

Indo China Trade: Problems and Prospects

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ABSTRACT:

The competitors for the next big economic superpower have seen worsening bilateral ties beginning this year and the recent Ladakh political stand-off has pushed Indo-China trade relations on the worst edge. Boycott Chinese products movements have raged across India after the clash in the Galwan valley. The anti-China sentiment has reinforced the Aatmanirbhar or self-dependent scheme in India. However, is it really possible to boycott Chinese goods that alone accounts for 10% of Indian trade and 30% of Indian trade deficit¹? Is it realistic to boycott a country on whom we are heavily dependent on for many commodities ranging from electronic equipment to pharmaceuticals?

This paper seeks to highlight the trends of Indo-China bilateral trade relations over the past few years and the commodities that India is most dependent for China on. The article then sets forth the measures taken by the Government to reduce Indian dependency on China and sets forth whether it is pragmatic and plausible for India to boycott Chinese goods. The paper lastly puts forth the three approaches available to India at this junction and which one is the most feasible.

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I. INTRODUCTION:

The competitors for the next big economic superpower, India and China, have seen worsening bilateral ties beginning this year with the Indian Government tightening the Foreign Direct Investment norms² and the recent Ladakh political stand-off pushing Indo-China trade relations on the edge. However, the relations between these two Asian giants have not always been one of rivalry or tension.

2,000 years prior to the 1962 Indo-China war, India and China had very strong economic, and cultural relations. The Second Century BC saw the linking of the cities of Xi'an in China and Pataliputra in India through a branch of the interconnected ancient trade routes known as the Silk Road that contributed significantly to growth of these two civilizations. Buddhism travelled to China from India in 67 AD through the silk road and as per a Beijing university scholar Hu Shih, Sixth Century AD was marked by the "Indianization of China." Even through the 1930s and 1940s India and China shared good relations. India supported China in its struggle for Independence by boycotting Japanese products, carrying out marches and sending a medical group to aid Chinese in 1937. Furthermore, India was the second non-Communist country to recognize an independent China in 1950. Although the Indo-China bilateral ties suffered greatly as a result of the 1962 Sino-Indian war, July 2006 saw the opening of the Nathu La Pass that connected Sikkim in India and Tibet in China.³

The process of initiating economic ties again started in 1984 when India and China signed a Trade Agreement that provided both the countries Most Favored Nation Status (MFN). 1992 marked the beginning of full-fledged bilateral ties of India and China. In 1994, these Asian giants signed a Double Taxation Agreement and took initiative to become negotiation partners in ASEAN. The 2003 Bangkok Agreement established trade preferences between India and China and another agreement in the same year initiated open border trade via the Silk Route. India and China's bilateral trade has quadrupled in the past decades.⁴

However, the balance of trade has been increasingly tilting in China's favor. By 2008 China became India's largest goods trading partner. In 2019, bilateral trade between India and China reached a significant high of 95.54 billion dollars with India's trade deficit being 56.77 billion dollars.⁵ The graph below shows the difference in India's exports and imports with China in the past four years.

¹www.indiatv.in Cloud Over India-China Trade Ties: Can India Afford to Boycott China?

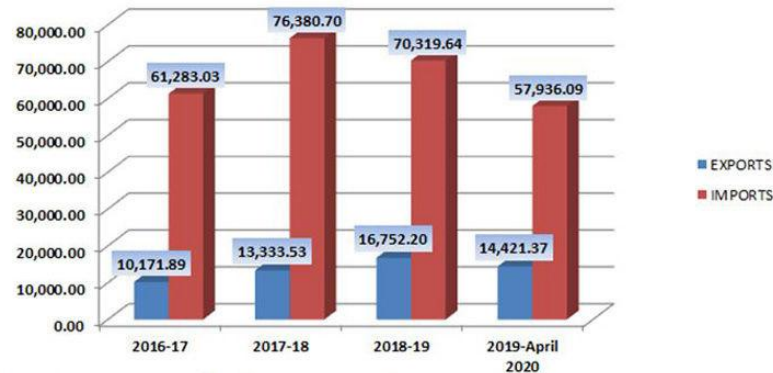
²www.indiatv.in Cloud Over India-China Trade Ties: Can India Afford to Boycott China?

³<https://hbr.org/2007/12/china-india-the-power-of-two>

⁴PHD CHAMBER OF COMMERCE AND INDUSTRY (2018). *India – China Trade Relationship: The Trade Giants of Past, Present and Future*.

⁵<https://www.hindustantimes.com/business-news/govt-plans-to-cut-import-dependence/story-vidPYBME2Wahf1JXldgwhM.html>

INDIA'S EXPORT-IMPORT WITH CHINA LAST 4 YEARS (value in US\$ millions)

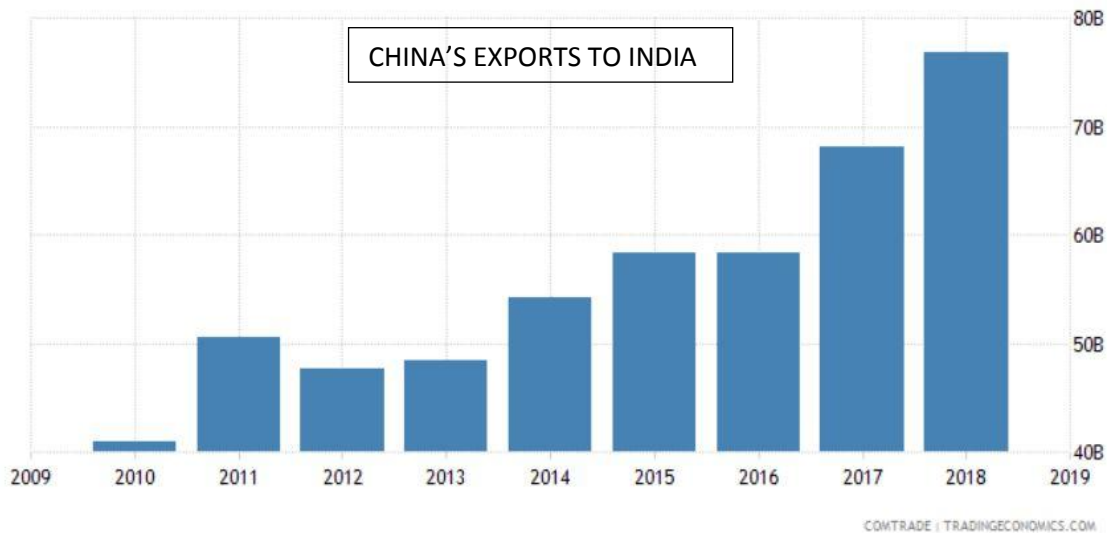


Source - Trade statistics, ministry of commerce and industry, govt. of India

As can be seen in the graph, in the financial year 2019-20, China alone accounted for 10% Indian trade and 30% of India's trade deficit. India imported \$70.32 billion from China and exported only \$16.75 to China in the financial year 2019-20. Thus, the trade balance in China's favor in the year 2019-20 was a massive \$53.57 billion.⁶

The graph below shows the Chinese Exports to India.

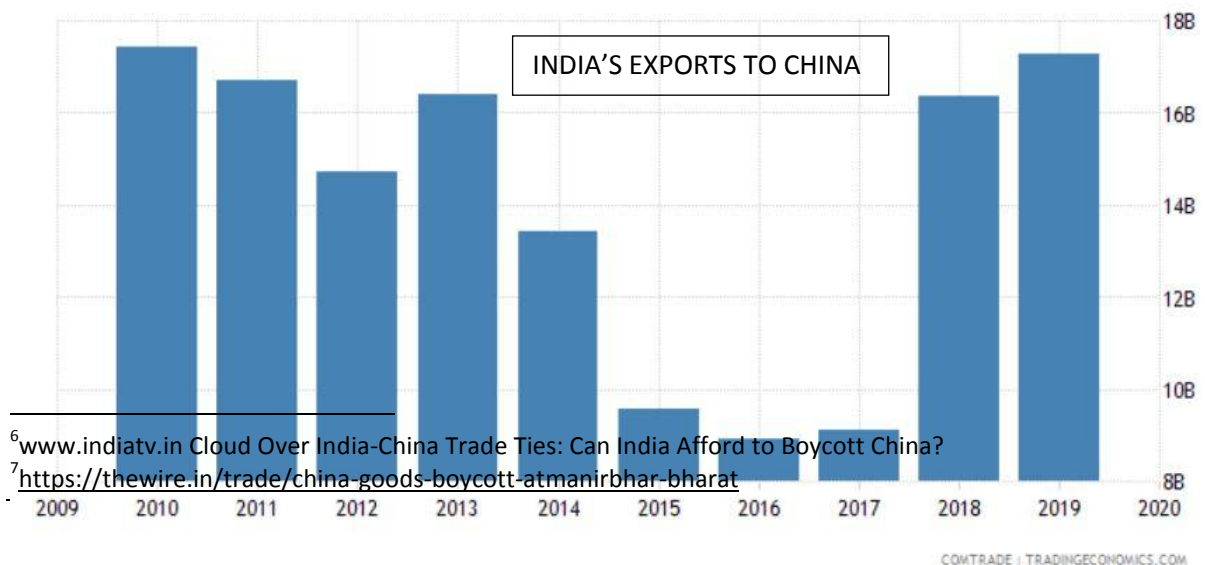
As can be seen by the graph above, the Chinese exports to India have raised significantly from about 41 billion



dollars in 2010 to approximately 76 billion dollars in 2018.

However, the Indian exports to China is nearly seven times lesser.⁷

As can be seen by this graph, India's exports to China have seen no particular trend with the Indian exports in 2018

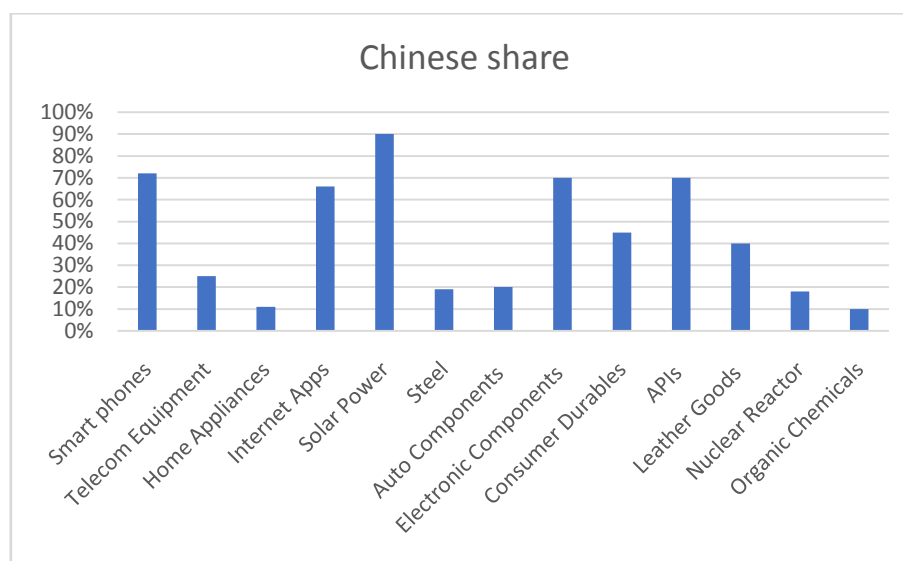


⁶ www.indiatv.in Cloud Over India-China Trade Ties: Can India Afford to Boycott China?

⁷ <https://thewire.in/trade/china-goods-boycott-atmanirbhar-bharat>

being slightly lesser than the exports in 2010.

India is dependent on China for an array of imports ranging from raw materials such as Active Pharmaceutical Ingredients (APIs), and critical components such as Capital goods.⁸ The main goods that India is dependent on China for can be seen in the graph below.



As can be seen in the graph above, 72% of Smart phones, 25% of Telecom Equipment, 11% of Home Appliances, 66% of Internet Apps, 90% of Solar Power, 19% of Steel, 20% of Auto Components, 70% of Electronic Components, 45% of Consumer Durables, 70% of APIs, 40% of Leather Goods, 18% of Nuclear Reactor and 10% of Organic Chemicals are imported by India from China.¹⁰

The graph shows that India is heavily dependent on China for most of its electrical components and essential pharmaceutical goods including antibiotics and drugs that treat tuberculosis and leprosy. India also massively relies on China for consumer durables smart phones and solar power. 60% of the Indian smartphone market, 90% of the Indian toy market and 50% of the Indian bicycle market is dominated by the People's Republic of China. Furthermore, according to a Gateway House report, Chinese techs such as The Alibaba Group and Tencent Holdings have invested \$4 billion in Indian start-ups.¹¹ Studies have also shown that out that Chinese firms invested 29,000 crore rupees in major Indian start-ups such as Paytm, Snapdeal, Ola and Byju's. Out of 30 big Indian start-ups, 18 have Chinese investors.¹² Thus, some major Indian sectors such as solar energy, electronics and pharmaceuticals are heavily dependent on imports from China.

MEASURES TAKEN TO REDUCE IMPORT DEPENDENCY ON CHINA

The call for Aatmanirbhar Bharat or self-reliant India by Prime Minister Modi has been further strengthened by the Galwan valley face-off. The wide trade deficit with China in the financial years ending 2019 and 2020 had already been a concern to the Government. Finance Minister Nirmala Sitharaman had said in her Budget speech that domestic industries were being put at a big disadvantage as a result of the unchecked flow of imports under the Free Trade Agreements (FTAs).

The Indian Government is seeking to reduce import dependency on China by boosting domestic manufacturing and local capacity. The Government is using amalgamation of Make India initiative and Aatmanirbhar Bharat Abhiyan.

⁸<https://www.moneycontrol.com/news/business/moneycontrol-research/how-dependent-is-india-on-china-here-is-what-trade-data-reveals-5346201.html>

⁹ www.indiatv.in Cloud Over India-China Trade Ties: Can India Afford to Boycott China?

¹⁰<https://www.moneycontrol.com/news/business/moneycontrol-research/how-dependent-is-india-on-china-here-is-what-trade-data-reveals-5346201.html>

¹¹<https://thewire.in/trade/china-goods-boycott-atmanirbhar-bharat>

¹² www.indiatv.in Cloud Over India-China Trade Ties: Can India Afford to Boycott China?

The Make in India Campaign started in 2014 by Prime Minister Modi aim at boosting entrepreneurship and establishing India as a global manufacturing hub by developing the manufacturing sector, promoting foreign direct investment and setting intellectual property rights. This campaign aims at increasing the contribution of the Indian manufacturing sector to 25% of the Indian Gross Domestic Product (GDP). Led by the Department of Industrial Policy and Promotion, the Make in India initiative targets developing 25 economic sectors including Information Technology (IT), Automobile and Business Process Management (BPM). This campaign is based on the four pillars of new processes, infrastructure, sectors and mindset. Under new processes, the Government aims at introducing reforms that will help in increasing the ease of doing business and foster new business partnerships that will boost the local economy. The Indian Government targets at establishing industrial corridors and building a trained skilled force that will aid in building a strong manufacturing sector. In order to help the 25 target economic sectors highlighted under the Make in India campaign, the Government has allowed 100% FDI in Railway, Defence and Pharmaceuticals. The Make in India Campaign also aims at shifting the Government's role to facilitator from regulator to aid the economic development with the corporate sector under its pillar of new mindsets. Thus, through all these schemes, the Make in India projects aims at promoting the manufacturing sector and boosting the local economy. The main vision of this campaign is to increase Indian exports. As Prime Minister Modi said in his speech introducing the Make in India campaign, "Come make in India. Sell anywhere, [but] make in India."¹³

Aatmanirbhar Bharat or self-reliant India is based on the five pillars of economy, infrastructure, system, demography and demand. Through this program, the Government aims at curbing the economic impact of COVID-19 pandemic by establishing an economy capable of bringing quantum change, infrastructure that can modernise India, system based on new efficient technology, vibrant demography that can promote self-reliance and effective utilisation of demand to boost the local economy. The main vision of this package is to promote local products, develop cottage, small-scale and home industries, and aid farmers and workforce to establish a self-reliant India. Under this scheme, the Indian Government has implemented several packages that focus on helping Businesses including MSMEs, small and migrant farmers, migrant workers and street vendors.¹⁴

Under the Aatmanirbhar Bharat Abhiyaan, economic support has been extended to small and marginal farmers of the rural economy to help them meet post Rabi and current Kharif financial requirements through approval of 63 lakh loans, extension of refinance support by NABARD of Rs 30,000 crores to RRBs and Rural Cooperative Banks to help meet crop loans. In context of workers, work is being provided to about 2.33 crore wage seekers besides increase in the average wage rate to Rs. 202 under the MGNREGA scheme. This will help boost employment and help in the development of a skilled workforce for a self-reliant India.¹⁵

Moreover, actions have also been taken to provide economic aid to Indian Micro, Small & Medium Enterprises (MSMEs). Not only the low threshold MSME definitions are being revised with the investment revised upwards but also several other provisions have been made to curb the economic impact on them. These include Rs 3 lakh crores automatic and collateral-free loans, Emergency credit lines from NBFCs and banks upto 20% of outstanding credit as on 29th May, 2020, and Rs 20,000 crores as subordinate debt for those MSMEs that required equity support. Moreover, Rs 50,000 crores Equity will be infused for MSMEs as they face severe Equity shortage through Fund of Funds and Global tenders will not be allowed upto Rs 200 crores to safeguard the Indian MSMEs from foreign competitors. These measures will help to strengthen MSMEs and boost local production.¹⁶

To reduce import dependency on China, the Government of India is also implementing a sectoral strategy that aims to boost India's manufacturing hub and restrict the imports of sub-standard quality products. Under this strategy, the Indian Government is taking measures to create value chains and attain self-reliance in areas including furniture, technical textiles, footwear, defence production, electronics and medical equipment. These sectors will receive fiscal incentives such as credit support and trade safety from cheaper imports, especially Chinese. In order to increase local manufacturing, the Government is also reviewing custom duty exemptions and will strike those off that hurt domestic firms by end of quarter FY-2021. In addition, the Indian

¹³<https://www.makeinindia.com/article/-/v/make-in-india-reason-vision-for-the-initiative#:~:text=new%20processes-,Prime%20Minister%20Narendra%20Modi%20launched%20the%20Make%20in%20India%20initiative,their%20Oproducts%20within%20the%20country.>

¹⁴<https://aatmanirbhar-bharat.com/>

¹⁵Government of India. *Aatmanirbhar Bharat Part II- Poor, including migrants and farmers*. India: Government of India, 2020

¹⁶Government of India. *Aatmanirbhar Bharat Part I- Businesses including MSMEs*. India: Government of India, 2020

Government is planning to implement the policy of several developed countries that stress on big industries having to use domestically produced raw materials like steel. This will not only boost local economy but also help in curbing sub-standard steel and steel products. In this context, the ministry has urged state-run to use local iron and steel products.¹⁷

In addition, the Government has put technical regulations including quality and safety standards on about 370 products to restrict low quality Chinese imports. This initiative will also help to cut import on non-essential items such as consumer electronics, heavy machinery, telecom goods, food, pharma, fertiliser, and textiles. Other measures to reduce import dependency on China include posing tariff barriers on Chinese imports, attracting investments from Multinational Companies looking for substitute worldwide supply chains except China. Moreover, the Indian Government has made it mandatory to get its approval for foreign investments by India's bordering countries to curb "opportunistic takeovers" of domestic firms. This step will help to restrict Chinese Foreign Direct Investments. Besides, restrictions have also been imposed on import of tyres. Furthermore, to establish India as a global supplier and reduce India's import bill, the commerce ministry has identified 12 economic sectors that will be developed and given a boost including electronics, furniture, textiles, masks, industrial machinery ventilators and food processing and auto parts. As mentioned earlier, India depends on China for 70% of its APIs supply. In order to cut this import dependency, the Government had approved a Rs 13,760 crore package in March to boost local production of medical appliances and bulk drugs and export more of the same. The Government has also set up a project development cell (PDC) in its ministries and departments to encourage investments to India and a group of secretaries under the cabinet secretary.¹⁸

HOW REALISTIC IS IT TO BOYCOTT CHINESE PRODUCTS?

The Ladakh stand-off has created an anti- China sentiment in India and boycott China goods movement have raged across the country. However, while the idea of a self-reliant India is much needed, a realistic blueprint has to be followed to gradually decrease import dependency.

Besides, three important points have to be kept in mind. First, while China accounts for 10% of Indian trade, India accounts for only 2% of China's total exports. Hence, boycotting Chinese goods will not hurt China as much as India. Second, history shows that boycott movements are not successful many times. Examples of this are China's boycott of Japanese goods in 1930s and US consumer forums boycotting French goods in 2003. The reason for all such unsuccessful boycotts is just one: economics resists all restraints perpetuated by emotions and isolationism. Third, India's exports will be sharply hit by a Chinese goods boycott movement since India depends on China for the raw materials for many of its final products that it exports. An apt example of this is India's hydroxychloroquine (HCQ), which was in a great demand as a possible cure for COVID-19, is made from APIs, 70% of which is imported from China. Furthermore, in order to decrease import dependency on China, India will have to come up with alternatives that can overtake Chinese goods in both cost and quality. For this, proper research and development facilities are required. However, according to statistics provided by the National Science and Technology Management Information System (NSTMIS), while R&D expenditure in India increased by three times from 2004-05 to 2014-15, it only remains 0.7% Indian GDP. This is low as compared to the 2% of GDP spent by China in 2015 and 1.2% of GDP spent by Brazil in 2014 on R&D.¹⁹

Therefore, imports have to be reduced in a phased strategy and Indian companies have to be geared technologically and made cost-competitive.²⁰ Concrete initiatives will have to be put in place to make India self-reliant. Simply boycotting Chinese products would not result in indigenisation. The COVID-19 pandemic has already had massive ramifications on the Indian economy. India cannot side-line its economy now due to a political stand-off. In order to curb import dependency, India has to take gradual and not sudden measures that will disrupt supply chains and hurt our economy by creating a time lag.

However, besides producing on one's own or indigenization, there are two other approaches that can be adopted by India to curb its import dependency on China in a quicker and efficient manner. The two ways are either importing from some other country or collaborating with another country in the production of import substitutes at home.

¹⁷<https://www.hindustantimes.com/business-news/govt-plans-to-cut-import-dependence/story-vidPYBME2Wahf1JXldgwhM.html>

¹⁸<https://timesofindia.indiatimes.com/business/india-business/government-working-on-steps-to-cut-import-dependence-on-china-boost-manufacturing-report/articleshow/76449578.cms>

¹⁹<https://thewire.in/trade/china-goods-boycott-atmanirbhar-bharat>

²⁰<https://www.hindustantimes.com/business-news/govt-plans-to-cut-import-dependence/story-vidPYBME2Wahf1JXldgwhM.html>

The Government of India has been looking for alternative sources of imports to reduce dependency on China. In case of electrical machinery and its parts, potential substitutes can be Brazil and Vietnam. Plastics can be imported from Brazil and Mexico and Furniture can be imported from Mexico. Potential alternative sources for automobiles and motor parts are Chile and Colombia. Apparel and clothing can be imported from Sri Lanka and Bangladesh and toys and games from Brazil and Mexico. Optical, surgical and medical instruments can be bought from Colombia and Brazil. India can itself increase its production of electrical machinery, motor parts, automobiles, apparels and clothing and instruments required in the field of medicine. Switzerland and Italy are potential sources for antibiotics. However, finding an alternative source of supply of electronic equipment and smart phones is extremely difficult since China has complete dominance over these markets.²¹ Another major impediment is solar power. India relies on China for over 80% of its solar cells and modules supply²². Alternative import sources for these could be Germany, Japan, Italy and the United States²³. However, China, the largest producer of solar instruments, also supplies cost competitive equipment that cost significantly lower. Furthermore, India's non-availability of Lithium makes it heavily dependent on China for lithium batteries for Electric Vehicles. To decrease its dependency on China for pharma products, India can import from European nations and the United States. Moreover, the increased relations between the United States and India also creates potential import sources to reduce import dependency on China. However, the main reason that these alternative import supply sources may be ineffective is due to the cost edge that Chinese imports have. Most Chinese imports would cost lesser than other import supplies and if the Indian manufacturing sector is unable to absorb the shock of high prices, then it would lead to increase in prices for consumers. Furthermore, this approach does not even fulfil the mission of India becoming self-reliant, it merely shifts India's import dependency from China to other countries.

The last approach that the Indian Government can adopt to decrease import dependency on China is joint venture or collaboration with other countries to set up manufacturing hubs in India and boost the production of those goods that India depends on China for. For example, the joint venture projects of Hindustan Aeronautics Ltd (HAL) with Mikoyan-Gurevich (MiG) and Rosoboronexport, Aviazapchastof Russia, Rolls Royce Holdings Ltd of UK, and Edgewood Ventures of the USA among many others helped to boost India's self-reliance in defence equipment along with benefitting its partner countries.²⁴ Joint ventures with other countries will not only decrease import dependency on China but also help meet the vision of self-reliance. Furthermore, India should also look into joining partnerships such as the Regional Comprehensive Economic Partnership which India had backed out off on the grounds that it did not address key economic issues.²⁵ However, there is no harm in participating in the meetings and negotiating key issues that India felt should be addressed. In case, they are not agreed upon, India can back out of the Partnership then. Furthermore, India should also collaborate with like minded countries including Australia, Japan, Canada and South Korea²⁶ that are trying to reduce their trade dependency on China.

The best way forward for India today is to collaborate with other countries in Joint Venture projects that aim at boosting production of cost competitive and good quality import substitutes. For example, India could enter into a joint venture project with Germany for production of solar equipment, with Brazil for electrical machinery, with Chile and Colombia for automobiles and motor parts and with European nations and USA to produce APIs and pharma products.

Cutting down import dependency on China will have to be done gradually-indigenization or import substitution cannot occur in a day. At this point, India should not act on emotions but be realistic. In order to save the economy from major setbacks and repercussions, India cannot directly boycott Chinese goods that will create a time lag for the country. India instead has to focus on decreasing its import dependency in phases by carrying out joint venture projects with countries specialising in different commodities so as to produce better quality and more cost competitive goods than China. It is time to act on pragmatism than emotion.

²¹<https://timesofindia.indiatimes.com/business/india-business/india-starts-hunt-for-alternatives-to-china-to-source-over-1k-items/articleshow/74421762.cms>

²²<https://www.theweek.in/news/biz-tech/2020/06/25/solar-companies-dependence-on-china-may-prove-to-be-a-challenge.html>

²³<https://www.investopedia.com/articles/investing/092815/5-countries-produce-most-solar-energy.asp#:~:text=As%20of%202015%2C%20China%20is,sell%20the%20energy%20to%20utilities.>

²⁴<https://thingsinindia.in/joint-venture-companies-in-india/>

²⁵<https://economictimes.indiatimes.com/news/economy/foreign-trade/india-decides-to-opt-out-of-rcep-says-key-concerns-not-addressed/articleshow/71896848.cms?from=mdr>

²⁶<https://www.bbc.com/news/world-australia-52915879>

