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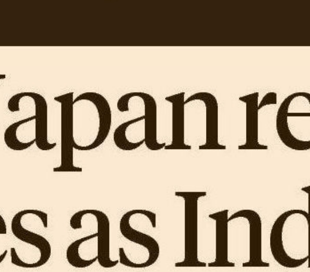
China, Japan revive trade ties as India fades

India does not provide an opportunity comparable to China's 'Made in China 2025' initiative

Amidst the frenzy of the US-China trade war, an important development has escaped attention. There is a perceptible thaw in the hitherto strained political relations between Japan and China and a parallel revival in their trade and economic relations. The visit of Chinese Prime Minister Li Keqiang to Japan in May 2018 was a breakthrough and this was followed by Japanese Prime Minister's trip to China in October 2018, the first by a Japanese Prime Minister in 11 years. The two sides have begun to improve their strained relations in response to the unpredictability created by the US under Trump and his targeting of both countries on trade related issues. The Chinese are courting Japanese business and industry in earnest as their access to the US market and, more importantly, to advanced technologies and equipment is being increasingly restricted. Japan is an attractive alternative though within limits. The recent shutting out of Huawei from the Japanese telecom market is a pointer.



SHYAM SARAN

China-Japan relations became strained in the new millennium over territorial and security related issues. They reached a low point in 2012 over the disputed Senkaku islands. Japanese FDI into China reached a recent peak of $7.4 billion in 2012 but declined over the next several years to a level of $ 3.1 billion in 2016. In annual surveys, more Japanese companies were expressing their intention to exit China than those who wished to expand operations. The increasingly tense relations between the two countries had led Japanese business to adopt the "China Plus One" strategy, or diversifying investment away from China. This is how India came on the radar screen of Japan, both as a security partner as well as a destination for Japanese investment and trade. A rapidly growing Indian economy began to be seen as offering a scale and market comparable to China. While Japanese FDI into India has increased significantly from about $85 million in 2006-7 to $4.7 billion in 2016-17, the anticipated surge in Japanese FDI has not materialised. The accumulated stock of Japanese capital in China is over $100 billion. For India, the figure is only $25 billion. With China once again emerging as an attractive destination for Japanese investment, India may be pushed to the margins. Japanese FDI into China revived to a level of $ 3.2 billion in 2017 and is expected to maintain an upward trajectory. According to a JETRO official, "Our current conclusion is that Japanese business would act more positively towards investing in China from now on."

Japan-China trade has also resumed an upward trajectory, after declines registered post 2012, and was about $300 billion in 2017. India-Japan trade has been declining in recent years from $18.5 billion in 2012-3 to $13.5 billion in 2016-17. Indian exports halved from $6.1 billion to $3.8 billion in the same period.

Japanese business considers China's "Made in China 2025" initiative as a major opportunity. The initiative has identified 10 sectors, including Artificial Intelligence, Robotics, Electronic Vehicles and Quantum Computing, where China plans to emerge in the ranks of the most advanced countries by 2025. These are precisely the areas where Japan has significant capabilities. Recently, several important collaborations have been announced— for example, between Japan's robot maker, Yaskawa, and China's auto-maker Chery, to tap the electric vehicle market. National Panasonic's research and development hub in Shanghai is collaborating with China's Alibaba and Baidu to develop connected devices and also instrument panels for next generation vehicles. Unlike the US and western European countries, which see the Made in China initiative as a threat to their technological dominance, Japan appears to have taken a different tack. India does not present a comparable opportunity.

Japan had initially opposed China's Belt and Road Initiative (BRI) when it was announced in 2013. It responded with its Partnership for Quality Infrastructure (PQI) in 2015, offering a financially viable and transparent alternative to countries in Asia and Africa, seeking infrastructure development. In 2017, India and Japan together announced the Asia-Africa Economic Growth Corridor (AAEGC), to extend joint infrastructure funding to Asian and African countries. However, in June 2018, Japanese PM Abe reversed course to offer to work with China in third countries to develop infrastructure. Fifty such collaboration projects were announced during his visit to China in October 2018, including a rail project in Thailand. AAEGC has receded into the background. Japan is now on board the BRI.

Japanese business continues to have reservations about investment climate in India. In the latest Joint Report of the India-Japan Business Leaders' Forum, the Japanese side called upon the Indian government to "streamline and speed up the GST system and related procedures, promote tax system reorganisation and rationalisation, assure internal consistency of tax system including revisions to the Master File requirements; amend and consolidate labour laws, ensure the free flow of data by rescinding regulations on data localisation, promote infrastructure development and reform the project bidding system; improve transparency of and consistently enforce legal and institutional frameworks; develop and digitise general rules on administrative procedures and ensure transparency and fulfilment of administrative contracts."

China today does not offer a better set of terms for FDI but Japan continues to retain a higher comfort level doing business with China and South-East Asia than with India.

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