India and East Asia: Case for a stronger Economic Partnership

Mukul Asher
LKY SPP, NUS
E-mail: sppasher@nus.edu.sg

and

Rahul Sen
ISEAS
E-mail: rahul@iseas.edu.sg

Presented at the RIS, New Delhi, February 10, 2005

Organization

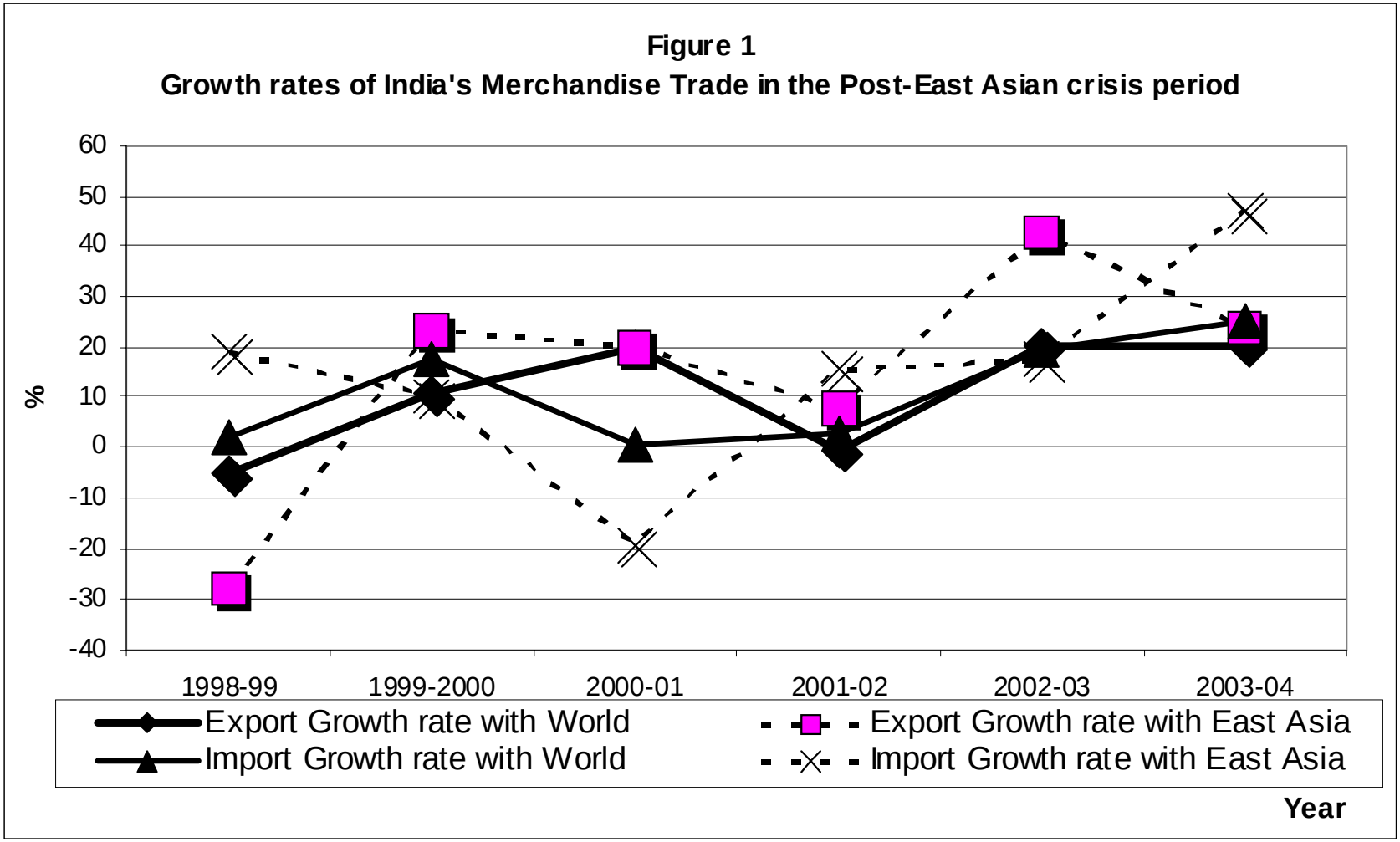
- Introduction
- Merchandise Trade relations
- Services Trade and Investment flows
- Why Partner India?
- Concluding Remarks

Introduction

- Greater economic coordination and cooperation among major Asian countries essential to manage globalization challenges and to enhance Asia's role
- India's unilateral liberalization and deregulation, and shift in economic paradigm towards integration with the world economy, and forging alliances have contributed to a favorable environment for the emergence of New Asia
- There is now convergence of outward-orientation policies between India and rest of Asia
- India's relatively greater reliance on domestic entrepreneurship and demand could provide a country risk diversification for rest of Asia, esp. as India's GDP is set to exceed USD 1000 billion by the end of the decade
- India's look east policy has gained substance, and prospects for further deepening of economic and strategic linkages with East Asia are encouraging
- India has made good progress during the past decade in constructively engaging key countries and regional organizations around the world. This has been made possible as India continues to translate its economic potential into actual performance, and pursues strong and creditable national security policies.

India's Economic Partnerships

Partners/Grouping	Status of Agreement, 2005
ASEAN	Framework Agreement signed
China	Proposed
Korea	Proposed
Singapore	Under negotiation
Sri Lanka	Agreement in force
Thailand	Agreement in force
BIMSTEC	Framework Agreement signed
SACU	Proposed
COMESA	Proposed
MERCOSUR	Framework Agreement signed
Mauritius	Under negotiation
GCC	Proposed
Chile	Proposed
SAARC/SAFTA	Agreement in force



Source : Computed from CMIE (2004)

with the exception of Japan, India's trade with other East Asian countries has increased rapidly since the crisis of 1997-98. Thus, barring few exceptions, the growth rate of India's exports to and imports from East Asian economies (viz. China, Japan, Korea and the ASEAN-6) was in general higher than that of India's exports and imports to the world

Merchandise Trade-1

- India's overall merchandise trade with East Asia more than doubled from about US$ 13 billion in 1997-98 to about US $ 27 billion in 2003-04 registering a compound annual growth rate of 13%

- bulk of this increase was contributed by the rapid increase in bilateral merchandise trade between India and China, which expanded more than four-fold from about US $ 1.7 billion in 1997-98 (US $ 0.7 billion in exports and US $ 1 billion in imports) to about US $ 7 billion in 2003-04 (US $ 3.0 billion in exports and US $ 4.0 billion in imports) to about 12 billion by end 2004.

India's Exports to East Asia: 1997-98 to 2003-04
(US $ million)

	1997-98	1998-99	1999-2000	2000-01	2001-02	2002-03	2003-04
World	35048.7	33211	36760	44147	43976	52856	63622
China	719	427	539	830	955	1981	2967
	(2.1)	(1.3)	(1.5)	(1.9)	(2.2)	(3.7)	(4.7)
Korea	468	307	476.5	447	473	646	764
	(1.3)	(0.9)	(1.3)	(1.0)	(1.1)	1.2	(1.2)
Japan	1901	1651	1685	1782	1515.6	1869	1719
	(5.4)	(5.0)	(4.6)	(4.0)	(3.4)	(3.5)	(2.7)
ASEAN-6	2419.6	1589.2	2190.3	2813.7	3390.2	4528	5700
	(6.9)	(4.8)	(6.0)	(6.4)	(7.7)	(8.6)	(9.0)

Source : CMIE (2004)
N.B: Figures in parentheses indicates share in India's total world exports.
ASEAN-6 includes Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam

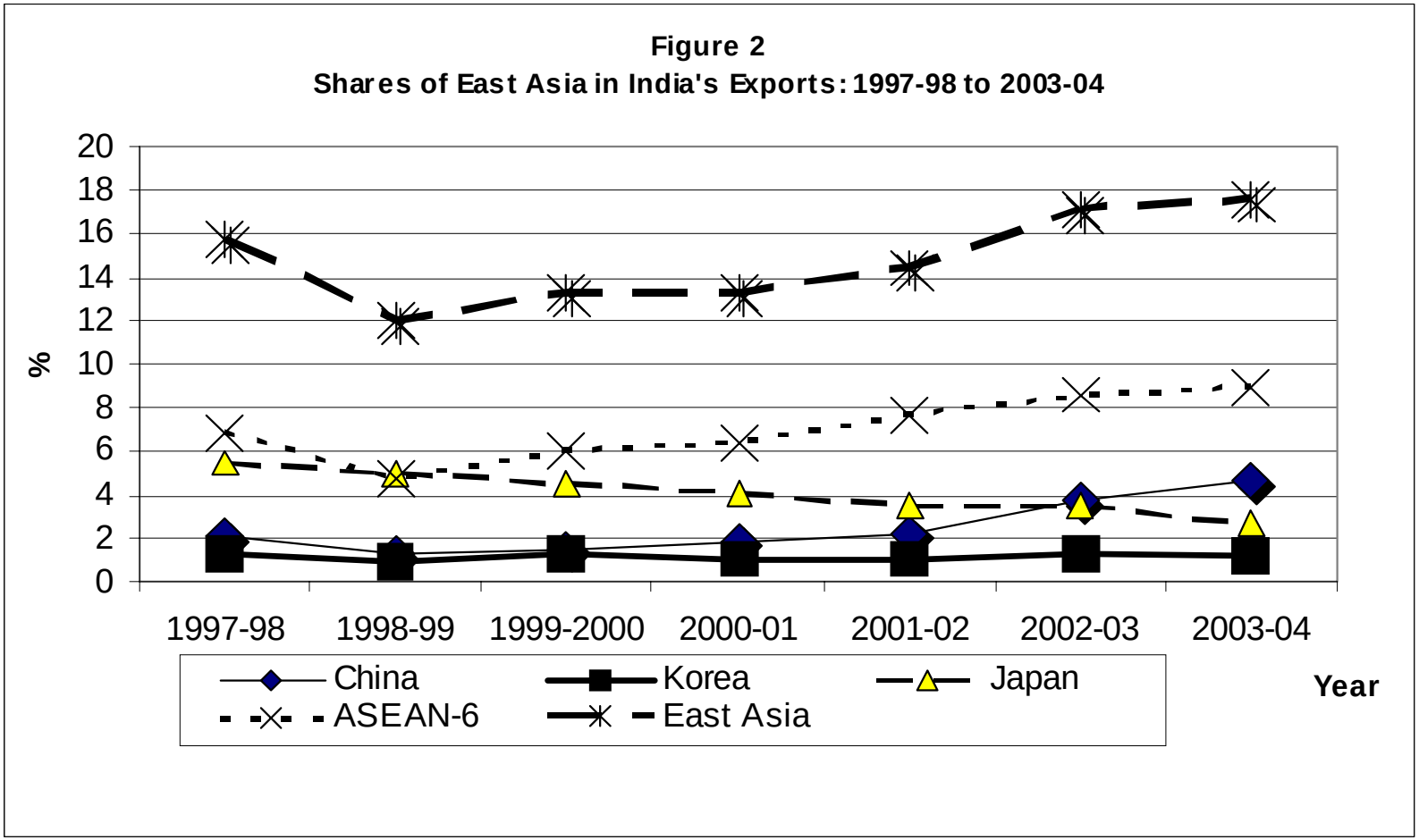
India's Imports from East Asia: 1997-98 to 2003-04
(US $ million)

	1997-98	1998-99	1999-2000	2000-01	2001-02	2002-03	2003-04
World	41534.6	42379.2	49798.6	50056.3	51588.4	61571.6	77237
China	1120.7	1096.5	1288.3	1494.9	2043.3	2799.3	4059.1
	(2.7)	(3.3)	(2.6)	(3.4)	(4.6)	(5.3)	(6.4)
Korea	1002.9	1394.1	1274.9	891	1145.3	1525.9	2460.1
	(2.4)	(4.2)	(3.5)	(2.0)	(2.6)	(2.9)	(3.9)
Japan	2147.5	2465.2	2538.9	1835.5	2153.7	1841.1	2649.3
	(5.2)	(7.4)	(6.9)	(4.2)	(4.9)	(3.5)	(4.2)
ASEAN-6	3382.3	4142.6	4918.9	3881.2	4025	4825	6959
	(8.1)	(9.8)	(9.9)	(7.7)	(7.8)	(7.8)	(9.0)

Source : CMIE (2004)
N.B: Figures in parentheses indicates share in India's total world imports.
ASEAN-6 includes Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam

Merchandise Trade-2

- East Asia's share (except that of Japan) in India's exports has been increasing particularly since 2000-01, with that of India's imports also exhibiting similar trends. In particular, China's share in India's exports and imports expanded from 1.9% and 3.4% to 4.7% and 6.4% respectively, while that of ASEAN-6 increased from 6.4% and 7.7% to 9% respectively for both flows
- India's bilateral trade with ASEAN-6 expanded from US $ 5.8 billion in 1997-98 to US $ 12.7 billion by 2003-04; while the corresponding increase with Korea was from about US $ 1.5 billion to US $ 3.2 billion
- Malaysia, Singapore, Thailand and Indonesia are all emerging as strong trading partners of India. This has significantly increased the prospects for achieving India-ASEAN bilateral trade goal of US $ 30 billion by the end of the decade.



Source : Computed from CMIE (2004)

Merchandise Trade-3

- India's vigorous unilateral liberalization (its tariff levels are approaching those in ASEAN), and its pursual of bilateral trade pacts, could facilitate expansion of economic relations with East Asia.

- India and Sri Lanka after highly satisfactory experience with limited FTA, are negotiating a Comprehensive Economic Partnership (CEP) Agreement which will also include investments and services.

- Further, the India-ASEAN FTA is also likely to be operational in 2005 with an "Early Harvest" scheme involving 105 products. This is likely to be expanded to include other areas in due course. A similar arrangement is in force as part of the Thailand-India FTA.
- Concomitantly, the Comprehensive Economic Cooperation Agreement (CECA) pact between India and Singapore is reportedly progressing towards the concluding stage.

- India is engaging China and Korea in studying feasibility of a bilateral FTA agreement.

Services Trade and Investment flows-1

- The analysis of service transactions for Asian economies is seriously hampered by data limitations. This is because unlike the OECD countries, the Asian countries do not publish the relevant data which are comprehensive, detailed, timely and internationally comparable.

- With trade liberalization in services gaining greater focus at the regional and bilateral levels (apart from the multilateral level under the GATS), recent RTAs and bilateral FTAs, (involving India and various East Asian economies), have focused on this as a key negotiation area along with merchandise trade. In this context, good quality and accessible data on trade in commercial services trade at a detailed sectoral level becomes absolutely essential for Asian countries, including India.

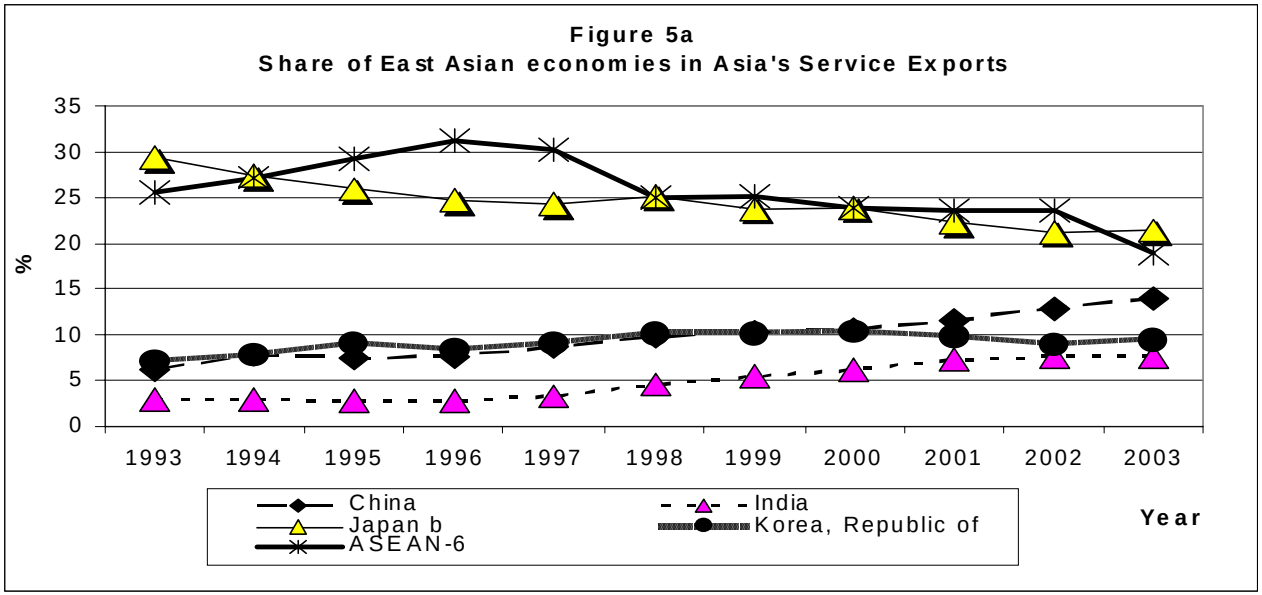
Leading Exporters and Importers in world trade in commercial services, 2003
(Billion dollars and percentage)

Rank	Exporters	Value	Share	Rank	Importers	Value	Share
1	United States	287.7	16.0	1	United States	228.5	12.8
2	United Kingdom	143.4	8.0	2	Germany	170.8	9.6
7	Japan a	70.6	3.9	3	United Kingdom	118.3	6.6
8	Netherlands	63.0	3.5	4	Japan	110.3	6.2
9	China	46.4	2.6	8	China	54.9	3.1
10	Hong Kong, China	44.6	2.5	14	Korea, Republic of	39.0	2.2
17	Korea, Republic of	31.3	1.7	17	Singapore	27.2	1.5
18	Singapore	30.4	1.7	19	Hong Kong, China	25.2	1.4
21	India	25.0	1.4	20	Taipei, China	24.8	1.4
28	Thailand	15.7	0.9	21	India	21.6	1.2
29	Malaysia	13.5	0.7	25	Thailand	18.3	1.0
40	Indonesia b	6.4	0.4	26	Indonesia b	18.0	1.0
				28	Malaysia	17.3	1.0

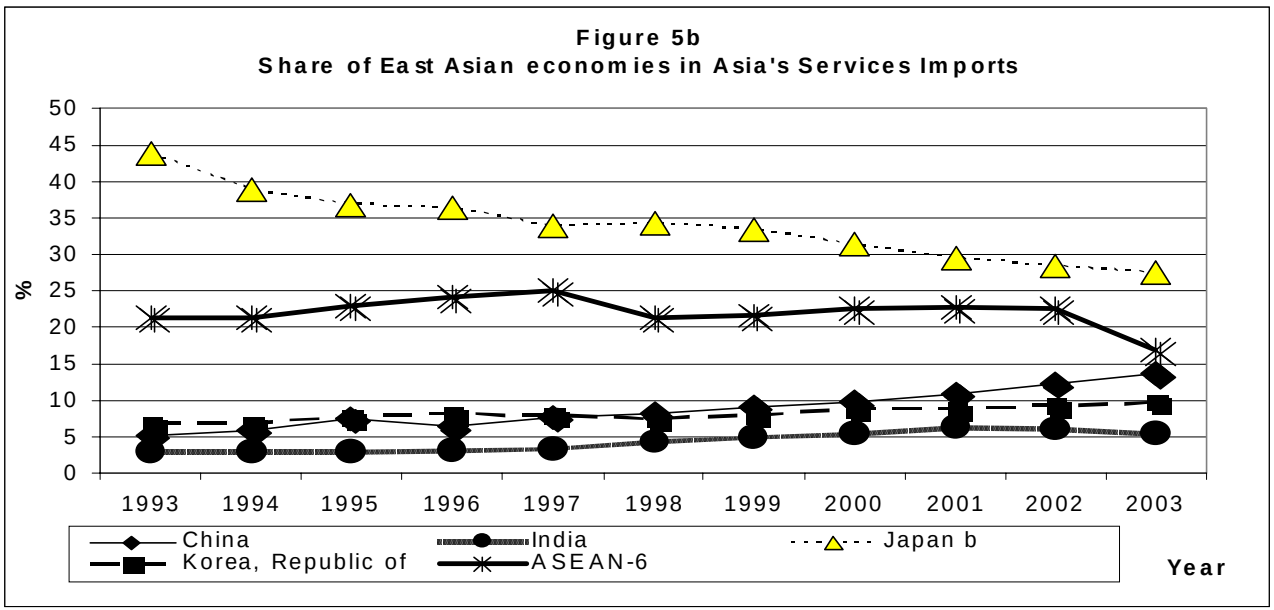
a WTO Secretariat estimate for exports in 2003 based on the methodology applied by the Bank of Japan up to 2002.
b WTO Secretariat estimate.

Note: WTO (2004)

India's 2004-2009 Foreign Trade Policy envisages service exports to grow to US $ 150 billion by 2009, of which software will account for US $ 65 billion. To the extent these targets are realized, India's global ranking in services trade may improve further.



Source: Computed from WTO (2004)



Source: Computed from WTO (2004)

Services Trade and Investment flows -2

- Anecdotal evidence, however suggests that India is increasingly becoming integrated with East Asia in the area of services trade; the slogan “served in India for the world” captures India’s aspirations in the services area well. It is widely acknowledged that in many services, not just the ICT services, Indian businesses are globally competitive, and that they have made important contributions to enhancing competitiveness of firms around the world.

- More than 100 of the Fortune 500 companies have set up R&D or design centres in India. Some of the activities are dedicated to bringing about future high technology products. The East Asian firms have been relatively less pro-active in setting up such centres in India. There are indeed untapped opportunities for firms from Japan, Korea, Singapore, Malaysia as well as China to partner India in setting up such centres for mutual benefits.

- East Asia is particularly strong in the logistics sector. This is an area of comparative weakness for India. This could provide considerable commercial opportunities for the East Asian businesses. India needs to develop an integrated strategy towards developing logistics and IT infrastructure and also enhancing its industry base, and partnering with East Asia could reap reach dividends, as the latter has already developed a significant expertise in this area

- As air connectivity between India and East Asia improves further and as India follows ASEAN and China in emphasizing the role of tourism sector in its own economic growth and employment generation strategies, the volume of service transactions relating to tourism trade are also expected to rise rapidly. India has already an open sky policy for all airlines as far as cargo is concerned; and is committed to facilitating substantially greater air connectivity for its own airlines and for those from ASEAN.

Services Trade and Investment flows -3

- In 2003-04, India actually received US $ 4.7 billion in FDI (equivalent to 0.6% of GDP), and US $ 11.4 billion in portfolio investment (Reserve Bank of India, 2004). As maybe expected portfolio investment flows have exhibited much greater volatility than the FDI. India is increasingly aligning its FDI reporting with the international practice which includes re-investments, external commercial borrowings and loans to affiliates As the stock of FDI continues to grow, the reinvestment and other components will become increasingly important in providing a steady base of FDI inflows.

- It is worth noting that since a significant proportion of FDI has been in the R&D and service sector facilities, which do not require large investments, the linkages and employment multiplier impact of such FDI is also higher per each million dollar of FDI as compared to the situation where most of the FDI is in capital intensive manufacturing and other activities.

- In recent years, as India's foreign exchange reserves position has become comfortable and it is not attempting to passively accumulate higher and higher forex reserves (As at end December 2004, India's foreign exchange reserves were US $ 131 billion), and as Indian companies begin to regionalize and globalize, the outward flow of FDI from India has also been increasing

- India's total FDI stock abroad is estimated to be around US $ 6 billion and rising rapidly. As an example, Tata Steel's recent acquisition of National Steel based in Singapore will impact several Southeast Asian economies where National Steel has manufacturing facilities. Similarly, Tata Motors' acquisition of Daewoo's truck plant in South Korea will enhance its presence in East Asia.

Services Trade and Investment flows -4

- Encouraging the formation of the Indian diaspora and leveraging on their strengths could be an element of the strategy of some of the East Asian countries in deepening linkages with India.

- It is also worth noting that in almost every Asian country, India's internationally competitive and culturally compatible professional and semi-skilled human resources is making important economic contributions as managers, technicians, professionals and semi-skilled workers. These do not get captured in the usual statistics but nevertheless are an important indicator of India's integration with East Asia. The Diaspora has also been instrumental in expanding India's civilizational influence in Asia and rest of the world.

Why Partner India ?

- India has entered into strategic partnership with EU and US; with the latter, economic relationship under the second term of President Bush will accelerate
- Provides large market for exports from partner countries
- Total Goods and Services Trade to reach USD 500 billion by the end of the decade; and GDP to exceed USD 1000 billion
- East Asia's share in India's world imports is already a quarter and rising. Some think this is a small share. Is not slightly smaller share of a mega economy at least as important as somewhat larger share of economies of USD100 billion or so?

Partnering India-2

- Provides a market-determined and secure avenue for channeling East Asia's excess savings into investments - both direct and portfolio
- India's bond advantage could be an asset in developing the Asian bond markets
- Third largest number of daily transactions in the world; Second lowest transactions costs for institutional investors in India's stock markets
- Nearly USD 30 billion invested in India's stock markets and rising- East Asian financial institutions are conspicuous by their absence
- More than 80 % of foreign companies are profitable in India within a short period; profitability rates are high and predictable

Partnering India-3

- Strong complementarities in demographic cycles- East Asia moving from demographic gift phase to the burden phase, India the reverse

- This has also strategic implications as countries such as Japan and Korea could partner India in core technologies

Partnering India-4

- India's growth strategy based on strong and increasingly globally competitive and networked domestic companies could provide a balance for highly trade and FDI dependent East Asian economies. Therefore the finding that business cycles in east Asia are highly correlated is an argument for its greater integration with India, whose business cycle is not so highly correlated with them

Partnering India-5

- Setting up knowledge based activities in India could be a vital competitive tool and enable East Asian companies to take advantage of India's human resources

- East Asian economies can substantially extend its economic space and its technological capabilities and capacities through partnership with Indian firms, particularly in biotechnology, pharma IT, space and certain manufacturing areas such as auto design. Such partnerships will permit them to access knowledge professionals from India without necessarily requiring the physical movement of these professionals. Many East Asian economies, viz. Japan, would thus be able to extend its economic opportunity set, and diversify global business risk.

- energy security and trade flows between India and East Asia are heavily dependent on secure routes through the Indian Ocean. India has common interests with these countries, viz. Japan in keeping this vital sea route secure, and is developing capability to constructively cooperate with Japan in this area.

Partnering India-6

- The presence of East Asian financial institutions in India's increasingly sophisticated and competitive finical and capital markets is also extremely limited. Foreign Financial Institutions (FII's) have invested about USD 60billion in India's stock markets alone.

- East Asian economies, viz. Japan has limited presence in venture capital and private equity funds in India. There are many small and medium size Indian companies and startups in high technology areas, which provide substantial opportunities for private equity and venture capital firms.

Partnering India-7

- In particular, strong case for a strategic partnership between India and Japan
  - **Economic- Trade, Investments and knowledge intensive activities, Core technologies**
  - **Demographic Complementarity**
  - **Energy /Trade Routes Security: Mainly through Indian Ocean**
  - **Leveraging on each other's strengths and aspirations**
- It would be useful if the joint study group agreed upon by the Prime Ministers of the two countries in November 2004, gives priority to considering specific ways to bring about the wider and deeper engagement between the two countries

Concluding Remarks

- Time to put behind cold war division of Asia and institutions; Essential that all major Asian economies are represented in the post-cold war New Asia

- India's policymaker, business community, media, and researchers on their part need to make concerted and focused efforts to mitigate substantial information and perception gaps in East Asia about India. Proficiency in commercial diplomacy and soft power skills will be vital in this task. India is competing for influence with other Asian countries, such as China, Japan and Korea. More strategic and tactical nature of its diplomacy and its business expansion in the region is needed.

- The ultimate determinants of India's success in engaging not only East Asia but also other major powers will continue to be its economic and governance records, and perusal of strong and credible national security polices.

THANK YOU !