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Sino-Indian Trade
Present Tense, Future Perfect?

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The ongoing global financial crisis seems to be taking its toll on world trade and trade relations amongst all great powers have sneeked into a recession mood. Bilateral trade between China and India, is no exception. For the first time since the two countries gave a 'big push' to economic engagement between them, the bilateral trade remained lower in the first quarter of 2009 against the comparative figures for the same period in 2008: both in absolute volume and in the growth rate. Add to this, the off and on acrimony over trade-related disputes such as the ban, until recently, on Chinese toys.

Suddenly, the bilateral trade that was riding a high tide seems to be in troubled waters and scepticism has overshadowed this fastest developing aspect of relations between the two countries. Will this slump be momentary? Will the bilateral trade relations be back on track once the recession period is over? What is the future of Sino – Indian trade relations?

I
SINO-INDIAN TRADE: THE PHENEMENOL HISTORY

Until the mid-1980s, economic relations were virtually non-existent. Rajiv Gandhi's visit to China in 1988 led to development of trade between the two sides. By that time, China's success and recognition for its export-led growth had its admirers everywhere and India under Rajiv Gandhi sniffed an opportunity. Both the countries had certain comparative advantage, complementarities and trade specialisations that provided enormous potential for bilateral trade. Starting with a low base (US$200 million) in 1989, the bilateral trade has zoomed in recent times and touched almost US$52 billion in 2008. The upsurge has been on account of numerous factors. China's hunger for raw materials, intermediates and components saw big leap in the Indian supply of the same.

China, on the other hand, has been exporting value added items, especially machinery to India. There was also plenty of space to cover, given that trade relations were negligible till two decades back. Sustained political patronage by the leaderships of the two countries also provided the required impetus. The growth trajectory of the bilateral trade made even Indian Prime Minister Dr. Manmohan Singh wonder during his January 2008 trip to China, "if China and India have been underestimating their capabilities of their respective industries and their strong urge to do business with each other". Dr Singh had reasons to sound optimistic. By the end of 2007, China had already emerged as India's largest trade partner overtaking the US. As late as 2001, Sino – Indian bilateral trade was barely half of Indo – US trade; in fact, UK, Belgium, Germany, UAE and Switzerland were all larger trading partners of India than China.

Optimism and euphoria not withstanding, there are fundamental concerns in Sino – Indian trade relations. First, bilateral trade is still not commensurate with the rising power profile of the two countries. China had higher trade figures with EU (US$436 billion), US (US$409 billion), Japan (US$236 billion) and ASEAN (US$231 billion) in 2008; India comes at number ten in the pecking order. The Joint Study Group (JSG), commissioned during Atal Behari Vajpayee's visit to China in June 2003, identified numerous measures related to trade and economic cooperation, and recommended their expeditious implementation. However, India is likely to remain behind China's major trade partners in the foreseeable future.

Second, bilateral trade with China also means trade deficit for India with the gap widening every year (pegged at US$10 b in 2008). China's large manufacturing base enables it to offer a large basket of manufactured goods to the Indian market while the inadequate development of the Indian manufacturing sector prevents the expansion of Indian exports to China. India still depends on raw materials – with iron ore constituting 60 percent of its exports.

Third, while both the countries have carved out various trading agreements with their neighbours and other significant countries, they are yet to warm up to each other on a mutual Free Trade Agreement (FTA). While the JSG had recommended an India – China Regional Trade Agreement (RTA), the issue is pending with a joint task force. It appears that China is more interested in an RTA given its export-based economy and advantages in manufacturing sector. It also wants ‘market – economy’ recognition from India. However, the Indian industrial associations find it bit premature for India when the country exports mainly primary commodities to China and its services sector is fragile vis-à-vis China. On its part, the Government of India fully empathises with their stand.

Fourth, although both countries are parties to a bilateral investment promotion and protection agreement (BIPA) since November 2006, mutual investments are paltry. While India accounts for less than 1 per cent of China’s total FDI receipts, actual investments by China account for merely 0.01 per cent of total foreign investment in India, ranking 63rd. Indian companies have invested in steel, textiles, chemicals, automobile components, pharmaceuticals and IT apart from service sectors like restaurants, entertainment, culture and banking. The Chinese companies are investing in telecom, metallurgy, transportation, electrical equipment and financial sector. So far, the relative benefit has been largely on the Chinese side.

II
BILATERAL TRADE: THE RECENT DECLINE

Growth in trade is linked closely to growth in GDP. The global trade growth in fact came down to 6 per cent in 2007 due to a reduced growth in the world GDP to 3.4 per cent. Weakening demand from developed economies, realignments in exchange rates and fluctuations in the prices of commodities such as oil and gas were the background factors. In 2008, the decline became rather more pronounced with growth plummeting towards the final months. As rising economies with a rising share in global trade, China and India have come under the ‘domino impact’, though not in the same proportion as many of the western economies.

> Sino – Indian bilateral trade has had to bear the brunt. The bilateral trade in January 2009 fell by 37 percent over the same period in 2008. So, in the first month of this year, Sino – Indian trade was less than US$3 billion; normally it should have been more than US$4 billion.

The Chinese economy that was almost overheating at the beginning of 2008 began to fumble in the second half of the same year necessitating stimulus plans by the government. The GDP growth rate came down from 13 per cent in 2007 to 9.5 per cent as 2008 came to a close. The potential GDP growth rate in 2009 is estimated to be around 6.5 per cent according to the World Bank estimates though the Chinese themselves are more optimistic. Consequently, China’s bilateral trade with other countries has also been growing slowly. At the end of 2008, China’s foreign trade ticked US$2.56 trillion, going up by 17.8 per cent compared with 2007 in terms of absolute value but down 5.7 per cent in terms of growth rate.

Thus, for the first time in seven years, the growth rate had dipped below 20 per cent. Exports were up 17.2 per cent to US$1.43 trillion and imports up 18.5 per cent to US$1.13 trillion but the annual export growth rate slowed by 8.5 and imports by 2.3 percentage points. According to the latest estimates, total foreign trade for China was US$124.95 in February 2009, down 24.9 per cent year-on-year. China’s exports plummeted 25.7 per cent year-on-year in February 2009, the worst decline in more than a decade. Exports contracted for the fourth month in a row to US$64.9 billion while imports slumped 24.1 per cent to US$60.05 billion. The trade surplus narrowed to US$4.84 billion, less than one seventh figures for January. The continuous slump in trade surplus is threatening to erode its seminal role in China’s growth, forcing the country to look towards domestic consumption to sustain the same. So far, all hopes for an early recovery have been belied as reflected from the latest trade figures for the month of March where the trade volume of US$160.02 billion was still down by 20.9 per cent year on year.

India’s GDP has also been impacted by the global meltdown. While the GDP grew on an average by 8.8 per cent in last five years and by 9 percent in 2007-08 fiscal year (1April to 31 March), it was down to 7.8 per cent in the first half of the current financial year (2008-09) and the Indian Government expects to pull a figure between 7 to

8 percent in 2008-09; an optimism not necessarily shared by the international institutions. The latest IMF forecast says that India's GDP growth would slow to 6.3 percent in 2008-09 and to 5.3 per cent the following year. Logically, therefore, India's foreign trade has shown tardy progress. As per the provisional estimates, India's exports shrank by 15.9 per cent in January 2009 compared to the figures for January 2008. During the same period, imports also came down by 18.2 per cent. Similarly, in February 2009, India's exports figure came down by 21.7 per cent at US$11.9 billion comapred to February 2008 of US$15.2 billion. Imports slumped by 23.3 per cent at $ 16.8 billion in February 2009 comapred to US$21.9 billion in February 2008. The estimates for the month of March 2009 show that the downward slump would continue.

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III
THE POSITIVE SIDE

The slump and the tensions notwithstanding, certain factors do engender positive outlook. First, the sharp decline in the bilateral trade has not come from the official policies of the two countries. Rather, it reflects the current swing in the global trade where major trading powers including China and India have become victims

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of the ongoing global slowdown both in economic growth as well as trade among nations. The bilateral trade of China and India have gone down not only with respect to each other but also where other nations are involved.

However, compared to other nations, the two countries have suffered relatively lesser meltdown and indeed continue as the 'important sources of growth'. Second, the so-called trade tensions are mere reflective of the general recessionary mood where all countries are apprehensive of sliding trade statistics and have taken measures to preserve, protect and promote their foreign trade. China and India are no exceptions to this ubiquitous trend. Similar spats recently also happened between the US and Mexico. Third, China and India have institutionalised regular financial dialogue to thrash out trade disputes as and when they surface.

Thus, when the dispute over the banning of Chinese toys flared up, the commercial representatives of the two sides met in New Delhi in the third week of March and after the Chinese side agreed to meet some of the safety concerns raised by India, the ban on imports of toys was by and large lifted. This has provided China a renewed access to the US$500 million (Rs.2,500 crore) Indian toys market. Such meetings also provide platforms to explore further enhancement of trade relations. India, for instance, used the recent meeting to impress upon China for granting market access for certain categories of fruits and vegetables.

IV
THE FUTURE

There are numerous reasons to believe that the present lull in the Sino – Indian bilateral trade could be just a temporary phenomenon. First, economic aspects remain the fastest growing element in the bilateral relations and the trend will continue. Bilateral trade grew at over 30 per cent a year till 2002 and at an average of 50 per cent a year between 2002-2006 and even if the rate slumps to 25 per cent in future, Sino – Indian trade would still stand at over US$75 billion by 2010 and

US$225 by 2015. These are certainly large numbers.

The two countries have been working on ways and means to sustain the momentum. Given the fact that the border trade between the two neighbours is still marginal, regional FTA is yet to take off and many sectors are yet to become part of this trade, there is a huge space for growth. Second, the emergence of China as India's largest trade partner since 2007 has created an opportunity that the two counties would like to seize upon to construct a sound economic partnership. India would like to move up the ladder from its present tenth position in the Chinese pecking order of trade partners.

Also, given that China enjoys a huge trade surplus, India would also look towards diversifying and expanding its export basket to bridge the deficit. Third, the export profile of the two countries is largely complementary. There are only 25% items where they compete in the global market. Hence, the India vs. China debate may not hold substance at least in trade sector. Even in items where they are supposedly in competition, such as oil, the two countries are learning to cooperate. Therefore, for the foreseeable future, both sides have agreed to 'diversify their trade basket, remove existing impediments, and optimally utilise the present and potential complementarities in their economies, in order to sustain and further strengthen bilateral commercial and economic cooperation'.

Together, the two countries can do a lot in the interest of developing countries on the global financial and economic stage. Fourth, without taking sides in the 'flag follows trade' hypothesis versus 'trade follows flag' hypothesis, economic interdependence through increased trade has created new stakes in the bilateral relationship. As the protagonists of this thought argue, this should have a stabilising effect on the bilateral relations for 'it is not so much the quantity and quality of economic intercourse between Beijing and New Delhi that will mitigate their security vulnerabilities, but rather conscious policy choices in each country to avoid military entanglements during this period of domestic consolidation'.

Fifth, since economic engagement has proved to be one of the reliable confidence building measures (CBMs) in bringing China and India closer, economic engagement will continue to get priority by the top political leadership of the two countries in reaching out to each other. The two countries would look forward to expand the trade relations, build trade alliances inside and outside the WTO and seek enhanced stakes in the emerging international economic order. A mutually beneficial arrangement can emerge only if China and India seek to support, sustain and raise the level of the present economic engagement between them. Thus, there are enough reasons to expect that the spring season in Sino – Indian trade relations would return sooner rather than later.

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