No. 177, November 2011

Sino-Indian Economic Strategic Dialogue

Beyond the Beijing Round

Dr Bhartendu Kumar Singh
Indian Defence Accounts Service

It was trade that helped China and India to take their political-military relationships out of woods beginning with late eighties and enabled them to keep sweeping tensions under the friendship rug. In the process, the phenomenon debunked the traditional logic of 'trade following the flag' and the primacy of politics in bilateral and international relations. However, recently there have been frictions derailing the entire progress in the Sino – Indian relations.

Nothing concrete may have emerged from the first round of Sino – Indian economic strategic dialogue, but, both countries agreed to stay committed to deepening their economic ties based on 'pragmatic cooperation'. Unless India identifies the contours of this 'pragmatic cooperation' and invests in the future dialogue process, there is a probability that the two countries would soon face a virtual stand off on economic relations. This essay highlights the need to continue India's economic engagement with China,

I
SINO-INDIAN TRADE: AN ANALYSIS

Though the Sino – Indian bilateral trade jumped from $200 million in 1988 to $61 billion in 2010, there were substantial issues. First, this figure is no match to the bilateral potential of the two countries. China had higher trade figures with US ($385 billion) and its other neighbours like Japan ($297 billion), South Korea ($207 billion), and Taiwan ($145 billion) etc for the same period. Even countries like Australia, Malaysia and Brazil rank above India. Second, countries like Australia, Malaysia and Brazil are enjoying higher growth rate in their bilateral trade with China than India. Thus, even if the $100 billion target is achieved much before 2015, the bilateral trade should be considered as almost 'choked'!

New Delhi had taken some initiatives in agreement with the China to lift the bilateral trade volume. However, many of these initiatives are non-starters or have not yielded the desired results. The joint study group (JSG) on comprehensive trade and economic cooperation had identified scope for expanded economic cooperation between the two countries in trading of goods, services and investments and had even submitted a favourable recommendation for a China – India regional trade agreement (RTA) in 2008. However, not much action has been seen on the proposed RTA or other regional trade initiatives like the Kunming initiative and BIMSTEC as India does not enjoy a level-playing platform with the Chinese economy.

Similarly, the opening of the Stilwell Road or India's northeast to China's Yunnan Province has been a painful process. Until recently, opening up of Stilwell Road was blocked by mutual political differences and security considerations of all India, China and Myanmar. Only this year, Myanmar seems to have finally overcome its long standing reluctance to open the road and has awarded the road-building contract to a Chinese company. The reopening of the Stilwell road could cut by 30% the cost of transporting goods between India and China, providing a boost to Sino-Indian overland trade in a few years. The two areas that the road will link - India's northeast and China's Yunnan - are 'isolated, economically backward and

This brief is part of a larger initiative on developing Sino-Indian relations and regional cooperation undertaken by the China Research Programme at the IPCS. This project is supported by the Mac Arthur Foundation.

B-7/3, Safdarjung Enclave,
New Delhi, 110029
91-11-4100 1900
www.ipcs.org

landlocked' and the trade the Stilwell road will encourage is likely to bring in its wake economic development to these regions (Sudha Ramachandran, 2011). However, both China and India would have to cross many a hurdles before trade through Stilwell could become a reality, more so since it needs access to Chittagong port that comes under Bangladesh.

The opening of Nathu La in India's Sikkim province for trade between the two countries has also not been a successful experiment so far, despite over five years of existence. The trade has been limited both in the number of items that can be cross-exchanged and the volume that is a forgettable figure in the overall bilateral trade. Apparently, the infrastructure bottlenecks are the main hurdle. Also, post-1962 period, the trajectory of the erstwhile trade through Nathu La has shifted to other routes and it is indeed a difficult task to reorient the same. Today, the pass that was once witness to a significant amount of Indo – Tibetan trade, is being increasingly doubted if it will ever regain its old posture and serve as an economic bridge between China and India.

II
SINO-INDIAN TRADE: UNDERSTANDING THE INDIAN CONCERNS

The bilateral trade with China has become problematic for India for several reasons. First, the disproportionate balance of trade in China's favour by $20 billion in 2010, is likely to grow further. What is more disturbing is the slow growth of exports to China, and little progress in addressing long-persisting difficulties in diversifying exports in information technology, pharmaceuticals, and engineering sectors, which Indian officials have been pushing in recent months (Ananth Krishnan, 2011). For one reason or another, Beijing has been refusing to take full notice of these issues. This has led to a situation where China is being perceived as a potential economic threat amongst the policy makers and economic strategists in India who are unwilling to treat recurring trade deficit as 'business as usual'.

Second, China is also set to emerge as a 'manufacturing threat' to India. According to a recent report, the National Security Council (NSC) has projected that by 2014-15, over 75% of India's manufacturing will depend on imports from China. Currently, 26% of India's manufacturing GDP is dependent on Chinese goods. India's manufacturing GDP is $304 billion and $79 billion of this is linked to imports of all kinds, including raw materials, from China. The NSC projects that China's share in Indian manufacturing GDP will rise to $321, i.e. 75% of the total industry output which itself will touch $429 by 2014-15. By then, India's GDP is expected to top $2.68 trillion (K A Badarinath, 2011). These projections may be far-fetched and unrealistic, but the fact remains that China is emerging as a 'slow killer' for India's domestic manufacturing industry through cheap imports that are not able to compete with Chinese imports on cost factor. Further, they are not export-oriented or simply unfit for exports as revealed by large share of primary products and raw materials in India's export basket.

The opening of Nathu La in India's Sikkim province for trade between the two countries has also not been a successful experiment so far, despite over five years of existence.

Third, even in areas of added advantage, Indian companies face penetration and expansion hurdles in China. Indian officials have pressed China, on several occasions, to provide better market access for Indian pharmaceutical and information technology companies which have struggled to penetrate the Chinese market despite faring better on cost competitiveness factor. While China is one of the fastest growing drug markets with an expected value of $50 billion, India's advantage in the pharmaceutical sector could make it the ideal choice for China's sourcing of affordable, cost-effective and life saving drugs. This, in the process, could also take care of some part of India's trade deficit with China. However, Chinese state agencies put some or the other stumbling blocks. Similarly, Indian IT companies with a presence in China, including Infosys, Wipro and Tata Consultancy Services (TCS), have so far struggled to obtain contracts from State-owned enterprises (SOEs). TCS bagged a $100-million contract from the Bank of China — a deal, that has remained an exception rather than the watershed when it was announced in 2007.

III
SHOULD ONLY CHINA TAKE THE BLAME?

Perhaps not! When Sino – Indian trade relations kick started in late eighties, India was on advantageous note and enjoyed trade surpluses till early nineties. Indeed, even then, India was one of the few countries enjoying trade surpluses with China.

The balance of trade shifted in China's favour in due course for several reasons. First, there was a fundamental difference between the economies of the two countries in the nineties that remains even today. While China is an export-oriented economy, India is not. Moreover, China had the advantage of an early start for its economic reforms and export promotion schemes. India opened up its reforms process twelve years later.

Second, while China has swamped the Indian market like the rest of the world with its cost-effective light weight consumer items and electronic products; India has been exporting mostly primary products to China like it has been exporting the same stuff to the rest of the world. The so-called advantage for India in pharmaceutical and IT sector is ephemeral and likely to be contested by China in due course. Third, India's manufacturing sector, despite two decades of structural reforms and incentives, is still not resilient and productive. Labour is as cheap in India as it could be in China; the bureaucratic hurdles are almost similar in the two countries; and corruption is as endemic in India as it is in China. But the manufacturing sector in India is yet to emerge out of the mindset of 'departmental production units' that characterised manufacturing in Government –owned production units in India during the license-raj day and even today. Finally, China benefits from systemic defaults in international economic relations. It retains the 'developing country' status for itself thereby seeking more and more favours for itself in trade negotiations. Its justification of 'unfair trade practices' such as artificial pricing of Chinese currency makes it a ruthless mercantilist state pushing its economic products in all global shops. India just happens to be a victim of this system.

Given that trade deficit has been an enduring feature of India's foreign trade, the Government has been working on several options to moderate this trade deficit. In August 2009, the Government announced 'foreign trade policy 2009-14', with a goal of doubling India's exports of goods and services by 2014, with the long term objective of doubling India's share in global trade by 2020 through appropriate policy support. The policy is still mid-way before it can be objectively analysed for its effects. Similarly, the Indian Government has also come out with a 'strategy' for doubling exports in next three years, i.e. 2011-14, by pushing the exports towards a compound average growth rate of 26.7% per annum.

These policy initiatives, however, do not address India's specific trade concerns with China. Apparently, an alarmed National Security Council and the Ministry of Commerce are working out on an action plan, both long term and short term, to loosen China's grip on the Indian economy. Over the past six months, they have held several rounds with officials of the ministry of industry, external affairs, telecom, information technology, pharmaceuticals, power and agriculture (K A Badarinath, 2011). The deliberations have finally led to a China specific strategy that is under the consideration of the Government, as announced by India's Commerce Secretary, Rahul Khullar. The five-pronged strategy seeks to:

As a neighbour with barrage of other frictional issues with China, India can ill-afford to let economic and trade relations slip beyond manageable limits and open another front for heated exchanges between the two countries.

- get China to invest and produce in India, not just trade;
- raise duties on products where India is not dependent on it;
- create non-tariff barriers where dependence is high;
- ensure Chinese state-owned procurement agencies buy in bulk from Indian companies; and
- leverage the huge domestic market to gain access to Chinese markets, at least in areas where India has significant strengths.

IV
THE BEIJING ROUND & BEYOND

The first round of the economic strategic dialogue in Beijing was gainful for numerous reasons. First, it provided an institutional platform aimed at salvaging the simmering differences in Sino – Indian economic and trade relations. The inaugural round provided India a diplomatic environment to sensitise the Chinese audience about its trade concerns even though the exclusive dialogue was meant for discussing 'bigger picture'. Before and during the meet, the Chinese media including the State-controlled CCTV did highlight India's concerns on rising trade deficit with China, a fact that got sympathetic ears even from Wen Jiabao, the Chinese Premier. Dr Ahluwalia, during his interactions with the Chinese side, urged them to open the Chinese market to Indian IT and pharma products and let them do 'business in China'. Second, it provided Indian interlocutors an opportunity to get a feel of 'Chinese mind' on their grievances and work on the inputs. The Beijing round, therefore, will be of immense help when Indian officials sit to work on their proposed strategic action plan against China with suitable amendments and modifications. Third, the dialogue brought in open about the Chinese interests in crucial sectors such as railways, water conservation and renewable energy and in coming years we may have some Sino – Indian partnership in these areas, as agreed to in the dialogue.

The Beijing round may not have provided immediate solution to India's trade concerns but there are many reasons for the dialogue to continue. First, trade has been a significant aspect of bilateral relations enabling China and India to live in 'relative peace' with each other despite differences over the border and other issues. Not talking over it could make it equally contentious like other issues in China – India relations. Second, all economic forecasts predict an accelerating shift of global economic power characterised by increasing lead space for China and India (eg. RAND, 2011). Sustained trade friction or unmanageable balance of trade could push them towards economic conflict that could have a domino effect over other areas. Third, it offers a long term incentive for accelerated resolution of political and military disputes by increasing the 'opportunity costs of war'. Incidentally, it puts India in the same basket of countries like Japan, US and even Taiwan that are witnessing an upsurge in their trade relations with China despite sustained political differences. Fourth, as the Beijing round reflected, the scope of dialogue could be expanded to include collaboration in international forums like WTO, G-20, climate change as well as multiple issues in the financial sector. As it stands, China and India do not have much to differ on these international economic issues; it is just that the bilateral differences are too much to focus on international collaboration.

IV
CONCLUSIONS

One good thing about the entire Sino – Indian trade friction is that India is not the only country that is at the receiving end of Chinese export-oriented economic domination. Most countries that have vibrant trade relations with China are suffering trade deficits, including the US. Exports apart, China's economic superiority would be complete in next 20-25 years and all countries would have to live in China's shadow or make friends with it. The US has institutionalised an economic strategic dialogue to resolve its trade concerns with China and the two countries have made decent progress in talking out mutual trade concerns. Beijing is increasingly responsive to Washington's allegation of 'unfair trade practices', primarily as a result of these talks.

As a neighbour with barrage of other frictional issues with China, India can ill-afford to let economic and trade relations slip beyond manageable limits and open another front for heated exchanges between the two countries. New Delhi can take lessons from the US – China example to avoid any future economic conflict with Beijing. The just-launched economic strategic dialogue should be exploited as a primary mechanism for resolving all outstanding trade concerns with China and explore bilateral cooperation in new areas. Concurrently, it must not shy away from implementing the proposed 'strategic action plan' for containing the trade deficit with China. However, New Delhi must consolidate its domestic manufacturing sector for resilience against Chinese imports. Then only India can negotiate from a position of strength in the future rounds of the economic strategic dialogue.

Note: Views are personal

References

Ananth Krishnan, 'Trade deficit with China widens to $14 billion', The Hindu (New Delhi), 13th August 2011.

Ashok Malik and Rory Medcalf, 'When the flag follows trade', The Times of India (New Delhi), 3rd May 2011.

'China's top trade partners, 2010', https://www.uschina.org/statistics/tradetable.html

'China rising: ministries work on action plan', The Indian Express (New Delhi), 1st September 2011.

K A Badarinath, 'China set to conquer India', http://www.mydigitalfc.com/news/china-set-conquer-india-300 20th September 2011.

Peter Wonacott, 'China, India stoke 21st century rivalry', Wall Street Journal, 23rd October 2009.

RAND, China and India 2025: A Comparative Assessment (RAND Corporation, 2011), available on www.rand.org

Sino – Indian trade friction intensifies', http://en.zgxu.com/2010_07__Sino-Indian-trade-friction-intensified.html 13th July 2010.

Sudha Ramachandran, 'Stilwell to be reborn', Asia Times, online edition, www.atimes.com 21th January 2011.