China’s Rise and the U.S. Trade War With India

Washington and New Delhi may be natural allies, but that doesn't mean that they see eye to eye on economic ties.

BY CARTER DOUGHERTY | SEPTEMBER 28, 2015

Listen closely to how American diplomats talk about India, and you'll detect a curious, unrequited yearning about the world's largest democracy. Pluralist, the source of a vibrant diaspora, and prone to taking one step back for every two steps forward, India seems like our kind of democracy — a natural fit for an ever closer relationship with United States.

Yet the chief irritant in bilateral relations — trade — looms large enough to threaten the dream of an “IND-US Civilization,” as a Times of India headline once put it, creating a policy dilemma that will become only thornier with the continued rise of India and China. Indian Prime Minister Narendra Modi, who met with U.S. President Barack Obama on Monday morning, may go down as the Indian leader who cemented a national strategy of hardheaded mercantilism, one protected by a close security relationship with the United States. The trick, on this trip by Modi and in the future, will be to convince U.S. businesses that there are enough investment opportunities in India to trump complaints over trade policy and to keep Washington's eye on the fast-developing security ties between the countries.

At a recent discussion at the Peterson Institute for International Economics, Arun Singh, India's ambassador to the United States, didn’t hesitate to hammer home that point. C. Fred Bergsten, the founding director of the institute — a man as ebullient about free trade as any human can be — had just delivered a 10-point sermon on what India stood to gain from channeling its inner Adam Smith: $500 billion in additional annual exports 10 years out and 8 to 10 percent growth per year. All that New Delhi had to do? Reduce barriers to imports, welcome more foreign investment, and take some of those steps unilaterally to gain international credibility. Singh responded with a call to respect “different political economies” and not to lose sight of the "strategic dimension to this relationship" — keep an eye on the bigger picture, in other words.
That bigger picture, for now and for the foreseeable future, is circumscribed by China. Indeed, U.S.-India defense cooperation has accelerated in the past three years, all with a wary eye toward Beijing. In June, U.S. Defense Secretary Ashton Carter renewed the U.S.-India defense framework agreement, the basis of security cooperation between the countries. That accord solidified a partnership that has been in full swing since 2012 to develop militarily useful technologies, with a focus on jet engines, unmanned aerial vehicles, and aircraft carriers. The two countries may even one day jointly patrol the Strait of Malacca (known in Beijing as “China’s windpipe” because it’s a vital shipping lane). “A greater partnership with the United States is now much more palatable in India than it was until very recently,” Richard Rossow, a senior fellow at the Center for Strategic and International Studies, told me.

In fact, it’s probably necessary. In a May visit to Beijing, Modi undiplomatically called on China to “reconsider its approach” to relations with India, a deceptively compact phrase that encapsulated gripes about a disputed border, a massive trade imbalance, and Chinese ties with Pakistan — now more an irritant for India than a lodestar for its foreign policy. It’s no coincidence that Modi is challenging China as he builds bridges with the United States.

But Washington remains unhappy with Modi on trade. Part of that frustration reflects a measure of dashed expectations. Modi’s Bharatiya Janata Party is supposed to be the free market party in India, or at least freer than the long-governing Congress party. “We’ve seen some progress, but we’ve recognized some headwinds,” Nisha Biswal, U.S. assistant secretary of state for Central and South Asian affairs, said at the Peterson Institute. She referenced “strong conversations” with Indian counterparts about India’s treatment of intellectual property and emphasized her “violent agreement” with Bergsten’s remarks.
To show India that it means business, Washington has mounted several challenges to Indian trade policy at the World Trade Organization (WTO). In 2014, U.S. Trade Representative Michael Froman upped the ante with a special review designed to address what a 2015 report by the Office of the U.S. Trade Representative called “serious questions regarding the future of the innovative climate in India.” The criticism reflects both the complaints that pharmaceutical and entertainment industries have with India and their sway with the U.S. government. A broad, multilateral agreement on easing bureaucratic impediments to trade has stumbled repeatedly over India’s efforts to prevent the WTO’s anti-subsidy rules from becoming the basis for challenging the country’s grain-stockpiling program. India has a significant services industry, but is decidedly unenthusiastic about a WTO negotiation for that sector. Amid these tensions, U.S.-India investment treaty talks have largely stalled.

This tension has also led to open hostage-taking. India has long sought entry into the Asia-Pacific Economic Cooperation forum, the ungainly 21-member group around which much regional commercial diplomacy clusters. The United States has responded that India could boost its case if it took some steps of the sort Washington is looking for on trade. But Modi isn’t snapping at that carrot.

The reason: He has his eye on developing India’s manufacturing sector, which accounts for some 16 percent of its GDP, a much smaller share than in most developing countries. On track to become the world’s most populous country by 2020, and with a labor force too dependent on basic agriculture, India needs job-creating investments in manufacturing to develop and avoid social upheaval. In a good year, India pulls in about $40 billion in foreign investment — less than half of China’s tally and trained largely on its services sector.

Modi’s signature effort here is his “Make in India” campaign, a series of reforms built around labor policy, land use rules, and taxation. Above all, it’s a strategy of “gradual reform rather than sweeping changes to India’s business environment,” as a report by the intelligence firm Stratfor put it. It’s a form of mercantilism that bets on the lure of India’s 1.2 billion people, including a substantial and growing middle class, to attract foreign capital that won’t be intimidated by the business environment and that can be harnessed to generate export-driven growth.
That strategy has more in common with China than Modi — or Americans — might care to admit. “India is a big enough opportunity that you already see countries willing to make big exceptions for it in different ways,” Vikram Singh, vice president for national security and international policy at the Center for American Progress, told me.

“It’s a big market and it’s growing.” From the perch he left last year as the Defense Department’s top official for India, Singh watched the dynamic play out in security policy. The world now treats nuclear-armed India, at the U.S. State Department’s behest, as a responsible power, even though it hasn’t signed the Nuclear Non-Proliferation Treaty, he said.

Other parts of the U.S. government are more circumspect about India. Law enforcement officers feel behind the curve on how Sino-American relations have unfolded and are starting to ponder what economic challenges could emanate from India, according to people working with them. Modi wants to dramatically expand growth. That route could be entirely legal, but some Indians might take to economic espionage. India, with many talented software developers and engineers, could become a source of cyberpiracy. India is already a source of malicious consumer fraud in the United States over debt collection. Indian political influence in the United States, perhaps channeled through the diaspora, could stand in the way of effective law enforcement, the FBI fears.

It’s a potentially fraught mix. A country welcoming investment, but skeptical of trade; one that’s eager for exports — but imports, not so much. One apt to partner with the United States as the world contemplates China’s renaissance, and with a diaspora that has given to its adopted country and has gotten back amply in return. For the United States, India could turn out to be like Japan, the latest Asian country that won’t embrace the free-marketeering American way, but whose importance to U.S. national security interests generates friction over how much objectionable economic policy Washington should let slide.

In the 1980s, President Ronald Reagan’s defense secretary, Caspar Weinberger, famously brandished a map highlighting Japan’s role in containing the Soviet Union — the island country looked a bit like a huge aircraft carrier off Vladivostok — and assiduously defended Tokyo at a time of rising trade deficits. One day, a successor of his may very well produce a map showing India as a base facing China’s blue-water navy in the Indian Ocean. The message: Bilateral disputes over trade with New Delhi aren’t worth fighting over.

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