Decoupling from Chinese Manufacturing - An Assessment - I

What is the issue?

- The border clashes with China and the COVID-19 pandemic has given way to concerns on India's dependence on Chinese manufacturing.
- In this context, here is an assessment if India could really decouple itself from Chinese manufacturing and the options before it.

How dependent is India on Chinese manufacturing?

- India's imports from China in 2019-2020 reached $65 billion.
- This is out of the $81 billion two-way trade.
- Currently, India is exporting a lot of raw materials and intermediate products.
- On the other hand, it is importing finished products from China.
- It is also importing certain key intermediates such as active pharmaceutical ingredients from China.
- **Sectors** - In terms of capital goods, Indian manufacturing is highly dependent on supplies from China.
- This includes a wide variety of machineries, including electrical machinery, semiconductor driven machinery etc.
- India also imports fertilizers from China.
- Many limited value consumer goods, to a very large extent, have flooded the Indian market.
- Whether these are actually required to be imported or not is itself not clear however.

What are the challenges in addressing the imports concern?

- **Alternatives** - For a variety of reasons, India's dependence on imports is localised.
- In other words, there is no wide diversification of countries from which India is sourcing its imports.
- E.g. Most of the critical medical supplies imported for frontline healthcare workers in the COVID-19 situation comes from China

- This essentially means that apart from China, there are probably 3 or 4 countries on which India's dependence is increasing.
- So it would be a difficult choice for India to get out of Chinese dependence and search for alternative partners.

- **Essentials** - Concern arises not with imports that are not really a matter of choice but with those products that are crucial and essential.
- E.g. the humidifiers, medical masks, liquid soap being utilised in the COVID-19 battle
- For these and other such essentials, China remains the main source.

What should India's approach be?

- India's approach has to go much deeper and has to develop sector specific strategies.
- It should prioritise in terms of the areas in which it can, relatively, more easily move back away from the Chinese dependency.
- India should now probably replicate what China did in the 1990s.
- However, the global environment and global value chains are much different from how they were 30 years back when China was opening up.

How different are the global value chains now?

- Policymakers suggest that India is set to become more open and that there is going to be more reliance on the global markets.
- Unfortunately, that possibility is far from reality.
- China's strategy in 1990s was a global market-driven industrialisation strategy, an export-driven strategy.
- Global value chains are now in fact becoming more local.
- Countries are depending more on their own economies rather than on global markets.
- This is perhaps an impact of the great recession of 2008.
- So China's strategy in 1990s may not work for India now.

What gives China its central place in global manufacturing?

- China is so central to a very large number of global and regional supply chains.
- One is because China offers the capacity to businesses to develop the supply chains by considerable lengths within itself.
- Not just the geography, China also has a broad-base that it has developed over different sectors, and by and large in most products.
- China’s biggest value comes as a final stage assembler and that's where China’s proficiency in value chains happens.

- Importantly, alongside being an exporter of assembled final products, China has also become a major consumer for final products.
- In the post COVID-19 situation, the businesses' emphasis is to make value chains shorter, resilient and durable, and locate them closer to the final demand markets.
- In this context, undeniably, China is more advantaged.
- China continues to remain a major source of the final demand market.
- China's geography offers tremendous agglomeration advantages of moving back and forth across borders and integrated facilities.

So, is relocation possible?

- Given the above factors, shifting supply chains physically out of the Chinese geography and it’s connected arms (such as Hong Kong and Taiwan) would be hard.
- Whatever relocation was possible has already happened after the onset of the U.S-China trade war driven by tariffs.
- So, seeing that kind of relocation is unlikely anymore.
- Nevertheless, companies have moved out and are moving mainly to South-East Asia.
- This offers scope for limited relocations, and India should see ways of attracting these.

Did Make in India succeed in this regard?

- Make in India initiative was a good opportunity for India to get the manufacturing sector back on track.
- But the country has not taken advantage of what it had actually planned for.
- In the past 5 years, with Make in India programme in place, the dependency on China has actually gone up.
- The Make in India strategy talked about FDI into manufacturing.
- But data reveal that foreign investors had preferred service sectors.
- And many of these sectors are those where India does not need any investment. E.g. IT services

What is to be done?

- Despite being one of the most open economies and offering attractive terms to foreign investors, India has attracted little investments.
- India should now analyse the gulf between FDI inflows into China and into India.
- The policies should look at the wholesome picture to address the varied factors (*Click here for Part II*) that go into making 'attracting investments'

work.

Source: The Hindu