# India’s China trade challenge

***A strategic response is needed to tackle the burgeoning trade deficit with China, which reached alarming proportions at $101.02 billion in 2022. What we have instead is a dose of whataboutery from the government.***


For the first time since India lost 20 soldiers in a deadly clash with China’s People’s Liberation Army at Galwan in June 2020, China’s defence minister was in Delhi last week. Li Shangfu was attending the Shanghai Cooperation Organisation meeting of defence ministers and held a bilateral meeting with his Indian counterpart Rajnath Singh.

Later this week, China’s foreign minister Qin Gang is scheduled to be in Goa, to attend the SCO meeting of foreign ministers. He was last in India in March for the G20 foreign ministers meeting where he met foreign minister S. Jaishankar. China’s President Xi Jinping, recently elected for an unprecedented third term, is also expected to be in India twice this year—in June and September—to attend the SCO and G20 summits.

This flurry of diplomatic visits by Chinese officials and leaders to India suggests a sign of normalcy in bilateral ties, contrary to Jaishankar’s claim that “today the state of our relations with China is not normal” because of the situation on the Line of Actual Control. Meanwhile, the three-year-old border crisis continues unabated. As evident from the failure of the 18th round of talks between corps commanders on 23 April, the Chinese refused to discuss either disengagement at Depsang and Demchok, or de-escalation from areas where disengagement has taken place.

Then again, China has not appointed a new ambassador to India after the previous incumbent, Sun Weidong, moved back to Beijing last year. On the pretext of retaliating against India’s restrictive policy on Chinese journalists, Beijing recently cancelled the visas of two Indian journalists working in China. If all this counts as normal, then it must be the new normal.

Besides diplomacy and security, there is another domain in which India’s bilateral ties with China ought to be examined: trade. India’s bilateral trade with China has been flourishing, showing no signs of abating even after the Galwan clash. Nearly 70% of India’s batteries and 65% of the pharmaceutical industry’s inputs come from China. Even the Vande Bharat trains run on Chinese wheels.

Not only has bilateral trade reached record levels, but more worryingly the trade deficit in China's favour has risen at an even sharper rate. The Narendra Modi government's response to this stunning fact has been muted, with its reply to questions in Parliament delving into whataboutery about the rise in trade during the two UPA governments rather than answering questions about its own record.

Unfortunately, this dependency is one-sided. While China figures in the top two of India's trading partners, India doesn't make it to the top 10 on China's list. Leave alone the EU, the US, Japan and Brazil; even Vietnam and Indonesia figure higher on the list than India. And while Chinese goods account for 16.4% of India's imports, they make up just 3.3% of China's overall exports. India cannot do without China as a trading partner, but the reverse does not hold true.

## The dependency on China

India's trade with China picked up only after the communist country became a member of the World Trade Organization in 2001. India was China's 18th-biggest trading partner in 1998-99, 16th-biggest in 1999-00 and 12th-biggest in 2000-01. The upward march started in 2002-03, but the real impetus came after the 2008 global economic crisis, which saw China emerge as a winner. By 2011-12, China had become India's top trading partner and has remained in the top two since. Instead of any delinking, India has been coupled even more tightly with China in the last few years.

An aside: The discrepancy between trade data released by Beijing and Delhi is hard to reconcile. While China claimed that its trade with India was $103 billion in the first nine months of 2022, India's official data showed it to be only $91 billion. A similar divergence in 2021-22 allowed India to claim that China is its second-largest trading partner after the US, while accepting Chinese data would mean it was India's foremost trading partner.

Some difference between the trading figures of the two countries is understandable. China's export values of products would generally reflect the market value or free on board (FoB), whereas imports include cost, insurance and freight (CIF) of around 10%, meaning India's import value ought to be higher. Surprisingly, it is the opposite in the case of China-India bilateral trade. This discrepancy is significant, which means that under-invoicing by Indian importers is rampant to avoid tariffs or gain extra due to foreign exchange rate fluctuations. For example, an Indian importer asks for a supply of Chinese cargo worth $100,000, but invoices it for only $80,000 to avoid Indian tariffs and pays the rest via Dubai or Singapore.

## High trade deficit

The exact figure notwithstanding, there is no discrepancy in the fact that India's trade deficit with China has been on an upward trajectory. It rose from $0.34 billion in 2002 to $20.1 billion in 2010, $46.6 billion in 2016 and crossed $100 billion for the first time in 2022. Of a total trade of $135.98 billion last year, the imbalance in China's favour was $101.02 billion. Only three countries provide a greater trade surplus for China: the US, Hong Kong and the Netherlands. In January, the Indian government summoned 18 ministries to discuss ways to bring down imports from China and reduce the trade imbalance. The outcome is neither known nor visible so far in policies, when the fire alarms should have been screaming out loud in Delhi.

The Indian embassy in China has a twofold explanation for this burgeoning trade deficit. First, it argues that India exports a narrow basket of commodities—mostly primary—to China; and second, China places market access impediments for most of India's agricultural products and the sectors where India is competitive in, such as pharmaceuticals, IT and IT-enabled services, etc. The embassy accepts that India's predominant exports have consisted of iron ore, cotton, copper, aluminium and diamonds/natural gems. Over a period, these raw material-based commodities have been overshadowed by Chinese exports of machinery, power-related equipment, telecom equipment, organic chemicals and fertilizers.

In 2021-22, the top Chinese item in Indian imports was the personal computer (laptops, palmtops, etc.) at $5.34 billion, followed by ‘monolithic integrated circuits-digital’ ($4 billion), lithium ion used in batteries ($1.1 billion), solar cells ($3 billion) and urea ($1.4 billion). The same year, India’s top export to China was light naphtha at $1.37 billion. Ores, slag and ash ($2.5 billion); organic chemicals ($2.38 billion); mineral fuels, mineral oils and products of their distillation, bituminous substances and mineral waxes ($1.87 billion); iron and steel ($1.4 billion); aluminium and aluminium articles ($1.2 billion), and cotton ($1.25 billion) were among the other items on the Chinese import list.

## Is there a way out?

For India, the challenge is humongous. This message is driven home in a new research paper by Indian Institute of Foreign Trade professor Sunita Raju, titled ‘Impact of imports from China on Indian manufacturing performance: an analysis of trade competitiveness’. The paper found that of the 32 product subcategories imported from China, it was the cheapest supplier in more than 30% of cases. For the rest there were cheaper alternatives available, and yet the Chinese product was preferred by Indian manufacturers because of better quality or specifications. For 16 products, China was the sole supplier, which meant Indian manufacturers had nowhere else to go for such specialized components.

Essentially, the paper argues that “manufacturing imports from China have a positive association with manufacturing output and exports. As these imports are mainly capital and intermediate goods, the rising dependence on China points to domestic non-availability thereby making them critical for production.” Evidently, barring resource products like chemicals, China supplies low- and medium-technology products that are not available in India.

“The current policy thrust on ‘Self Reliance or Atmanirbhar Bharat’ will not be effective unless the domestic manufacturing is propelled to high technology products. Then rising imports will not be a concern as they lead to an increase in exports. This necessitates a policy thrust to reduce the trade barriers and complement domestic with foreign technologies,” concludes the paper.

Going by its stance on the Regional Comprehensive Economic Partnership signed by other Asia-Pacific nations and the trade leg of the Indo-Pacific Economic Framework, both of which India has refused to join, and the recent problems with the WTO provisions on tariffs, the Narendra Modi government has made clear its reluctance to reduce trade barriers. Even the free trade agreements being negotiated with the UK and the EU have not progressed. The early outcomes of the production-linked incentive policy to attract manufacturers have been a mixed bag, and its results can only be assessed in the long term.

If India can’t do much about reducing the trade deficit with China, the other alternative is to have a very high volume of service exports that would make up for the shortfall in exports of goods. Beijing is ensuring that that doesn’t happen. The only other way to bridge the very high trade deficit is through foreign direct investment from China, but this can’t be done because of strategic reasons. India would not want Chinese money in critical sectors and has already erected regulatory barriers after the deaths at Galwan. In the immediate term, India doesn’t seem to have a coherent response to the Chinese challenge. Going by the discourse after nine years of the Modi government, there are no signs of a medium- or long-term reply either.

Is India then doomed to the fatalistic pessimism of Jaishankar who confessed that “Look, they (China) are the bigger economy. What am I going to do? As a smaller economy, I am going to pick up a fight with the bigger economy? It is not a question of being reactionary, it’s a question of common sense…”? Well, common sense also tells us that the world is flat.

## Obiter dicta

*What should India do before the next Taiwan Strait crisis?* A new paper on the subject by Vijay Gokhale, the former foreign secretary, ambassador to China and diplomatic representative to Taiwan, is illuminating and informative. Two of the best global podcasts on China are The Sinica Podcast, a weekly show hosted by Kaiser Kuo, and The Spectator magazine’s Chinese Whispers, a fortnightly show hosted by Cindy Yu.

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