A Study on Prospects for India-Japan Economic Collaboration after Covid-19

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Abstract

Extensive economic cooperation has become a key component of "India and Japan's" Tactical and Transnational Collaboration since its inception in 2006. Japan has been one of India's most significant trading allies and third-largest investor. Notably, Japan is India's most significant bilateral contributor of development aid, especially for infrastructural development. Despite the economic complementarities, bilateral economic and trade relations have stayed below capacity in actual fact.

With the present COVID-19 epidemic posing significant difficulties to the world economy, India and Japan must recruit crucial players in their corresponding economic growth plans and enhance bilateral economic participation. In this perspective, this paper examines the present state of "India-Japan economic relations", including international trade, investment, and ODA. It highlights the synergistic benefits of "Japan's COVID-19-related" policies to assist companies in diversifying their manufacturing sites and distribution networks, as well as the changes India is doing to allow more global and domestic distribution network convergence. This article also discusses policy measures that would enable equally advantageous socioeconomic cooperation between India and Japan gain traction in the post-COVID era.

Keywords: Bilateral trade, China Factor, Covid-19, Investment, Economic Cooperation

Introduction

The geopolitical and international relationship between India and Japan has always prioritized more vital financial collaboration. The Comprehensive Economic Partnership Agreement (CEPA) between India and Japan was reached in 2011, and bilateral trade between the two nations was close to US$ 18 billion in 2018-19[1]. Japan is also India’s third-largest foreign investor. Another significant element of the rising trend in India-Japan economic ties, especially after the turn of the century, has been “Japan’s overseas development aid (ODA)”. Since 2003, India has been the leading receiver of Japanese yen loans, primarily for infrastructural construction projects. Regarding the financial synergies, bilateral economic and trade partnerships have stayed below capacity in actual fact.

With the present COVID-19 epidemic posing severe economic difficulties for the world, India and Japan must engage as crucial players in their corresponding economic growth plans and enhance “bilateral economic” participation. Therefore in context, this research paper examines latest events in "India-Japan economic relations, such as trade, investment, and ODA"; it also highlights collaborations between "Japan's COVID-19" enmeshed assistance to help manufacturers expand their manufacturing units and supply chains and reforms which India is implementing to accommodate full participation in global and national supply chain operations. The article also highlights policy initiatives to help India and Japan develop mutually beneficial economic cooperation in the post-COVID era.
The Current State of Economic Relations between India and Japan:

Trade

Bilateral trade between India and Japan reached about US$ 18 billion in 2018-19 [2]. (Chart-1). Simultaneously, “Japan’s exports to India were $12.77 billion, while imports totaled $4.86 billion. Japan’s exports to India accounted for 2.48 percent of the country’s total imports, while India’s exports to Japan accounted for 1.47 percent of the country’s total exports. Petroleum products, chemicals, elements, compounds, non-metallic mineral goods, fish and fish preparations, metalliferous ores and scrap, apparel and accessories, iron and steel products, textile yarn, textiles, and machinery are among India’s most important exports to Japan. Equipment, electrical machinery, iron and steel goods, plastic materials, non-ferrous metals, components of motor vehicles, organic chemicals, metal manufactures, and other items are among India’s main imports from Japan” [3].

Chart-1; India-Japan Bilateral Trade (Billions of US Dollars)


“The Comprehensive Economic Partnership Agreement” between the two nations was concluded in 2011 (CEPA). Despite the low utilization of the CEPA, it has had a significant influence on commerce between “India and Japan”, which has risen from “US$ 10.4 billion in 2010” (before the CEPA’s implementation) to US$ 17.6 billion in FY 2018-19, a 69 percent growth. Nevertheless, the trade balance has remained in “Japan’s favor, with India’s trade deficit with Japan” increasing from US$ 3.54 billion in 2010-11 to US$ 7.91 billion in 2018-19 as a result of CEPA (chart-2).

Chart-2: The trade deficit between India and Japan (in billions of US dollars)


“The Federation of Indian Export Organizations (FIEO)” estimates that Japan’s “untapped export potential is more than US$ 3 billion in areas such as jewels and jewelry, medicines, marine goods, rice, bovine meat, knitted t-shirts, and so on. For instance, article 54 of the CEPA deals particularly with generic pharmaceutical cooperation
between the two nations and provides, among other things, for national treatment in terms of registration and additional permissions that must be fulfilled within a reasonable time frame”[4].

However, in 2018-19, Japan was placed 25th amongst India’s pharmacy export markets, with the United States topping the list[5]. “The value of pharmaceutical goods shipped to Japan was US$ 58.2 million, less than 1% of India’s overall exports in this category, in the backdrop of difficulties presented to the Indian pharmaceutical industry in Japan” [6]. In 2018, the Japanese markets for prescriptive and non-prescription medicines reached US$ 87 billion, with the United States accounting for 23.5 percent of imports[7]. Japan has implemented 64 non-tariff restrictions on Indian imports as of May 2020. “In a letter to Japanese Trade and Industry Minister Hiroshi Kajiyama in December 2019, Indian Commerce and Industry Minister Piyush Goyal stated that market access for India’s goods and services with partner countries is crucial, but despite commitments in CEPA from Japan, market access for India’s goods and services remains elusive.” [8]

Investment

Japan is the Indian economy’s third largest investor, with accumulated FDI inflows of approximately US$ 30.74 billion from 2000 to June 2019, amounting to “around 7.2 % of overall FDI flows obtained by India during that time”[8]. FDI flows from Japan have risen substantially during the CEPA, from US$ 1.56 billion in 2010-11 to US$ 2.96 billion in 2018-19. (Chapter-3). According to JETRO data, India’s proportion of total outbound FDI in Japan is just 2%. FDI from Japan has gone chiefly into India’s automotive, “electrical equipment, telecommunications, chemical, finance, and pharmaceutical industries”.

Chart-3; Inflows of FDI from Japan’s equity market (in millions of US dollars)

During 2010 and 2018, the proportion of Japanese-affiliated businesses in India almost doubled (Chapter-4). As of October 2018, approximately 1441 Japanese businesses were registered in India, according to a joint study conducted “by the Consulate of Japan in India and the Japan External Trade Organization (JETRO)” [10]. “There are 5120 business establishments in India for these 1441 companies, including liaison and branch offices in India and local subsidiaries”[11].

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According to the latest surveys, India has risen to the top of the most appealing FDI locations for Japanese investors. “Over 65 percent of questioned Japanese companies in India selected “expansion” as their future strategy to future business plans/activities in the next 1 to 2 years, according to the 2019 Japan External Trade Organization (JETRO) Survey of Business Conditions of Japanese Companies in Asia and Oceania”[12]. Similarly, India was rated first in “the Japan Bank for International Cooperation’s (JBIC) 2019 Survey Report on Overseas Business Operations by Japanese Manufacturing Companies, while China was ranked second”[13].

In “2014, the two nations established the India-Japan Investment Promotion Partnership, under which Japan has committed to investing JPY 3.5 trillion (US$ 33 billion) in India over the next five years via public and private investment and finance. To attract, facilitate, fast track, and handhold Japanese investments across sectors, the Indian government has established a unique management team called “Japan Plus,” which consists of four delegates from the Indian government and three representatives from the Japanese government, which include one from the Ministry of Economy, Trade, and Industry (METI) and one from the Japan External Trade Organization (JETRO). The Japanese Ministry of Foreign Affairs has created a Contact Point for Promotion of Foreign Direct Investment in Japan to assist Indian businesses interested in investing in Japan to enhance the promotion of inbound FDI”[14].

The proposed deal “to develop 12 prospective sites as Japan Industrial Townships (JITs)” is another crucial effort within this cooperation (Figure-1).

Figure 1: Prospective Locations for “Japan’s Industrial Townships”.

“Source: Department for Promotion of Industry and Internal Trade, Ministry of Commerce and Industry in India”
According to the plan, the JITs will be “integrated industrial parks with ready-made operating frameworks, well-equipped with world-class infrastructural facilities, plug-in-play factories, and investment advantages for Japanese businesses,” according to the plan. The goal is to duplicate the achievement of “the Japanese zone in Neemrana”, Rajasthan, where 45 Japanese businesses already operate, “including Daikin, Nissin Brake, Mytex Polymer, and Nippon Pipe, among others”. As of October 2018, six of the twelve planned JITs were functioning.

Development Assistance

Japan’s rise in providing overseas development aid (ODA), especially after the turn of the century, is a significant element of the rising trajectory in India-Japan economic ties, even as Japan's total economic support has encountered financial limitations. Since 2003, India has been the leading receiver of Japanese yen loans, overtaking China, which had held the status for many years. Actual ODA disbursements have risen in recent years, which is a notable good trend (Chart-5). “From 2007-08, Japan has also implemented a ‘Double Track Mechanism’ for granting ODA loans, allowing India to submit project ideas to Japan twice a year”.

Priority topics for “Japanese ODA include electricity, transportation, environmental projects, and projects that address fundamental human needs. Japan is promoting the development of transportation hubs and network infrastructure in the fields of railroads (including high-speed trains and metros), national highways (including expressways), power transmission, and other infrastructure to improve connection among major industrial cities and economic zones, as well as regional connectivity, via essential projects such as the telecommunications network (CBIC)”.

![Chart-5: Japan’s ODA disbursements to India (YEN billion)](chart)

Source: “Embassy of Japan, India”

The Global Economy and the COVID-19 Outbreak

The COVID-19 pandemic, which has placed the globe on “high alert,” has an increasingly negative effect on the global economy. The magnitude and speed with which worldwide economic activity has collapsed since the onset of the outbreak are unprecedented. The crisis is really “global,” with early projections from the International Monetary Fund (IMF) in April 2020 predicting a -3 percent drop in worldwide growth in 2020[13]. This is a 6.3 percentage-point decrease from January 2020, a significant change in such a short time [16]. The worldwide GDP loss from the outbreak is projected to be about US$ 9 trillion in 2020 and 2021. “Global GDP is projected to decline even further this year, by an additional 3% in 2020 if the epidemic lasts longer this year, and by an extra 8% next year if the pandemic lasts until 2021”[17].

The World Bank’s Worldwide Economic Prospects, published in June 2020, forecasts a “global GDP loss of 5.2 percent in 2020, the worst global recession in decades. Nevertheless, the report warns that this outlook may be too optimistic and that if the COVID-19 epidemic continues, global growth may contract by almost 8% by 2020. Internal demand and supply, commerce, and finance are expected to be significantly disrupted in advanced countries by 2020, resulting in a 7% drop in economic activity. The emerging market and developing economies

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(EMDEs) are projected to decline by 2.5 percent this year, marking the first time they have contracted as a group in at least sixty years”[18]. Below is the World Bank’s prediction for major economies (Chart-6).

Economic Partnership between India and Japan Possibilities

The “Indo-Pacific’ area accounts for a significant portion of the “Global Value Chain (GVC)” issued goods. Electronics, automobile components, agricultural goods (primary and processed), clothing, and footwear are the main exports from the area, and China has been a critical hub in GVC networks throughout the years. However, increasing labor prices in “China and the developing US-China trade war have caused global businesses to re-evaluate strategic supply chains to minimize the effect of this instability, with several considering moving out of China”. With nations across the world fighting the COVID-19 epidemic, the problem has taken on even more importance, hastening the discussion over the widely publicized ‘China-Plus-One’ strategy, which refers to the practice of foreign companies operating in China coupling their investments with a second facility, usually in another Asian economy[19].” The ‘China Free’ strategy, which proposes excluding China from manufacturing, is at the other end of the spectrum[20].

The Japanese government, led by Prime Minister Shinzo Abe, was among “the first in the world to define a national policy response to COVID-19-related supply disruptions”, owing to the country’s over-reliance on China. The Prime Minister said “on March 5 at the 36th Council on Investments for the Future.” He said, “There are some concerns over the impacts of the decline in product supply from China to Japan on our supply chains. In light of that, as for those products with high added value and for which we are highly dependent on a single country, we intend to relocate the production bases to Japan. Regarding products that do not fall into this category, we aim to avoid relying on a single country and diversify production bases across several countries, including those of the Association of Southeast Asian Nations (ASEAN)”.[21]

Soon after, on April 7, a Supplementary Budget for the Fiscal Year 2020 plan was published, which contained “about JPY 240 billion (roughly US$ 2.2 billion) as a strategy to assist Japanese businesses in shifting output out of China. The goal is to offer additional incentives to encourage Japanese firms to return to Japan and diversify their operations into other Asian nations[22]. This stimulus spending comprises JPY 220 billion to transfer manufacturing back to Japan and JPY 23.5 billion to promote global supply chain diversifying in an attempt to mitigate the catastrophic consequences of the COVID-19 epidemic”[23].

Companies looking to “diversify their manufacturing locations and supply chains away from China must evaluate several factors, including labor prices, infrastructure, and nation risk” [24]. However, according to Nomura research, just three of the 56 businesses that moved their manufacturing out of China between April 2018 and
August 2019 selected India [24]. Indeed, internal obstacles to India’s involvement in GVCs include land, labor, and capital market inefficiencies, poor connectivity and logistics chains, and highly restrictive goods and services financial regulation. “India needs a targeted reform agenda following a four-pillared” approach to gear up and creates a favorable economic climate, which includes:

(i) Trade liberalization via lower tariffs and more market access
(ii) Facilitation of commerce
(iii) Facilitation of trade and investment, and
(iv) Skill development and technology transmission.

Indian Prime Minister Narendra Modi has made a promising start in this direction, urging the country to convert “the COVID-19” issue into a chance to grow into self-sufficient - Atma Nirbharta - and “emerge as the global nerve center of complex contemporary multinational supply chains in the post-COVID-19 world” [25]. He believes that today’s nation needs goods “Made in India yet Made for the World” [26]. To this aim, “the Indian government” is focusing on “the next wave of ‘Ease of Doing Business Reforms,’ which includes easy property registration, quick resolution of commercial disputes, and a simplified tax regime [28].” In the World Bank’s annual “Doing Business Report” (DBR), India is now placed 63rd place in its 2020 report.

India is also developing a massive land pool of 461,589 hectares to entice companies to leave China. It has targeted ten industries as priority areas: “electrical, pharmaceuticals, medical devices, electronics, heavy engineering, solar equipment, food processing, chemicals, and textiles” [29].

Similarly, aggressive attempts by many Indian states to recruit Japanese businesses have gained traction. According to media sources, during a video conference with “Japanese Ambassador Satoshi Suzuki, the Government of Uttar Pradesh” provided labor law “exemption for nearly three years, excellent connectivity via airports and expressways, and the easy availability of land parcels for building industrial units and technology parks as some of the attractions to Japanese businesses intending to move to Uttar Pradesh” [30]. The government has also established a “Japan-specific support desk”. Gujarat, which has significantly benefited from Japanese FDI, provides subsidies and incentives for manufacturing in more than 30 industries [31]. Punjab has established “four industrial parks and has addressed several Indian embassies, including Japan’s, offering all feasible assistance in terms of land, infrastructure, and other amenities” [32]. Rajasthan is forming “a special Task Force to finalize a strategy and package that may be presented to prospective investors based on the achievements of the two Japanese zones in Neemrana and Ghilot” [33]. The Assam government talks with JETRO about establishing a Japanese Industrial Township in the state to lure Japanese investment [34], [58] Meanwhile, “Tamil Nadu, which already has over 600 Japanese businesses, has formed a high-level group, including officials from Japan and South Korea, to develop a special incentive package and investment facilitation procedure” [35].

Moving Forward

The idea of India becoming a global manufacturing center is enticing; but, creating an enabling climate for more FDI from Japan would require significant governmental measures. Japanese firms have been drawn mainly by India’s local market’s development potential, with little interest in the nation as “a manufacturing base for exports”. India has not developed a robust value chain with Japanese businesses. This study emphasizes the following points in this context:

1. For a long time, Japanese businesses have been concerned about India's lack of quality infrastructure. “As India aims to create more industrial estates based on a plug and play infrastructure model, it would be advantageous to expedite the Japan Industrial Townships (JITs)’ designed in partnership with Japanese government entities such as “JETRO and JICA”, especially with the goal of attracting “Japanese SMEs”. Another thing to notice is that, although Japan has provided significant ODA assistance for infrastructure development in India, efficient use of ODA pledges “from Japan has been slow, and many of these
projects, such as the Delhi-Mumbai Industrial Corridor”, have been postponed. This also has a detrimental effect on the views of both current and prospective Japanese investors.

2. In increasingly complicated global supply chains, skill-intensive inputs, mainly services, are being used more often. Around this servitization process, upstream operations like “R&D and product design and downstream activities like branding and promotion” are gaining a more significant proportion of the value contributed, while intermediate manufacturing of products and materials and final assembly are losing ground. To attract FDI from Japan, India should use its strengths in services and make it easier for Japanese firms to build up R&D facilities and global in-house centers (GICs) in India, using its talent pool, expanding startup environment, and cost-effectiveness. In this regard, it would also be beneficial to examine the difficulties that Japanese-led R&D units presently functioning in India confront and to adopt suitable corrective measures.

3. High import tariffs, inter impediments, and insufficient regional connections impede the efficient flow of products across national boundaries and have a significant effect on GVC integration. Taxes and other protective measures, in reality, add a substantial cost to the price of the completed item when intermediary inputs are transferred across borders many times; this, in turn, impacts the operating and consumption choices of companies engaged in GVCs. More than 200 Japanese businesses in India questioned lately by JETRO said that if India entered the Regional Comprehensive Economic Partnership (RCEP), which seeks to establish an integrated market with 16 nations, they would retain or expand their local manufacturing in India. Japan has taken the lead in urging India to return to the talks after India chose not to join the RCEP last year. Since a result, India should reconsider the RCEP pragmatically, as it is expected to enhance possibilities for international trade and investment from Japan. In addition, the assessment of the India-Japan CEPA must be expedited to resolve India’s remaining problems and concerns.

4. It is also widely acknowledged that “cross-border transportation corridors” are critical structural components in the multi-layered strategy of economic corridors that connect regional industrial networks and supply chains while generating broader economic and social advantages. Increased regional connectivity with ASEAN via the rapid execution of projects such as the IMT (India, Myanmar, Thailand) expressway and its expansion to Laos, Cambodia, and Vietnam, as well as increased digitization of trade processes for convenience of border crossings, can thus be an additional catalyst in reviving the India-Japan economic relationship, with particular advantage to India in terms of trade facilitation (NER).

5. While India’s rating for “Ease of Doing Business” has progressed considerably in recent years, other areas such as “Starting a Business,” “Registering Property,” and “Enforcing Contracts” continue to be a source of worry. “Domestic regulatory and procedural changes, such as administrative processes needed to start and run a company, regulatory standards, regulatory institutions, foreign currency limitations, ownership limits, sectoral ceilings, dispute resolution, complicated taxes, land acquisition, profit repatriation, and intellectual property rights, must therefore be prioritized. It would also be advantageous at the state level to establish specialized Japan desks, as in Uttar Pradesh”, and engage Japanese officials in developing incentive schemes, as in Tamil Nadu.

Conclusion
Over the past two decades, India and Japan have recognized the value of collaboration in a changing global context. The extremely belligerent Chinese behavior in “the South and East China Seas”, its eagerness to military conflicts, and its desire to control East Asian sea lanes have brought New Delhi and Tokyo closer together in security and strategic areas, as evidenced by “the Japanese ability to participate in Malabar naval exercises” and the resurgence of Quad-2. Both have similar Indo-Pacific outlooks and collaborate to provide an alternative to China’s exploitative Belt and Road Initiative through the Asia Africa Growth Corridor. India also favors more Japanese participation in infrastructure development in South Asian nations. This long-term synchronization of interests has become more pronounced post-Covid-19. On the economic front, there is broad recognition of Japan and India’s strong complementarities in various areas. According to many studies, both nations benefit
greatly from collaboration in the automotive, pharmaceutical, chemical, electronics, textile, and food processing industries. In each of these instances, India provides a solid industrial base and a market for Japanese companies.

Indian authorities must go beyond platitudes and advertise, touting strong Indo-Japanese economic ties and solving problems that hinder Japanese investment. India competes with China and ASEAN nations, which have a track record of enticing foreign direct investment via established infrastructure and effective regulatory systems. Only by addressing these issues – which are basically internal political economy issues – will India be able to radically alter the economic partnership between the two strategically allied countries, which has thus far stayed an unfulfilled promise.

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