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India-APEC Products Trade: Importance of Trade in Intermediate Products and the Challenges Ahead

India's principal trade partners are countries/economies in the Asia-Pacific Economic Cooperation (APEC) region, and over the last decade the share of APEC in India's trade has been growing. Specifically, India's trade share with East and Southeast Asian countries has been increasing significantly. Given that APEC's share in world trade increases year on year, as well as its share in India's trade basket, there is a need to look deeper into this.

Deeparghya Mukherjee¹

Over the last 13 months, India's products exports have declined consistently as has its imports.²The discouraging trade scenario in the face of a stagnant manufacturing sector that currently accounts for only about 16% of India's GDP is a cause of concern on various counts. As trade is an important tool to foster growth in the absence of strong domestic consumption growth, improving trade prospects in the manufacturing sector is important to address India's

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²See "December Exports fall for 13th month, exporters brace for tougher times" <http://www.reuters.com/article/india-trade-idUSKCN0UW0AU>

growth ambitions as well as concerns over employment for India's large body of low to semi-skilled work force.

In order to kick start the manufacturing sector the current government at the centre has undertaken various initiatives to build India as a brand. The prime minister himself has visited a number of countries inviting entrepreneurs to invest in India. A number of chief ministers of various states have also followed suit visiting countries like Singapore, China, Japan, the United Kingdom etc. in order to attract investment in their respective states. However, despite such efforts, the manufacturing sector is yet to show signs of development and the only encouraging signs have come in the form of announcements of a couple of foreign investments which are yet to materialise at a practical level.

Under these circumstances as Indian policy makers strategise for the future, it may be wise to dig deeper into India's recent trade statistics identifying regions in the world with which India's trade relations have grown, the ones which have potential for becoming more active trade partners, as well as sectors which have done well either in trade of intermediates or final products. As we try to address these issues, we also look at the trade scenario in the world today and comment on developments which might impact India's future trade potential.

World trade has shown signs of slowdown and the prospects for a revival are slim in the short term.³ Asia-Pacific Economic Cooperation (APEC) as a region accounts for more than half of world trade as well as about 57% of the world GDP as of 2014 (US\$44 Trillion).⁴ A significant amount of the trade occurs within APEC members itself and is comprised by products which are used further in production of a commodity suitable for final consumption i.e. in trade of intermediates. In short, international trade has been increasingly taking the shape of trade in intermediate products and hence supply chain trade or value chain trade has become the order of the day due to which any product gets made across various countries.

Looking closely at India's trade statistics, one realises that India's principal trade partners are countries/economies in the APEC region, and over the last decade the share of APEC in India's trade has been growing. Specifically, India's trade share with East and Southeast Asian

³See "Becalmed" <http://www.economist.com/news/finance-and-economics/21665040-slowdown-global-trade-growth-bad-news-many-emerging-markets-becalmed>

⁴ Statistics quoted from publications by the APEC policy support unit "APEC in Charts 2015"

countries has been increasing significantly. Given that APEC's share in world trade increases year on year, as well as its share in India's trade basket, we look deeper into this.

Figure 1 below shows us how India's exports and imports with APEC countries have changed over time. India runs a persistent increasing trade deficit with APEC resulting from imports growing at a rate higher than growth of exports.

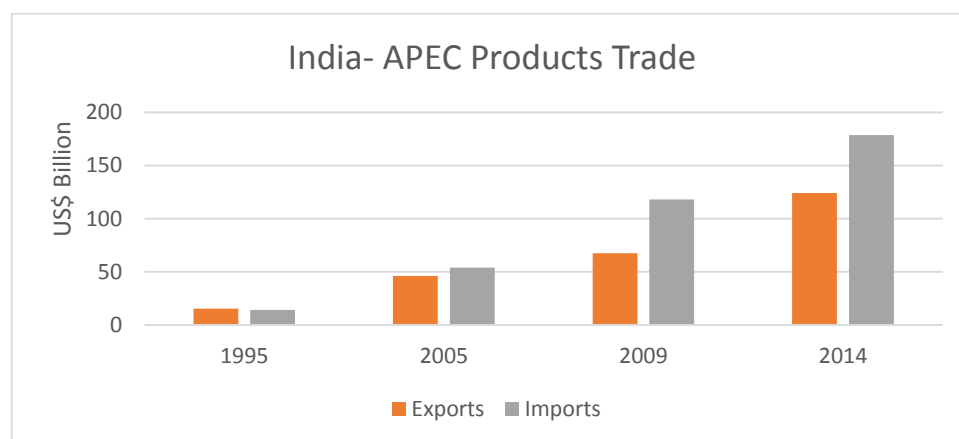


Figure 1: India's product exports and imports with APEC economies

Source: UN Comtrade Statistics

A variety of reasons are offered as to why India's exports have not picked up as much as the imports in the said period. The most important of these is the competition that Indian products face from China. This is also a reason behind India's exports decline over the last 13 months. The Yuan devaluation has hit the prospects of Indian manufacturers abroad.

When one looks at the trade in east and south east Asian countries (which has shown the greatest growth potential in the last few years) one realises that trade in parts and components currently forms the bulk of regional trade. The multiple trade agreements that have been signed including ASEAN and other Asian countries like China, Australia, Korea and Japan look to facilitate value chain trade throughout the region.

Taking a closer look at the India-APEC trade statistics, India's trade with APEC has increasingly taken the form of trade in intermediates as well.⁵ Figure 2 below shows the increasing importance of trade in intermediates. The statistics presented cover a time period ending in 2012 when Indian exports were still growing and the present slump had not started. Over the last decade and a half, intermediates comprised of about 70% of India's exports to APEC and more than 60% of India's imports from APEC.

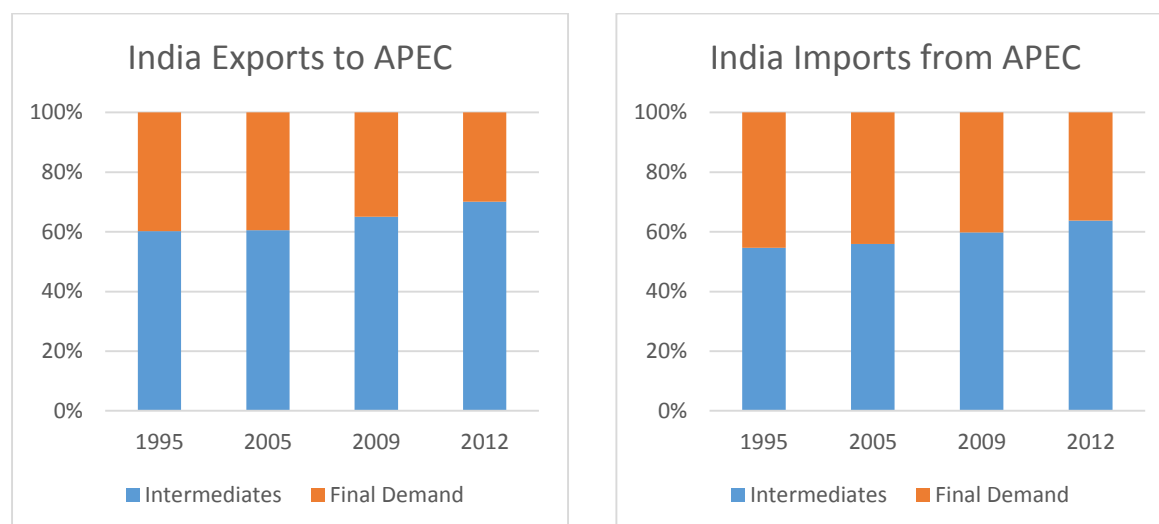


Figure2: India APEC trade in intermediates and final products

Source: UNCTAD EORA statistics

The sectors that stand out in India's intermediates trade with APEC are: Agriculture, Food and Beverages, Textiles and wearing Apparel, Petroleum, Chemical and non-metallic mineral products, Metal Products and Electrical machinery. These are sectors which appear in both India's top exports as well as imports with APEC as far as intermediates trade is concerned. Hence, it may not be wrong to interpret that India has started participating in value chains of these product categories. We cannot however infer anything about the stage in value chain (upstream or downstream) where Indian products enter. Some sectors that have been revealed to be most important include ones in which India has had a comparative advantage in world trade. This is true for Agriculture, food and beverages and textiles. India's presence in the downstream stages of refined petroleum products exports help figure petroleum as one of the significant products exported by India to APEC. Significant private investments as well as

⁵ We define imports (exports) of intermediates as any import (export) that is further utilised in production by a particular sector of a country and does not directly get consumed by a final consumer.

government support has helped India achieve this position in world trade.⁶ The importance of electrical machinery and metal products are also important from a value chain perspective. Several reports suggest India's growing role in automobile value chains where trade in parts and components have been growing.⁷

Recognising the growing importance of intermediates in world trade as also reflected in India-APEC trade statistics, we seek to find how India's advantages in these sectors fare in the face of current developments in world trade. The current bottlenecks faced by India in expanding trade in manufacturing products need to be addressed on two counts. First, global trade would first need to pick up through consumption growth and second, India must be able to remain competitive at least in sectors where it has had an advantage as well as develop competitiveness in others. A few recent developments may pose a challenge to India's competitiveness going forward.

One of the most crucial trade deals concerning the APEC region, namely, the Trans Pacific Partnership (TPP) has been negotiated and countries await its ratification and implementation in the current calendar year. The TPP having been christened the most modern trade agreement makes way for reduction in import tariffs across the board and sets the highest standards of trade liberalisation till date. India and China are not a part of the TPP. The agreement brings down trade costs amongst member countries in an unprecedented fashion apart from easing investments and market access. The developing countries which are signatories to the TPP stand to gain by ways of inward foreign investments which would generate export revenues and substantial employment effects. Countries like Viet Nam which have been undertaking multiple reforms are scheduled to benefit significantly both through increase in investments and greater market access in countries like the US and Japan.⁸ Since China is not a member of the TPP, Vietnam may benefit from new business ventures tapping its lower labour costs and conducive business environment in the short to medium term. Additionally, Vietnam would benefit from already being present in the value chain of certain products where China is

⁶See "India's downstream petroleum sector: Refined product pricing and refinery investment" International Energy Agency Working Paper (https://www.iea.org/publications/freepublications/publication/Indian_Petroleum.pdf)

⁷ See "Building World Class Automotive Supply Chains in India" AT Kearney and CII joint study (https://www.atkearney.com/documents/10192/2659569/Building+World-Class+Automotive+Supply+Chains+in+India.pdf/3b40aab5-765c-403e-bc51-bf16e7357cc7)

⁸See "Vietnam looks for reform and investment boost from TPP deal" (http://www.ft.com/intl/cms/s/0/e104d4b8-6c11-11e5-aca9-d87542bf8673.html#axzz3yLY0AkmV)

important like electronic products. Vietnam may move up the value chain taking advantage of the new opportunities.

India's perceived reticence towards trade liberalisation coupled with less than fruitful negotiations in the India-EU trade agreement, as well as the World Trade Organisation (WTO), now look to corner India and thereby pose a challenge towards utilising its trade potential. The Trans-Atlantic Trade and investment partnership (TTIP) between the US and the EU once negotiated and implemented may further dent India's prospects in terms of market access in APEC countries and otherwise.

Amidst these agreements which appear to impact India's trade prospects negatively, the only one which is under negotiation and can help India's interests in the APEC is the Regional Comprehensive Economic Partnership (RCEP). The agreement currently under negotiation has several TPP members apart from all the ASEAN countries in addition to China and India. The number of developing countries in the RCEP are higher than those in the TPP. Currently, the RCEP does not set as high standards as the TPP but will surely be impacted by the TPP given the common members. Given that the TPP is already negotiated, RCEP negotiations may now gather speed so that countries outside TPP do not lose out as much as they would without the RCEP.

The presence of multiple developing countries in RCEP which are not in a position to adhere to the TPP standards as well as the presence of China (which should dominate the proceedings and stands to lose out the most due to its absence from the TPP), the RCEP may well aim for a diluted version of the TPP in terms of liberalisation standards. India's negotiations at the RCEP hold the key at this point in determining its future trade potential with Asia and APEC at large. It would also determine how well India can "Act East" on the economic front.

In sum, the increasing share of trade in intermediates between India and APEC reflect India's gradual integration with the Asian regional value chains especially for sectors like Agriculture, textiles & wearing apparel, petroleum, metal products, electrical machinery etc. However, recent trends of a slump in Indian exports and trade in general, coupled with the signing of the TPP may require attention from Indian policy makers if its limited manufacturing trade advantage needs to be improved. The APEC and specifically East and South East Asia would be of key importance for India's exports in the medium to longer term and in this respect the

negotiations at the RCEP would be of primary importance. A successful RCEP which may be significantly influenced by the agreed terms in TPP (given the common membership) would ensure India's growing participation in value chains in the Asian region as well as development of a dynamic manufacturing sector in India. This would be instrumental in facilitating the manufacturing sector achieve the targeted share of 25% of Indian GDP by 2025 from its current share of 16%.

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