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"Acting East": Aligning Economic and Strategic Goals

by Ambassador Hemant Krishan Singh

Prime Minister Narendra Modi has consistently prioritised expanded economic ties with key foreign partners to secure investment, technology and knowhow essential for advancing India's economic rise. He has urged foreign investors to come and expand India's lagging manufacturing sector under the "Make in India" initiative and his government has implemented reforms to improve "ease of doing business" in the Indian market.

Not surprisingly, addressing a think tank conference on June 13, 2016, Dr. S. Jaishankar, who ably leads Indian diplomacy, spoke eloquently about the criticality of aligning business and strategic goals. He pointed out that the global strategic landscape looks increasingly like a business environment; indeed, business provides the ballast for many of India's important relationships. He also spoke about strengthening the ability of Indian businesses to effectively compete abroad by "batting for your business". So far, so good.

However, wading into an area where the Ministry of External Affairs has no policy making role, Jaishankar had no option but to fall back on a defensive and dated official Indian trade policy line: "Global trade discussions cannot indefinitely frontload goods and investment at the cost of services and labour mobility".

If, as in Jaishankar's words, "Make in India is not Make for India", and "the real game is to integrate more deeply into the global supply chain and gain better market access abroad", does the solution lie in maintaining a constrained trade posture?

Continuing restrictions on market access and a partially liberalized business environment are hardly likely to improve prospects for either "Make in India" manufacturing or export competitiveness. The argument that India's trade pacts have produced no export gains and tariff revenues are necessary for fiscal balance is a recipe for economic underperformance and India's exclusion from international rule making on regional trade instruments. Oddly, for a country with "leading power" ambitions, India will remain a "rule taker" on trade, with adverse consequences for its economy.

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My intention here is not to advance any particular reform agenda, which the Modi government is in the best position to determine in the light of India's developmental priorities. But it is useful to recall that the post 1991 liberalisation era, the 25th anniversary of which has just gone by without much fanfare, has boosted both overall growth and competitiveness across several sectors of the Indian economy. If we now set up "Make in India" and mega regional trade agreements as contradictory impulses, we might well end up eroding these gains of 1991 and fall further behind in competitiveness.

Foreign Secretary S. Jaishankar delivering his keynote address "Aligning Business with Strategic Goals" at the Gateway of India Dialogue

So, a reality check is essential to see if there is policy coherence between the economic mandarins of the Government of India tasked with enhancing India's engagement in the global economy and the Prime Minister's vision which an "activist" Foreign Office is vigorously projecting.

Well, this does not so far appear to be the case. Broadly speaking, the contradictions of India's economic decision making are hard to mask: a gradual openness to investment alongside entrenched reticence towards trade liberalization and holdback on concomitant domestic reform.

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Major regional trade agreements are strategically driven but intended to induce policy changes in the domestic space for achieving enhanced, long term welfare gains. For our trade and investment policymakers, there is trepidation even about the "price" India will have to pay for the membership of APEC, whose economies account for nearly 40% of our external trade. Given the voluntary and non-binding nature of APEC's trade and business facilitation programmes, it in fact provides a "soft" template for incentivizing reforms that can make India's manufacturing sector more competitive.

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Trade policy experts familiar with these issues say that with reformist impulses largely absent in the political economy, Indian trade negotiators are unable to negotiate meaningful instruments as they remain fixated with the denial of market access on trade in goods. Not only are India's tariff barriers high, we also resist any real liberalization of the services sector. Indian regulations militate against foreign service providers and the complexities, half-measures and frequent changes of our FDI regime, from single to multi-brand retail and e-commerce, make India's market both difficult and unpredictable. Multiplicity of regulatory standards does not help either. As for our tired refrain on the movement of professionals, our leading trade partners are already far more liberal than we are. We are unlikely to secure really meaningful openings for IT professionals, nurses and yoga teachers to adequately balance our competitivity concerns on trade in goods. With growing shortages of skilled workers in our own economy, we also may not have the luxury of an unlimited surplus of professionals in any case.

An efficient manufacturing sector which produces trading strength in goods requires deeper and wider domestic reform, not continuing barriers to trade. To illustrate this point, let me cite a recent article by Arvind Subramanian, our Chief Economic Adviser[1]. In the context of recently announced incentives for the apparel sector, he points out that the space vacated by China because of rising

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wage levels is being filled not by India but by Bangladesh and Vietnam; even Indian apparel producers are relocating abroad. India's competitors enjoy better market access by way of lower or zero tariffs to the two major importing markets of the US and EU. In addition to this external disadvantage, Indian exporting firms mainly face domestic challenges, from logistics and de facto labour costs to a tariff policy which shields an inefficient man-made fibre sector, undermining our clothing industry's competitiveness. According to Subramanian, "the government is taking very seriously the impact of Indian exporters being disadvantaged in foreign markets." But then he also falls back to the traditional default position that "India will still need to carefully weigh the benefits and costs of negotiating new free trade agreements".

With intensifying regional competition for investment, India is unlikely to gain from its present "we have liberalized enough" stance. And continuing strains over trade policy issues undermine the sustainability of our security convergences with key strategic partners.

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Now, let us look at the broader regional context for trade. The major growth area of the world economy extends from India to East and Southeast Asia. Taken together with the US, nations to our east are our largest trade partners and greatest economic opportunity. And yet, we appear to have reached an impasse with our ASEAN Plus Five partners over the ASEAN-led Regional Comprehensive Economic Partnership (RCEP) negotiations. Our partners want to move towards greater trade liberalization and a more ambitious instrument which benchmarks higher rules and standards governing an open environment for enhanced economic activity and business. On our side, there is a nominally stated aspiration to influence decisions from within RCEP negotiations, but a much more real emphasis on continuing "moderation" in our negotiating stance.

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A clear prioritisation of RCEP negotiations and APEC membership to derive maximum gains from region-wide economic integration is largely absent. Our Asian partners are exasperated, while the USTR remains opposed to an obstructionist India joining APEC.

Prime Minister Narendra Modi addressing the opening session of the 'Make in India Week' in Mumbai on February 13, 2016

It is hardly surprising that in terms of respective trading importance among India, US, China, Japan and ASEAN, it is India which stands out with the lowest footprint and integration into global value chains. China, on the other hand, is the predominant trading partner for all.[2]

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The pull of the Chinese market and trade linkages are the principal generators of China's influence across East and Southeast Asia. This benefit is now eroding because of China's economic slowdown as well as its territorial assertions and island-creeping strategy in the South China Sea. ASEAN unity has been undermined by Chinese pressure[3] for the second time following the acrimonious ASEAN-China Special Foreign Ministers' meeting on June 14, impacting mutual trust and confidence. China's policy of alternating inducements and threats will inevitably provoke ASEAN resistance.

"India, on the other hand, enjoys multiple strategic and soft power advantages as it builds strategic space and influence in the region."

India, on the other hand, enjoys multiple strategic and soft power advantages as it builds strategic space and influence in the region. It has growing partnerships with the US, Japan, Australia and several ASEAN states based on security convergences. It enjoys considerable goodwill and receptivity from its civilisational soft power. There is a growing demand for India to play a larger diplomatic role in reassuring ASEAN countries, giving them room to make independent choices in national interest without coercive Chinese influence. India's maritime security presence as a benign and dependable neighbour to ASEAN in the Andaman Sea is another distinct asset.

But eventually, if India is to become a leading influencer of regional security, it must also actively seek to become an important trade and economic partner of the world's most dynamic economies.

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Adopting a new approach towards RCEP negotiations and proactive pursuit of APEC membership would be a good way to start. This is not a campaign which India's diplomacy can fight alone.

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[3] "According to one ASEAN diplomat quoted by *The Straits Times*, 'Malaysia releasing it [the joint press statement] was a manifestation of the extreme frustration of the original five ASEAN members plus Vietnam at the particularly crude and arrogant behavior of the Chinese.'", Carl Thayer, "Revealed: The Truth Behind ASEAN's Retracted Kunming Statement", *The Diplomat*, June 2016.

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