

Interview with Prof. Sachin Chaturvedi, Director-General at RIS, India

Trade Liberalization: a Key Industrial Policy Encouraging Competitiveness in South Asia

By Japan SPOTLIGHT

In talking about the path to economic development and growth, trade and investment liberalization is today considered a key industrial policy that helps create a pro-competition business environment. Many South Asian nations have now reached middle-income status, an economic development stage where competition and free trade can help ensure the best resource allocations and thus the highest economic efficiency and growth. Industrial policy used to be considered a champion of protectionism but it is not the case anymore.

Prof. Sachin Chaturvedi, director-general at RIS, the Research and Information System for Developing Countries, a Delhi-based autonomous think tank and one of the T20 global think tanks working for the G20, talks about the policy implications of trade liberalization for South Asia in the following interview.

(Interviewed on July 15, 2023)

New Implications of Industrial Policy

JS: We'd like to ask you for your views on trade liberalization as a means of industrial policy to promote economic growth. All countries are now very keen on promoting industrial policy, even the United States, though it used to claim that industrial policy is another form of protectionism. So first of all, what is your view of the growing popularity of industrial policy all over the world?

Chaturvedi: Thank you for inviting me and giving me this opportunity. You're absolutely right. The US has given a major lift to the idea of industrial policy, and it has now even adopted instruments and modalities to advance the cause of industrial policy. The Inflation Reduction Act and the CHIPS and Science Act are both actually advancing the purposes of industrial policy. The US has now adopted something that it had opposed. All the modalities are there for the promotion of industries in some way, and even protecting them and going two steps further from the "buy America" approach, so that the chain is now being protected from "buy to produce" and from "produce to market".

I think it is also important here to realize that the new industrial policy that we are seeing is different in some respects from the previous incarnation of industrial policy, where we found more general protectionism. Here, we find in the new sort of modalities



Prof. Sachin Chaturvedi

more sector- and product-specific protection, or local production measures. What is important here is that this industrial policy is now getting more and more linked with the supply chain challenges that we are facing; the new industrial policy is actually being prompted by supply chain disruptions.

There are some countries in the world that are willing to continue with their dominance in the supply of rare earths and critical metals and minerals, even damaging the production structures of other countries. So, from that perspective, it is important that we adopt instruments which are actually safeguarding continuous supply for consumers, for industrial firms, and also for national markets.

JS: I think today's new industrial policy is less a sector policy, as it does not have much focus on raising specific sectors, but seeks to create a good business environment for all sectors. For example, the digital economy is a very important target for industrial policy, particularly in Asia, and in India as well, perhaps. But this is not specifically targeting some high-tech sectors, but the overall digital economy, which is more of a general concept than a sectoral concept.

Chaturvedi: Absolutely. We have to realize what is a sector and what is a product, and what is a generic policy framework. When industrial

policy was made in the 1970s and 1980s, the idea was to protect the economy as a whole, and block all others from exporting to respective countries so that domestic firms could expand. Now when you say digital economy or other sectors related to digital economy, you are realizing not products but a subset of the larger economy. The CHIPS and Science Act or even the Inflation Reduction Act of the US are not protecting the whole economy of the US; they are protecting some specific areas where these applications may come in. For instance, with the Inflation Reduction Act, there are now growing efforts to have it also cover pharmaceuticals or other products. Those efforts are being made, but at this point it covers largely digital products, the products that are important for semiconductors or even other sorts of digital products that are needed for value chain continuation and its protection. So you are absolutely right, it covers not the generic but some subset of the larger economic trends.

Areas Highlighting Role of Industrial Policy

JS: In this regard, what areas of industrial policy would be key to encouraging economic growth in South Asia, in particular in India or any part of India? We talked about the digital economy, but what else? Some people say small and medium-sized enterprises, or energy and the environment.

Chaturvedi: I would very much like to say that efforts are needed for countries like India to constrain what is coming out in terms of cost of production. How do we keep the cost of production low? And from that perspective the restrictions, the challenges that are there on energy supply, they are extremely important. The availability of resources, and particularly the input cost of energy, is something that I think is important. With the new initiative that has been launched in India, the green hydrogen transition program, I think it is absolutely important for us to bring in – it is something like 13,000 crores (\$1.56 trillion) – to the green hydrogen transition program. From that point of view, it is important that India brings down the cost of production to the extent manageable. That would be important for SMEs and small and micro enterprises going forward.

This is from the perspective of industrial competitiveness, but also within South Asia. At this point, my colleagues are working in terms of how value chains in the agriculture sector are possible across India, Thailand, India, Myanmar, and Bangladesh, including Bhutan and Nepal. I think that would be extremely important.

JS: India is well known for its excellent digital economy and digital technologies. Are Indian SMEs enjoying the benefits of digital technologies?

Chaturvedi: Yes, a large number of firms are now using digital platforms for payment architecture. They have also been insulated after the Covid crisis from the credit challenges that they had. And RIS, my institution, has just taken a survey of all the MSME firms in India – we are trying to survey around 7,000 firms in India to find out their ability to leverage electronic payment platforms going forward.

This is also going to be supplemented by the national logistics policy that India has introduced to reduce transaction costs. We have also enabled our domestically developed electronic digital payment transfer systems through the central bank, the Reserve Bank of India, and this has helped in terms of reducing the cost of transactions for MSMEs.

Trade Liberalization as an Important Industrial Policy

JS: I see, thank you. Our main subject today is trade liberalization. Trade liberalization and competition policy could be seen as important industrial policies, enhancing the competitiveness and vitality of industries. What do you think about this overall?

Chaturvedi: This is extremely important. We need to take measures that are important for strengthening competition policy and also allow space for trade liberalization. Of late, we see that some of the tariffs in India have gone up and as the government has announced, efforts will be made to reduce tariffs and enhance all the measures that are needed to support and further facilitate the rise of MSMEs' competitiveness.

I think this would be important in terms of, as I said earlier, reducing the cost of imports, and reducing the cost of accessing credit. If both are managed well, the firms will be competitive and that would give confidence in terms of reducing tariffs. That would also be important for competitiveness to come in. And in terms of mindsets, I think more partnerships, more opening up would be important.

JS: The Indo-Pacific area is now attracting growing attention as a center of geopolitics and also as a center of the economy in terms of growth. This

means industrial policy is becoming more international. I would think the benefits of exchanging views on each country's industrial policy might be enormous today. In that sense, should the Indo-Pacific area focus on industrial policy issues as well – not only geopolitics, security, and social policy, human rights or whatever? Industrial policy might also be a good subject for us to discuss and exchange views and learn from each other.

Chaturvedi: This is a very good idea, and I think it's high time that the Indo-Pacific region comes out of the security and defense-related issues and widens the landscape to address economic and investment-related issues. It should also strengthen the dimensions that are important from the point of view of our engagement with participation and with the private sector coming to the table. Policymakers would have to introduce measures that are bringing in firms and entities, and agencies that are responsible for competition policy in our respective countries. Competition policymakers, competition policy regulators would have to come together in the Indo-Pacific region, and also in the Quad where we are also trying to bring greater coherence to our investment strategies. I think that would be extremely important. For the Indo-Pacific, I think that would help us ensure a larger take on what economic partnerships look like and they would be a future source of security and strength, and we should not lose too much time in discussing only security and defense-related issues.

Including Industrial Policy Issues in IPEF

JS: The Indo-Pacific Economic Framework for Prosperity (IPEF) initiative launched by the US confirmed security and also some other social policy aspects, but unfortunately it doesn't include market access, and some people would say that's why many countries do not have the incentive to promote the initiative. If it were to include issues like industrial policies, as you said, or perhaps regulatory reforms or whatever, do you think that would perhaps make this initiative more attractive to many countries?

Chaturvedi: I think with the launch of the IPEF by the US, we are seeing a sort of a four-pillar approach that the US has defined. And if we leave the first pillar of trade aside, the other three pillars are

largely strengthening the trade facilitation measures that are needed, they're more trade supporting, trade facilitating. Here, the issue is not so much about market access, but more about the convergence of our investment measures, the convergence of our trade facilitating measures and more so, I would say, in terms of how we bring in the major dimensions that are important from the point of view of industrial policy. In my view, a pillar should be added to the IPEF that strengthens the industrial policy production structures because that's where the value chains would come in, and that's where major challenges posed to global production architecture by China come in. And I think it important for us to take measures where access and equity for everyone is ensured, and we bring in that there is space for all to have quality products and quality infrastructure to deliver those products. I think this is important from the perspective of efficiency standards that are needed. The CPTPP and IPEF would have to see that they are actually contributing to an expansion of the market, that they are contributing in terms of expansion of trade, and they should not just end up with more bureaucratic organizations that are just talking shop.

Balance Between Economic Efficiency & Security

JS: In the IPEF, as well as in many other international forums, people are talking about economic security as an important policy target today. However, trade policy practitioners are concerned about this concept growing too much because so-called disguised protectionism could emerge in the name of economic security. In particular, WTO supporters and FTA supporters are now thinking about how to balance security and economic efficiency. How can we balance those two important policy goals?

Chaturvedi: Absolutely right. I think we need to bring in a balance between efficiencies and values that we have in our discussion. At the same time, we also need to ensure that we encourage competition and cooperation, and they are not counterproductive to each other. President Joe Biden in 2021 promoted the idea of having 140 countries come together for a global accord on a 15% global minimum tax on entities, and this could only become possible because we have faith in coming together. This also has the element of cooperation. Cooperation is a strength, but if, as you rightly said, we only bother about competition with others, then it is going to be a

challenge. In March 2023, for instance, the US and the EU announced an FTA for critical minerals when European Commission President Ursula von der Leyen visited the US, at that point for electric vehicles.

The US-EU agreement on coordinating chip subsidies, coordinating the FTA for critical elements, in a way is viewed by some people as cartelization and the continuation of that. This is something that we should avoid in favor of healthy competition, and we should encourage efficiency and a value system for trade that is free, open, and inclusive. I also think it is important for us to bring up the fact that the Inflation Reduction Act does not include pharmaceuticals. Now, many new sectors are coming up where they want support. We can understand this if the US keeps it open for friendly countries, but if it is only US companies who can get these subsidies, this is de facto encouraging protectionism, and we should stay away from this for the healthy growth of trade, investment, and cooperation.

JS: I think the excessive use of the concept of economic security is reflected in what we call coercive policy, meaning weaponizing the interdependency between economies, and some countries try to coerce partners to do what they want them to do. That is perhaps another type of protectionism, and if we leave those coercive policies as they are, the global supply chain could be disrupted. What should be done to save the global supply chain from these coercive trade policies? Recently, there was an article by our friend Shiro Armstrong in the *Nikkei* newspaper saying that perhaps in order to avoid the negative impact of such coercive policies, we should encourage rules-based international trade, such as the WTO, FTAs, CPTTT, RECP or whatever. Do you agree?

Chaturvedi: These are very encouraging remarks, certainly, but the trouble is that not all countries believe in a rules-based trade order. In the FTAs, the closed-door partnerships were visible, they were excluding countries. Now the disruption of the supply chain by China is another disbelief in a rules-based order. If countries that are leading powers in trade – and we have seen this on the part of US, we have seen it on the part of China – if they undermine the rules-based order, then where would other countries go? Everyone believes in going toward FTAs or the WTO or rules-based order, and

we are going in that direction, provided all countries follow this all the time, and not just according to their convenience. We need to create that position, and I think that will be important.

JS: One more question. We've been talking about industrial policy. In the future, what industrial policy issues is South Asia facing, what do you think will be more important than anything else? We talked about the digital economy, SMEs, and energy and the environment, and some have talked about aging. In India, aging may not be a big issue, but what else will be the important issues for industrial policy?

Chaturvedi: I think one very important thing that South Asia requires, and South Asia would need, is to follow what Japan did several years ago in establishing the institutions that are needed for financing industrial enterprises. I think that is something where several South Asian countries still have a long way to go. Japan established the Japan Development Bank and the Industrial Bank of Japan. These have provided the necessary support and engagement with several actors that are important, and both have contributed immensely in terms of how industrialization is supported and the economy pumps up its base.

Over the years, we find that South Korea also developed the same structure, but we do not see similar entities coming in India. India has very recently floated one development finance institution (DFI) and that DFI is now supporting industrial infrastructure, but it also has to support industrial and infrastructure requirements through the kind of institutional framework that is needed. So, I think for promoting industrial policy, one big thing that is needed is the necessary institutional financing, and through that the systemic evolution of the industrial development bank experiment which is seen in many other countries, where the funding base including debt and equity issuance resources and other financial institution and government transfers all have come together. I think this is probably the most important requirement. **JS**

Written with the cooperation of David S. Spengler, who is a translator and consultant specializing in corporate communications.