Trade imbalances between India and China - Causes, Consequences and Potential solutions

Abstract

India and China stand amongst the world's largest growing economies. However, due to improper implementation of industrialization and ignorance to certain sectors, India found it difficult to achieve top place in the global supply chain. China, on the other side, adopted an open market economy with speedy reforms and boost in manufacturing, which gave it a big role in the world market. They started producing cheap-finished goods which caused India's domestic market favoring them over relatively costlier Indian goods. This led to import-export imbalance between India and China, further causing a trade deficit. Less exports, more imports, Chinese devaluation of Yuan, lack of market access are some of the reasons for this trade deficit. This trade deficit had a huge impact on the Indian economy as its GDP growth rate slowed down. How can we bridge this deficit? Boosting the Manufacturing sector, bringing in reforms in the space sector and developing the Renewable energy sector can help India to overcome its trade deficit.

Introduction

Being two of the oldest civilizations in the world, India and China share some traits in common, and these are growing population and growing economy. Both the Nations have been each other's diplomatic partners since 1st of April 1950, when India was the first non socialist country to develop diplomatic ties with the PRC (People's Republic of China). Although, the diplomatic relations were formed in 1950, Bilateral trade between the two started in late 1980s when the then Prime minister Shri Rajiv Gandhi visited China. Both the countries have signed various agreements together including the Double taxation avoidance agreement (DTAA) which was amended recently. This showcases their emerging bilateral relations.

By 2008, China became India's largest trading partner. On the other hand, India became the 12th largest trading partner for China by 2019. But, these growing ties had a drawback on the Indian economy. Even Though, India got availability of low-priced goods and commodities through it's trade with China, it's dependence on such imports increased along with it's trade deficit. With policies like 'Make in India' and 'AatmaNirbhar Bharat', the current government is trying to rebuild a strong base for the Indian Manufacturing Sectort, even after such great initiatives, the trade deficit has increased in 2021 by almost 52% and has been increasing y-o-y. This deficit had a negative impact on the Indian economy as unlike it's dependence on countries like Russia, Saudi Arabia and UAE for irreplaceable commodities like Oil, the Chinese imports can be replaced to a certain extent, but the increasing dependency for such commodities is causing problems for the economy. This paper analyzes the trade deficit for the Indian economy in the Sino-Indian trade relations and its causes, consequences and some potential solutions to it.

Overview of India - China trade relations

The Indian economy went through a lot of hurdles with the 1991 Balance of payment crisis, but, with it's timely adaptation of economic reforms and efforts, the 'Indian Elephant' managed to transform itself into the 'Indian Tiger'. The Chinese Dragon, on the other hand, had a quick but fluctuating start with the opening of the economy in the 1980s. The Sino-Indian trade ties have been continuously growing since the early 1990s, when both the Asian giants were trying to rebuild a strong economic base in the world of globalization. The trade ties began when both the nations signed a trade agreement in 1984. Later on, this led to the "Most Favored Nation" treatment for both. The then Prime Minister Shri Rajiv Gandhi visited China in 1988 which further favored the growing trade ties between the two.

Both India and China signed DTAA i.e., Double Taxation Avoidance Agreement with each other in 1994. This DTAA was signed with a motive to avoid being taxed twice for the same income for the people residing in those countries signing the DTAA. For example, if a person residing in China invests in an Indian company (maybe in stocks), when they receive their income from this investment, then that income might've been subjected to be taxed by both India and China. However, with DTAA, the income earned will only be taxed in one country (either India or China). This encouraged business and trade between both the countries. Further, the opening of Nathu La Pass in 2006, facilitated cross border trade relations between India and China. By 2008, China became India's largest trading partner (a spot which was held by UAE earlier). Indo-Sino bilateral trade saw robust two-digit growth in 2017 and 2018. By 2019, India became China's 12th largest trading partner. However, due to the impact of Covid-19, the Indo-Sino trade ties faced a reduction of nearly 13% in the period of January to September 2020 ($60.5 Billion) as compared to it's trade in 2019 ($69.7 Billion)[1].

China's exports to India mostly consist of Automobile and computer parts, mobile phones, organic chemicals, electrical machinery, nuclear reactors, toys, fertilizers etc. This shows how diversified Chinese exports to India are! India, on the other hand, exports goods and commodities like mineral fuel and oil, copper, iron ores, lithium, aluminum, natural gems, petroleum oils, cotton yarn etc. This shows that India's exports to China mostly contain Raw materials. However, this trade is filled with many imbalances and the negative impact of which is mostly faced by the Indian economy. The Indo-Sino bilateral trade was $125.62 billion in 2021 with a trade deficit of $69.56 billion, which increased up to $136.26 billion in 2022 with a trade deficit of $101.28 billion[2]. This showcases the fact that India needs to work to curb its imports from China, while also increasing its exports, to maintain the trade balance.

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[1] Ministry of External Affairs report on " India - China Bilateral Relations", December 2020

[2] https://www.eoibeijing.gov.in/eoibejing_pages/MjQ,

Comparing trade imbalances of the year 2021 with the year 2022

Trade imbalance between India and China is a matter of concern for the Indian economy. According to the General Administration of Customs China (GACC), there was actually a slight decline in the deficit in 2019 by 1.88% (for the first time since 2005[3]). The deficit went from $58.04 billion in 2018 to $56.95 billion in 2019. According to the Indian embassy in Beijing, it further decreased by 19.39% in 2020 to reach $45.91 billion due to the covid-19 pandemic. However, this trade deficit has been increasing since 2021. It reached up to $69.56 billion. This shows that there has been a 51.51% increase in the trade deficit. In 2022, India crossed the number of $100 billion of trade with China with a 45.60% increase in the trade deficit. Indian imports from China expanded from $97.52billion in 2021 to $102.25 billion in 2022. This points towards increasing trade deficit and import dependency on China. What must be the possible reasons for this increase in trade deficit since 2021?

1. Narrow basket of export commodities to China
2. Lack of access to the Chinese market by Indian companies
3. The Indian manufacturing sector was gradually recovering from the covid 19 pandemic in 2021, hence, we see high imports. India imports Active Pharmaceuticals Ingredients (API) and electronics from China, so, the pandemic caused troubles for the Indian manufacturing sector in 2020.
4. Many experts say that the rise in intermediate imports is actually a sign of industrial recovery and greater demand for inputs, as Indian exports are also growing gradually.

The imports further increased in 2022 and further the trade deficit has reached up to $83.2 in FY23.

Bilateral trade deficit

Both India and China have been rapidly engaging in trade relations with each other since the past two decades. There was a time when China was economically behind several countries like Singapore and Belgium in 2001, but due to its open market policy, along with it getting a WTO (World Trade Organisation) member status, the Chinese dragon got a speedy start to development. However, this led to increasing trade imbalances between India and China. China has maintained a stable economic growth rate of about 10% over the decade and this is why today China stands as World's Largest Exporter. China emerged as India's largest trade partner in 2008, but its trade deficit kept on increasing. It went from $0.34 billion in 2002 to $20.1 billion in 2010 and further went from $29 billion in 2012 to $44.8 billion in 2015. This issue of trade deficit was the main area of discussion during PRC President Xi' visit to India in 2014. Both sides agreed to work together on reducing the trade deficit. Nevertheless, the trade deficit still continues. Bilateral trade deficit is speculated to cross

[3] https://www.eoibeijing.gov.in/eoibejing_pages/MjQ

$100 Billion in FY2023 as it has already crossed $89 Billion in 2022. This trade deficit has negatively impacted the Indian economy. It shows our severe dependency on Chinese imports, which harms the indigenous producers.

Causes of trade deficit

a) Narrow export of commodities to China:

India's exports to China have gone down from $28.03 billion in FY21 to $17.49 billion in FY22. This is one of the many causes of the trade deficit between India and China. India exports a very narrow basket of commodities to China, which consists of copper, organic chemicals, jams, cotton, spices (mainly chillies), aluminium, plastics, coffee, tea, etc. This shows that India mostly exports primary raw materials to China. Over a period of time, these exports have been overshadowed by Chinese exports of bold-finished goods, which are relatively more profitable as raw materials incur less cost. China exports many cheap finished goods, which makes them more pocket friendly as compared to indigenous goods. This leads to an influx of Chinese goods into the Indian market, further causing trade imbalances. Indian exports often face challenges regarding competitiveness and market access in China. This is because of non-tariff barriers like regulatory hurdles, product standards, certification requirements, etc, which make Chinese market access difficult for Indian exports.

b) Indian withdrawal from RCEP:

The Regional Comprehensive Economic Partnership (RCEP) was a trade deal between 16 countries, but with India opting out of it in 2019, it has become a 15 member agreement. This RCEP was built to be the "largest regional trade agreement" with almost half of the world's population contributing over a quarter of world exports. So, what must be the reason for India to opt out?

1) India pulled out of this agreement as it was majorly China backed and failed to address India's core issues.
2) RCEP contains India's FTA with many countries (except China). This leads to an increase in imports more than exports. According to NITI Aayog's paper on "A note on free trade agreements and their cost for India", India has a trade deficit with most of the RCEP member countries[4]. This could be disadvantageous to India as RCEP eliminates or reduces tariffs on imports.

However, with India's withdrawal from RCEP, it has missed the chance to attract its place in the global supply chain as RCEP members are more likely to form strong value chains among themselves. By staying in RCEP, India could've had a chance to counter China, therefore bringing balance to the bloc and further impacting the decision it takes. Withdrawal from RCEP can also lead to issues for India's

[4] Saraswat, V.K., Priya, P., and Ghosh, G., 2017, “A Note on Free Trade Agreements and their Costs,”, NITI Aayog, New Delhi.

bilateral ties with other RCEP members. The upcoming India-Japan-Australia network to counter China by building a supply chain would also be affected by it. India would be less attractive for foreign investment as foreign firms producing in India would be deprived of access to the RCEP market. While India is true in its stand of opting out of RCEP as it will impact the Indian producers due to lesser tariff duties on the imported foreign goods, withdrawal will also result in less market access to RCEP countries, further causing problems for Indian export.

c) Heavy import reliance on China:

In order to understand India's heavy import reliance on China, let's classify the items of trade into raw materials, intermediate goods, capital goods and consumer goods as per the classification led down by the World trade organization.

Table : Composition of India's Trade with China in 2013 (WTO Classification)

India's Exports to China	Proportion	India's Imports from China	Proportion
Intermediate goods	49%	Capital goods	47%
Raw materials	36%	Intermediate goods	33%
Consumer goods	7%	Consumer goods	14%
Capital goods	7%	Raw materials	6%

Source: Authors' calculation using UN COMTRADE Database.

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(Image taken from Economic and Political weekly)

The above given table shows that about 85% of Indian exports to China consisted of raw materials and intermediate goods. While on the other hand, 80% of our imports from China are mainly capital and intermediate goods. This shows that India's export spectrum is mainly in labor-intensive and resource-based products. Whereas, China exports bold finished goods to India. Raw materials being cheaper than finished goods, Indian export value often falls less than its import value. This is also the way China carved its place in the global supply chain post 1990s. China has been utilizing it's large population and manufacturing capacity to achieve "Economies of scale" in various industries. This "Economies of scale" is basically when a Company or a Country can reduce its production cost by increasing the scale of its operation. This allows the Chinese manufacturers to produce commodities at lower costs, thus competing effectively in the global market. Due to the low cost manufacturing capacity, China became the hub of global manufacturing. One of the reasons why Chinese goods gained popularity in India, was that they were low priced with relatively to-do quality (for example Xiaomi phones, which were insanely popular in India due to being cheap, user-friendly and durable). China exports finished goods from electronic items to textiles or even toys to India. This shows their vast export spectrum. This is also the reason why India is heavily dependent on Chinese exports. This shows that the affordability factor should be kept in mind while exporting goods to developing or under developed countries, as due to low income, the chances of your cheap priced product being sold quickly are quite high.

How does it affect India?

1. From a political perspective, political and security challenges increase when a country depends too much on an unfriendly country (as India and China have been having disputes over border with border clashes like the Galwan conflict recently) for its imports. These are called "Dependency risks". Excessive dependency on an unfriendly nation can increase the risk of economic pressure by the country. China can politicize its dominance and impose unfair conditions, manipulate prices or even trade restrictions. This can negatively impact the Indian economy. As far as the security challenges are concerned, India and China have a long withstanding border dispute over LACC, so, too much of economic dependence can maybe weaken its bargaining power.
2. It is speculated that around 25% of coal generated in India might be coming from the plants that are using equipment imported from China. This may come forward as a security challenge. Also, due to this dependence, cutting off Chinese imports might cause the Indian power industry to suffer high costs.
3. India has been importing most of its Active Pharmaceuticals ingredients (API) from China. This caused problems during the Covid-19 Pandemic as India was too dependent on China.
4. Another threat to India is Politicisation and Weaponization of supply chains by China. According to the "Annual Threat Assessment" report by the National Intelligence of the United States, China is already using its dominance in the global supply chain to force foreign companies and countries to transfer their technologies and intellectual property to it[5]. During a speech at the strategic dialogue conference in Pune, Army Chief General Manoj Pande has accused China of using weaponization and predatory economics of supply chains to increase its influence[6]. Politicization and weaponization of supply chains is basically using trade as a tool of coercion to achieve political or strategic influence, with making trade as a key element of foreign policy. Currently, the Chinese dominance in the global supply chains, along with Indian dependence on China for imports, is raising threats for the Indian Economy. This is because, if the import dependence increases, China can use it as a weapon against India. It can carry out predatory pricing attacks. Also, with too much Indian import dependence, if China

[5] Office of the Director of National Intelligence of United states of America report on "Annual threat assessment", February 6, 2023

[6] https://www.google.com/amp/s/indianexpress.com/article/cities/pune/army-chief-china-using-weaponisation-of-supply-chain-to-expand-its-influence-8522595/lite/

decides to shift some of its imports from India to Pakistan, it can again cause problems with the trade deficit.

d) Lack of Tariff barriers:

Even though there is no direct FTA (Free Trade Agreement) between India and China and even after India imposing Anti Dumping Duty on few Chinese goods, the Chinese import influx to India is still very high. It went from $97.52 Billion in 2021 (According to the Indian embassy in Beijing) to $102.25 Billion in 2022. This is because there are less tariffs on inputs (majorly components and sub-assemblies) and India's import duty being lower than other economies, the production cost here is very high. If you increase your import tariffs, but don't have sufficient capacity to produce, the cost of production increases and this leads to the country losing competitiveness as it will be taxed instead of subsidized. So, what needs is perhaps more planning in this field of tariffs to reduce the trade deficit.

e) Improper implementation of Industrialization:

India had adopted a "trickle- down" economy based on a heavy industrial plan with a vision to make the resulting economic development reach grassroots through industrial development. However, amidst this process, less attention to agriculture caused high poverty, low economic growth and low demand in India. Important social sectors like the Education and Health sector's expenditure too were ignored. This led to unemployment which hampered industrial development from reaching its full potential. India also lacked far behind in its economic potential due to improper policies for land, labour and capital utilization . While, at the same time, China opened itself for investment and international trade and had begun production of cheap finished goods to which India felt lethargic. The manufacturing sector, too, was getting very little attention from the government. Also, due to License Raj, excessive regulations, licenses and permits for Industrial activities, the growth of the Manufacturing sector was restricted and it caused bureaucratic hurdles, limiting competition and discouraging private investment.

f) Lack of Investment, Infrastructure and Machinery in the Automobile and Electronics sector:

One of the major problems behind our trade deficit with China lies in our dependency on others (mostly China) for high technology manufactured goods. Chinese companies invest huge amounts in the mobile/cell phone business, power and telecom sector. These Chinese technological goods are popular among middle class and low income families in India due to them being pocket friendly and even somewhat durable these days. Popularity of smartphone brands like "Redmi " is the best example to take. Despite efforts like "Make in India " and "Vocal for Local", the Indian manufacturing sector is still finding it difficult to self produce some of the high technology goods. The main reasons behind this are lack of machinery, infrastructure and investment in the automobile and electronic sector. Let's take an example of manufacturing smartphones. One might wonder why a country like India which is among the top 5 largest producers of mobile devices doesn't have a big smartphone under its name. 'Make in India' initiative was helpful in giving India the role of smartphone manufacturing, but, using the term "manufacturing" here might be a little misleading since we don't actually make smartphones, we mostly only assemble the imported parts for brands like Oppo, Vivo etc. Hence, the main money goes to the countries owning these brands. Now the several reasons why India can't make it's own smartphone are lack of machinery, investment and high expenses with inadequate infrastructure. Making a smartphone or any electronic device requires Chips or processors or integrated circuits (IC) which are made from sand. Making an electrical chip is a complex process where sand is converted into silicon ingot to wafers which then goes under the process of lithography and then we finally get the electrical chip. Lithography is the step where we face problems. This is because of EUV (Extreme Ultraviolet) lithography machines. These machines cost $160 million each and are currently majorly made in ASML, a Netherlands based company. India lacks these EUV machines whereas China contains many of them. Apart from this, the maintenance cost of these EUV machines are quite high and one has to make sure that there are less than 10 particles of dust present around it. On the contrary, China invests huge amounts when it comes to technology. With its "Made in China 2025 policy" (announced in 2015), China made a $300 billion investment to become a high end producer for such equipment. It is speculated to have more than 7 semiconductor factories with each about 50 ASML DUV/EUV machines. Currently IC and semiconductors are what India is falling short on.

India lacks infrastructure and logistics facilities and this results in much higher transaction cost for exporters. This makes Indian goods less competitive in the Chinese market. Even though India has its own smartphone brand which is Haryana- based "Micromax", it doesn't share the limelight anymore. This shows how lack of infrastructure, machinery and investment is affecting the trade between India and China causing a deficit.

g) Imbalances in Currency Exchange Rate:

The Currency Exchange Rate between two currencies plays an important role in defining a trade deficit. When a country's exchange rate increases as compared to its trade partners', the prices of its goods and services also go up. Hence, imports become cheap which causes problems for domestic producers. This results in more imports and less exports. Recently, many instances like Covid 19 pandemic, Russia Ukraine war have resulted in a fall of 7 to 8% in exchange rate of Indian currency as central banks have resorted to several harsh monetary tightening policies. India's huge foreign reserve is what helps it maintain stability. But, to maintain healthy foreign reserves, a country needs a trade surplus. Hence, it is a complete cycle which goes like trade surplus-foreign reserves-currency exchange rate. In this case of India-China's trade relations, a huge deficit is seen which is affecting the reserves which is further affecting exchange rate which in turn increases the trade deficit. One Yuan counts for ₹11.75. This shows that the Indian Rupee has been relatively weaker than the Chinese Yuan which further makes the Indian exports more expensive for the Chinese buyers and Chinese goods cheaper for the Indian buyers. This broadens the trade imbalance.

h) Lack of access to the Chinese market :

Chinese market access is a huge issue for many Indian companies till today. Strict governmental control and regulations by the Chinese government hampers Indian companies from utilizing the Chinese market to the fullest. Pharmaceuticals, IT service and Agriculture are the sectors in which India has a stronghold in, but due to the strict government restrictions, Indian companies are unable to access the Chinese market. According to a research conducted by CII core group of China, Indian companies have a serious knowledge and information deficit about the Chinese market. This is also the reason why they are unable to fully access it. This discrimination is more with respect to the service sector in which Indian companies are globally dominant. The Chinese administration plays a major role with it, as one party controls the entire political economy of the nation, there are less checks and balances and so the policies are quickly implemented. On the contrary, India being a democratic system takes a little longer than China for policy implementation. For example, if a policy with more involvement of the profit-making private sector is introduced, it might face backlash from the opposition parties. Unlike these, Chinese investors are very competitive with each other along with the government keeping them in check with positive discrimination and institutionalized preference in favor of its state owned enterprises or PSUs (some of which are speculated to be against International law). Nevertheless, this way both of their private and public sectors flourish.

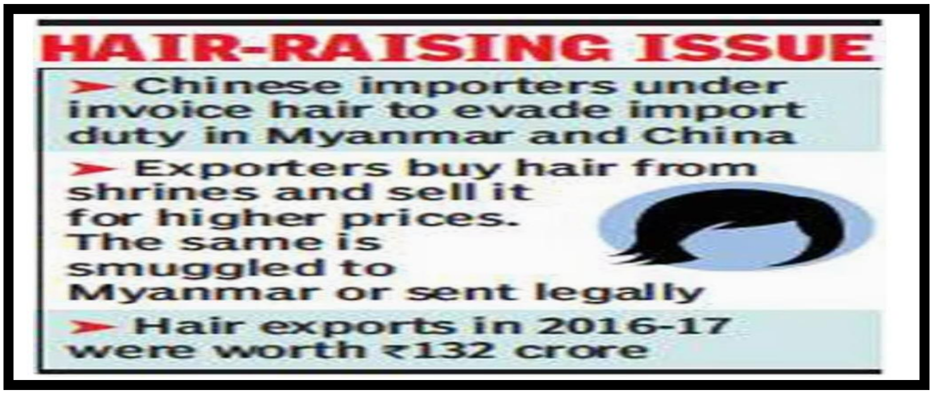
i) Impact of Covid 19 pandemic:

Covid-19 lockdowns under China's "Zero Covid" approach had more impact on consumption than production in China. This led to less demand for Indian goods in the Chinese market, further causing issues for Indian exports (which is already less than our imports).

j) Smuggling and Illegal imports:

Over ₹1000 crore worth smuggled goods from China were seized in 2016-17 by the DRI (Directorate of Revenue Intelligence) - India's chief anti-smuggling intelligence and investigation agency. A group of Chinese nationals were arrested for smuggling of gold from China and Taiwan to India in 2019. Again, in 2021, DRI stated that Chinese traders were smuggling out Human hair from India. They had made Hyderabad as their smuggling and illegal trade hub by under-voicing hair to evade import duty in China and Myanmar. These Illegal activities are also causing a trade deficit as many unregistered Illegal imports are entering India.

(Image taken from Times of India)



k) Deliberate devaluation of Yuan:

In 2015, the China central bank had devalued the Yuan (Chinese currency) by nearly 2% against the US dollar. This was done to boost Chinese exports and to take a step in becoming an official reserve currency. This was repeated again in 2020 when People's Bank of China (PBoC) devalued Yuan by 0.34% on 3rd January 2020, then again 0.2% on 6th January and 0.5% on 7th January 2020. The reason was speculated to be the continuous decline of manufacturing in China. Nevertheless, this cost a huge blow to the global market! How will it affect India? Devaluation of currency strategy is often used to bridge the Balance of Payment (BoP) gap. This is possible as currency devaluation increases the cost of imports and makes exports cheaper. Applying this logic, devaluation would make Chinese imports (India's exports to China) expensive and Chinese exports (Indian imports from China) relatively cheaper, further widening the trade deficit. Even in the International market, devaluation of Yuan would give an upper hand to Chinese exports as they are relatively cheap.

Analyzing India's "Anti-dumping duty" on Chinese goods

Indian producers are finding it difficult to compete with the cheap products dumped by China. With China involving itself in many unfair trade practices like special concessions to state owned enterprises, under invoicing, excessive export subsidies, non transparent trade practices etc, gives an unfair advantage to the Chinese exporters over Indian producers. This affects the Indian domestic industry. Dumping is basically when an exporter "dumps" goods to a foreign market at a price lower than its home country. This is considered as an unfair trade practice to which "Anti-dumping" is a major suggestion by WTO (World Trade Organisation).

The Anti-dumping duty is suggested according to article 6 of the GATT (General Agreement on Tariffs and Trade). This duty is imposed to protect the local producers from low-priced foreign goods. India had imposed Anti dumping duty on more than 90 Chinese products along with other 24 China related investigations going on at that time. The legal framework for this Anti-dumping duty is given in the section 9 of the Customs Tariff act of 1975 (Amended in 1995) and in Custom Tariff

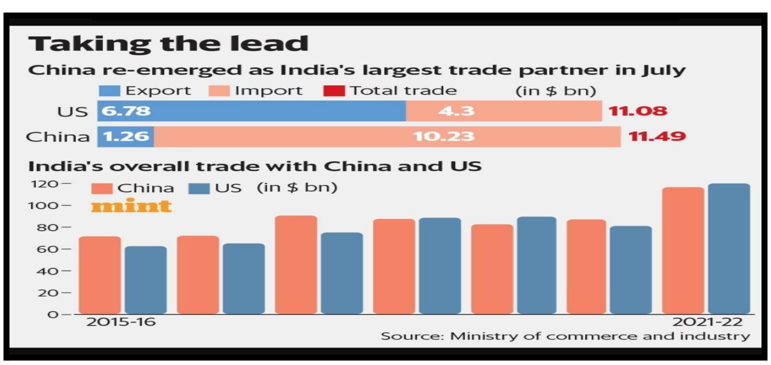
(Identification, assessment and collection of countervailing duty on subsidies articles and for determination of injury) Rules, 1995. Again in 2021, India imposed anti-dumping duty on 5 Chinese products including Aluminium, Silicon sealant (used for thermal power and solar photovoltaic modules), Sodium Hydrosulphite (used in dye industry), Hydrofluorocarbon and Hydrofluorocarbon blends (both used in refrigeration industry). On the recommendations of DGTR (Directorate General of Trade Remedies), the Ministry of Finance imposed this duty. India has imposed maximum Anti-dumping cases against China. This Anti-dumping duty is aimed to protect the domestic market from "injury". But due to shortage of personnel at DGTR, the effectiveness of the measures in providing timely relief is less. Nevertheless, the trade deficit between India and China still continues with our imports still exceeding our exports.

Comparing India-China Trade relations with India's trade relations with other countries

Let's compare India-China's trade ties with India's trade relations with USA and Taiwan:

1. **India-USA**

There has been constant tussle going on between the United States of America and China for becoming India's largest trading partner. Hence, India-China trade dynamic can be compared to Indo-US trade ties. India's relationship with the USA has been growing progressively in the past few years due to both sharing democratic values, common interest in regional safety and economic ties. On the contrary, India's relations with China have become a little complex due to increasing border tensions. In 2022, USA overtook China as India’s largest trading partner for a while, but China soon took over the position again with trade of $11.49 billion worth of goods in July 2022. The diagram given below showcases this dynamic pretty well.



India’s exports to the USA increased by 0.41% while imports from China increased by 45%. Recent Covid-19 crisis led to problems in US-China relations and many countries started finding alternatives for China. India was a best example for the role of alternative, considering its similarities with China in terms of large market and working force. This has brought the Indo-US ties even closer. Also, the USA is among the countries with whom India enjoys a trade surplus. As in 2021-2022, it's trade surplus reached up to $38.2 billion! This shows how India-Us ties are significant to tackle the increasing Chinese dominance.

2. **India - Taiwan**

India-Taiwan trade ties can be compared to India's trade with China as Taiwan doesn't share quite so friendly ties with China. Taiwan is among the 4 Asian tigers and is a developed manufacturing country. Taiwan is specifically known for manufacturing and exporting Electronic items (an industry which consists of a significant share of India's imports from China). Taiwanese manufacturers have opened their plants in India as the USA-China trade conflict caused high costs for sending goods from mainland sites to the US. Taiwan is a huge supplier of semiconductors and its supplies form 60% of world semiconductors share. Infact, technology related goods and services form nearly a third of Taiwan's GDP. India, too, is continuously researching on Semiconductors. This makes the India-Taiwan trade Partnership more favorable.

3. **Vietnam - a possible competitor?**

Apart from this, Vietnam has been emerging as a tough competition for India with it's economic reforms since the launch of Doi Moi in 1986. These reforms took Vietnam from one of the poorest to a middle income economy in just a few years. Today, the USA receives more garments from Vietnam than from India. In the world's "plus one" strategy to find an alternative for China, Vietnam stands tall in competition with India, to be the favored choice.

Hence, these comparisons show us that India can perhaps replace China for its trade by instead trading with countries USA or Taiwan. Taiwan plays an important role in the global supply chain and with it being one of the Asian tigers, India can divert its technical and electronic imports from Taiwan instead.

Analyzing the 'PLI', 'AatmaNirbhar Bharat' and 'Make in India' schemes

The Government of India has been planning to curb India's trade deficit with China by introducing a number of measures. Some of them are 'Make in India', 'PLI' and 'AatmaNirbhar Bharat'. Aatmanirbhar Bharat or "Self reliant India " is an initiative by the Government to reduce India's import reliance on China. The Product Linked Incentive (PLI) schemes under India's AatmaNirbhar Bharat initiative was introduced in the budget 2021-2022. How will this PLI work?

1. Incentives will be provided to the companies to manufacture more. So, more self made goods.
2. The more the country produces, the more the amount of foreign investment it gets! This also leads to earning a major place in the global supply chain.

The Indian government has adopted the PLI scheme for various sectors including telecom and networking, pharmaceutical drugs, electronic products etc. These are also those sectors where India mostly imports goods from China. So, this PLI initiative will aim to make India self-sufficient for

manufacturing the goods, which it mainly imports. One such example is the PLI scheme encouraging India to Manufacture semiconductors which can get India a strong place in the global supply chain!
The 'Make in India' scheme was launched in 2014 by Prime minister Shri Narendra Modi to boost India's domestic manufacturing sector. The Government of India aims to encourage foreign businesses to invest and manufacture in India by improving its 'Ease of doing business' index. One may ask why "Make in India"?

1. Service sector has been India's strong point for decades and has helped to strengthen the BPO and Indian IT sector. This resulted in India being called the "Back office of the world". However, it's contribution was still less in overall share for the economy, and, manufacturing sector, too, needed to be enhanced to further boost employment.
2. The Indian manufacturing sector needed to be strengthened as the overall share of the Indian manufacturing sector was still lower than many East Asian economies. Therefore, there was a need to encourage business and self reliant manufacturing.

Even Though, this great initiative had resulted in positive changes like improvement in the manufacturing system, it faced challenges in the form of inadequate infrastructure and high cost of capital.

Consequences

The trade deficit between India and China had a negative impact on the Indian economy. Let's have a look at how this trade deficit affects the Indian economy:

1) Increasing Trade deficit might mean that there is a lack of competition in the domestic market and the people prefer these imported goods over domestic goods. This will lead to a decrease in GDP of India.
2) Trade deficit has resulted in weakening of the Indian Rupee.
3) Unemployment has been decreasing with the increase in the trade deficit. This is because India imports more than it exports. Let's understand it with the help of an example. Let's say, a country shifts from manufacturing mobile phones to importing phones from different international markets. This will negatively impact the manufacturing sector.
4) The widening trade deficit is causing harm to India's Industrial growth path, as there is more demand for the low-priced Chinese goods in the Indian domestic market, further harming the manufacturing sector.

These above effects on the Indian economy are the major consequences of this trade deficit, which should be regulated in order to witness a blooming Indian economy.

China's "Digital China Construction Plan" - A potential threat

Recently, a "Digital China Plan" has been issued by the Central committee and state council of China. What is this "Digital China" plan? The plan for the global layout of digital China Construction is an upgrade to PRC President Xi Jinping's "Digital China" strategy (introduced in 2017). The date is set to be 2025 this time. This plan will help China to promote a strong "Digital Economy". This can be a potential threat to India as the Digital sector is a new yet still progressing field. So, if China catches its monopoly in this sector too, then it would be difficult to counter its dominance. China has also been leading the revolution to bring in CBDC (Central Bank Digital Currency) in daily use. China has recently announced that they are in the final stage for developing their CBDC pilot, to which work was started in 2020. Changsu province in China is also planning to pay its public institution workers and civil servants in digital Yuan currency in the near future. This will lead to further increase in Chinese dominance, causing problems for India to reduce the trade deficit.

Potential solutions/Recommendations

1) I would propose bringing in a new scheme called "Pradhan Mantri UTPADHAN Yojana" (प्रधानमंत्री उत्पाधन योजना). This scheme will aim to unleash the potential of India's manufacturing sector. Main provisions of this scheme will be:

a) **Infrastructural investment**: Through this scheme, various hubs can be formed in each state. This will also improve the center-state connectivity especially with North-eastern states. It will also improve quality and availability of infrastructure like ports, roads, power supply, etc, which would attract more businesses and investment in the manufacturing sector. Even though schemes like Special economic zone (SEZ) and Development of Enterprise and Service hubs (DESH) bill exists, their major drawback was the size of these hubs. The Indian SEZs are quite small in size (average size of Indian SEZ is up-to 1 sq.km while Chinese SEZs like Shenzhen is spread across 2000 sq.km, with Hainan being their largest SEZ with 34,000 sq.km area[7]) compared to the Chinese SEZs, giving the Chinese counterparts a benefit. Even though the newly proposed DESH bill entails features like increasing exports along with boosting domestic manufacturing and job creation, the issue of "Mega SEZs" is still not taken up. This "Pradhan Mantri UTPADHAN Yojana" will look forward towards building Mega SEZs. How can we do so?

1) Conducting a comprehensive feasibility study for various factors like location, market demand, legal framework and economic impact.

[7] https://www.deccanherald.com/opinion/we-need-desh-and-more-to-catch-the-manufacturing-bus-1176838.html

2) Selecting a suitable location considering various factors like availability of land, proximity to transportation hubs, access to utilities, existing infrastructure, climatic conditions and potential for future expansion.

3) Developing a legal and regulatory framework favorable to these SEZs, as earlier many companies were allegedly moving away from the SEZs in India due to improper policies[8].

4) Actively attracting local and foreign investments through activities like organizing investment conferences, marketing campaigns to showcase the various advantages and incentives offered within these Mega SEZs and corporate roadshows.

5) Establishing a regular monitoring and evaluation framework to track the regular process and progress of these Mega SEZs.

b) **Skill training and development**: As shortage of skilled labor is a challenge faced by the manufacturing sector, providing vocational training courses and incentivising businesses to invest in employee training will be another feature of this scheme. Even though schemes like "Pradhan Mantri Kaushal Vikas Yojana" under the Ministry of Skill Development and Entrepreneurship exist , India is still facing the problems of lack of skilled labor. According to the PIB report of January 2023, since 2015, 9.7 million students have been trained as of october 2022[9]. While, on the other hand, as per the data by the ministry of education of People's Republic of China, more than 30 million students have enrolled for vocational education and training[10]. This shows that India is still behind China in terms of skilled labor force. The 32nd report on the Demands for Grants (2022-2023) of the Ministry of Skill Development and Entrepreneurship shows that there have been budgetary cuts and low placements as ₹1,643 crore budget was allocated for skill development as compared to the ₹3220.94 crore proposed[11]. There were many issues like the registered candidates did not join in and even if they did join, they dropped out. Also, many candidates did not appear or failed in the assessments. Problems like less participation by the private sector, considerable gap

[8]https://www.business-standard.com/podcast/current-affairs/why-have-special-economic-zones-sez-not-taken-off-in-india-122070700036_1.html &
Rob Jenkins, Loraine Kennedy, Partha Mukhopadhyay, Kanhu C. Pradhan, "Special Economic Zones in India: Interrogating the Nexus of Land, Development and Urbanization", National Institute of Urban Affairs (NIUA), SAGE Publications, 2015

[9]https://pib.gov.in/PressReleasePage.aspx?PRID=1894912#:~:text=National%20Apprenticeship%20Promotion%20Scheme%20provides,under%20the%20Apprentices%20Act%2C%201961.&text=Since%202015%2C%2091.7%20lakh%20students,as%20on%2030%20October%202022

[10]https://www.globaltimes.cn/page/202206/1267895.shtml

[11]https://www.google.com/amp/s/frontline.thehindu.com/economy/skill-india-grounded-problems-plague-technical-training-ecosystem-unemployment-crisis/article65675733.ece/amp/

between the Industries' demands and skill supply, along with the lack of compliance to international standards are restricting these schemes from achieving their full potential. Hence, This "Pradhan Mantri UTPADHAN Yojana" will seek to more private sector involvement by forming legal procedures for the private firms to get in touch with the student/candidate and to set up regulations to address different questions like hours of apprenticeship, incharge of student at the employer's etc. Now, how can we encourage these private firms to participate in the VET (Vocational Education and Training) as they are often reluctant to do so?

1) Providing tax incentives like tax credits, tax deductions or other financial incentives can help offset the costs associated with training and can also encourage involvement.
2) Initiating recognition and reward programs to acknowledge the private sector organizations engaging in vocational training. Recognizing the organization publicly can help popularize their brand image, reputation and Corporate Social Responsibility (CSR).

c) **Start-up plan 2.0**: An addition to the earlier Start-up plan bought in 2021, this Start-up plan 2.0 will aim to encourage private participation in the Space sector. The Indian space sector is preparing for a new era and has the potential to reduce the trade imbalances between India and China. Even though India has achieved success in the field of space exploration, involvement of the private sector in the commercial space programmes is still less. India's space programmes are mainly handled by Indian Space Research Organization (ISRO) and are mostly Government-funded. Even though India's space economy was estimated to be around $9.6 billion in 2020, the Indian space sector contributes only 2% to the global space economy[12]. Hence, Private investment in the space sector is necessary for boosting the Indian space economy. Government of India's revolutionary decision to open up the space sector in 2020 has helped Private firms like SpaceX, Blue origin, Virgin Galactic and Arianespace to enter the space market, which has helped to reduce costs and turnover time[13]. However, the lack of proper legal framework to provide clarity in rules and openness is restricting more private investments. This Start-up plan 2.0 will look forward to the formation of a proper framework of rules and regulations, in the form of Space laws, to govern the functions of these private firms and to maintain harmony between public and private entities in the Indian space economy.

[12] https://www.google.com/amp/s/www.financialexpress.com/business/defence-boosting-the-space-sector-for-indian-private-playersnbspnbsp-2915038/lite/

[13] ISRO's report on "Enhancing the private participation in Space activities", India on a track to serve global needs, March 2023

d) **Improving access:** This scheme will aim to improve access to credit and other finances for Small and Medium sized Enterprises (SMEs). How will this happen?
    1) India can establish and strengthen its credit bureaus to improve the quality, availability and accessibility of credit information. This can be done by developing a "credit reporting system" which will help to record SMEs' credit history, further making it easy for the lenders to assess their creditworthiness.
    2) Providing for financial literacy among the SME holders so that they can understand various loan options and other necessary information.
    3) Another way is simplifying the loan application process by reducing complex paperwork can also help to make access to credit easier.

e) **Export-focused manufacturing**: It will look forward to forming an export focused manufacturing model by providing help and encouragement to the businesses looking to enter new markets and to increase their competitiveness.

2) Renewable energy sector is a growing field and has the scope for India to emerge as a strong power. Encouraging this sector will help India to carve its place on the global supply chain. How can India Encourage this sector?

a) Setting up Energy targets, both at National and State level, can help to drive investment and create a sense of urgency. These Energy targets should include a good implementation plan and system for monitoring and evaluating.

b) Boosting campaigns about the awareness of benefits provided by Renewable energy over the non Renewable energy and the advantage of clean energy. This will also include having public participation in Renewable energy projects like community solar initiative to inculcate a feeling of ownership and support towards this sector.

c) The Government of India has already taken up schemes like "Pradhan Mantri Kisan Urja Suraksha evam Utthaan Mahabhiyan Yojana(PM-KUSUM) to encourage farmers to switch to solar power, but an addition to it can be switching to drip irrigation system to save power and water with increased crop output.

3) India has been undergoing research in the Semiconductors and Ultraviolet lithography field and amidst this, with Samsung building its factory in Noida, will help India to be competitive. This is because Samsung has the best quality of display panels and majority of its manufacturing takes place in South Korea, Taiwan and China. So, if Samsung is setting up a factory in India, we can get to know and grow in the field of manufacturing display panels too. Why are these display panels so important? Display panels are basically the only component in a smartphone or an electronic device that doesn't need Chips or IC. These ICs or Chips are made through machines called EUV lithography machines and these machines cost $160 billion each and are available with only a few countries, which explains why few are monopolizing the Electronics sector.

4) Improving diplomatic ties between both the countries might help to get the Indian IT sector into the Chinese market. There are few ways to achieve this. Those are:

(A) Cultural Diplomacy - Cultural aspects can help to restore the India-China bilateral diplomatic ties. How can one carry out this Cultural diplomacy?

1. Cultural Exchanges: Encouraging cultural exchanges can help promote people to people's contact, further building trust. This can be done through activities like cultural festivals, art exhibitions, joint musical or dance performances etc. Showcasing each other's cultural heritage can help to create opportunities for dialogue and interaction which will inculcate appreciation and empathy for each other (Example - the "culture of Yoga" is becoming very popular amongst Chinese youth these days, So utilizing such practices can help improve Cultural ties).
2. Language and Literature: Promotion of each other's languages [Example - Mandarin and Indian languages (Mostly Hindi as it is one of the official languages of India) can help facilitate communication and cross-cultural understanding. Various activities like language learning programs, translation initiatives, and literary exchanges can help people to engage with each other, advancing appreciation for their shared history and contemporary perspectives.
3. Sports and Tourism: Friendly sports events and competitions can serve as a powerful point for cultural exchange. Tourism, too, is a focal area for promoting mutual understanding between Indian and Chinese citizens. This can help to disperse stereotypes and promote cultural exchange between the two. This can be done by facilitating easier Visa processes, travel packages, joint marketing campaigns and development of tourist attractions.

(B) Track II diplomacy - Track to diplomacy is basically engaging non governmental actors like think tanks, scholars, civil societies, academia etc for dialogues to improve bilateral relations. This can provide for academic, cultural and civil society exchanges, fostering people to people interaction between both the countries. India and China have been engaging in this Track II diplomatic dialogue since 2005 when Indian council of world affairs (ICWA) and Chinese people's institute of Foreign Affairs (CPIFA) signed a memorandum of understanding (MoU) for bilateral cooperation[14]. However, the first proper dialogue began in November 2013, and in the following year, another MoU was signed between India's ministry of external affairs and Chinese Academy of social science, during PM Shri Narendra Modi's visit to China. This kicked off a series of think tank dialogues between India and China[15]. However, due to the Galwan and Doklam border clashes, along with border tensions going on, the scope of this Track II diplomacy hasn't been completely utilized. Improving this Track II diplomatic dialogues can help to further strengthen the bilateral diplomatic ties. Along with this,

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[14] https://www.orfonline.org/expert-speak/india-china-treading-track-ii-53094/?amp

[15] https://www.orfonline.org/expert-speak/india-china-treading-track-ii-53094/?amp

regular high level diplomatic dialogues like bilateral summits and ministerial meets can provide avenues for discussion and communication to develop ties.

5) **Plus one strategy**: After the Covid-19 pandemic and due to the US led trade war with China, numerous countries are looking for a volition for China with a "China plus one" strategy. This is a golden occasion as India has a similarly large market and big working force feature like China, making it a favorable choice. India is also progressing with it's manufacturing sector (specifically with electronics), So, this will result in good trade ties with other countries, improving exports and thus reducing deficit. Also, due to the US-China trade war, the Netherlands based ASML has imposed restrictions on trade with China, making it difficult for China to manufacture electronic goods. India can use this opportunity to build good ties and invest in EUV lithography machines and manufacture electronic goods, reducing the trade deficit.

6) Bringing in local substitutes for "Low value(price), High volume" goods will also help reduce imports from China. How can we do so?

a) Conducting a proper market research to identify the products that have high demand but are mostly dominated by Chinese Imports. Further, we need to look for local substitutes for these products and evaluate their quality, pricing and production capacity. Some of the examples can be substituting local wooden toys for the chinese toys, substituting indian footwear and clothing brands like Sparx and Pantaloons for foreign brands like Reebok, Adidas or Zara.

b) Analyzing the cost structure of the local production and finding different ways to optimize it. This can be done by various methods like negotiating better deals with the suppliers and leveraging economies of scale. We should aim to reduce production cost by simultaneously maintaining the quality.

c) Branding, highlighting and advertising the local substitutes by advertising their quality, affordability and advantages can help create awareness, further driving demand. We can take help of social media and various digital platforms for doing the same.

7) Encouraging big companies like Apple to manufacture in India, So, India not only will assemble parts but also make them. This will help boost both the manufacturing sector and trade surplus. According to Commerce and Industry Minister Shri Piyush Goyal, India offers a Rule of Law with Transparent governmental policies and business models, which makes it a favorable place for foreign investment[16]. Recently, i-phone maker Apple is seeking to manufacture in India and have already started with 5-7% of their manufacturing here. Just like China, India has a large working force with a huge market, So, with the recent "one plus strategy", the companies seeking alternatives to China, can manufacture their spare parts in India. India needs to take this point in consideration and promote

[16] https://www.outlookindia.com/business/apple-looks-to-scale-up-manufacturing-in-india-piyush-goyal-news-255966

industry collaborations between Foreign companies and Indian manufacturers. This can be done by organizing Industry conferences, trade shows and matchmaking events to bring companies and manufacturers together. Along with this, actively promoting India as a favorable destination for investment for companies by participating in trade fairs, engaging in targeted market campaigns and giving leverages to various diplomatic channels to promote India's potential.

8) Reducing the trade deficit goes with a two-way policy - curbing imports and increasing exports. If India wants to increase exports, it needs to realize its "Export Potential". Export potential is basically when you import a particular product only from a particular country and not from anywhere else. This Export potential is seen when products have : a) inadequate demand in China b) adequate supply capacity and capability in India.

9) Another way to reduce the trade deficit is by creating exports by manufacturing products where China is losing its cost advantage, largely due to changing demographic setup. For example - China has been witnessing a declining working population as it's number of working people has fallen by more than 41 million in the past three years. This results in an imbalance between trade and supply labor in China. However, with India having a low cost labor force as well as an advantage in demographic structure, it can overcome the trade deficit and replace China.

Conclusion

To conclude, this paper mainly focused on the various reasons behind India's trade imbalances with China. The Indian tiger and the Chinese Dragon have been extensively engaging in trade with each other since the 1990s. Once a slow growing economy, China took speed in becoming the world's largest exporter and dominating the global supply chain by adopting open market reforms in the late 1980s. India, on the other hand, too was developing economically due to the 1990s economic reform. However, due to China exporting cheap goods and services, India started to become dependent on it. This led to an increasing trade deficit between the two (which mostly affected the Indian economy). In order to convert this deficit into surplus, India must bring in the best of its manufacturing sector. Along with this, as India is already ahead in Service sector, and many countries are looking for an alternative for China, it can use its position to attain a place in the global value chain. This way, India can increase its exports and shift the curve to trade surplus.

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