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Article

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Isabella Gourevich, Dorothee Hillrichs and Camille Semelet

India – A Giant in the Making?

KEY MESSAGES

- **India has become a key player in services, and critical in pharma and food security in the Global South**
- **India is setting course to be a manufacturing hub with a mix of targeted subsidies and trade integration**
- **First successes are visible: India now exports more machinery and the quality of its goods is increasing**
- **The EU's share in Indian trade has fallen since the 1990s, while China became its main trade partner**
- **Trade negotiations with the EU began in 2022. Success is a must for both sides but will be difficult to achieve**

The 2024 BRICS enlargement is a step towards the formation of a political and economic bloc set to represent the Global South in a multi-polar world. While widely interpreted as a success for China, its rival India could stand to benefit. A founding member of BRICS, India has long had significant weight in the global economy. With a population above 1.4 billion, it surpassed China in 2023 as the world's most populous country. It ranks 5th in terms of GDP and, with a year-on-year growth rate of 7 percent, India outpaced all its BRICS peers in 2022 – including China. In recent years, however, India moved to center stage for other reasons. As the world grappled with supply chain disruptions during the Covid-19 pandemic, attention turned to India's potential to mitigate the West's overwhelming reliance on China. Tech giants like Apple and Microsoft lead the move for diversification and are starting to expand production in India (Forbes 2023). Against the backdrop of rising geopolitical tensions between Western democracies and India's BRICS peers, Russia and China, new partnerships

are being formed. Given the increasingly autocratic composition of BRICS, strengthening ties with India now appears paramount for many Western countries.¹

In this article, we portray India's integration into the world economy to assess its current role and path forward. We begin our analyses by highlighting sectors in which India is already indispensable. Next, we decompose India's trade flows and shed light on its linkages with the BRICS countries and the EU. We then discuss recent developments in India's industrial and trade policy and point to promising signs in the country's exports.

INDIA'S ROLE IN GLOBAL TRADE

As European and American governments seek to reduce their dependence on China, they are setting their sights on India as a "safe" new alternative. The country has already established itself as a worldwide supplier in a diverse set of industries. In services, India is the 14th biggest exporter worldwide and ranks fourth in information and communication technology (ICT) services, according to OECD data. The global surge in demand for ICT services due to the Covid-19 pandemic boosted Indian services exports by 26 percent between 2019 and 2021,² twenty percentage points above the year-on-year average growth rate in the previous decade.

In goods trade, India is a critical supplier of products ranging from primary minerals to luxury goods. Worldwide, the country is one of the leading jewelry and spice exporters. At the same time, more than 40 percent of global exports of iron and non-alloy steel as well as granite originate in India. For many developing countries, India plays a vital role in food security and health.

¹ All data cited in this paragraph are from the World Bank.

² Service trade data in OECD-BATIS ends in 2021.



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Table 1

India's Critical Role in Food Security and Health by World Region

World Region	Rice (HS4 1006)			Insecticides, fungicides, herbicides (HS4 3808)			Medicaments (HS4 3004)		
	Import share > 50%	Import share > 75%	Top-5 supplier	Import share > 50%	Import share > 75%	Top-5 supplier	Import share > 50%	Import share > 75%	Top-5 supplier
East Asia & Pacific	2	1	19	0	0	16	2	0	22
Europe & Central Asia	0	0	23	0	0	7	0	0	7
Latin America & Caribbean	0	0	10	0	0	11	3	0	30
Middle East & North Africa	12	6	20	1	0	13	0	0	6
North America	0	0	2	0	0	1	0	0	1
South Asia	5	4	6	2	2	6	4	2	7
Sub-Saharan Africa	19	11	45	0	0	29	18	3	48

Note: The table presents the number of countries from each of the seven World Regions for which India accounts for more than 50 percent or 75 percent of the imports of the three selected product groups. In addition, the third column of each product represents the number of countries for which India is one of the top five suppliers of the given product.

Source: UN Comtrade; authors' calculations.

In August 2023, India gained much negative publicity with a ban on rice exports. While the government defended the measure by citing fear for domestic food security, the ban shone a spotlight on India's role in global food security, as the country supplies 40 percent of global rice exports. Developing countries in Sub-Saharan Africa, the MENA region,³ and South Asia are especially vulnerable to Indian trade restrictions. As Table 1 shows, India supplies more than 50 percent (75 percent) of the rice imports of 38 (22) countries. Neighboring Bhutan and Nepal purchase almost all their rice, and Sri Lanka more than 90 percent, from India. The main rice-producing areas are in India's north, a region predicted by World Bank climate change experts to experience more severe droughts in the future. Investments in climate change adaptation strategies are therefore not only critical for India, but for many other countries as well.

Next to services and primary goods, India is a key player in the chemicals and related industries. These industries, too, produce goods critical for food security, such as insecticides and herbicides. Moreover, many countries depend on India for pharmaceutical supplies, with 27 countries spending more than 50 percent of their medicament expenses on Indian products. As with rice, most of these countries are in Sub-Saharan Africa: 18 out of 48 countries in the region obtain more than half of imported medicaments for retail sale from India. Ethiopia, another new BRICS member, receives 64 percent of its medicament imports from India, while for Ethiopia's neighbor, Eritrea, India's share lies above 80 percent. The importance of India as a

pharmaceutical supplier to the Global South makes intellectual property rights a contentious topic in ongoing trade negotiations between the EU and India. Where European pharma companies point out the importance of strict patent laws to recuperate high up-front investments in R&D, NGOs warn that constraining Indian production of generic medicines would have severe effects for medical care in developing countries.

AT A CROSS-ROADS: TRADE LINKAGES WITH BR(I)CS AND THE EU

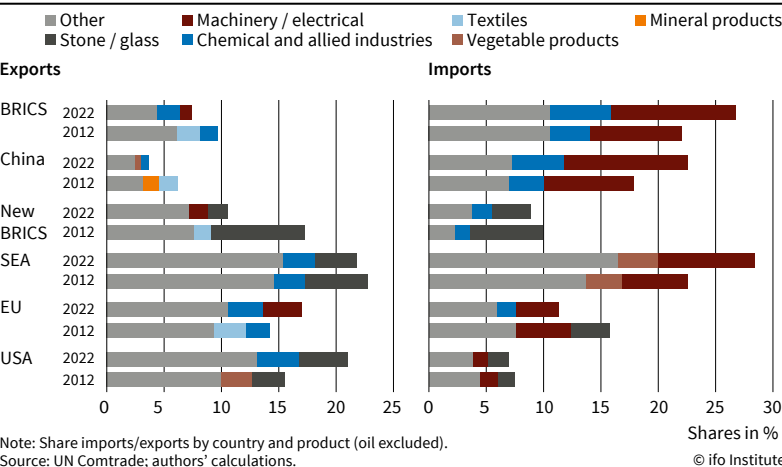
Trade with the BRICS nations plays a pivotal role in India's economic landscape. Oil trade in particular ties India to new and old members. Over the past two decades, crude oil consistently ranked as the top imported product, comprising 9 to 14 percent of total imports since 2005. Saudia Arabia and the United Arab Emirates supply around half of India's crude oil imports. In 2022, the import share surged to 20 percent, in parallel with the export share of refined oil, a likely consequence of the Western sanctions imposed against Russia.⁴

Excluding oil, China and the UAE are India's main partners within the BRICS. In 2022, the BRICS represented over one-fourth of India's total imports (Figure 1). India's imports from China have steadily increased since 2001, reaching almost USD 50 billion in 2022. Exports to China is dominated by machinery, electrical products, and chemicals. Agricultural products account for 30 percent of India's exports to China. While India and the UAE share strong

³ Middle East and North Africa.

⁴ UN Comtrade 2023, authors' calculations.

Figure 1
With China as a Backbone of Indian Trade, India Is Expanding Its Exports of Machinery and Chemical Products to Western Markets



ties, since 2009 both China and the UAE have gradually reduced their imports from India.

Trade with the EU has evolved significantly in the past decade. India expanded its machinery and chemical exports, moving away from simpler agricultural produce and textiles. The EU share in Indian exports dropped from 23 percent in 1995 to 14.4 percent in 2012, and has recovered only slowly, standing at 17 percent in 2022. The evolution of Indian-EU trade in the 2000s reflects the global shift of the textiles value chain towards South and South-East Asia. Textile industry supplies (cotton and yarn) represented over 35 percent of exports to the EU (of which over 30 percent went to Germany) in the 1990s, falling to 13 percent in 2022. The recent recovery of exports to the EU are driven by sales in chemicals, machinery, and electronics to the Netherlands, Belgium, France, and Italy.

The EU lost in importance, too, as a supplier to India. Its share in the Indian import basket plummeted from 29 percent in the 1990s to 12 percent in 2022. Belgium, and Germany, once leading EU exporters of precious stones and machinery to the Indian market, respectively, have decreased their exports by more than half in the span of 20 years.

In contrast to manufacturing, export patterns in services have been more stable. India's exports are dominated by ICT and business services, comprising consulting and legal services. Between 2005 and 2021, the share of ICT in global service exports by India grew from 32 to 36 percent. Business services grew by 16 percent over the same period, making up 41 percent of India's total service exports worldwide.⁵ The US is India's most important service destination, accounting for 15 percent of total exports. The UK and China rank second and third, making up approximately 8 percent and 5 percent of India's service exports, respectively. India faces increasing competition

⁵ OECD data, author's calculations.

from China, where the share of ICT service exports rose from 3 percent in 2005 to 19 percent in 2021.

ALL EYES ON MANUFACTURING: PM MODI'S PLAN FOR A DEVELOPED INDIA 2047

Since Prime Minister Narendra Modi took office in 2014, the government has been working to advance India's manufacturing sector. His government pursues a three-pronged strategy: (1) strong government support for the manufacturing sector, (2) a single domestic market, and (3) greater openness to international trade and foreign direct investment (FDI). It is a balancing act of strengthening the domestic economy with subsidy programs while abiding by WTO rules.

Three Pillars

The "Make in India" campaign, launched in 2014, targeted foreign investment and was accompanied by the introduction of the National Intellectual Property Rights (NIPR) policy in 2016 (WTO 2021). The Atmanirbhar Bharat Abhiyaan campaign followed in 2020 and aims to promote self-reliance. At its core is the Production-Linked Investment Scheme, which seeks to improve the global competitiveness of India's manufacturing sector by subsidizing domestically produced goods.

The creation of a single market within India has been crucial, too. Despite being the world's fifth-largest economy, India's complex local levies and inadequate infrastructure have hindered inter-state trade. The introduction of a nationwide goods and services tax (GST) in 2017 and significant improvements in transport infrastructure have paved the way for a robust Indian single market (The Economist 2022).

In spring 2023, India's government announced its latest international trade strategy. Dispensing with the rhythm of 5-year plans, the new strategy is designed to be adaptive and for the long term. It promotes trade through e-commerce and incentivizes districts to identify local export potential. Small and medium-sized enterprises (SMEs) in particular stand to benefit from this initiative. It also includes special provisions for capital goods imports to help advance India's lagging manufacturing sector and upgrade the quality of its products.

Promising Signs

The government's efforts are bearing fruit. According to World Bank data, FDI inflows increased by a remarkable 44 percent between 2014 and 2019, an essential step towards deeper integration into global value chains (Liu et al. 2021). The increasing significance of machinery and chemicals in its exports and imports indicate India's path forward. What's more, between 2014 and 2022 the composition of India's export basket gradually shifted towards products with

greater potential for quality differentiation (Figure 2), signaling a move towards more complex goods. Moreover, unit values, a proxy for quality of differentiable goods, have risen for many products.

INDIA'S TRADE POLICY

Going forward, India has set its sights on establishing its position in the global economy. While India has been a WTO member since 1995, it has ratified few trade agreements since, keeping comparatively high tariff and non-tariff trade barriers. The trade-weighted average tariff on agricultural products stands at 49 percent, while non-agricultural products typically face import tariffs of about 9 percent (WTO). The average tariffs applied lie substantially below the maximum tariffs India pledged to apply to WTO members (113 percent for agriculture, 36 percent for non-agriculture), making its trade policy unpredictable. Still, the country maintains trade relationships with most countries worldwide. India's export share of GDP began growing continuously with the first trade liberalization period in the mid-1980s, peaked in 2013 at 25 percent, and stood at 21 percent in 2022.⁶

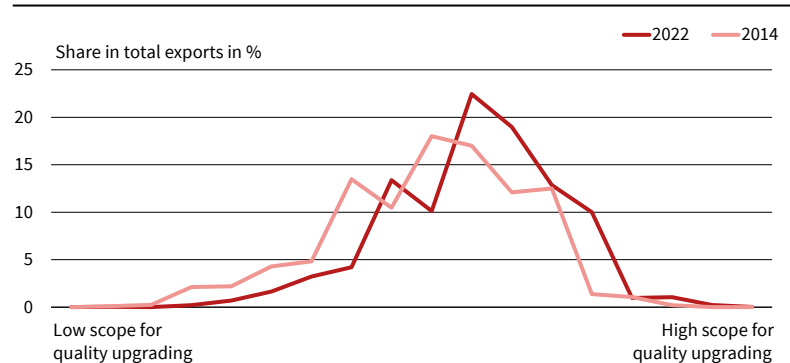
India-EU Trade Negotiations

After a decade of no trade agreements, the Indian government ratified agreements with Mauritius in 2021, and Australia and the UAE in 2022. More negotiations are ongoing. Most importantly, in June 2022 India re-entered negotiations with the EU after the failure of the first round of negotiations between 2007 and 2013. In a move to increase the likelihood of success, what is typically part of a comprehensive agreement was split: the two parties are negotiating three separate deals on trade, investment protection, and geographical indications. Nonetheless, an agreement will not come easy. India, which in 2022 ranked last on the Yale Environmental Performance Index, struggles to meet the ambitious sustainability requirements of the EU Green Deal. The EU laments India's weak labor protection laws, too, and human rights watchdogs criticize India on several counts (Human Rights Watch 2023). India, on the other hand, is concerned about highly subsidized European agricultural products flooding its market and worries that its SMEs in manufacturing may not be ready to compete against European suppliers.

While the two parties are still far apart, pressure is high to conclude the deal successfully. India needs the European suppliers to advance its manufacturing sector, while Europe cannot miss out on the Indian market and professionals in IT and engineering. What's more, if the negotiations fail, the Indian-European geopolitical partnership would lack substance. For India, deeper integration into the world economy

Figure 2

Indian Exports Shift towards Products with Potential for Quality Upgrading



Note: This graph depicts the distribution of Indian export shares across quality ladder lengths.

A quality ladder is assigned to each product and represents the vertical differentiation possibility of a product. A higher ladder indicates that the scope for quality differentiation is high for a given product, while the opposite holds for low ladders. Goods with greater scope for quality differentiation are likely to be more complex, higher value-added products.

Source: Khandelwal (2010); UN Comtrade; authors' calculations.

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is necessary if it is to achieve developed-country status by 2047, PM Modi's wish for the country's 100-year anniversary (Modi 2023).

POLICY CONCLUSION

India's ongoing reform efforts signal a positive trajectory towards higher economic development. While the direction of India's reforms is encouraging, the country needs to prove its reliability as a fair player in the global trade game. Climate change adaptation strategies are urgent to ensure continued global food supply, but also to protect the growing manufacturing sector from adverse weather events. As for the EU, trade negotiations with India will reveal once more the environmental and social cost at which geopolitical alliances are forged.

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