Advanced talks with US lower risk of high reciprocal tariffs on India

India and the US are engaged in bilateral talks to address significant import tariff and non-tariff imbalances. Early reports indicate India might reduce tariff duties selectively and explore ways to improve US market access. This, in our view, significantly lowers the risk of a blanket reciprocal tariff on Indian imports

Indian Prime Minister Narendra Modi and US President Donald Trump

Why are reciprocal tariffs important for India?

India looked relatively safe when the first round of tariffs targeted countries with significant trade surpluses with the US. As of 2023, India had a small trade surplus of 1.1% of GDP with the US. However, as trade wars escalate, India came under scrutiny due to high import duties and substantial non-tariff barriers. Here are a few key reasons why India can't ignore the looming threat of reciprocal tariffs:

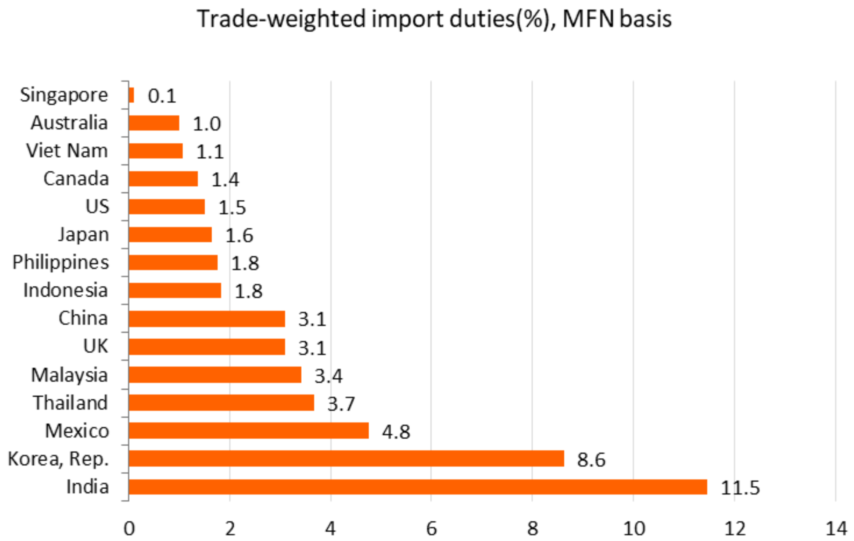
- **Import tariff duties levied by India are the highest in the region** – India's trade-weighted duties on goods imports stand at 11.5%, 10ppt higher than those imposed by the US. On certain goods, such as imported cars, duties can be as high as 100%.

- **Non-tariff barriers** – By value, 47% of India's imports encounter one or more tariff barriers.

Textiles and food products face non-tariff barriers on nearly all items. Though fuel, transportation, metals, and chemicals have fewer non-tariff barriers, they remain significant.

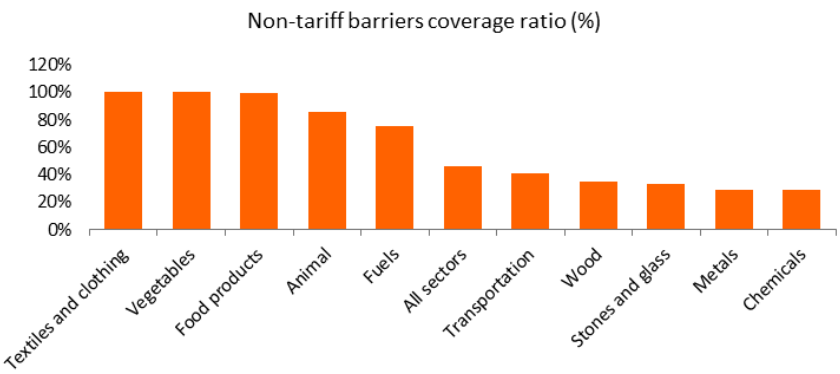
- **India's linkages to global trade are rising** – This is evident in the country's expanding export market share, primarily driven by the electronics sector. The trend remains positive, supported by India capturing a significant portion of FDI inflows into Asia. And being a big beneficiary of supply chain shifts.

Import tariff duties levied by India are the highest in the region



Source: World Bank

Very high non-tariff barriers for textiles, and food products



Source: World Bank

The coverage ratio is calculated by determining the value of imports of each commodity subject to Non-tariff measures, and expressing the value of imports covered as a percentage of total imports

India and US are already negotiating a bilateral trade agreement

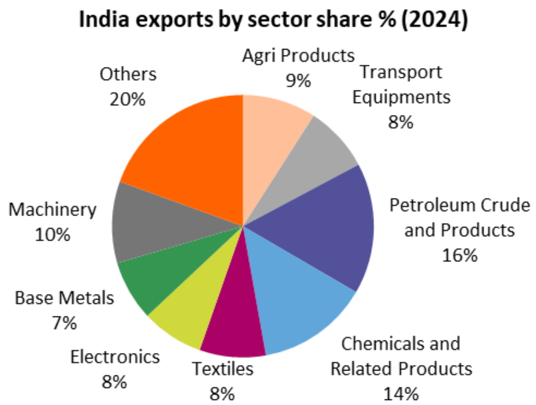
On 5 March, US President Donald Trump highlighted that India's tariffs were high during his

Congressional address and proposed tariffs on pharmaceuticals. Since then, India and the US have been in talks on a broad bilateral agreement ahead of the 2 April deadline on reciprocal tariffs. Official talks began on 26 March. The aim is to reach a deal by autumn this year.

The bilateral deal is likely to focus primarily on issues related to tariff imbalances on goods, while keeping more delicate issues like immigration and exports of IT services out of scope. According to Indian officials, the two governments are actively working to build a framework for the bilateral trade agreement (BTA) which would aim to expand trade, enhance market access, reduce tariff and non-tariff barriers, and deepen supply chain integration. India has already announced plans to eliminate the 6% equalisation levy on digital ads from 1 April, which should benefit tech companies like Google and Meta. It's also actively considering a notable reduction of import duties on certain items.

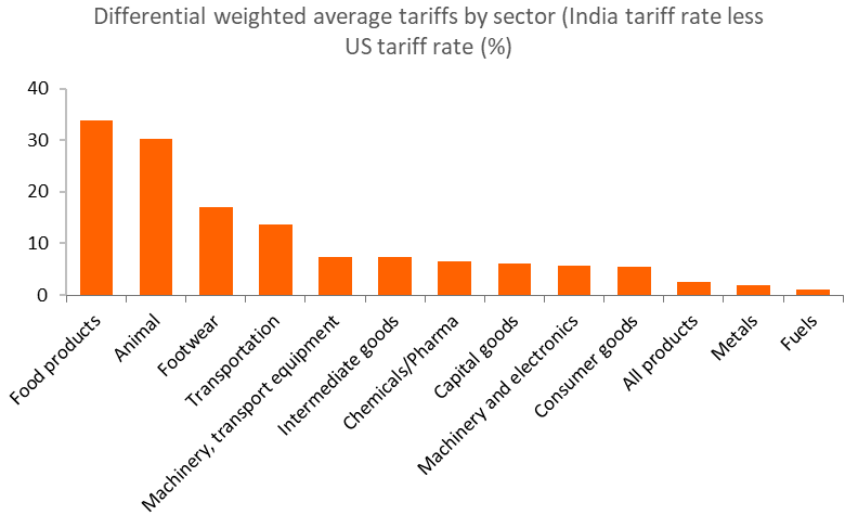
Based on Trump's recent comments, we anticipate that agriculture, pharmaceuticals, textiles, automobiles, and energy – sectors that make up approximately 50% of India's total exports – will be the primary focus. Among these, agriculture has the highest tariff imbalances and faces significant non-tariff barriers from India. Textiles have the fewest imbalances, but still encounter high non-tariff barriers. Pharmaceuticals fall in the middle, having relatively fewer non-tariff barriers. Below, we outline how we think bilateral negotiations in these sectors might unfold.

Almost 50% of India's exports are under the tariff scanner



Source: CEIC

Agriculture product tariff imbalances are the highest



Source: World Bank

The average of effectively applied tariff rates, weighted by the product import shares corresponding to each partner country

Agriculture – higher market access for the US to be a focal point

The agriculture sector faces a significant import duty disparity. India imposes a hefty 40% effective weighted average tariff on food products from the US. The US charges only 6% on Indian imports, creating a substantial differential of around 34%. Reducing tariffs in this sector is particularly challenging, as over half of India's population relies on agriculture for their livelihood. It also remains largely untaxed, making significant policy changes a major political issue.

However, we think there's scope for India to increase market access for US agricultural exports to India. The US is a huge exporter of cotton, corn and soybeans; India imports these commodities, and these three main crops could be around which discussions revolve.

Pharmaceuticals – large export exposure but US constrained by lower cost alternatives

In 2024, 15% of India's total exports to the US were from the pharmaceutical sector. India primarily exports low-cost generic drugs, which have low profit margins, making the potential impact of higher tariffs significant. In contrast, the US mainly exports patented and innovative drugs in which India has lesser competitive advantage. If the US were to match India's 8-10% tariffs on pharmaceuticals, US tariffs would need to increase by 6.5-8.5%, negating India's labour and manufacturing cost advantage. However, this could lead to generic drug shortages in the US, especially at lower costs, at a time when the US government is under budgetary pressure.

Automobiles – reciprocal tariff concessions possible on component exports, in return for greater market access for US autos

Auto trade between the US and India is relatively small, as India doesn't export vehicles to the US. A large part of the trade between the two countries is auto components, where India sells to the US at an import duty of around 1-2% on some but zero percent on most. India, on the other hand, imposes duties across multiple slabs in the range of 5-15% for the components coming from the US.

In FY2023-24, India exported $21.2 billion worth of auto components, with North America accounting for 32% of these exports. If the US were to eliminate the tariff differential and tax auto component imports at a maximum differential of 14-15%, it would cost India $1bn, or 0.03% of GDP. Given the importance of auto components to India's exports, India is likely to sweeten the deal for US imports.

When it comes to car imports, India has a long-standing tradition of protecting its domestic car industry. Reducing some of these duties could enhance efficiency, especially in the green energy sector, to attract higher investments and technical expertise. India recently announced some tariff reductions on electric vehicles (EVs). It also stated it will work towards gradually lowering import duty on auto/car imports. This could pave the way for the likes of Tesla to enter India's market.

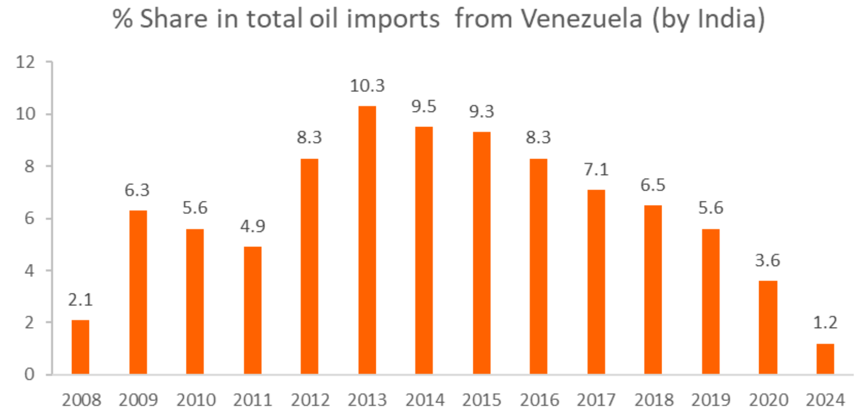
Energy – sanctions on Venezuela oil would increase India's import bill, but not materially

Trump announced a 25% tariff on oil and gas imports from countries purchasing Venezuelan crude, which could have implications for India's energy sector. Crude oil continues to be India's most valuable import, with a dependency of 85%.

India was already an importer of Venezuelan oil before the sanctions (up until 2020), and the country resumed its oil trade with Venezuela in 2024. However, Venezuela's share of total crude oil imports was tiny at 1.2% in 2024 vs the peak of 10% in 2013. After that, it declined steadily.

Last year, Venezuelan crude was on average $15-19 per barrel cheaper than the Indian crude import basket. This means the import bill for India — even at these lower import quantities — could increase by $300-$400m or 0.1% of GDP annually. In the larger scheme of things, India could lose the flexibility to import oil in the most cost-effective way.

Share of Venezuela in total crude oil imports fell to 1.2% in 2024 from a peak of 10% in 2013



Source: Oil ministry, India

Textiles – benefits from low tariff differential, and India's high comparative advantage

Interesting, when it comes to the textiles industry, both the US and India levy similar import duties. Neither country holds a differential advantage in terms of tariffs. This is also the sector where India has a big comparative advantage versus the US, suggesting lower price elasticity and potentially a lesser hit to India's exports.

Overall, while India is in the direct line of fire from Trump's reciprocal tariffs, the launch of bilateral discussions is positive for the country. India is actively considering lowering tariff and non-tariff barriers across sectors. For the US, better access to Indian markets in certain sectors like auto, energy and agriculture, might sweeten the deal further. This should partially offset the imbalance in tariffs and non-tariff barriers that India has with the US.

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