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Shifting Supply Chains from China into India as an Effective Grand Strategy in the Indo-Pacific Region

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PACIFIC FORUM

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Executive Summary

Between 2016 and 2020, nations of the Quadrilateral Security Dialogue (Quad) became patently aware of the risks posed by an authoritarian state such as China controlling much of global value chains. This realization among leaders of the Quad nations can be attributed to a general rise in populism around the globe—which ignited a debate on globalization—to the COVID-19 pandemic, China's acts of economic coercion against Australia and aggression against India in the Galwan Valley. To prevent China from weaponizing interdependence, nations of the grouping have launched several supply chain diversification and economic security initiatives such as the Supply Chain Resilience Initiative (SCRI) and Economic Prosperity Network (EPN). While these initiatives are a step in the right direction, a larger reformatory initiative is needed to prevent diversification projects from becoming a flash in the pan. Shifting supply chains out of China and into India has the potential to be that much needed reformative initiative. This exploratory study of the challenges and opportunities associated with shifting supply chains into India tests this hypothesis by examining the domestic political economy in India and the complexities of the US-India relationship.

This study observes major impediments to a supply chain diversification project. One, trade protectionism is a common feature among Indian administrations. India's diverse political landscape has warranted coalition governments, which has prevented administrations from taking reformative action on liberalizing the economy. Two, the US-India relationship historically had ups and downs. The two democracies even came to the brink of war in 1971, and 20 years later, the US unleashed economic sanctions on India for their nuclear tests. A concerted recalibration of the US-India relationship is required to solidify any form of economic partnership, short of an alliance.

To summarize, the Indian government should continue liberalizing its economy through the land, labor, and corporate governance reforms. The US should adopt a more conciliatory approach to India's domestic issues to avoid fissures in the relationship. Subsequently, the US, Australia, and Japan will be able to capitalize on the opportunities the Indian economy and the Indo-Pacific economy at large present for supply chain diversification. These opportunities can be capitalized through creating a trade bloc exclusive for the Quad and establishing a wealth fund to fund investments in the wider region.

INTRODUCTION

The COVID-19 pandemic brought to light the Quad nations of Japan, India, United States, and Australia's dependence on China for basic emergency needs such as masks, ventilators, and personal protection kits. The pandemic exposed the vulnerability of Quad nations to supply chain disruptions and their overreliance on Chinese manufacturing for their domestic consumption and the Chinese consumer market for their exports. The row between Australia and China,[1] where Australia's demand for an international probe into the origins of the coronavirus was met[2] with banning of beef imports and by issuing tariffs on barley and wine was a tocsin for the Quad grouping on China's ability to weaponize interdependence.[3] Global trade was conducted via closely integrated value chains allowing China unprecedented power, which controlled hubs of production. If limited to a conventional security grouping, the Quad would curtail its ability to take corrective action toward China over fears of economic reprisal. A coordinated effort on redesigning trade and supply chain architecture is required to decouple from China and achieve economic security, in turn solidifying a conventional security grouping.

In a world of weaponized interdependence, economic policy and security policy intersect at varying points, requiring trade-offs between prosperity and peace. To strike the necessary balance between the two, formulation of international economic policy will need to form an intrinsic part of international security policymaking. [4] While it may not be commercially feasible to shift entire supply chains out of China in the short term, a gradual shift is needed for a conventional security architecture to have significance. Through an exploratory study, this paper analyzes the opportunities and challenges associated with adopting the "shifting of supply chains from China to India and thereby positioning India as a regional balancer[5] to China" as a grand strategy in the Indo-Pacific region.

India has been discounted[6] as an alternative to China by the same economists and pundits who have championed the rise of China over the past few decades. However, scholars of international relations and security have sounded the alarm. Mearsheimer has lamented that "America had foolishly fed the rise of China" over the course of the last two decades.[7] The US and the political establishments of the developed world had conceded to the demands of their private sectors, to base economic decisions solely on business sense and cost-efficiency parameters. This myopic method of conducting international affairs had reduced American competitiveness in sectors vital to national security interests and aided China's ascent to the top of the hierarchical economic network.

Furthermore, while the revival of a discussion on globalization can be attributed to the rise of populism around the world, the death and destruction unleashed by the COVID-19 [8] pandemic made nation-states patently aware of the dangers posed by economic integration, especially when multiple critical supply chains were controlled by an authoritarian state such as China.

This paper addresses the concerns of the private sector and macroeconomists by analyzing India's implementation of economic reforms, vital to the liberalization of its economy. Consequently, I examine the challenges that persist and the opportunities that can be leveraged. The paper is broadly divided into three sections: domestic political economy, international relations, and policy recommendations.

"In a world of weaponized interdependence, economic policy and security policy intersect at varying points, requiring trade-offs between prosperity and peace. To strike the necessary balance between the two, formulation of international economic policy will need to form an intrinsic part of international security policymaking."

The domestic political economy section focuses on India's domestic political landscape and its historical political economy. This section is broken down into chapters focusing on domestic politics in India, macroeconomic reforms implemented under Narendra Modi and other initiatives taken by the administration to transform India into a manufacturing hub. I analyze India's historical socialist economic structure and challenges, such as the horseshoe theory[9], a perennial obstacle to economic reforms under successive administrations. Subsequently, I trace India's economic motivations to its ideological roots in ancient realist thinker Chanakya, offering lessons for

[1] Khorsed Zaman, "Australia-China Dispute Over Barley Trade at the WTO: Challenges Ahead and Possible Outcomes for Australia." *Global Trade and Customs Journal,* 2021.
[2] Henry Farrell, Abraham L. Newman. "Weaponized Interdependence: How Global Economic Networks Shape State Coercion." *International Security,* 2019.
3 Weaponized interdependence (WI) is defined as a condition under which an actor can exploit its position in an embedded network to gain a bargaining advantage over others in a contained system.
[4] Amrita Narlikar, "India's foreign economic policy under Modi: negotiations and narratives in the WTO and beyond." *International Politics,* 2020.
5 Offshore balancing is a strategic concept used in realist analysis in international relations. It describes a strategy in which a great power uses favored regional powers to check the rise of potentially-hostile powers
[6] Rakesh Joshi, " Will the Modi forumula work?" *Business India.* June 28, 2020. https://www.businessindia.co/magazine/will-the-modi-formula-work.
[7] John Mearsheimer, interview by Rahul Kanwal, June 2020.
[8] Narlikar 2020.
[9] Horseshoe Theory says that the right and left are not on opposite ends of a linear political continuum. Instead, the political spectrum is bent, like a horseshoe, with the far right and far left at the ends bending around so they almost touch each other.

potential foreign investors and scholars seeking to broaden their lens beyond contemporary realism to analyze India's policymaking.

In the international relations section, I examine India's evolving role in the world and US-India relations under different American presidents, highlighting the factors that have affected US-India relations during the Cold War and post-Cold War times. Underscoring the need to expand the scope of the Quad security grouping to economic spheres, I offer an analysis of the policies that converge and diverge between the Modi and Biden administrations. I cite examples of India's relative successes in leveraging its economic statecraft in the Indo-Pacific region to offer insights into arenas for potential cooperation between the US and India. I conclude the section by arguing that moving supply chains to ASEAN, as advocated by macroeconomists, will not represent diversification at all, since ASEAN is a participant of the Belt and Road Initiative and thus highly vulnerable to China's weaponization of interdependence.

In the policy recommendations section, I present my findings and offer concrete policy recommendations for both the Indian and US governments to move supply chains into India .

DOMESTIC POLITICAL ECONOMY— LOOKING FROM WITHIN

Domestic politics and the political economy significantly impact–a nation's ability to attract foreign investment and supply chains.[10] The Chinese political establishment's stability[11] has been an enticing factor for macroeconomic investors and corporations interested in setting up factories in the country. Similarly, East Asian democracies attracted industries and supply chains through policy consistency.[12] Thus, it is vital to analyze the Indian political structure to better understand the opportunities and challenges it presents for investors and corporations seeking to move supply chains into the economy.

Political history

India attained independence from British colonial rule in 1947. Since its independence, India has organized its economy on both socialist and capitalist principles, creating a mixed economy. India's first prime minister, Jawaharlal Nehru, adopted a nonalignment foreign policy, and both socialism and capitalism for its economic development. In 1947, the newly founded nation prioritized lifting its burgeoning populace[13] out of poverty and building vital infrastructure that would help attain the former objective. Nehru was not a proponent for free enterprise—his administration nationalized several existing corporations and levied taxes and tariffs on imports, making it difficult for foreign enterprise to invest and reap returns. It took an epiphanic balance of payment crisis in 1991[14] for the Indian government to implement the IMF and World Bank's proposed structural reforms and liberalize the economy partially to imports and investments.

Prior to the 1991 crisis, India was a closed economy—import restrictions limited the free exchange of goods and services, stringent antitrust laws did not allow businesses to grow, various sectors of the economy had public monopolies that operated very inefficiently and finally the "License Raj"[15] complicated the process of opening new businesses. After 1991, the Indian government eliminated the industrial licensing requirement for most sectors; removed limits on capital accumulation; eliminated licenses for imports; reduced tariffs and bank reserve requirements and restrictions on interest rates.

However, with the Indian National Congress (INC) government unable to win a majority of the seats in the houses of parliament,[16] the party had to rely on socialist and communist regional political parties to establish a government in the center. This reliance on socialist and communist parties has shaped public policy to such an extent that, liberalization measures have not gathered pace even with the easing of restrictions in 1991. Between 1991 and 2014, coalition governments led by the party failed to push through land, labor, and corporate governance reforms to liberalize the economy. The continual protectionism of the economy did not curtail the prevailing rent-seeking among bureaucrats and extended the form of the License Raj that prevailed in the pre-1991 era.

Between 1947 and 2014, the Congress party led by the Nehruvian family held power for more than 55 years. The right-wing Bharatiya Janata Party, also known as the BJP, came to power through a coalition and completed one full five-year term between 1999 and 2004. In that term, the government led by the late Prime Minister Atal Bihari Vajpayee expanded the process of economic liberalization.[17] His government initiated the privatization of state corporations, began the establishment of special export processing zones, information technology and industrial parks across the country to bolster industrial production and exports. Between 1999-2004, the Vajpayee government launched the Pravasi Baharatiya Samman and initiated plans to establish the concept of overseas citizenship to make it easier for nonresident Indians to invest and conduct business in India. His government also expanded efforts to encourage foreign investment,

[10] Katja B. Kleinberg and Benjamin O. Fordham, "The Domestic Politics of Trade and Conflict." *International Studies Quarterly* pp. 605-619, 2013.
[11] Kim Haksoon, "Political Stability and Foreign Direct Investment." *International Journal of Economics and Finance 2(3),* 2010.
[12] Ahsan Khan, Samina Sabir, "Impact of Political Stability and Human Capital on Foreign Direct Investment in East Asia & Pacific and South Asian Countries." *Asian Economic and Social Society, vol. 6(3)* 245-256, 2018
[13] Brij Kishore Sharma, "Jawaharlal Nehru's Model of Development." *Proceedings of the Indian History Congress Vo.73,* 2012.
[14] Valerie Cerra and Sweta Chaman Saxena, "What Caused the 1991 Currency Crisis in India?", *International Monetary Fund,* 2000.
[15] The License Raj or Permit Raj was the system of licenses, regulations, and accompanying red tape, that hindered the setting up and running of businesses in India between 1947 and 1990.
[16] Mukesh Rawat, "The Lok Sabha seat Congress could not win since 1951." *India Today*, May 22, 2019.
[17] Prosenjit Datta, "How Atal Bihari Vajpayee's economic policies paved way for India's growth." *BusinessToday*, August 16, 2018.

especially from Europe and the United States. Apart from Vajpayee's term in office, no other right-wing government had come to power, and prior to 2014, no right-leaning government held single majority.

In 2014, India witnessed a single party majority right-wing government under Prime Minister Narendra Modi. The BJP under Modi's leadership won 282 out of 543 seats in the Lok Sabha, earning an absolute majority to form a government.

Modi's absolute majority in parliament presented the opportunity to enact reforms that would have been impossible under a coalition government. A single-party majority government meant the Modi administration faced no democratic impediments to his objectives. Furthermore, in 2019, the BJP once again came to power with over 303 seats,[18] beating the estimates of many scholars and analysts who had predicted either a loss for the BJP or a scenario warranting a coalition. Consecutive majority governments in New Delhi had resulted in policy consistency and had assisted in realizing Modi's election campaign promise of "minimum government and maximum governance," in other words, addressing red tape, bureaucracy, and rent-seeking prevailed in the economy.

To reorganize the partially open economy into a laisser-faire economy and to transform it into an attractive investment destination for foreign investors, the Modi administration enacted reforms in land acquisition laws, labor laws, and in corporate governance—addressing the factors of production and creating an ecosystem for businesses to operate without hindrances. This reform became a harbinger for change addressing corruption, red tape and bureaucracy across government departments.

According to the Fraser Institute's economic freedom index, India under Modi has fared well in opening up its economy, with its position in the index moving from the 122nd to the 96th position between 2014 and 2019. Similarly, with the World Bank's *Ease of Doing Business Index* India's ranking went up from 142nd place in 2014 to 77th place in 2019.[19]

Multiple factors that influence decisions involving supply chains include political, macroeconomic and national security interests. Political stability and policy consistency will enhance the opportunities for building synergies between two economies such as the United States and India. While realpolitik drives national security decisions, policy and economic factors will aid in establishing India as an alternative to China—as a producer and as a market for the American consumer and enterprise respectively.

Reforms

While political stability and policy consistency will determine India's and other East Asian economies' potential to be an alternative to China and other East Asian economies as a manufacturing hub, the economic reforms and their implementation will be the true litmus test of the Indian government's ability to cater to international investors and transform the closed economy into a free market economy. Over the years, investors and industries have found three major challenges with the Indian economy—land acquisition, labor laws, and corporate governance issues.[20]

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Labor

As illustrated in the domestic politics chapter, India's first prime minister adopted both socialist and capitalist concepts to organize the economy during early years. Post-independence had profoundly impacted the governing structure for the years that followed. While the Indian economy embarked on a liberalization drive post the balance of payment crisis in 1991, several aspects of its socialist past have lingered on. One would be the labor laws. India had over 200 labor laws,[21] with 52 of them at the center and the rest dispersed among the federal level governing bodies. Several of these labor laws had not seen any reform since 1946. The most restrictive codes among them were the Industrial Disputes Act and the Industrial Employment Act which required companies with 100 or more workers to get government permission to terminate employee contracts. Similarly, the Standing Orders Act required employers in firms with 100 or more workers to seek permission to change an employee's job description. These restrictions tied the hands of many industries, ranging from garments to electronics manufacturing. The garment industry selected Bangladesh over an established pioneer in the field such as India due to such restrictive labor codes. Furthermore, Thailand, Vietnam, and China have been able to leverage their human capital and availability of resources to manufacture electronics owing to a liberalized labor code.[22]

In 2020, the Modi administration reformed the labor laws by consolidating several labor codes and creating a simpler code to attract investors. In particular, 29 out of 40 labor

[18] Eric Bellman and Corinne Abrams, "India's Narendra Modi Wins Re-Election With Strong Mandate." *Wall Street Journal*, May 23, 2019.
[19] Swaminathan S. Anklesaria Aiyar, "A Reform Agenda for the Next Indian Government." *The Cato Institute,* 2019.
[20] Ibid.
[21] Ibid.
[22] Christian Lansang and Darrell M. West, "Global manufacturing scorecard: How the US compares to 18 other nations." Brookings Institute, 2018.

laws were subsumed into the four codes of industrial relations. including, occupational safety, health and working conditions, social security, and wages. Shekhar Gupta, editor-in-chief of *ThePrint* put it well: "The simplification of the existing laws is a reform in itself.[23] These reforms take away the redundancy of multiple educator forums, particularly in labor law disputes. Now there will only be two forums—a conciliation officer and tribunal."

Prime Minister Modi reformed and tailored the 70-year-old labor codes to meet the requirements of the 21st century hyper competitive global marketplace.[24]

Land acquisition

For any multinational corporation or an enterprise seeking to operate out of India, land acquisition will be the most cumbersome and challenging endeavor. Every step in the process of land acquisition involves an opportunity for rent seeking by a politician or a government official. Land acquisition is one of the factors of production that still has remnants of the pre-1991 License Raj era. Adding insult to injury, the process is followed by high taxation, with some regional states taxing the purchase of land at 10% and over. Moreover, with over 60% of land in India put to agricultural use, rezoning of land from agriculture to industrial or commercial purposes presents yet another rent-seeking opportunity for state-level politicians to slow down the process. Currently, the reforms pertaining to the governance of land acquisition lies with the state governments. This decentralization has created an opaque and distorted environment for investors and has stalled several projects over the years with many legal disputes pending at the district courts. Numerous government infrastructure projects have stalled and been delayed due to court challenges and protests over rezoning of agricultural land.

The Modi administration reformed the half-century old labor codes to create a 21st-century manufacturing hub ecosystem. Land acquisition laws require a bold and radical move from the center to ease the process of establishing an industry or setting up a factory in the country.

Corporate governance

The dregs of the pre-liberalization era are noticeable in the corporate governance sphere, with numerous private corporations with highly leveraged balance sheets and low-quality assets availing multimillion dollar loans from India's national banks. There have been multiple controversies and corruption scandals surrounding the bad debt accumulated by state-run banks and financial institutions through these accounts. While India's capital markets have been partially liberalized since 1991, public sector banks account for over 70% of loans. Of the 70%, businessmen connected to people in power, farmers, and small-scale industries make up the lion's share of bad debts. Over the years, political parties have refrained from privatizing state-owned banks over the fear of backlash from the electorate, i.e. farmers, campaign contributors, and private sector industrialists. However, the insolvency and bankruptcy code of 2016 has rebalanced the rights of promoters, vendors, banks, and employees. The insolvency and bankruptcy code have:

- Prevented corporations from abusing bankruptcy proceedings to stall recovery action by lenders
- Addressed the 10 trillion rupees (about $134 billion) in stressed assets challenging the Indian banking system
- Improved the asset quality of banks to issue fresh credit and stimulate investments.

In 2015, Modi announced the creation of the National Institution for Transforming India or NITI[25] Aayog, replacing the planning commission of the Nehru era. This government-run think-tank identifies public sector units to be sold and privatized. Post-independence, the government was involved in sectors ranging from insurance to energy. NITI Aayog has identified certain sectors as strategic and others as not relevant for government administration. This privatization drive has brought out multiple sectors for foreign investment previously cordoned off.

Policy consistency and continuation of the reform initiated by the Modi administration will be vital to build the business ecosystem required for a global manufacturing hub. In that regard, the labor codes and corporate governance measures have undergone the necessary reform and are moving in the right direction. However, land acquisition laws and the rent-seeking mechanisms prevailing in the process of land acquisition need to be addressed for a successful "Make in India."

MAKE IN INDIA & ATMANIRBHAR

Modi launched the "Make in India" initiative in his first year in office in 2014. The initiative encouraged companies to manufacture in India and incentivized dedicated investments into manufacturing. It was designed to facilitate investment, foster innovation, enhance skill development, protect intellectual property, and build the country's best-in-class manufacturing infrastructure. The initiative has three stated objectives:

- To increase the manufacturing sector's growth rate to 12-14% per annum;
- To create 100 million additional manufacturing jobs in the economy by 2022;

[23] Gupta Shekhar, "How Modi government's 3 new labor codes were passed in Parliament, and the changes they will bring." *ThePrint.* Sept. 24, 2020.
[24] Manish Singh, "India approves Apple partners and Samsung for $143 billion smartphone manufacturing plan." *TechCrunch,* Oct. 7, 2020.

[25] The NITI Aayog is a public policy think tank of the government of India, established with the aim to achieve sustainable development goals with cooperative federalism by fostering the involvement of State Governments of India in the economic policy-making process using a bottom-up approach.

- To ensure that the manufacturing sector's contribution to GDP is increased to 25% by 2025.[26]

Post-independence, India focused on its agricultural sector to reduce poverty levels and prevent famine across the country. Over the 21st century, the Indian economy became a service sector-led economy, with the service sector, as of 2021, accounting for 54.77% of India's GDP by itself. The manufacturing sector has remained below the 15% mark and any progress in the sector has been heavily reliant on land, labor, and corporate governance reforms. Post-liberalization, successive governments failed to foster and develop the private industrial sector and relied on the public sector and import goods to cater to the needs of India's billion-plus population. This increased the import bill, thereby affecting the strength of the currency and the foreign exchange reserves. The Modi administration, despite measures that were considered obstacles to cultivating a manufacturing sector—such as demonetization and its overnight rollout of the goods and services tax—successfully planned and executed several production-linked incentive schemes to cultivate a strong manufacturing sector in the economy. Apart from the macroeconomic reforms, the administration also focused on microeconomic reforms and tailored measures to address manufacturing challenges in the country.

electronics, and advanced technologies, the Modi administration doubled down on its "Make in India" project and the Atmanirbhar Bharat through production-linked incentive schemes and other sector-specific subsidies. The Narendra Modi government popularized the phrase "Atmanirbhar Bharat" that translates to "self-reliant India" to promote and reduce reliance on authoritarian states for vital supplies and increase capacity to indigenously produce vital goods and services.

In the financial budget of 2021, Finance Minister Nirmala Sitharaman announced an outlay of $2 billion for the Production-Linked Incentive (PLI) scheme for 13 strategic sectors.[28] The plan, aimed to boost domestic manufacturing under the Atmanirbhar initiative, reduces import bills and the cost competitiveness of goods in the economy. The success of the PLI can be witnessed in the mobile phone manufacturing sector. In 2014, 50 million mobile handsets were made in India, making up 19% of its domestic demand and in 2020, 260 million mobile handsets were made in India,[29] accounting for 96% of domestic demand. This development wiped out the need for imported mobile phone handsets. With the government extending the PLI to other sectors affected by COVID-19 and those vulnerable to China's economic coercion, India's ascent to global manufacturing hub is not out of reach.

"Modi's measures have enhanced economic freedom, but have been accompanied by protectionist measures to ward off competition for indigenous industries. This practice of blowing hot and cold will eventually create a ceiling for India's manufacturing—manufacture for Indians but not for the globe. This will be the most significant challenge for diversifying supply chains out of China and into India."

For over 40 years, liberal international relations scholars have argued that trade and interdependence will prevent conflict and maintain peace between nation-states while realists have argued the opposite, that interdependence will eventually lead to conflict over the supply of raw materials and goods.[27] Challenging the assumptions that underpinned the post-war economic system, which associated economic integration with peace, Farrell and Newman identified the phenomenon of weaponized interdependence. The COVID-19 pandemic exposed the vulnerabilities in networks and the pernicious effects of a nation-state exploiting interdependence. Moreover, the Galwan Valley clash was a warning for the Indian government. To prevent antagonistic powers such as China from gaining leverage through their position of power in certain asymmetric networks such as pharmaceuticals,

Horseshoe theory asserts that the far left and far right, rather than being at opposing ends of a linear political continuum, resemble one another (like two ends of a horseshoe). The Communist Party of India's (CPI) agenda on protectionism and that of the Rastriya Swayamsevak (RSS)—India's equivalent of the US Tea Party movement—can be explained using the horseshoe theory. While the pandemic presented an opportunity for the Modi administration to double down on its "Atmanirbhar" efforts, the administration's general protectionist streak is not to be discounted[30]. Atmanirbhar is reminiscent of Nehru's self-sufficiency drive during the early years after independence. Both the RSS and the CPI emphasize the need to levy tariffs and protect domestic interests. The RSS champions domestic industry, and the CPI champions the labor force. At the opposite ends of the political spectrum,

[26] Promit Mukherjee, "Modi's 'Make In India' racks up $222 billion in investment pledges." Reuters, Feb. 18, 2016.
[27] Dale C. Copeland, "Economic interdependence and war." Princeton University Press, 2015.
[28] Kshitij Bhargava, "PLI Scheme to create jobs, says Finance Minister; will help create, nurture global champions in India." *Financial Express*, Feb. 1, 2021.
[29] Sanjana Simlai, "India's growth story to be led by PLI Scheme: Piyush Goyal." *Inventiva*, June 1, 2021.
[30] Amrita Narlikar,"India's foreign economic policy under Modi: Negotiations and narratives in the WTO and beyond." *International Politics,* 2020.

both organizations have restricted India's opening to global markets.

As administrations in India incentivize investments, reform 100-year-old laws, and cut red tape, the protectionist tendencies of successive administrations, whether through the influence of CPI or the RSS, have restricted India's liberalization drive. Modi's measures have enhanced economic freedom, but have been accompanied by protectionist measures to ward off competition for indigenous industries. This practice of blowing hot and cold will eventually create a ceiling for India's manufacturing—manufacture for Indians but not for the globe. This will be the most significant challenge for diversifying supply chains out of China and into India.

The 1.4 billion population is a large market, represents a lucrative proposition in and of itself for multinational corporations around the globe. To better understand the challenge associated with the protectionist wing of the BJP, it is vital to analyze Indian realism and how it impacts its foreign trade and economic policy.

INDIAN REALISM: CHANAKYA TO CONTEMPORARY REALISM

India's foreign policy carries three major burdens from its past. One is the 1947 Partition, which reduced the nation both demographically and politically. An unintended consequence was to give more strategic space in Asia. Another is the delayed economic reforms that were undertaken a decade and a half after those of China. The 15-year gap in capabilities continues to put India at a great disadvantage. The third is the prolonged exercise of the nuclear option. As a result, India has had to struggle mightily to gain influence in a domain that could have come so much more easily earlier.

- External Affairs Minister of India, Subramaniam Jaishankar, *The India Way* [31]

Jaishankar's analysis of the burdens that India carries from the past, places India's realism in context. India's primary foreign policy interest has been its immediate neighborhood. Unlike China, India does not have grand ambitions of shaping the world to its liking. India's soft power is evidence of that paucity. India does not use its cultural belongings such as yoga or the hundreds of languages it is home to for strategic ambitions as China does through its Confucius Institutes. [32] Indian cultural exports and India's primary soft power have come through its diaspora, not its consulates. Nevertheless, it would like to assert its unique identity and place on the world stage without undue influence from the West—or the East. That does not imply that India will not find policy congruence with states in either hemisphere. Since independence, India has chosen non-alignment and over the past 30 years, chosen to meet its economic and strategic needs by responding to shifting priorities of its populace. India's economic reforms made it an attractive market for Western companies. Upon the collapse of the Soviet Union, India has found more common ground with the West than in the years prior. India's economic needs, its climate change commitments, and its growing competition with China, have made it a compatible partner to the United States, Japan, and several European Union states. India's alliances have been a product of realpolitik and its domestic priorities, over ideological groupings as created by the West post-war and during the Cold War years.

Under the Modi administration, India's domestic and foreign policy is largely influenced by one of the ancient world's foremost realist thinkers, Chanakya. Roger Boesche [33] describes the elements of an ideal state that Chanakya envisioned: "the most important element of the state, according to Chanakya, is neither the government nor the army, but the treasury." Chanakya's influence on the Modi administration is evident from the administration prioritizing radical economic reforms, its unremitting protectionist tariffs to reduce the import bill, and the use of economic statecraft to address foreign policy challenges, such as with China. Western realist scholars will be ill-advised to analyze India using the Machiavellian lens, which places a disciplined army as central to a nation's wellbeing, or other European thinkers that place peace and harmony as the central task of the state.

As Narlikar notes, "The BJP manifesto revealed that the Modi regime was not going to be a poster-child for a Washington style of market opening. The manifesto that showed so much economic ambition also promised to put 'India First.'"

"Indian cultural exports and India's primary soft power have come through its diaspora, not its consulates. Nevertheless, it would like to assert its unique identity and place on the world stage without undue influence from the West—or the East."

The BJP's manifesto paid attention to several important goals, from cutting red-tapism to ending corruption. However, the manifesto clearly stated: "We should no longer remain a market for the global industry. Rather, we should become a 'Global Manufacturing Hub.'" This manifesto has profoundly influenced the administration's

[31] Subramaniam Jaishankar, *The India Way: Strategies for an Uncertain World*. New York, Harper Collins Press, 2020.
[32] Zhe Ren, "The Confucius institutes and China's soft power." IDE Discussion Papers 330, *Institute of Developing Economies*, Japan External Trade Organization (JETRO), 2012.
[33] Roger Boesche, *Kautilya: The First Great Political Realist*. New York, Harper Collins Press, 2017.

reform agenda, and its ease of business and economic freedom rankings testify to that fact. High tariffs are likely to remain with the BJP protecting the Indian industry. As a consequence, a supply chain diversification project should be undertaken not only from the vantage point of the American enterprise—gaining market share in an economy with a billion-plus population—or through the national security apparatus—supporting a large army and navy to act as a countervailing force to China. The vantage point of the Indian electorate—creating employment and development—should also be considered.

INTERNATIONAL RELATIONS: LOOKING OUTWARD

India's evolving role in the world and American domestic politics

From bipolar to unipolar to multipolar world order

US-India relations have had their share of ups and downs over the last 50 years. Post-independence, India chose non-alignment and avoided alliances with major world powers. The Nixon era is cited as one of the lowest points,[34]with the two nations nearly coming to the brink of war in 1971. In the 1970s, with the escalating situation in East Pakistan (modern-day Bangladesh), Prime Minister Indira Gandhi sought the help of the Soviet Union[35] to thwart any form of offensive from the United States, who had allied with Pakistan under Nixon. Interestingly, the events of 1971 were the backdrop for Nixon and Kissinger's rapprochement efforts toward China in 1972. Furthermore, the United States under Nixon allied with Pakistan and did not want an India that could morph into a threat to China or Pakistan, since it was allied with the Soviet Union. This fear evident with the Nixon administration pleading with the Chinese to station troops along its borders with India.[36] As a precursor to Nixon's 1972 trip, both Kissinger and Nixon desired to lay the foundation for friendly Sino-US relations and did not want the escalating situation in South Asia to be a detriment to that effort. Administrations that succeeded Nixon were less antagonistic toward India, though 1998 represented another low point, with the Clinton administration unleashing economic sanctions on India for its nuclear tests.[37] Nevertheless, the sanctions did not dent the Indian economy, nor did it drastically alter the US-India relationship, as Nixon's measures had in the 1970's.

Between 1970-2019, excluding the Nixon and Clinton administrations, all other American presidents have favored friendly relations with India and sought to promote economic and cultural ties between the two democracies. Under President George W. Bush, the United States and India expanded their partnership to the security sphere. It is no coincidence that President Bush was the first US president to position India as a regional balancer to China. Since Kissinger, the US-India relationship has been analyzed through the prism of US-China relations. The United States has the opportunity to leverage India's deteriorating relations with China to its own ends—to position it as a regional balancer.

In order to pressure India to back out of the conflict with Pakistan, the Task Force 74, part of the 7th fleet, was deployed[38] to the Bay of Bengal in December 1971. Fast forward 50 years, and the United States 7th fleet and Indian Navy conduct joint navy and air operations in the Bay of Bengal over a mutual interest in maintaining a "Free and Open Indo-Pacific (FOIP)."

The multipolar world in 2021 faces different challenges and the alliances of the 1970s are no longer in place. The US-Pakistan relationship is at "frenemy" status[39] and, in the words of the Biden administration's Indo-Pacific coordinator Kurt Campbell—"the age of engagement with China is over, we are entering a new era of competition." He goes on to opine, "US should engage Russia [and the] Quad … specifically India in its endeavor to counterpoise the Chinese threat."[40]

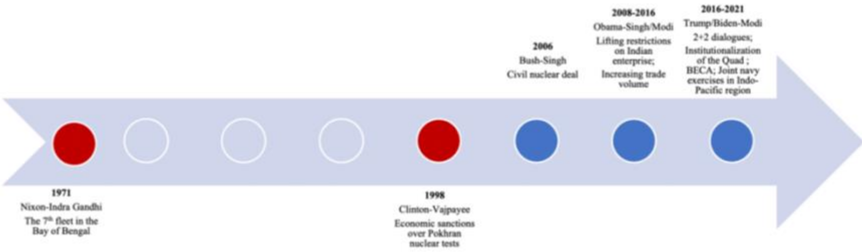

Figure 1 The high and low points in the US-India relationship over the course of 50 years.

Over the last 50 years, the US-India relationship has grown exponentially and as former US ambassadors to India have pointed out, 20 years of strong bilateral relations in international relations years is a stage of infancy. The relationship is just getting started. As successive American administrations place economic competition as a top priority over conventional security threats with China, the large Indian consumer market and the Indian economy will play a significant role in the United States' foreign policy calculus. In particular, the Modi and Biden administrations have been enacting legislation, plus foreign and economic policies that address the challenges associated with economically competing with China.

[34] Press Trust of India (PTI), "US pleaded with China to 'menace' India during 1971 war." *Outlook Magazine*, 2007.
[35] Anvesh Jain, "Interpreting the 1971 Indo-Soviet Cooperation Treaty as a Turning Point in South Asian Strategic History." *Utsynergyjournal,* 2020.
[36] Ibid.
[37] Brahma Chellaney, "Technology Control Regimes: Dealing with India." *India Quarterly,* 2002
[38] Asif Mahfuz,"US Fleet in Bay of Bengal: A game of deception." *Daily Star*, December 2013.
[39] Laurel E. Miller, "The United States and Pakistan: Best Frenemies Forever?" Rand Corp., January 2018.
[40] Kurt M. Campbell and Jake Sullivan, 2019. "Competition Without Catastrophe: How America Can Both Challenge and Coexist With China." *Foreign Affairs*, September/October 2019.

There are several policies by the two administrations that directly or indirectly address the economic competition with China. These policies present an opportunity for the administrations to build synergies, addressing the mutual threat of China.

- Strategic competition act—India's FDI bill & Ban on Chinese apps
- Infrastructure bill & Supply Chain Review—Indian Private Sector
- Foreign policy for the middle class—Vasudhaiva Kutumpakam ("The world is one family")
- Aid—vaccines and oxygen concentrators

The Biden administration's Strategic Competition Act of 2021[41] addresses the multifaceted problem of competition with China. The bill focuses on global infrastructure development, digital technology, connectivity, and economic statecraft that addresses the "China challenge." India under Modi has embarked on a similar economic decoupling drive with its foreign direct investment bill that screens Chinese investment into sensitive and strategic sectors, as identified by the Indian Ministry of Commerce.

"Over the last 50 years, the US-India relationship has grown exponentially and as former US ambassadors to India have pointed out, 20 years of strong bilateral relations in international relations years is a stage of infancy. The relationship is just getting started. As successive American administrations place economic competition as a top priority over conventional security threats with China, the large Indian consumer market and the Indian economy will play a significant role in the United States' foreign policy calculus."

President Biden's infrastructure bill, which received bipartisan support, revitalizes the American manufacturing sector and simultaneously commits to competing with China as a global leader in clean energy. It reduces dependence on China for manufacturing and revitalizes the sector in the United States. The supply chain review of the Biden administration initiated an analysis on the US' overreliance on China for raw materials and for finished goods in vital strategic sectors such as EVs, batteries, semiconductors, and pharmaceuticals. The review assisted in allocating funds to these sectors and making them highly competitive to take on China's state-supported conglomerates.[42] The administration's focus on industrial policy to compete with China is strikingly similar to the Modi administration, which roped in the private sector to manufacture several components of solar panels, and next-gen battery storage facilities to reduce dependence and overreliance on Chinese imports for India's transition to a green economy.

Biden termed his foreign policy as the "foreign policy for the middle class" in his address to Congress.[43] His administration's measures at reviving American manufacturing and reshoring factories from China, as well as withdrawal of troops from Afghanistan, signals prioritization of the American middle class. In a similar vein, Prime Minister Modi invoked the Sanskrit phrase *Vasudhaiva Kutumbakam* ("the world is one family")[44] in his UN address to the leaders of the world, signaling his administration's commitment for worldly causes such as climate change, peace, and stability. Modi has championed the growing young workforce, such that in every trade deal, his administration has prioritized free movement of its labor to foreign markets.

COVID-19 created a dire situation for developing nations with limited supply of personal protective equipment (PPE), oxygen, and vaccines. In 2020, China and India competed in initiatives to vaccinate the developing world and exhibit leadership potential to the Global South. India provided 58 million doses of the vaccine to 71 nations, of which 8 million were sent as gifts. Of the 71 nations, 37 got the vaccine for free and more than 50% of the least-developed countries received vaccines from India. On the other end, China had transformed its flagship Belt and Road Initiative to address health challenges and used the connectivity initiative to export vaccines to more than 40 countries.[45] In addition, India supplied hydroxychloroquine, personal protective equipment, and COVID testing kits to over 100 countries, while China has assisted across the world with treating COVID-19 patients. While the United States could not export even its surplus vaccines due to the export restrictions put in place by Trump in 2020, the Biden administration was quick to circumvent the policy and release excess vaccines in its warehouses to support the developing world. Furthermore, the administration delivered vital oxygen and medical supplies to India at the peak of the pandemic in 2021.

[41] US Congress, Senate Committee on Foreign Relations. "Strategic Competition Act of 2021." 117th congress, 1st session, 2021.
[42] United States, Executive Office of President Joe Biden, "Building Resilient Supply Chains, Revitalizing American Manufacturing, and Fostering Growth." Executive Order No. 140147, June, 2021.
[43] Dan Baer, "Tracking Biden's Progress on a Foreign Policy for the Middle Class." *Carnegie Endowment For International Peace*, 2021.
[44] Narayan Lakshman, 2014. "'Vasudhaiva Kutumbakam' is India's philosophy: Modi." *The Hindu*, Sept. 28, 2014.
[45] Akhil Ramesh, "On vaccines, globalists are nationalists and nationalists are globalists." *The Hill*, April 27, 2021.

These policy synergies that have the potential to lead to further convergence do not paint a complete picture of the US-India relationship, though. While select American administrations have overtly positioned India as either a security threat to its allies (including Pakistan in 1971) or as a violator of international norms (over its nuclear tests), there are other perennial barriers to the US-India relationship. There are two issues that demonstrate the US' inconsistent approach to India and India's aversions to a formal alliance with the US:

Trade Disputes—India is the US' eighth-largest trading partner, and every year it continues to grow. However, 20 years of cordial relations have also been marred by long-standing trade disputes on issues ranging from dairy farming practices to intellectual property regulations. India continues to hold onto certain protectionist measures in place pre-liberalization. Horseshoe theory prevents India from liberalizing the entire economy. Certain sectors are heavily lobbied for by Indian industry, such as motorcycles, medical devices, and dairy, and there are others that Indian administrations place as strategic to its national security, such as defense. Some of these disputes have been running for over three decades. For example, the US' issues with India's intellectual property rights can be traced to 1989, the year of the first "Special 301 report" mandated by Congress to identify intellectual property issues in trade. India was one of the eight countries placed on the watchlist, where it remains.

While the Modi administration deserves credit for further liberalizing the economy through lifting foreign direct investment restrictions, India's protectionist streak continues through several regulatory mechanisms. On the US' part, its restrictive immigration policy has stifled the growth of the Indian information technology (IT) sector, that seeks visas for its workforce to work out of client sites in the United States. India's IT sector is the world's largest and one of the largest contributors to its GDP. Given its significance to the Indian economy, successive administrations have advocated for less restrictive measures on the US' part. Trade negotiations have been slow and have not resulted in significant reforms over two decades. This stalemate could become a major impediment to advancing US-India relations and position India as an alternative to China in the US's supply chain diversification project[46].

Religious Freedom & Domestic Interference—The Office of International Religious Freedom under the Department of State releases a yearly assessment of religious freedom around the globe. India has not fared well in their assessment of religious freedom, and especially under Modi, the religious freedom report has scathingly criticized his administration's actions, which it interprets as a violation of India's constitution mandating a secular state. These reports by the US government and nonprofits, plus American government officials opining on what the Indian government perceives to be its internal affairs during Congressional hearings such as the one on India's Citizenship Amendment Bill does not bode well for US-India relations[47].

The United Kingdom's experience should serve as a guiding principle for the possibilities of "tit for tat diplomacy" between nations.[48] In March of 2021, the Indian government sent out a message to the Foreign Office in Britain that if the British parliament can debate India's internal affairs, so can the Indian parliament debate the internal affairs of Britain. This was a response to the UK Parliament deciding to debate India's farm laws, and in particular, the Indian government's actions toward the farmers protesting the bill. As a retaliatory measure, the Indian External Affairs Minister initiated a debate on issues of racism that the Indian diaspora experiences in the United Kingdom. Nevertheless, the External Affairs Minister's debate in parliament did not have the same impact as the UK parliament's since the issue was not taken up by the Indian media as the farm laws were taken up by the British media. However, as analysts note, reprisals in the form of restricting British goods into the Indian market will have a lasting impact on the British economy.[49] The Indian government's aversion to foreign governments, as some analysts would characterize as moral posturing is not an isolated and exclusive practice of the right-wing government in India. The socialist government under Indira Gandhi in the 1970's vehemently opposed the British media's characterization of her governance and the political environment in India[50]. The US's actions that are deemed as domestic interference have the potential to impact ties between the two democracies and push India further from aligning with Western interests on China or other challenges.

As noted in earlier chapters, India has been a hesitant partner to the United States and has made a concerted effort to stay out of formal alliances. India's chosen path of non-alignment has presented it with significant challenges in the past and has prevented it from reaping rewards from the US-India defense partnership. However, the non-alignment policy has provided the United States a key partner in Asia to balance China, without committing military troops or defense aid, as is needed with NATO, Japan or South Korea. India's commitment to the Quad security grouping is one such commitment that does not cost the American taxpayer and has simultaneously pushed the envelope on India's changing foreign policy approach to global powers. The new approach has been termed as multi-alignment by Indian External Affairs Minister Jaishankar.[51] While India and the United States explicitly name China as their single biggest economic competitor, neither have signaled the need to form a defense pact or treaty. In the absence of such a formal agreement, both nations are responsible for their own security and do not

46 Alyssa Ayres, "A Field Guide to U.S.-India Trade Tensions." Council on Foreign Relations, 2020.
47 "In Congressional hearing, US lawmakers critical of India's actions in Kashmir." *The Wire,* October 23, 2019.
48 Rezaul H. Laskar, "Will discuss racism issue with UK when required': Jaishankar." *Hindustan Times*, March 16, 2021.
49 Sanjay Suri, "India's Tit-for-tat Diplomacy over UK Parliament Debate is Working, and isn't." News18, March 15, 2021.
50 Kaveree Bamzai, 2019. "BBC to New York Times – Why Indian governments have always been wary of foreign press." *ThePrint*, Sept. 15, 2019.
51 "Non-alignment was for Specific Era, India Not a Bystander Today': External Affairs Minister Jaishankar." *News18*, July 21, 2020.

rely on each other's defense forces. This informal grouping presents an opportunity to reimagine partnerships beyond conventional security groupings. Furthermore, the United States and India do not find policy convergence on Russia nor Pakistan.[52] While the United States continues to identify Russia as a threat to its democracy, India has maintained strong relations with its largest arms supplier. Similarly, the US has relied on Pakistan for its "war on terror" in Afghanistan and continues to engage and embrace the nation in a frenemy status, while India and Pakistan find each other as their arch nemeses. Thus, the US-India relationship's strongest component will be economic, and better strengthened through timely initiatives such as public health initiatives during a pandemic but will not evolve into a "treaty ally" status in the near future. US Ambassador to India Richard Verma's three recommendations for building the US-India relationship sum it up well, "1) absent a treaty, work with Congress, Congress will be crucial to institutionalize the relationship, they have in the past with the civil nuclear deal 2) bring the Indian American diaspora in as much as you can and get them involved in key issues, they are a potent force, 3) end the divide between strategic and economic issues and revive strategic and commercial dialogues along with the existing 2+2 dialogues."[53]

Notwithstanding, the question remains as to whether India will transform into a rival or competitor to the United States in the decades to come, following the path of China, which was once a partner to the United States and later turned into its primary competitor[54]. It will be crucial to address this question prior to crafting a grand strategy that positions India as the regional balancer. To address the question on the future of US-India relationship, it is vital to place India's foreign economic policy and economic statecraft in context.

INDIA IN THE QUAD: LOOKING BEYOND CONVENTIONAL SECURITY

India, Japan, the United States, and Australia first came together for rescue and relief efforts following the 2004 tsunami that wreaked havoc across Southeast and South Asia[55]. The cooperation provided the foundation for the first iteration of the Quad security grouping. Japanese Prime Minister Abe Shinzo played an instrumental role in bringing together these four nations and has played a vital role in setting up the ideological foundations of the grouping. A grouping that came together for disaster relief evolved into a security grouping with military exercises such as Malabar and eventually transitioned into an economic grouping, matching the demands of the times.

Trump expanded the scope of the Quad to address economic challenges in the Indo-Pacific region.[56] Through initiatives such as the Blue Dot Network, Supply Chain Resilience Initiative, and Economic Prosperity Network, the Trump administration expanded the scope of the security grouping and the Biden administration followed suit. COVID-19 was a wake-up call to Quad nations once Australia's demand for an international probe into the origins of the coronavirus was met with bans on beef imports and tariffs on barley and wine.[57] Antithetical to the forecasts of analysts, the decoupling initiative of the Trump administration was not a partisan decision or one with a limited shelf life. The initiative was formalized by the Biden administration and leaders of the Quad have unanimously supported initiatives to diversify their trading partners and not rely on China's market nor Chinese exports for day-to-day needs.

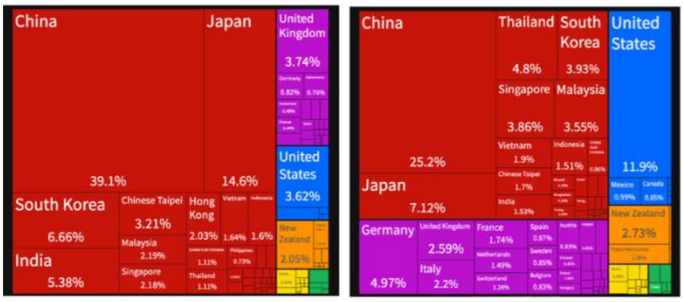

Figure 2.0 Australian export (on the left) and import destinations (on the right) as of 2019. Source: The Observatory of Economic Complexity

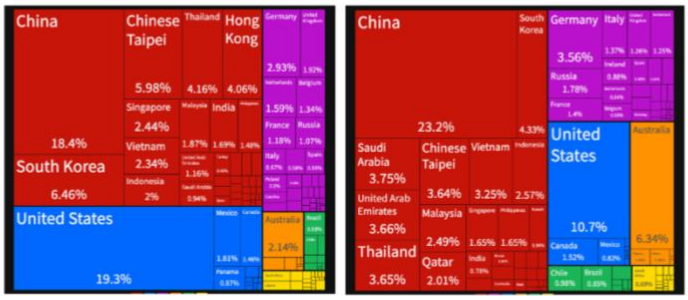

Figure 2.1 Japanese export (on the left) and import destinations (on the right) as of 2019. Source: The Observatory of Economic Complexity

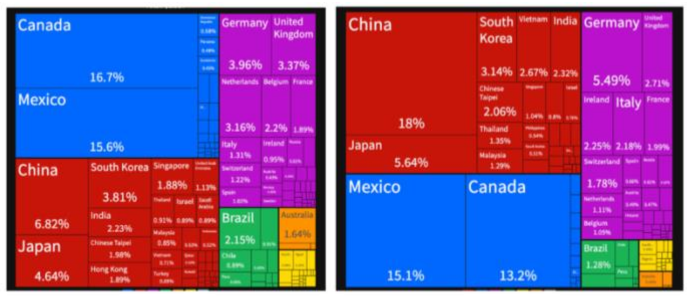

Figure 2.2 American export (on the left) and import destinations (on the right) as of 2019. Source: The Observatory of Economic Complexity

[52] Raja C. Mohan "India and the great power triangle of Russia, China and US." *Indian Express Online*, YouTube video, April 13, 2021.
[53] Ambassador Richard Verma, interview by Richard Fontaine, Center for New American Security, March 18, 2021
[54] Zhang Han, "India won't fall into US appendage as Japan given major power ambition, economic reliance." *Global Times*, March 19, 2021.
[55] Tanvi Madan, "What you need to know about the 'Quad,' in charts." Brookings Institution, 2020.
[56] Vivek Mishra, "Transforming Quad – Trump's bet on India." Observer Research Foundation, 2020.
[57] Tan Dawn Wei, "Barley, beef, wine: Australia pays price for incurring China's wrath." *The Straits Times*, Sept. 5, 2020.

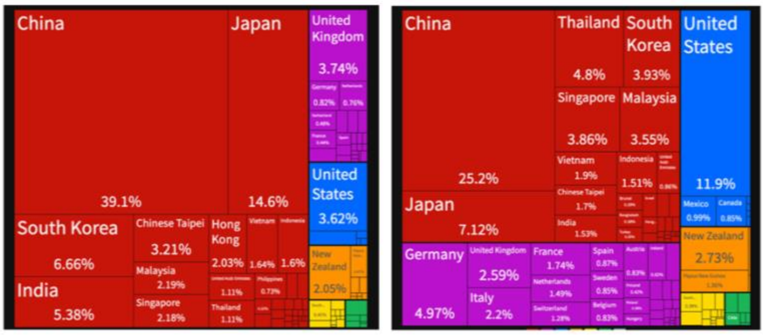

Figure 2.3 Indian export (on the left) and import destinations (on the right) as of 2019. Source: The Observatory of Economic Complexity

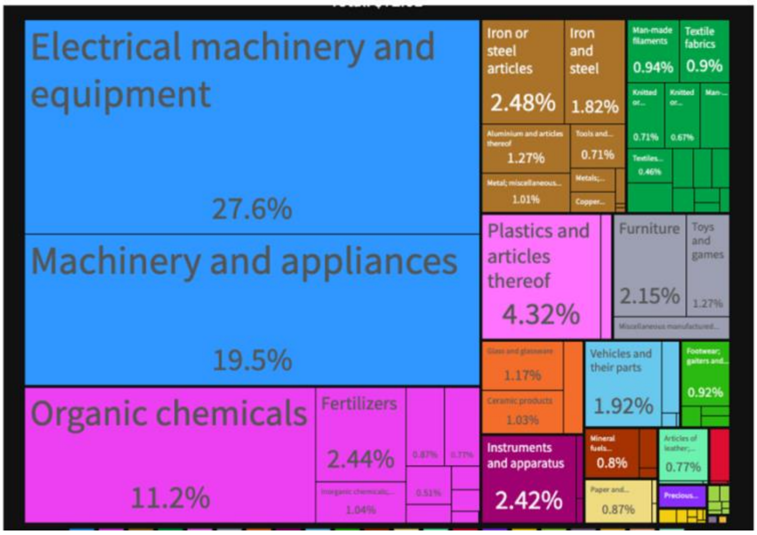

Figure 2.4 Type of Goods imported from China to India as of 2019. Source: The Observatory of Economic Complexity

After the pandemic exposed the vulnerabilities and susceptible nature of the Quad economies, any actions addressing China's border disputes with its Asian neighbors or its adventurism in the South China Sea have demonstrated to be less effective as long as the economies of the Quad are tied to China's. This realization has rightly broadened the scope of the Quad grouping from a conventional security grouping to one that addresses supply chain and economic security through the Supply Chain Resilience Initiative, infrastructure development through the Blue Dot Network, and health, trade, development and aid through the Economic Prosperity Network.[58]

Contrary to popular opinion, India has not been the hesitant partner nor the weakest link in the proverbial Quad chain. In 2008, it was Australia under the leadership of Prime Minister Kevin Rudd that unilaterally announced that it would not propose a second round of dialogue between the four nations, and formally left the Quad.[59] Only after eight years of China's destabilizing activities in the region did the group find a foreign policy convergence. Activities ranging from China's island-building projects in the South China Sea to its "debt-trap" diplomacy initiatives in South and Southeast Asia have brought together the Quad to work toward the common agenda for a Free and Open Indo-Pacific. While India's domestic policy oscillates between free market capitalism and socialism, its foreign policy has been consistent under different governments. The same cannot be said with Australia's foreign policy and this is largely to do with its dependence and overreliance on the Chinese economy, as illustrated in figure 2.0.

Economic statecraft

India's government and Modi in particular, positions China as the nation's strongest competitor and a security threat at the border and in the cybersecurity sphere. Strikingly, the Indian government decided to use economic measures following the clash between Indian and Chinese troops in the Galwan Valley over conventional security measures. The Indian government banned several mobile apps of Chinese origin over alleged national security concerns. As figure 2.4 illustrates, few sectors of the Indian economy are heavily dependent on China, both for raw materials and as a market. The Modi administration proactively and strategically targeted its PLI schemes to these sectors, such as next-gen battery storage manufacturing, solar panel manufacturing, and high-value added manufacturing in the technology sector to decouple from China and reduce the Indian economy's overreliance on China for strategic goods.

It is vital to note, that among the four Quad nations, India is the emerging market with favorable macroeconomic factors of production to shift supply chains into as part of the Quad's decoupling drive. It has invested in several infrastructure initiatives within its own borders, such as Sagar Mala,[60] the initiative to enhance the performance of the country's logistics sector. The program envisages unlocking waterways and the coastline's potential to minimize infrastructural investments. It entails setting up new mega ports, modernizing India's existing ports, developing 14 coastal economic zones (CEZs) and coastal economic units, enhancing port connectivity via road, rail, multi-modal logistics parks, pipelines and waterways, and promoting coastal community development, with the aim of boosting merchandise exports by $110 billion. And across nations with the Bay of Bengal Initiative for Multisectoral Technical and Economic Cooperation (BIMSTEC), seven South and Southeast Asian nations come together to cooperate along technological and economic lines in 14 sectors.

There are four main factors that elevate India as an economic regional balancer to China in the Indo-Pacific region:

[58] Jagannath Panda, "India, the Blue Dot Network, and the 'Quad Plus' Calculus." *Indian Ministry of Defense*, 2020.
[59] Indrani Bagchi, "Australia to pull out of 'quad' that excludes China." *Times of India*, Feb. 6, 2008.
[60] The Sagarmala Programme is an initiative by the government of India to enhance the performance of the country's logistics sector.

- **Identical market size and demographics**—With the world's second largest population and forecasted to be the world's first in the next two decades, India's population coupled with its growing middle class make it an ideal market and investment destination for investors. Furthermore, China's aging population reduces the size of the workforce and creates a larger section of the population needing government assistance. With the majority of India's population under the age of 35, it presents an attractive market for consumption, investment and, for sourcing human capital.[61]
- **China-targeted foreign policy and foreign direct investment policy**—The Indian Ministry of Commerce amended the foreign direct investment policy in 2020 to make investments from countries which share a land border with India face severe scrutiny, especially in sectors found to be of strategic significance. Similar to the Committee on Foreign Investment in the United States (CFIUS), the Indian government has used this mandate to screen investments. Strikingly, this effort is targeted at India's neighbors, in particular China, unlike the CFIUS which screens all investments perceived to be national security threats. Furthermore, the cases of debt traps by China's Belt and Road Initiative have been solved or addressed by India through financial aid or grants to the concerned party such as the $1.4 billion to Maldives and the $1 billion to Sri Lanka.[62] The Indian think tanks were the first to identify China's debt traps in the region and the Indian government has been swift to support nations affected by China's lending practices.[63]
- **Pre-existing conflict**—From the Belt and Road Initiative to standing up to China militarily at Doklam despite being the weaker State, to giving a push to the idea of issue-based coalitions in the maritime sphere or rejecting the Regional Comprehensive Economic Partnership pact (RCEP), before other nations were talking about economic decoupling from China—India made it possible to envision an Indo-Pacific order which is not dominated by China. The Modi administration's vision of a multipolar world, and in particular a multipolar Asia as expressed by the External Affairs Minister Jaishankar pegs India to be a competitor to China.
- **Indian defense budget not reliant on American support**—The European Union, Japan and South Korea receive financial support from the United States to protect their own sovereign territories. India does not receive any form of material or financial aid from the United States to protect its borders or in lieu of its defense requirements. While India's independent defense budget can be attributed to its "strategic autonomy" and it not being a treaty ally of the United States, this positions India as an effective balancer and assuages concerns of the American electorate that has over the years been displeased with tax dollars paying for the security of other nations.[64]

It is vital to compare and contrast India's strategic autonomy with ASEAN's hedging behavior to test the hypotheses of positioning India as the regional balancer to China over an ASEAN member. It is commonplace to conflate India's policy of strategic autonomy with hedging behavior. To place India's strategic autonomy in context, it is essential to understand ASEAN's embrace of Chinese investment and the influence of those investments on ASEAN's foreign policy, if any.

FOIP VS BRI

India's strategic autonomy vs ASEAN's hedging

According to scholars at the Institute for Defense Studies and Analyses, India's concept of strategic autonomy is "a mutation of realism and India's traditional non-aligned posture, best described as a dependence control strategy aimed at safeguarding its independence in both foreign policy decision making and protecting strategic assets against American pressure." [65] To contrast this with ASEAN's hedging toward the US and China, India's strategic autonomy benefits the US. India's preexisting territorial dispute with China and the perennial threat of China's economic and military might present the United States with the opportunity to embrace India's larger role in the region, including as a supply chain alternative to China. The majority of ASEAN states have chosen a path of non-confrontation since their economies are dependent on one or the other and furthermore do not possess the military capabilities to take on a regional hegemon such as China, as noted by the Philippines President Rodrigo Duterte. This is also evident from the former Malaysian Prime Minister Mahathir Mohamad's description of the Quad grouping as "an old strategy of encirclement where you try to encircle the enemy." His skepticism of the Quad grouping and his country's embrace of the Belt and Road Initiative (BRI) signal an indifference to China's hegemonic ambitions in the region and an aversion to a grouping that includes multiple Western powers.

In the past, decisions on supply chains have been made over business and economic considerations of efficiency and stability. However, scholars such as Mearsheimer have argued that such policies have been "acts of foolishness" on the part of the United States and has led to the growth of regional hegemons such as China. Moving supply chains out of China and into Southeast Asian states such as

[61] Hannah Ritchie, 2019. "India will soon overtake China to become the most populous country in the world." Our World in Data, 2019.
[62] Yuji Kuronuma, "India offers Maldives $1bn in loans to help repay China debt." *Nikkei Asia*, Nov. 28, 2018.
[63] Santhosh Pai, "New FDI rules may have unintended effects." *The Hindu*, April 18, 2020.
[64] Andrew Jeong, "Biden Shifts Focus Back to US Alliances in Japan, South Korea." *Wall Street Journal*, March 17, 2021.
[65] Guillem Monsonis, "India's Strategic Autonomy Dilemma and the Rapprochement with the United States." Manohar Parrikar Institute For Defence Studies and Analyses, Fellows Seminar, 2009.

Malaysia or the Philippines would be repeating that "act of foolishness" described by Mearsheimer. The ASEAN member states have leveraged Chinese aid and investments that are part of BRI to build vital infrastructure for creating the ecosystem required to attract the supply chains from the Western world that have shifted out of mainland China. By moving supply chains to ASEAN member states, the US would indirectly be supporting China's BRI. Furthermore, through trade pacts such as the regional comprehensive economic partnership (RCEP), the Chinese economy has built strong linkages with the ASEAN economy and several Chinese enterprises operate out of ASEAN to skate tariffs and taxes on its exports. China's tact uses the lack of "rules of origin"[66] or "country of origin" requirements by nations, especially large markets such as the US has given it significant leverage to exploit emerging markets and in turn circumvent tariffs levied on its exports.[67]

Members of ASEAN such as Vietnam and Indonesia have expressed concerns over China's incursions in the South China Sea and find policy convergence on multiple security issues related to China. However, the two members have not taken concrete steps to decouple from China nor have they opposed China's BRI. They have refrained from connecting security issues to economic independence. In the Indo-Pacific, Australia and India are the two nations that have taken concrete measures to address the influence of China's overbearing industry on their consumer markets. India has adopted sector specific production linked schemes and Australia has sought alternative markets for its mineral exports.

Furthermore, the longstanding issue of regulations involving "country of origin" tags on goods has been an impediment to India joining trade blocs that even the Quad member Australia is part of, such as RCEP. India's trade policy has been consistent on the guidelines involving the issue of "country of origin."

India's trade deficit with China burgeoned from $4 billion in 2005 to about $50 billion in 2020. Over the course of fifteen years, India's bilateral trade deficit grew with multiple Asian trading partners. As a matter of fact, India's trade deficit with Japan and China grew more under the Modi administration than under previous administrations. This ballooning trade deficit can be attributed to India's dependence on China for capital goods, chemicals and drugs that were not available at competitive prices domestically and India's manufacturing sector unable to get to scale. The COVID19 pandemic gave India even more impetus to act on decoupling and to work on its self-reliance drive through Atmanirbhar.[68]

KEY CONCLUSIONS & POLICY RECOMMENDATIONS

To diversify supply chains out of China and into India, both the US and India have to implement economic and trade reforms and mend their ways of conducting international relations. There are five key areas where both India and the United States have to work closely to successfully position India as a regional economic balancer.

The Indian administration should:

Increase strategic PLI

The Indian government should increase its production linked incentive schemes, targeting sectors that are dependent on imports from China. The government should direct investments and support small and medium enterprises with loan waivers.

Reform land acquisition

The Modi administration has reformed labor codes and corporate governance. Land acquisition needs to follow suit to remove rent-seeking mechanisms out of the process of establishing an industry in India. The land reform agenda has been withdrawn to the state-level and this has created an opaque environment for investors. The Modi administration needs to make land acquisition simpler and straightforward to transform the nation into a manufacturing hub.

Move beyond the impasse of the horseshoe theory

The Horseshoe theory summarizes the conundrum successive Indian administrations have had with implementing radical economic reforms. Due to the parliamentary system of governance, the central government has been at the mercy of political parties that foment its coalition government. While the Modi administration has a single party majority in the house of parliament, it has been wary of antagonizing right-wing trade unions and associations that protect indigenous industries. The Modi administration has to take advantage of its majority and should further accelerate the liberalization drive. In order to fulfill the promises in its election manifesto of not reducing India to a market for foreign enterprises but a source of manufacturing for the world, it should create a business ecosystem that is efficient and less bureaucratic. The vaccine diplomacy initiatives of the Indian government highlighted India's capabilities and potential to manufacture for the world. India should move beyond the Horseshoe theory and not limit its manufacturing for Indians but to all members of the family as espoused in Modi's favorite mantra of *Vasudhaiva Kutumbakam* (from his UN speech). In the past, Modi has evoked the Indian mantra in the context of acting on climate change and in the recent past the mantra has been practiced well with India's vaccine diplomacy initiatives. India should extend it to manufacturing for the world.

[66] Rules of origin are the rules to attribute a country of origin to a product in order to determine its economic nationality.
[67] Kirtika Suneja, "13 RCEP nations oppose India's strict country of origin norm," *Economic Times*, June 12, 2019.
[68] Dilasha Seth, "Double-digit rise in exports helps India nearly halve trade gap with China." *Business Standard*, Oct. 8, 2020.

The American administration should:

Adopt the French or Japanese model of diplomacy over American liberal Hegemony

India's aversion to any form of "interference" in its internal affairs are a product of its past as a British colony. India is highly suspicious of Western powers and any hint of imperialism emanating from the actions of the US creates fissures in the bilateral relationship. India is sensitive to any virtue signaling through Congress, the Senate, State Department, or other activism funded by the US government. Furthermore, the American administration's actions are discerned to be an act that diminishes India's place on the world stage as an equal player. This feeling of inequality, exacerbated through acts of virtue signaling by the United States on international forums does not sit well with Indian governments trying to assert India's unique identity on the world stage and sends mixed signals to the Indian populace and diaspora that champion the US-India relationship. To this end, the US should adopt the French or the Japanese approach to grow the bilateral relationship—not cultivating the bilateral relationship through a Cold War lens but through diplomacy that prioritizes shared interests in the economic and security sphere to address mutual threats in the Indo-Pacific region.

Settle outstanding trade disputes

The US and India should move beyond the stalemate in negotiations to sign a trade deal that includes the services sector. The outstanding issue of visas for Indian technology workers should be addressed through a specific visa category for professionals working on advanced technologies such as cybersecurity, robotics and artificial intelligence (AI). The United States faces an acute shortage in skilled engineers, especially in fields such as AI, robotics and next generation manufacturing. Over 56% of AI engineers in the US are Chinese nationals.[69] As the US-China competition in the advanced technology space takes shape, the US will have to reduce its dependence on China not only for raw materials, but for human capital as well. India's major bone of contention with free trade agreements have been their limiting nature for the movement of its human capital. Regional trade deals such as RCEP, to bilateral deals such as the ones with the US or Europe, India has advocated for easing of restrictions for free movement of its tech talent across shores. The US can assuage these concerns by offering India labor, sector-specific visas. The Quad fellowship offered for STEM students of Quad nations to pursue education in the US is a welcome measure. This will partially if not completely address the Chinese AI talent dependence issue and the outstanding trade issues with India.

Quad trade bloc

Upon addressing these outstanding issues, the US should leverage the comparative advantages of nations of the Quad security grouping to draft a trade bloc akin to the RCEP and CPTPP with an option for other Indo-Pacific nations to join later if they meet guidelines on rules of country of origin and other environmental regulations. The SCRI and EPP will be enhanced through a free trade bloc between the four Quad nations.

Quad wealth fund

Quad member nations jointly decided to deliver over a billion vaccines to Southeast Asia by 2023. The salient feature of that commitment was the division of roles—India will manufacture, America will provide technology, Japan will finance, and Australia will provide the logistics. This model of engagement should be adopted to compete with China and for development projects in the Indo-Pacific region.

The Indo-Pacific region has a high demand for high quality physical and digital infrastructure. By establishing a Quad wealth fund, the grouping can take advantage of Japan's monetary power, the US's technology and know-how, Australia's established relationships with the Pacific Islands and ASEAN members and India's engineering talent to build the region's infrastructure. This will provide the region with an alternative to China's BRI and earn goodwill from smaller states in the region. Similar to a sovereign wealth fund of a nation, this fund will pool resources of the Quad nations to execute infrastructure projects in the region by consolidating the SCRI and EPN initiatives. These measures will direct capital and resources to diversify supply chains and will enhance the trade architecture to "Make in India" for the Indo-Pacific region.

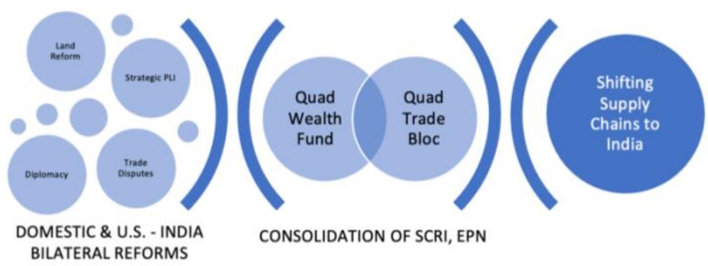

Figure 3 Policy Recommendations

[69] Amy Borrett, "The US is losing ground to China in the global race for AI leadership." *Tech Monitor*, March 10, 2021.

ABOUT THE AUTHOR

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