to studies relying on the partial equilibrium model but based on the assessment of trade effects resulting from the mutual zeroing of customs duties (Kofner 2020), such an approach allows us to model liberalization scenarios of different depths, assess both general and annual effects of tariff liberalization, and form the basis for a negotiating position and the subsequent assessment of effects based on the results of the agreements reached.

The calculations are based on the UNCTAD TRAINS database,⁴ which contains information on the volumes of foreign trade flows and customs duty rates for various product categories that apply to individual foreign trade partners.

Assessment of Potential Trade Effects

The results confirm the conclusions of several authors (Nenci 2011; Feenstra 2003; Peters 2002; Salvatore 2013; Ebrill et al. 1999) that the effects of tariff liberalization depend on: (1) the intensity of bilateral trade; (2) the current level of tariff regulation; and (3) the level of sectoral competitiveness.

Given the low share of bilateral trade between Russia and India, the average elasticity of Russian exports with regard to the rates of customs duties applied by India is relatively low: their symmetrical one-percent reduction will cause exports to grow by only 0.16%. In absolute terms, supplies of diamonds, coal and sunflower oil will grow the most (see Table 5).

Diamonds – Russia's traditional key export item – accounted for over 8% in 2019 (the third-largest export category). A potential increase in export revenues will be ensured, among other things, by forcing Belgian and UAE producers out of the Indian market. Hard coal is in second place (almost 14%). Russia currently accounts for almost half of India's imports, but demand for coal in India is set to grow (see above), and the implementation of the integration scenario is expected to strengthen the posi-

⁴ UNCTAD. Trade Analysis Information System (TRAIS). URL: <https://databank.worldbank.org/reports.aspx?source=UNCTADTrade-Analysis-Information-System-%28TRAIS%29> (accessed: 08.08.2021).

tion of Russian exporters in the Indian market and boost export revenues, thanks both to rising demand for Russian coal, and to the ousting of Australian, Indonesian and South African competitors from the Indian market.

Table 5. Trade effects for Russian exports if India cuts import duty rates by 1%

| | Total trade effect, thousand USD | Trade creation effect, thousand USD | Trade deviation effect, thousand USD | Basic weighted average customs duty rates, % | New level of customs duty rates, % | Russian exports in 2019, thousand USD | Growth in percentage, % |
|--|----------------------------------|-------------------------------------|--------------------------------------|--|------------------------------------|---------------------------------------|-------------------------|
| Total | 1,1391.4 | 7362.13 | 4,029.21 | 27.906 | 27.627 | 7,308,101 | 0.16 |
| Animal products (01–05) | 9.041 | 7.781 | 1.26 | 30 | 29.7 | 288 | 3.14 |
| Vegetable products (06–14) | 489.699 | 206.999 | 282.701 | 43.08 | 42.64 | 69,141 | 0.71 |
| Sunflower oil (1512) | 2,245.47 | 1,164.99 | 1,080.47 | 100 | 99 | 163 325 | 1.37 |
| Prepared foodstuffs (16–24) | 15.668 | 11.622 | 4.045 | 139.33 | 137.94 | 538 | 2.91 |
| Mineral products (25–27), including | 1,487.97 | 1,068.96 | 419.007 | 3.80 | 3.76 | 2,284,917 | 0.07 |
| Asbestos (2524) | 169.533 | 137.797 | 31.735 | 10 | 9.9 | 86 ,845 | 0.20 |
| Hard coal (2701) | 871.429 | 608.733 | 262.695 | 2.5 | 2.47 | 641,297 | 0.14 |
| Chemical products (28–38), including | 1,953.69 | 1,558.2 | 395.497 | 6.2661 | 6.2058 | 557, 312 | 0.35 |
| Phosphinates, phosphonates and phosphates (2835) | 458.768 | 447.216 | 11.552 | 7.5 | 7.43 | 20,880 | 2.20 |
| Nitrogenous fertilizers (3102) | 278.685 | 216.689 | 61.996 | 5 | 4.95 | 65,656 | 0.42 |
| Potassic fertilizers (3104) | 195.642 | 96.1 | 99.543 | 7.5 | 7.43 | 103,976 | 0.19 |
| Fertilizers (3105) | 712.461 | 643.828 | 68.633 | 5 | 4.95 | 174,862 | 0.41 |
| Plastics and articles thereof (39–40), including | 516.682 | 242.703 | 273.978 | 8.9707 | 8.8831 | 295,345 | 0.17 |
| Polymers of vinyl chloride (3904) | 207.366 | 106.357 | 101.009 | 7.5 | 7.43 | 80,330 | 0.26 |
| Polyamides (3908) | 138.524 | 58.413 | 80.11 | 10 | 9.9 | 61,187 | 0.23 |
| Synthetic rubber (4002) | 155.817 | 71.802 | 84.015 | 10 | 9.9 | 127 388 | 0.12 |
| Raw hides, leather and furs (41–43) | 110.413 | 99.058 | 11.354 | 10 | 9.9 | 7,751 | 1.42 |
| Wood and articles of wood (44–49), including | 1,190.76 | 867.729 | 323.027 | 9.83 | 9.73 | 446,149 | 0.27 |
| Wood (4409) | 146.895 | 142.57 | 4.324 | 10 | 9.9 | 4,730 | 3.11 |
| Newsprint (4801) | 543.132 | 305.911 | 237.221 | 10 | 9.9 | 247,454 | 0.22 |
| Kraft paper (4804) | 157.774 | 149.038 | 8.736 | 10 | 9.9 | 4,634 | 3.40 |
| Printed matter (4911) | 242.251 | 207.886 | 34.365 | 10 | 9.9 | 1,753 | 13.82 |
| Textiles and textile a (50–63) | 43.241 | 16.731 | 26.507 | 18.74 | 18.55 | 15,436 | 0.28 |
| Diamonds whether or not worked (7102) | 1,723.5 | 1,061.43 | 662.07 | 10 | 9.9 | 593,071 | 0.29 |
| Silver (7106) | 568.825 | 356.441 | 212.384 | 12.5 | 12.38 | 172, 579 | 0.33 |

Table 5 continued

| | Total trade effect, thousand USD | Trade creation effect, thousand USD | Trade deviation effect, thousand USD | Basic weighted average customs duty rates, % | New level of customs duty rates, % | Russian exports in 2019, thousand USD | Growth in percentage, % |
|--|----------------------------------|-------------------------------------|--------------------------------------|--|------------------------------------|---------------------------------------|-------------------------|
| Base metals and articles of base metal (72–83), including | 587.14 | 399.247 | 187.889 | 8.83 | 8.74 | 302,765 | 0.19 |
| Semi-finished products of iron or non-alloy steel (7207) | 120.27 | 105.63 | 14.64 | 10 | 9.9 | 0 | |
| Flat-rolled products (7225) | 83.275 | 36.4 | 46.875 | 8.75 | 8.66 | 54,463 | 0.15 |
| Beryllium, chromium, germanium, vanadium, gallium, hafnium, indium, niobium (columbium), rhenium, thallium and articles of these metals (8112) | 101.159 | 97.232 | 3.927 | 7.5 | 7.42 | 3726 | 2.71 |
| Machinery and mechanical appliances (84–90), including | 413.741 | 275.921 | 137.813 | 8.71 | 8.62 | 1,520,600 | 0.03 |
| Turbojets (8411) | 2.98 | 2.617 | 0.363 | 7.5 | 7.43 | 281,167 | 0.00 |
| Machinery and industrial equipment (8419) | 0.198 | 0.091 | 0.107 | 8.44 | 8.35 | 165,504 | 0.00 |
| Taps, cocks and valves (8481) | 5.193 | 2.433 | 2.76 | 7.5 | 7.43 | 38,822 | 0.01 |
| Measuring or checking instruments (9031) | 4.746 | 2.131 | 2.615 | 7.5 | 7.43 | 148,189 | 0.00 |
| Other goods | 35.501 | 24.309 | 11.193 | | | | |

Source: Author's calculations based on WITS Simulation Tool SMART. URL: <https://wits.worldbank.org/simulationtool.html> (accessed: 19.07.2021)

The results confirm the dependence of liberalization effects on the basic rates of customs duties (Ebrill et al. 1999; Ahmad et al. 2018). The higher the current level of customs duty rates, the stronger the effects of tariff liberalization.

In relative terms, the greatest benefit from the implementation of the integration scenario will be gained by the Russian exporters of certain agricultural products, primarily sunflower oil, the export of which will grow by 1.37% per year if import duties are reduced by 1%. And this effect will be driven as much by rising demand amid falling prices as it will by squeezing out competitors, primarily those in Ukraine and Argentina. Due to high basic rates of customs duties and the relatively higher price elasticity of demand, the export of other types of agricultural goods and finished products can grow faster, but in absolute terms, the potential benefits of exporters are insignificant because the share of these categories in the structure of Russian exports is not high.

As a result of creating a free trade zone, Russian exporters of certain categories of chemical compounds (phosphinates, phosphonates and phosphates, which will see an increase of 2.2%) and fertilizers are expected to benefit significantly. Exports of Russian silver will grow by 0.33% with linear tariff liberalization. Manufacturers of lumber and printing products will also be able to increase their export supplies (by 3.11% and 13.82%, respectively).

Meanwhile, we should not expect an increase in the supply of petroleum products: the relatively low rates of import duties (5–10%), coupled with the consistently low market share occupied by Russian exporters (not more than 1%) bring the potential effects to nothing. The same applies to hi-tech engineering products: the price elasticity of technological exports actually tends to zero, and the competitiveness of products is largely determined by non-price factors.

As follows from the above, the creation of a free trade zone will help strengthen the raw, low-tech orientation of Russian exports to India in the absence of a stimulating effect on engineering products and a very small chance that India will reduce import duty rates on agricultural products and foodstuffs.

The potential increase in Russian imports following the creation of the free trade zone will be significantly lower. A one-percent reduction in duties by the EAEU countries would allow Indian export volumes to increase by no more than 0.1%. In this case, the largest absolute increase in imports will be in medicines, which rank first and account for 15% of Russia's imports from India (see Table 6). Indian exporters of medicines will be able to strengthen their positions in a separate segment of the Russian market, ousting producers from Germany, the United States, Hungary, Switzerland, France and the Netherlands.

Lower import duties could boost demand for Indian stone, gypsum, cement and other products, including by reducing imports from China. At the same time, demand may pick up for leather goods, clothing and textiles, as well as jewellery, which have a relatively higher price elasticity. Indian tea and coffee producers are set to benefit from the creation of the free trade zone: a one-percent decrease in import duty rates by the EAEU countries will expand supplies to the Russian market by an average of 0.16%. Despite the relatively low elasticity of Russian import demand for machinery and equipment from India, their relatively higher share in the structure of domestic imports will provide a comparatively high absolute increase.

The potential effectiveness of a free trade zone between the EAEU and India is due to the relatively high level of protectionism on the part of India with regard to imports from member countries of the integration association. If multilateral negotiations result in agreements on a relatively high quality of integration, including intensive tariff liberalization schedules, the effect of creating a free trade area may be greater.

The effects of tariff liberalization largely depend on the basic level of tariff regulation. On the one hand, the example of a potential EAEU–India free trade zone confirms that low duty rates, limit the possibility of their further reduction and, consequently, the potential for tariff liberalization. On the other hand, lower rates are applied in most cases to raw materials and low-tech goods with low added value and low price elasticity. At the same time, relatively higher customs duties before the implementation of the integration scenario predetermine relatively more significant effects of tariff liberalization and a higher price elasticity of import demand.

A free trade zone could serve as an important tool to reinforce the position of Russian exporters of fertilizers and certain categories of agricultural products in the Indian market, the demand for which is growing rapidly in India. India, in turn, could gain a stronger foothold in the Russian market for medicines, while also increasing the share of textile products, jewellery and certain categories of agricultural products.

The elasticity of various categories of mineral fuels (including hard coal, coke, oil and oil products), which currently account for a significant share of Russian exports, is much lower than that of other commodity categories – certain types of agricultural products, fertilizers and some metals (nickel and silver). Accordingly, in case of a linear, balanced reduction of customs duty rates by India on most Russian export items, and even more so with a relatively stronger tariff liberalization for agricultural products, metals and chemical compounds, Russia has good chances to diversify the commodity structure of its raw material and low-tech exports to India, reducing the share of mineral fuels.

At the same time, tariff liberalization is unlikely to support Russia's exports of more technologically advanced, strategically important mechanical engineering products. The conclusion of contracts for the supply of military equipment, aircraft, or power engineering products is largely conditioned by quality characteristics, degree of reliability, and political will. The importance of the price factor and the effects of tariff liberalization are effectively reduced to zero. Integration effects in this part may turn out to be more indirect, due to the strengthening of a political partnership between the two sides.

In addition, due to the relatively higher price elasticity of Russian exports compared to import flows, symmetrical tariff liberalization will consolidate and expand the positive balance of bilateral trade, which is hardly in India's strategic interests in the context of a chronic trade deficit.

* * *

The potential effects of tariff liberalization within the EAEU–India free trade zone have not actually been studied in the academic literature. At the same time, due to the specific structure of mutual trade and foreign trade policy, this area of analysis is of great interest both in terms of academic discussion on the effects of tariff liberalization and the factors that predetermine them, and from a practical perspective – in order to develop Russia's foreign trade policy.

The following theoretical conclusions were drawn from the analysis, building on previous studies (Krugman 1979; Goldstein and Kahn 1978; Feenstra 1995; Peters 2002; Feenstra 2003; Nenci 2011; Salvatore 2013):

given the low interdependence and intensity of trade flows, the effects of tariff liberalization are limited, and the elasticity of trade flows with respect to customs duty rates is extremely low;

the higher the basic customs duty rates, the potentially higher elasticity of foreign trade flows;

lower-tech goods with relatively low added value and comparable rates of customs duties tend to have a higher elasticity than more technologically advanced machine-building products.

Moscow sees India as one of its key strategic partners in the Asian region. With a traditionally positive trade balance and the demand of Indian importers for Russian heavy engineering products, Russia is interested in expanding strategic cooperation. It was found that the implementation of the integration scenario could give impetus to the expansion of trade cooperation, and the relatively higher price elasticity of Indian imports could determine the outstripping growth of Russian exports over imports, expanding the surplus of bilateral trade for Russia.

India's trade integration with the EAEU may predetermine some changes in the commodity structure of Russian exports, but more towards the diversification of its raw material component, with limited growth in the supply of hi-tech engineering products. Against the background of the low price elasticity of demand for mineral fuels, their share in the structure of Russian exports will shrink. At the same time, coal supplies and, to a lesser extent, metals (aluminum, copper and metal products) are expected to grow.

The only way to achieve more significant results in line with the strategic interests of the Russian economy, as enshrined in the key documents of long-term strategic planning, is to properly formulate a negotiating position. In the field of tariff regulation, the key principles of Russia's negotiating position, which can form the basis of the EAEU's collective position, are as follows:

- reduction and zeroing by India of import duty rates on mineral fuels and metals (primarily copper, aluminum and silver), with a minimal transitional period of tariff liberalization;

- reduction of customs duty rates on organic chemistry products (phosphinates, phosphates, mineral and chemical fertilizers);

- accelerated tariff liberalization of trade in certain categories of engineering products (nuclear reactors and boilers, power engineering products, etc.) and agricultural goods (vegetables, cereals, primarily wheat);

- inclusion of textile products and certain food products (in particular, meat products and vegetables) in the list of sensitive goods for the EAEU member states, implying the establishment of longer transitional periods for reducing import duty rates.

That said, in addition to tariff liberalization, "India's willingness to lower the non-tariff barriers by which these markets are successfully regulated is a key condition, without which the potential benefits of the free trade zone will not be fully realized" (Eurasian Economic Union 2017).

The purpose of this study was to quantify the effects of tariff liberalization resulting from the creation of a free trade zone between the EAEU and India exclusively for Russia, and to identify the terms of the trade deal that best meet the strategic interests of the country. Further research should focus on quantifying the potential effects for the EAEU as a whole, conducting a comparative analysis of the interest of other EAEU

countries in integrating with India, correlating these results with the effects of free trade zones with Singapore and Vietnam. It is important to keep in mind that this study proceeds from an assessment of potential trade effects based solely on factors of mutual economic interest of the two countries in the development of trade integration. A crucial area for further research should be the assessment of foreign policy factors and sanctions trends that constrain the development of multilateral trade dialogue.

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Conflict of interests:

The author declares the absence of any conflicts of interests.

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