



Weekend Ruminations

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Advice for shoot-from-the-hip nationalists: Take aim before firing

It's all good to be tactical - keep China out of strategic markets; hit back in the same coin if it looks to keep India's key sectors out - but don't shoot yourself in the foot.

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The sight of seemingly demented people jumping and dancing on Chinese-made consumer durables raises some intriguing questions about the thinking processes of our shoot-from-the-hip nationalists. What do they think will happen when Chinese products are replaced by Korean or Japanese ones? China's total exports in a year are about \$2.5 trillion. India accounts for 3 per cent of that. China also has \$3 trillion in foreign exchange reserves, and a large trade surplus. So whom are we hurting? Some sellers of phone instruments, perhaps. Xi Jinping is unlikely to be impressed.

It is possible that Chinese suppliers will be replaced by Indians, not Koreans. I once asked the owner of a large retailing chain why he could not encourage more businessmen in India to become his suppliers, so that he would not have to import quite so much from China and elsewhere. His response was that India had virtually stopped manufacturing even the most ordinary goods. And even if they did make things locally, at what cost? One doesn't know, but it is almost certain to be higher. The end result might be that the producers of things (who are busy taking out full-page ads in celebration) make money at the expense of those dancing and jumping consumers who end up paying more.

And what if China hits back? India's imports from China are equal to about a fifth of total Indian manufacturing. If Chinese products have no ready substitutes domestically, the risk is of disruption along the supply chain. In the case of some products (like strategic materials) where it has market dominance, China could even deny sales to India as it did once with Japan during a dispute over some islands off the Chinese coast. At the least, sourcing from alternative suppliers would be at a much higher cost.

The free trade argument is not a matter of religion. Britain became a free trader only in the mid-19th century, when it established a clear lead in the Industrial Revolution. The United States, once the champion of free traders, is shifting position now ("America First!"). So import substitution (or self-reliance) is a valid tactic — if you know how to use it. Other countries have managed successful import substitution, as Naushad Forbes wrote earlier this week. But, as he showed, they did it by making sure that tariff support was temporary and reducing with time; those who failed to become efficient and competitive in a defined period would have to

shut down — thereby ensuring market discipline. India, predictably, is doing it differently. And it remains a soft state, vulnerable to special interests. So it will become a high-cost economy again, and Indian manufacturing even more uncompetitive. The lessons learnt on the way to 1991 have been forgotten.

The point about trade is that both seller and buyer are supposed to gain. Bring politics into it and the picture gets clouded. The most defective of all positions (one used often by President Trump, and by India in the past) is to seek trade parity with each trading partner. You might as well ask for the return of barter, or of rupee trade arrangements! India could have a trade deficit with oil exporters, and at the same time a surplus with the United States. And what it loses on merchandise trade it could gain through trade in services. If the overall balance is fine, or the deficit neutralised by capital inflows (as it has been for India), there is no need to complain of injury.

By all means be tactical. Don't allow China access to strategic markets, like telecom products, because of the possibility of spyware mischief. Also exclude China from product segments where the quality record is said to have been poor, such as thermal power plant equipment. And if China is looking for ways to keep out Indian pharmaceuticals or software services, hit back in the same coin. Even cancel railway contracts if project completion is hopelessly delayed, but bear in mind the time taken to get alternative bidders. In short, aim carefully and don't shoot yourself in the foot.