

India's Economic Development & Japan-India Relations

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India in the Global Spotlight

(1) Indian economy maintains growth

India is in the global spotlight. Its nominal GDP in 2022 was \$3.38 trillion, ranking fifth in the world. In country rankings of GDP (PPP), which takes price levels into account, India ranks third in the world. Goldman Sachs predicts that by 2075 India will overtake the United States to become the world's second-largest economy after China. In 2023, it was reported that India's population overtook China's to become the world's most populous nation. With a population of approximately 1.4 billion, India's strength lies in its huge middle class. India's economy, which is largely driven by domestic demand, is not easily affected by global economic slowdowns.

India's foreign exchange reserves exceeded \$600 billion at the end of 2023, ranking fifth in the world in terms of foreign currency holdings. Immigrant remittances from overseas Indians also support the Indian economy. While many Indian migrants in the US are highly skilled human resources such as IT engineers, many of those in Middle East countries such as the UAE and Saudi Arabia are part of the unskilled labor force that supports the oil-producing economy, and they remit most of their earnings to India.

The Indian government's debt is kept at 70% of GDP and fiscal discipline is maintained. In the recently announced provisional budget for FY 2024, the fiscal deficit as a percentage of GDP is 5.1%, down from 5.8% in the FY 2023 forecast. India also has a low external debt, currently at 25% of total debt, including domestic debt, and 19% of GDP.

(2) Promotion of the manufacturing industry

A weakness often identified in the Indian economy is its manufacturing sector. India's manufacturing sector accounts for about 15% of its GDP, considerably lower than that of East Asian countries, and the ratio has hardly changed over the past 20 years. Compared to China, which rode the wave of globalization and achieved high growth by leveraging its manufacturing exports, India, with its weak manufacturing sector, has not fully reaped the benefits of globalization. India's main exports are petroleum products, jewelry, steel, and chemical-related products, while its main imports include crude oil, jewelry, electronic equipment, and general machinery, a product mix that is far from that of developed country-type trade.

India's main export destinations are the US, the UAE, China, and

Bangladesh; its main import destinations are China, the UAE, the US, Saudi Arabia, and Iraq; and its trade deficit with China is particularly large and problematic. Against this backdrop, the administration of Prime Minister Narendra Modi, which took office in 2014, is striving to foster the manufacturing sector under such mottos as "Make in India", "Atmanirvar Bharat" (Self-Reliant India), and "Skill India".

A bright sign in this context is the expansion of smartphone production in India. In an effort to reassess where to invest in China alone, in 2017, Foxconn, Apple's contractor, began manufacturing iPhones in the suburbs of Chennai, and in 2022 production of the latest model, the iPhone 14, began. JP Morgan analysts expect that by 2025, 25% of iPhones, including the latest model, will be manufactured in India. In the manufacturing of Android phones, it is reported that Samsung will move some production facilities from Vietnam, its largest manufacturing base, to India. In addition to smartphones, the Indian government is trying to attract investment through Production-Linked Incentive (PLI) schemes, which support domestic production in key industries such as automobiles, auto components, electronic devices, semiconductors, and pharmaceuticals.

(3) Poverty and inequality

One of the major challenges of India is to eliminate poverty and reduce inequality. In India, the population living below the poverty line of \$1.9 per day reached 170 million as of 2015. Along with economic growth, disparities in assets and income among people are widening, and disparities between regions and between urban and rural areas are also serious.

Most of India's poor reside in rural areas. Agriculture, in which half of the total working population is engaged, accounts for only 16% of GDP, and productivity is extremely low. The Modi administration has been investing in infrastructure such as irrigation and rural roads, which previous governments have not done enough to address.

Eliminating gender inequality is another major challenge for India. Women's participation in politics is also lagging; a bill to reserve one-third of parliamentary seats for women was passed in September 2023, and early implementation is hoped for. The percentage of women in the total working population is 18.3%, not much increase from 10.6% some 30 years ago, and microfinance for women by NGOs such as the Self-Employed Women Workers Association (SEWA) is fostering women's entrepreneurship in India,

a country with a large NGO sector. Along with poverty and inequality, another serious problem is the prevalence of corruption. The Modi administration aims to eliminate corruption through e-governance, and has reduced rampant exploitation of subsidies by allowing all citizens to open bank accounts with the help of “Aadhaar” (unique personal ID numbers) and transfer subsidies directly to them. The government has also been reducing the exploitation of subsidies. Modi is expected to be re-elected in the upcoming general election in April/May, thanks to his efforts not only to improve the investment climate but also to combat corruption.

(4) Serious environmental issues

Environment is also a big issue. In New Delhi, where air pollution is serious, PM2.5 levels are 30 to 60 times higher than the WHO guideline. Water pollution is also a problem in India, with many children dying of diarrhea and hepatitis due to underdeveloped water and sewage systems. Various factories line the banks of the Ganges, the famous “holy river”, spewing sewage and dangerous chemicals into it. Urban settlements are problematic too, with 40% of the total population of Mumbai living in slums in poor conditions.

India, a major emitter of greenhouse gases, generates electricity mainly through coal-fired power generation, which has low energy efficiency. At the COP26 in 2021, Modi announced that India will increase its non-fossil fuel power generation capacity to 500 GW by 2030, aiming to have 50% of energy demand come from renewable energy sources by 2030, reduce projected GHG emissions by 1 billion tons by 2030, cut carbon dioxide emissions from economic activities by 45% by 2030, and reduce carbon dioxide emissions to zero by 2070. If this is achieved, India could slash its carbon dioxide emissions by 33-35% from 2005 levels. Since the prevention of global warming will be difficult to achieve without India’s cooperation, we look forward to seeing this achieved in the future.

(5) Consistent non-alignment diplomacy

India’s foreign policy has consistently been “non-alignment” since its independence in 1947. During the Cold War between the US and the Soviet Union, India remained neutral, not belonging to either camp. Even today, India maintains all-round diplomacy with major powers, and has maintained an attitude of “strategic autonomy”. It has established good relations with most countries, with the exception of Pakistan, with which it has fought three wars, and China, with which it has been facing border disputes.

The longest relationship of trust with post-independence India has been with Russia. Even after Russia’s invasion of Ukraine in February 2023, India did not criticize it. Moreover, India increased its imports of Russian crude oil. Russia has taken a neutral position on Sino-Indian relations, and from this perspective it is unlikely that India will be able to join the US camp.

Compared to Russia, US-India relations were historically slow to develop: the US sided with Pakistan in the Bangladesh Liberation War in 1971; unlike Russia, the US sanctioned India severely after the nuclear tests in 1998. During the administration of President George W. Bush, the US approached India to fight against terrorism, and subsequently the US-India Nuclear Agreement was agreed in 2005, but the good relations did not last long as the administration of President Barack Obama preferred China over India. The administration of President Joe Biden took a critical stance on the Kashmir issue and the Civil Rights Amendment Act; and US forces abruptly withdrew from Afghanistan without reporting to India beforehand.

However, as the power balance in Asia has shifted, the importance of India has increased, and US-India relations have become more strategic in recent years. Military exercises and joint weapons development have progressed; in June 2023, Modi was invited to the US as a state guest and received a bipartisan ovation for his speech to Congress. Obviously, the US steered a course toward tacit approval of India’s stance on the Ukraine issue. US-India relations have entered a new era.

France, which along with the US is a major arms exporter to India, is also strengthening its relationship with India. India has purchased 36 Rafale aircraft from France at a cost of \$9.4 billion. Subsequently, President Emmanuel Macron was invited as a state guest to attend the Republic Day parade in this January.

For India to advance multi-alignment diplomacy, the serious issue is its relationship with China. On June 15, 2020, 20 Indian soldiers were killed in a clash between Indian and Chinese forces in the Galwan Valley in Ladakh, northern India. It was the first time in 45 years that an Indian soldier had been killed in a clash with China. The Indian government took harsh measures, banning many China apps while restricting investment by Chinese companies, on the grounds that China had violated Indian territory. However, restricting trade with China is not so easy for India, which has been dependent on imports of industrial products from China. There are no prospects for future improvement in Sino-Indian relations, and a large number of soldiers from both sides are still stationed near the border. Moreover, India is nervous about China’s moves not only in its enemy Pakistan but also in Sri Lanka, the Maldives, Nepal, and other countries on India’s periphery.

(6) Leader of the Global South

India assumed the G20 presidency in 2023, when the world’s attention increasingly focused on the voice of the Global South nations, in the wake of Russia’s invasion in Ukraine. At the G20 Summit held in New Delhi in September, India was able to adopt a joint declaration amid the confrontation among the various countries over the Ukraine issue. The joint declaration called for coordinated

macroeconomic policies to support the global economy, as the cascading crises were creating difficulties for long-term economic growth.

The joint declaration did not directly condemn Russia, and language from a proposed UN resolution cited in last year's joint statement in Bali was deleted, but Western countries compromised because India could have lost face if the summit failed to issue a joint declaration. The summit also decided, with India's strong support, that the African Union (AU) will become a permanent member of the G20 from next year. In general, India succeeded in representing the views of many Global South nations.

Although the battle between Israel and Hamas in Gaza after the G20 meeting complicated India's position as the leader of Global South, Modi called for solidarity among the countries at the following Voice of Global South Summit held online.

In contrast, China, another major power of the Global South, is using its abundant financial resources to invest in countries one by one. In the future, smaller Global South countries are likely to maneuver between China and India according to their own circumstances and national interests. For example, while approaching China with the Belt and Road Initiative (BRI) with regard to trade and investment, India's approach will be more attractive for them when they want to negotiate with developed nations to seek changes in their prevailing institutions and practices.

India-Japan Relations

(1) Expanding direct investment

Relations between India and Japan are extremely good. India is one of the most pro-Japanese countries in the world, and relations have been deepened over the years through such factors as Buddhist exchanges since the 8th century, the dissenting opinions of Indian Judge Radhabinod Pal at the Tokyo War Crimes Trial, and raw material imports from India in helping Japan recover right after the war.

However, Japan-India diplomatic ties became weaker in the seventies and eighties, as India was getting closer to the former Soviet Union bloc. During the decades, there was not much direct investment by Japanese companies, except for Suzuki, in India.

In 1991, India finally started its economic liberalization, and FDI by Japanese started to come back again. In FY 2008, India became the top recipient of Japanese FDI among all Asian countries including China. After 2011, it saw a temporary decline for several years, but since the Modi administration came to power investment has begun to increase again. As a result, Japan's share of global FDI in India increased from 3% in the 2006-2010 period to 7% in the 2011-2021 period.

According to the Japanese Embassy in India and JETRO, there are

1,400 Japanese companies (and 4,970 offices) and 8,145 Japanese residents in India, as of 2022. Even though the number of Japanese companies in India has temporarily plateaued after the pandemic years, 72.5% of them said in a JETRO survey in FY 2022 that they will expand their business in the next one to two years, and this figure for India continues to be the highest in the world.

(2) Factors common to successful companies

The biggest success story of a Japanese company in India is Suzuki, which controls 40% of the Indian passenger car market. Early entry into the market was a wise decision by then President Osamu Suzuki. In January 2024, it was reported that Suzuki plans to invest more than 600 billion yen to build new plants in India in the future. Compared to the current production volume of approximately 1.9 million vehicles in India, Suzuki plans to have an annual production capacity of 4 million vehicles, including EVs, by 2030. In addition to Suzuki, there are some other successful examples of Japanese companies such as Honda, Daikin, Kansai Paint, and Unicharm.

On the other hand, quite a few Japanese companies in India have seen their earnings deteriorate due to factors such as intensifying competition. There is also a lack of success stories from small and medium enterprises. In the past, when business did not go well in India, it was often dismissed as being due to the investment environment in India, or put on hold "until India becomes a little more affluent". Recently, however, there have been calls to learn from successful Korean companies such as Samsung, LG, and Hyundai Motor.

One of the common factors in the success of these Korean companies is that they made large investments at the initial stage; LG and Hyundai Motor saw India as a strategic base at the time of their entry and made large investments. Korean companies sent their executive officer class from the beginning and made quick decisions. Among Japanese companies, Nippon Steel Corporation has recently teamed up with ArcelorMittal and is planning to make a very large investment in the construction of a steel mill in India, and there are high expectations for it.

Second, it is important to build good relationships with partners. Japanese companies often enter India through joint ventures. When Suzuki's joint venture partner, Maruti, was established, it sent an outstanding Indian government official to manage the company. Then, when a disagreement subsequently arose with Maruti over the appointment of his successor, Suzuki persuaded the Indian side without compromise.

Contrary to this, Daiichi Sankyo, which acquired local pharmaceutical giant Ranbaxy in 2008, was deceived by the owner family, and posted a huge loss. It is essential to conduct adequate due diligence and market research on partners using local networks.

Indian companies often lack transparency in corporate governance because the majority of shares are held by the founding family.

Third, I would like to emphasize the importance of localization. In the majority of companies not only in the US but also in Europe and South Korea, the top managers of local subsidiaries are excellent Indians who are entrusted with authority. A typical example is Hindustan Unilever (HUL), an affiliate of Britain's Unilever, which has developed locally integrated businesses on a large scale, but such examples are rare among Japanese companies.

Fourth, India's position in global business should also be clarified. Through active use of the Japan-India EPA and other free trade agreements, India should be integrated into the global strategy. Globalization is also necessary in human resource policies. US companies are conducting global human resource management by hiring talented people in India as candidates for executive positions at their headquarters and also dispatching Indians to Africa and the Middle East as well.

Fifth, personnel evaluation of Japanese expatriates must also be conducted with a long-term perspective. Even successful companies like Suzuki and Honda had considerable difficulties in India for the first decade of their entry. It takes time to succeed in business in India. Because the expatriation period is only three years, which is too short, many expatriates of Japanese companies do not take risks and spend their time there in a haphazard manner.

In Japanese companies, top management gives orders but does not touch the business itself, so the phrase "Okay, why don't *you* come and do it in Japanese?" is often heard among Japanese expatriates in India. Even if they have gained a thorough knowledge of the local situation after being stationed in India, they are often assigned to work outside of India after returning to Japan, and thus have not accumulated knowledge of India at the organizational level. Recently, an increasing number of young Japanese are going to India in search of a new home, but they are often not authorized to do so because they are locally hired.

(3) Stagnant trade and lack of people-to-people exchange

Compared to direct investment, Japan-India trade has been stagnant. More than a decade after the Japan-India Economic Partnership Agreement (EPA) entered into force in 2011, exports from Japan to India have increased, but exports from India to Japan have not increased in any way. Japan's share of India's total world exports and imports has remained between 1.5%-2.2% and 2.4%-2.8%, respectively, throughout the past decade, while India's share of total world exports and imports from Japan has remained between 1.2%-1.4% and 0.75%-0.82%. The commodity composition of India's exports to Japan, other than diamonds, is dominated by primary commodities such as shrimp and iron ore, which is a result of the weakness of the manufacturing sector.

India's service exports, which are its strength, have also not grown in Japan. Looking at Japan's share of India's IT exports, it has declined from about 4% to less than 2% over the past 30 years. In addition to language problems and a different work culture for software development, Indian IT companies do not have their own hardware divisions, which makes them difficult to work with Japanese manufacturing companies. Even in the field of back-office operations relocation, such as call centers, which is India's forte, there are few success stories due to language barriers.

People-to-people exchange is also not progressing. According to Japan's Ministry of Foreign Affairs, human exchanges between Japan and India are only one-20th to one-70th of that between Japan and China in various aspects, including the number of visitors, foreign students, Japanese language learners, and exchanges between local governments. The worst difference is in the number of foreign students. As of May 1, 2021, the number of foreign students from India in Japan was only 1,457, or 0.6% of the total in Japan, and India is 14th in terms of country ranking. This number is not only incomparable to China (114,255) and Vietnam (49,469), but also below Nepal, Sri Lanka, and Bangladesh. This is in stark contrast to the 180,000 Indian students around the entire world each year and the number of Indian students in the US, which has overtaken China for the top spot.

The exception to this dearth of human resource exchanges is the increase in the number of Indians living in Japan: from around 8,000 in 2007, the number of Indians in Japan has now exceeded 40,000. Many are software engineers and their families. About 10% of them live in Nishi-Kasai in Tokyo, known as "Little India", and even a few Indian schools have been established in the area. Japanese people are seeing more and more Indians.

In line with this trend, Japanese interest in Indian culture has also been growing. The number of visitors to "Namaste India", a cultural event held annually in Yoyogi Park, has been increasing each year, with a total of approximately 200,000 people attending the two-day event. Yoga, which originated in India, has also become popular, especially among young women. Also, several Indian movies have become hits in Japan. The number of Indian restaurants in Japan has exceeded 5,000, even though the actual workers are mainly Nepalese. Indian food has taken root in Japan.

(4) Top recipient of yen loan

Along with direct investment by private companies, Official Development Assistance (ODA) is a pillar of Japan-India economic relations. India, the first recipient of Japanese yen loans in February 1958, has received a cumulative total of 6,978.3 billion yen in yen loans from Japan through November 2022, more than any other country.

The majority of Japan's ODA to India is in the form of yen loans,

with few grant aid or technical cooperation projects. In the past, Japanese ODA to India was mostly in the areas of power, water supply, sewerage, and forestation. In recent years, however, there have been many projects in the transportation sector, including the Delhi Metro, the Dedicated Freight Corridor between Delhi and Mumbai, and the Mumbai-Ahmedabad High Speed Rail Corridor. The Delhi Metro is known as one of the most successful Japanese ODA projects in the world. The renowned engineer Ellatuvalapil Sreedharan, the managing director of the Delhi Metro Rail Corporation (DMRC), who was most instrumental in the success of the Delhi Metro, learned from the Japanese and instilled in India the concept of punctuality and meeting construction deadlines.

The next mega project was the construction of the Delhi-Mumbai Freight Corridor (DFC), which connects India's two largest cities by dedicated freight rail. Since many Japanese companies in India have their factories concentrated in inland metropolitan areas such as Gurgaon and Noida, the economic benefit of improving transportation infrastructure is significant for them.

The current flagship project is a bullet-train project connecting Mumbai and Ahmedabad, two major cities 508 kilometers apart. The journey between them currently take eight hours by regular train but the connection will be two hours once the bullet train, with a maximum speed of 320 km per hour, begins. The expropriation of the land needed for construction had been delayed, but is now moving forward again with the change of the Maharashtra state government in June 2022. Indian media have reported that the bullet train will start operating around 2030. In moving forward with this project, Japan is also training Indian nationals in safe operations management, which is expected to improve the safety of overall railroad operations in India.

(5) Strategic Japan-India relations

With the changing political landscape in Asia, the Japan-India relationship is becoming more strategic. During late Prime Minister Shinzo Abe's visit to India in 2007, the previous "Japan-India Global Partnership" was upgraded to the "Japan-India Strategic Global Partnership", which was further upgraded to the "Japan-India Special Strategic Global Partnership" later in 2014. Abe delivered a speech titled "The Intersection of Two Seas" to the Indian parliament, and the term "Indo-Pacific" has since become a global term, including its use by the US government.

The leaders of Japan and India take it in turns to visit the other country each year. Among Japanese prime ministers, Abe made a particularly significant contribution. He and Modi held a total of 15 summit meetings, and their personal relationship became the cornerstone of today's India-Japan relations. It was also thanks to Abe that the civil nuclear agreement between Japan and India, a nuclear power but not a signatory to the Nuclear Non-Proliferation

Treaty (NPT), was able to enter into force in July 2017. The bullet train project would also have been difficult to realize without Abe, whose assassination on July 8, 2022, sent shockwaves through India.

Fortunately, Abe's legacy has been carried on by his successors, Yoshihide Suga and Fumio Kishida. The Quad framework of Australia, India, Japan, and the US, advocated by Abe, has also taken root, providing a forum for the four countries, which share common values such as democracy and the rule of law, to confirm their cooperation in the Indo-Pacific region. The first Quad summit was held online in March 2021, following a joint military exercise by the four nations in Visakhapatnam, India, in November 2020.

Regular bilateral foreign and defense talks between Japan and India (2 plus 2) have also been held regularly: in 2020, the Mutual Agreement on the Cross Servicing of Goods and Services (ACSA) was signed, under which Japan's Self-Defense Forces and Indian military forces exchange food and fuel, and in May 2022, an India-Japan summit meeting was held in Tokyo, along with the Quad Summit. The invasion of Ukraine by Russia in February 2022 caused some differences of opinion between Japan and India regarding Russia, but as mentioned earlier, this did not become a major issue, partly because the US has stopped criticizing India on the Ukraine issue since Modi's visit to Washington in June 2023.

Conclusion

As the world's fifth-largest economy, India is now in the spotlight, and its relationship with Japan is only deepening. As China's slowdown in economic growth becomes more apparent, Japanese businesspeople are more interested in India than ever before.

Sharing common values, Japan and India seem to have overcome the hurdle of their disagreement over the Ukraine issue in 2022 and the misfortune of the assassination of Abe. There is no doubt that the relationship between India, a major power of the Global South, and Japan will further deepen both politically and economically. **JS**

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