8. India's Shifting Trade Policy: South Asia and Beyond

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8.1 Introduction

Since 1991, India's economy has undergone a remarkable transformation. Moving away from years of inward-looking economic policies, it has become a significant force in the global political economy. This chapter focuses on the evolution of India's new economic policies, particularly in trade, within the context of the larger transformation of Asia's economic and security architecture after the Cold War.

We utilize the institutional bargaining game framework introduced in Chapter One of this book to analyze the interplay of external shocks and internal political changes and explain shifts in India's trade policies. In particular, the three shocks of the fall of the Soviet Union, the Asian financial crisis of 1997-98, and the terrorist attacks of September 11, 2001 prove to be significant drivers of India's policies.[2] However, we also find that India's balance of payments crisis of 1991 and the decision of both India and Pakistan to test nuclear weapons in 1998 were also critical factors. Moreover, as the framework suggests, one needs to look at the interplay between shocks and key domestic political changes in India to explain policy changes. Specifically, we show how India moved away from its import substitution industrialization (ISI) policy to a more liberal

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[2] See the introduction to this volume by Aggarwal and Koo for a discussion of the analytical framework of this chapter.

domestic economic model and an increasing focus on improving its export competitiveness. In addition, we analyze India's recent turn toward bilateral trade agreements in the context of frustration with lack of progress in the Doha Round of the World Trade Organization (WTO)—a policy strategy common to Asian countries more broadly.

This chapter is organized as follows. Section 8.2 examines the context of the key shocks and dynamics that have influenced policymakers' choices in South Asia as well as in the broader Asian region. Section 8.3 then considers the historical evolution of India's policies in the aftermath of the three broad shocks, focusing on how each altered the dynamics of India's economic policies. Section 8.4 provides some possible scenarios for India's future trade policy based on our anticipation of possible new developments and India's likely responses. Finally, in Section 8.5 we offer some concluding thoughts.

8.2 The Cold War Security and Economic Environment

In the Cold War era, the so-called "San Francisco System," codified largely through the 1951 San Francisco Peace Treaty between the U.S. and Japan, provided Asian states with a mixture of bilateral and multilateral institutions.[3] It offered many Asian states, particularly Japan, access to the American market in return for a bilateral security alliance with the U.S. It also encouraged the United States' Asian allies to participate in broad-based, multilateral forums such as the United Nations (UN), the General Agreement on Tariffs and Trade (GATT) and the International Monetary Fund (IMF).

Although the San Francisco system was particularly important in East Asia, it is critical to keep in mind that it did not include all of Asia. Some states, such as China, allied with the Soviet Union while other smaller powers were either formally or informally tied to those two countries. For its part, India resisted this Cold War alignment of states and attempted to pursue a non-aligned security strategy (with an increasing tilt to the Soviet Union after 1971) and an inward-looking policy of ISI.[4] In India's case, as we shall see below, the fall of the Soviet Union, combined with its 1991 balance of payments crisis, came as a combined shock that threw its traditional economic policy into question.

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[3] This discussion of the San Francisco System draws on Aggarwal and Koo's introduction.

[4] A combination of high tariffs, an overvalued exchange rate, and import, financial and industrial controls characterized India's strategy of import substituting industrialization. This strategy biased economic activity toward production for the home market rather than for exports.

In terms of regional agreements in South Asia, the Cold War context also affected efforts to create minilateral agreements (involving more than two countries but not universal membership). The South Asian Association for Regional Cooperation (SAARC) was such an example. This accord was born out of the efforts of the smaller countries of South Asia such as Bangladesh, Nepal and Sri Lanka, which may have preferred a geographically concentrated minilateral regional framework to a region dominated by India's bilateral relations with its neighbors. Discussions in various international gatherings from 1977 led to the first foreign secretary-level meeting in 1981 and the first meeting of the heads of state in 1985. SAARC had the unenviable distinction of overseeing a reduction in intra-South Asian trade. Intra-regional trade as a proportion of total trade within the region dropped from 3.2 percent in 1980 to 2.4 percent in 1990.[5]

Indo-Pakistani security relations are central to understanding SAARC's inefficacy during and after the Cold War. Rival elite beliefs about national identity locked South Asia's two largest countries in a deadly conflict since the partition of India in 1947. Pakistan was created as a separate state at the time of India's independence, thus securing the interests of the Indian Muslims. India, on the other hand, had held that it would be a secular nation where people of all religions could leave peaceably.[6]

The geopolitics of the Cold War further complicated Indo-Pakistani relations. Given the U.S. support for Pakistan and its close ties with China during the Cold War, India could not have won the 1971 war without Soviet support. India signed a Treaty of Friendship and Cooperation with the Soviet Union that brought the security concerns of both countries very close to each other. This was a significant blow to India's stature as a non-aligned country. On the other hand, Pakistan, which had maintained close ties with the U.S. during the Cold War, became a frontline state after 1980 and benefited enormously from U.S. aid in return for supporting the United States against the Soviets in Afghanistan.[7]

The Cold War also deeply affected India's efforts to link up with the Association of Southeast Asian Nations (ASEAN) countries. In Indonesia, Suharto replaced Sukarno after a bloody regime change in Indonesia and pledged allegiance with the U.S in 1966. When ASEAN was established in 1967, it comprised a distinctly pro-American grouping that included

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[5] Dash (1996:202)

[6] Ganguly (1986)

[7] Jimmy Carter was trying to discipline Pakistan toward more democratic governance when the Soviet Union invaded Afghanistan. President Carter had to change his position on Pakistan and President Ronald Reagan had to offer substantial military and financial aid in return for Pakistan's support for the United States' fight with the Soviet-backed regime in Afghanistan.

Indonesia, Thailand, the Philippines and Singapore. They consolidated themselves against communism by proposing the Zone of Peace Freedom and Neutrality (1971) and the Treaty of Amity and Cooperation (1976).

The strategic rift between India and Southeast Asia hardened in the 1980s when Indira Gandhi recognized the Vietnam-backed Heng Samrin regime in Cambodia, which had friendly ties to the Soviet Union. Moreover, India did not support Indonesia's candidature for the Chairmanship of the Non-Aligned Movement at the New Delhi summit in 1983. When Rajiv Gandhi became Prime Minister, though, ASEAN countries grew optimistic about India's willingness to convince Vietnam to withdraw from Cambodia given his pro-liberal economic policy bent and his open mind about the U.S. Vietnam, on the other hand, would not tolerate the Chinese-sponsored Khmer Rouge, which the ASEAN countries preferred to Soviet domination. India's tilt toward Vietnam and Soviet Union was most easily visible during the visits of the Indian and Soviet Foreign Ministers to Vietnam, thus disappointing ASEAN members.

Southeast Asia worried about the rise of India's power both within and beyond South Asia during the Cold War. Most worrisome for ASEAN countries was the birth of India's blue water navy that was building the capacity to secure its interests in Southeast Asia. India had acquired a Soviet-built nuclear-powered submarine and an aircraft carrier. Indonesia accused India of letting the Soviets use its naval bases while Singapore's Prime Minister Goh Chok Tong worried about the U.S.'s withdrawal from its bases in the Philippines in light of India's rising naval power.[8]

India's trade with the ASEAN countries was also affected by the Cold War as well as its own ISI policies, which made India commercially less attractive over time. India could not attain the status of an ASEAN dialogue partner during the Cold War—a status that would have facilitated commercial relations between India and ASEAN and which had already been accorded to the European Economic Community, Australia, New Zealand, Japan, United States and Canada in the 1970s. Any possibility of India becoming a dialogue partner was ruled out after its support for the Heng Samrin regime in Cambodia in 1980. Bilateral meetings between Indian and Malaysian officials spent a disproportionate amount of time on the Cambodian issue. Mahathir bin Mohamad, one of the proponents of South–South solidarity, stated unambiguously that India's position on the issue had adversely affected its relations with Malaysia.

India's declining competitiveness due to its ISI policy also hurt its interests in Southeast Asia. ASEAN countries accessed capital and technology from advanced industrial countries, most notably Japan. However, India's restrictive investment laws ensured that there would be little room for ASEAN investments in India. Intra-industry trade in the

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8 On the relations between India and ASEAN during this period, see Sridharan (1995) and Sridharan (1996), Chapter 7.

presence of less restrictive investment laws could have been a trade-promoting factor in Indo-ASEAN trade. As ASEAN globalized faster than India, India became more dependent on trade with ASEAN than vice-versa. India's imports from ASEAN, which were 0.86 percent of its total imports in 1975, rose to 6.2 percent in 1990. Its exports to ASEAN countries, which were 2.6 percent of its global exports in 1975, were about 4.2 percent of its exports in 1990. On the other hand, India's trade with Singapore as a proportion of Singapore's trade with the rest of Asia came down from 15.49 percent to 12.03 percent between 1980 and 1990. Singapore was consistently the most important trading partner for India in the ASEAN region during this period.[9] Nevertheless, India's trade with ASEAN countries was more robust than its trade with South Asian countries.

Before we analyze the transformation of India's trade policies from the pre-Cold War era until the present, it is useful to systematically categorize India's accords based on their strength, the number of actors involved, and the geographical characteristics of the accords, as we show in Table 8.1. Table 8.2 provides a more dynamic analysis by considering how arrangements have changed in terms of their membership, scope, and strength.

As Tables 8.1 and 8.2 clearly illustrate, India's trade policy has shifted away from a regional focus on SAARC and a multilateral focus on the WTO. India is now involved in a large array of accords and is actively negotiating minilateral and bilateral accords. In particular, India's turn to the

[9] On the politics of Indo-ASEAN economic relations from the late 1970s up to the early 1990s, see Sridharan (1996), Chapter 8; Asher and Rajan (1995:176).

Table 8.1: India's trade arrangements

Strength	*Number of Actors*					
	Unilateral	Bilateral		Minilateral		Multilateral
		Geographically concentrated	*Geographically dispersed*	*Geographically concentrated*	*Geographically dispersed*	
Strong	(1) Policy of ISI Shift toward a more export oriented strategy (1991)	(2) India-Sri Lanka (2000) India-Mauritius negotiations	(3) India-Thailand (2003) India-Singapore CECA (2005) India-Japan (study group) India-EU (study group)	(4) SAARC (1985) SAFTA (2004) BIMST-EC (1997)	(5) India-GCC negotiations	(6) GATT/ WTO (1947)
Weak					ASEAN+6 ASEAN-India Framework Agreement (2002) India-New Zealand (under study)	

Table 8.2: Evolution of India's trade arrangements

Org. name	# of members at establishment	# of members now	Issue scope at establish-ment	Issue scope now	Strength at establishment	Strength now
ASEAN+6	16	16	Narrow	Narrow	Weak	Weak
ASEAN-India Framework Agreement	11	11	Broad	Broad	Weak	Weak
SAARC / SAFTA	7	7	Broad	Broad	Weak	Weak
BISTEC / BIMSTEC	4	7	Broad	Broad	Weak/under negotiation	Weak/under negotiation
India-Sri Lanka	2	2	Broad	Broad	Strong	Strong
India-Thailand	2	2	Narrow	Narrow	Strong	Strong
India-Singapore	2	2	Broad	Broad	Strong	Strong

negotiation of bilateral agreements has accelerated in the wake of the July 2006 breakdown in WTO negotiations. Examining how this evolution of policy has taken place from the pre-Cold War era to the current one is the task to which we now turn.

8.3 The Evolution of India's External Economic Policies in the Post-Cold War Era

The turn of the decade from the 1980s to the 1990s proved to be a decisive combination of shocks for India's traditional economic and security policies. In 1991, the brewing balance of payments crisis came to a head. That same year, the collapse of the Soviet Union and the end of the Cold War rendered India's "non-aligned" policy obsolete. India's response to this twofold crisis was a dramatic move toward domestic liberalization and the beginning of its "Look East Policy" (LEP). But just as the LEP appeared to be bearing fruit, the Asian financial crisis of 1997-98, together with India's decision to test nuclear weapons and Pakistan's own subsequent tests sharply set back relations with ASEAN and other East Asian countries. In this dramatically changed environment, India turned to its neighbor, Sri Lanka, to pursue trade liberalization. The next shocks of the 9/11 attacks and then the United States' turn to bilateral trade agreements dramatically altered both the security and economic contexts for India. Its relations improved with the U.S. relatively quickly, but it was also forced to imitate other states in their pursuit of bilateral agreements—given the paralysis of the Doha Round of the WTO.

To analyze the changes in India's economic policies, particularly in trade, we use the institutional bargaining game approach discussed in Chapter One of this book. In brief, the approach focuses on identifying key shocks that potentially alter the existing equilibrium. These shocks can change the nature of goods that are being sought by states and their reaction will be a function of their individual situations. These individual situations are defined by the position of the state in the international system, its domestic political configuration, and elite beliefs. State responses in creating or modifying existing institutions will be influenced by the pre-existing broader institutional context (for example, regional agreements will be constrained by the WTO). Finally, we consider the specifics of the new arrangements in terms of their strength, nature, scope, number of actors, and geography. These arrangements can, in turn, be affected by new shocks over time, setting in motion a new bargaining game.

8.3.1 Liberalizing and Looking East

India had long followed a classic ISI policy that had been advocated by a wide variety of economists including its lead exponent, Raul Prebisch. The so-called “License Raj” was marked by a maze of import controls, an overvalued exchange rate to facilitate the importation of necessary capital goods, the promotion of heavy industry, selective financial incentives to the private sector, and a large state sector. The lack of competition created powerful entrenched coalitions between business and labor interests that could not be overcome by the state during the Cold War years. Organized business wanted freedom to operate within the protected Indian market but did not want to risk exposure to foreign markets. Organized labor, which constituted less than 10 percent of India’s work force, was happy with job security and labor laws that protected them while the majority of workers in the unorganized sector endured hardships.[10] Inviting competition from other countries within or outside the region needed the support of a political economic coalition that would be willing to adjust to competition.

The Government’s reports from the late 1970s had acknowledged the problem of low productivity, the dearth of development finance, and the need for export promotion. Indira Gandhi’s second tenure (1980-83) had taken note of these problems.[11] Indeed, Rajiv Gandhi had tried to initiate economic liberalization since 1984, but substantial promotion of competitiveness and exports could not be achieved in the 1980s. Even Rajiv Gandhi’s comfortable majority in the Parliament could not overcome the political impediments standing in the way of India’s tryst with globalization. India remained one of the most autarkic economies in the world at a time when China was embracing global economic integration and the Soviet model was crumbling.[12] A clear statement of India’s economic liberalization program required a change in executive and technocratic orientation in conjunction with an exogenous shock: a balance of payments crisis.

Dual Shocks: Balance of Payments Crisis and the Collapse of the Soviet Union

The beginning of the 1990s brought with it dramatic economic change. By the end of the 1980s, India found itself in dire straits. Its fiscal deficit had increased rapidly to over 8 percent of GDP, inflation in 1991 was nearly 14 percent, and its external debt had increased from $18 billion in 1980 to

[10] On India’s inflexible labor laws, see Zagha (1999).

[11] On Mrs. Gandhi’s second tenure, and a critical look at past policy, see Dhar (1988) and Sengupta (2001).

[12] On the political economy of import substitution opposing trade orientation in the 1980s, see Kohli (1990), Chapter 11.

nearly $72 billion by 1991.[13] In the context of this negative secular trend came the Iraqi invasion of Kuwait in 1990. The result of this development was threefold: remittances from Indian workers in the Gulf states fell as they fled the region, exports to Kuwait and Iraq declined, and India faced a dramatically higher oil bill as the price of oil skyrocketed.[14] The adverse credit rating assigned by Moody's in October 1990 pointed to a rise in the debt-service ratio, the debt-export ratio, the budget deficit and dependence on short-term commercial borrowings. Between January and June 1991, gold had been shipped to the Union Bank of Switzerland and the Bank of England to shore up foreign exchange reserves. Despite this, India was on the verge of a liquidity crisis in June 1991, with insufficient foreign exchange to cover a fortnight of imports.[15] It was in this economic context that India found itself with the need to take dramatic action.

In the security realm, the end of the Cold War from 1989 to 1991 dramatically altered India's security and economic environment. India's nonalignment policy, with a tilt toward the Soviet Union after 1971, quickly became obsolete. Without the Soviet Union, India now had to cope with China directly and also seek some type of accommodation with the only superpower, the U.S. As we shall see, this dramatic change also led to a sharply different dynamic with Southeast Asia in particular, and helped to set in motion the LEP. But in addition to power changes, the market that the Soviet Union provided for internationally uncompetitive Indian goods (resulting from the inefficiencies generated by the ISI policy) also rapidly disappeared. Tables 8.3 and 8.4 show the trends in India's exports and imports from the 1980s to the current period.

The export pattern clearly shows a dramatic drop in exports to the Soviet Union (and then Russia) between the 1980s and the 1990s. Other important shifts include an increase in exports to ASEAN countries (with a fall after the Asian financial crisis), a rise in exports to the U.S. followed

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13 OECD, External Debt of Developing Countries, various.

14 See Joshi and Little (1994).

15 Mukherji (2007), Chapter 5.

Year	1980	1985	1990	1995	1998	2000	2005
World Exports	8,440.55	8,265.36	17,813.00	30,537.20	33,662.70	42,624.40	97,918.1
Exports to China (excluding HK & Macao)	28.55	21.45	18.02	282.92	499.90	758.23	6,444.83
% of total exports	0.34	0.26	0.10	0.93	1.49	1.78	6.58
Exports to China (HK and Macao)	165.74	153.76	545.13	1,822.55	1,894.90	2,609.43	4,267.78
% of total exports	1.96	1.86	3.06	5.97	5.63	6.12	4.36
Exports to Republic of Korea	64.20	73.44	163.60	394.29	347.83	457.25	1,624.64
% of total exports	0.76	0.89	0.92	1.29	1.03	1.07	1.66
Exports to Japan	775.83	920.61	1,656.00	2,130.40	1,713.62	1,767.22	16,362.64
% of total exports	9.19	11.14	9.30	6.98	5.09	4.15	2.43
Exports to US	967.03	1,563.34	2,693.68	5,304.65	7,102.75	9,083.25	16,362.50
% of total exports	11.46	18.91	15.12	17.37	21.10	21.31	16.71
Exports to EU	2,088.65	1,679.26	5,068.49	8,398.13	9,197.72	10,369.80	21,900.10
% of total exports	24.75	20.32	28.45	27.50	27.32	24.33	22.37
Exports to USSR/FSU	1,409.99	1,693.37	2,867.61	1,128.01	894.13	1,090.37	1,272.60
% of total exports	16.70	20.49	16.10	3.69	2.66	2.56	1.30
Exports to ASEAN	300.24	199.30	748.79	2,348.51	1,835.33	2,749.32	9,992.11
% of total exports	3.56	2.41	4.20	7.69	5.45	6.45	10.20

Table 8.3: India's merchandise exports (in millions of US$)[16]

16 International Monetary Fund, Direction of Trade Statistics, 2006. In 1980, ASEAN consisted of Indonesia, Malaysia, Philippines, Singapore, and Thailand. Brunei Darussalam joined the agreement in 1984, and is included in the data from 1985-2004. Vietnam joined in 1995, and is included from 1995-2004. Laos and Myanmar joined in 1997, and so are included from 1998-2004. Finally, Cambodia joined in 1999, and is included from 2000-2004. Data for FSU after 1990.

Table 8.4: India’s merchandise imports (in millions of US$)[17]

Year	1980	1985	1990	1995	1998	2000	2005
World Imports	14,822.20	16,329.00	23,991.40	34,483.60	42,161.80	50,335.80	134,690
Imports from China (excluding HK and Macao)	83.43	103.93	30.73	811.47	1,102.35	1,448.60	9,829.12
% of total imports	0.56	0.64	0.13	2.35	2.61	2.88	7.30
Imports from China (HK and Macao)	27.36	53.85	157.66	243.10	416.20	843.58	2,058.34
% of total imports	0.18	0.33	0.66	0.70	0.99	1.68	1.53
Imports from Republic of Korea	172.54	205.45	325.46	716.90	1,296.25	988.68	4,134.73
% of total imports	1.16	1.26	1.36	2.08	3.07	1.96	3.07
Imports from Japan	815.07	1,363.56	1,800.83	2,234.33	2,385.50	2,015.60	3,473.12
% of total imports	5.50	8.35	7.51	6.48	5.66	4.00	2.58
Imports from US	1,865.21	1,769.89	2,634.84	3,343.91	3,659.60	3,152.25	7,590.74
% of total imports	12.58	10.84	10.98	9.70	8.68	6.26	5.64
Imports from EU	3,494.72	4,515.23	8,009.32	9,171.22	10,779.50	10,690.40	22,166.70
% of total imports	23.58	27.65	33.38	26.60	25.57	21.24	16.46
Imports from USSR/FSU	1,233.22	1,574.23	1,321.73	1,112.91	761.09	721.00	2,689.16
% of total imports	8.32	9.64	5.51	3.23	1.81	1.43	2.00
Imports from ASEAN	877.23	838.95	1,474.01	2,295.52	4,136.77	4,381.72	10,236.88
% of total imports	5.92	5.14	6.14	6.66	9.81	8.70	7.60

17 International Monetary Fund, Direction of Trade Statistics, October 2005. In 1980, ASEAN consisted of Indonesia, Malaysia, Philippines, Singapore, and Thailand. Brunei Darussalam joined the agreement in 1984, and is included in the data from 1985-2004. Vietnam joined in 1995, and is included from 1995-2004. Laos and Myanmar joined in 1997, and so are included from 1998-2004. Finally, Cambodia joined in 1999, and is included from 2000-2004. Data only for FSU after 1990.

by a drop, and then a rise in exports to China—issues that we discuss later in the paper.[18] We can also discern a similar (albeit less dramatic) change in import patterns, with Russia playing a dramatically less important role after 1990 and China and South Korea a more significant role.

Factors Affecting India's Response

In view of the dramatic changes we have seen in India's balance of payments problems and the collapse of the Soviet Union, we now consider the factors behind its responses. With respect to the goods involved at the security level, it quickly became clear that India would have to find an accommodation with the only superpower. India was no longer in a position of being able to pursue a non-aligned policy and continue to seek benefits from the semi-public good nature of the balance of power that existed during the Cold War. In the earlier era, the standoff between the U.S. and the Soviet Union generated a public good that gave India room to maneuver and pursue an independent policy. As a result of India's new initiatives on this score, Indo-U.S. relations began to improve slowly during the 1990s. More cooperative relations included the U.S. being granted refueling rights during the Gulf War, joint naval exercises, and the establishment of a Defense Policy Group in the mid-1990s.[19]

With respect to trade issues, the public good aspects of the GATT-based trading system that had created open markets for its members (technically a club good) were potentially diminished with possible crowding in some sectors. India was hardly alone in its liberalization drive, with much of Latin America moving away from ISI policies in the aftermath of the 1980s debt crisis. Thus, as India made the transition to a more export-oriented model, it was under pressure to compete not only with East Asian but also Latin American producers for markets in rich countries. In some sense, then, the public good character of market access to developed country markets began to have more of a common pool resource characteristic as export competition increased.

In terms of its individual situation, the coalition to promote an outward looking policy remained shaky. The balance of payments crisis had empowered the P.V. Narasimha Rao minority government to undertake reforms. Yet with entrenched interests generated by ISI, reform was hardly simple and opposition slowed the pace of economic liberalization. The anti-competitiveness coalition was quite strong when Rajiv Gandhi came to power. His attempts did not succeed to a substantial extent even though he came to power in 1984 with a spectacular majority in the Parliament

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[18] Note that the IMF figures are for merchandise trade, and do not include service exports that are about 50 percent of India's exports to the U.S. in the last few years.

[19] Tomar (2002)

following the assassination of his mother Indira Gandhi. Although the budgets of 1984 and 1985 had made some headway, subsequent budgets had to roll back reforms, due largely to political pressure from within the Congress Party.[20] This anti-liberalization coalition remained powerful even after the balance of payments crisis of 1991. In particular, the so-called "Bombay Club" of industrialists began to voice their protest about competition from MNCs about allowing entry to multinationals after 1993, and trade unions struck against the "exit" policy that would displace jobs.[21]

At the elite level, however, the commitment to liberalization was strong and a consensus on the need to liberalize had been evolving among the technocratic elite prior to the crisis. Various government studies had emphasized the importance of promoting trade, and Rajiv Gandhi had made efforts to promote liberalization, albeit without success, in the 1980s.[22] India's most intensive period of autarkic import substitution lasted from 1969 until 1974. A very gradual process of economic liberalization had begun after 1974. The process gained some momentum when Indira Gandhi came to power in 1980, and when Rajiv Gandhi assumed office in 1984. Despite this, while Indian economic policy was beginning to promote competitiveness and private enterprise, it still remained far too closed an economy by the standards of the rest of the world.[23]

Finally, with respect to institutions, although India was a member of the GATT, as a developing country it had special provision (Part IV of the GATT), which allowed it to pursue an ISI policy. During the negotiations leading up to the Uruguay Round, India had been an active opponent to service sector liberalization and also served as leader of the so-called group of 10 that had called for services to be excluded from the GATT negotiations.[24] Thus, at least with respect to global negotiations, India had been seen as particularly recalcitrant.

Domestic Liberalization and the "Look East" Trade Policy

The Indian response to the 1991 crisis is well documented. The Narasimha Rao government came into power as a minority government. While Rao was personally seen to be relatively weak and simply a caretaker, he found a way to politically support economic policies that would take India away from import substitution and toward export promotion and

[20] Kohli (1991), chapter 11; Rubin (1985:942-957)

[21] Mukherji (2005b:20-21)

[22] Mukherji (2005b)

[23] Nayar (2005:1885-1890)

[24] Aggarwal (1992)

competitiveness. With the appointment of Manmohan Singh as Finance Minister, who had shifted away from a highly interventionist perspective to a more liberal one, the Rao government surprised critics and supporters alike. His credentials as both an economist and a practitioner of economic policymaking placed him in a position where he could pursue home-grown economic reforms that could sustain themselves in a plural polity. There is now clear evidence to suggest that Narasimha Rao and Manmohan Singh made virtue of necessity and pushed the reform agenda in a manner that impressed the IMF.[25] The response to the crisis in 1991 was substantially different from before because committed technocrats could use the crisis as a tactical weapon to promote India's competitiveness and export orientation.[26]

The reforms defined a new relationship between the state and the market in India. Industrial licensing was almost entirely abolished between 1991 and 1993. The average weighted tariffs were reduced from 72.5 percent to 29 percent within a decade. The currency was substantially devalued and in August 1994, the Rupee became convertible on the capital account. India's stock market was reformed, allowing it to become a source of funds for making Indian industry competitive. Reforms in the telecommunications sector were spectacular by world standards and became a great asset for the booming information technology sector.[27] What made these reforms interesting was that they were a home-grown process rather than one driven by IMF or World Bank dictates. Two examples illustrate the home-grown nature of India's adjustment: India was slow to reduce its fiscal deficit, and the telecommunications sector was made competitive without funds from the World Bank and without privatizing government-owned operators.[28]

In the liberalization context, a turn to the dynamic economies of East Asia may have seemed natural. India's engagement with Southeast Asia also had to wait till 1991. Yet this was not as obvious a turn as one might have expected. ASEAN-Indian relations had remained tense during much of the 1980s with India viewing ASEAN as a puppet of the U.S. in its anti-

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[25] See Sen (1998); Singh (1964). These views have benefited from personal interviews with Montek Ahluwalia, Deputy Chairman – Planning Commission, New Delhi, December 2005; Jagdish Bhagwati, University Professor, Columbia University, New York, November 1997. See also Bhaduri and Nayyar (1996:50)

[26] This view is based on interviews with Montek Ahluwalia, Deputy Chairman Planning Commission, New Delhi and Rakesh Mohan, Deputy Governor, Reserve Bank of India, Mumbai in December 2005.

[27] See Mukherji (2005b) for a good discussion of the political economy of reform in 1991.

[28] On telecommunications reform see Mukherji (2006); and, on stock market reform see Gent (2004).

communist stance and ASEAN seeing India as increasingly entrenched in the Soviet camp. Indeed, India had attempted to create a counter-proposal to the creation of ASEAN, viewing it as a Cold War bloc to be resisted.[29] Although ASEAN made various overtures to cooperate with India in the late 1970s, the latter's recognition of the Heng Samrin regime in Kampuchea, which was backed by Vietnam, chilled Indian-ASEAN relations once again. Throughout the decade, with minor exceptions, relations failed to improve.

Many analysts focus on the LEP as being a key focus for India's economic strategy almost immediately after the liberalization policy and the end of the Cold War.[30] Yet at this point, India was considerably more focused on mending relations with the major powers and international economic institutions in view of its dire need for financial resources and inward investment to transform its ISI-based economy to an export-oriented one. The attractiveness of the apparently successful East Asian model and the need to find trade opportunities led India to seek closer relations with ASEAN. Countries like Singapore were quick to grasp both the economic and strategic potential of the end of the Cold War and India's economic liberalization program. The end of the Cold War meant that the ASEAN countries were more comfortable dealing with India in the absence of the Soviet threat. Additionally, India's integration with the global economy opened it up as an investment destination, market and a source of imports. Senior Minister Goh Chok Tong played a key role in generating an "India fever" in Singapore in 1996. As part of the new "Look East" effort, the Rao government promoted a number of visits by high-level ministers, and Prime Minister Rao himself traveled to Japan and most of the Southeast Asian countries between 1993 and 1995.[31]

Relations with ASEAN improved rapidly, with India becoming a sectoral dialogue partner in 1992 on trade, investment, tourism, and science and technology. Following the ASEAN summit in 1995, India became a full dialogue partner (along with China and Russia). Meanwhile, on the security front, India made overtures to join the ASEAN Regional Forum (ARF). ARF had been established in July 1994 with 18 members, including the ASEAN states, dialogue partners, observers, and consultative partners. In 1996, India secured membership in ARF. It is worth noting that India's overtures in its LEP met with an interested ASEAN, who in the aftermath of the fall of the Soviet Union began to worry increasingly

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29 See Kaul (2001) for an analysis of ASEAN-India relations during the Cold War. The following discussion of Cold War relations draws heavily on her analysis.

30 Mukherji (2005a)

31 Saint-Mezard (2003)

about China's rising power.[32] In this sense, the LEP served both India and ASEAN's needs.

With respect to the LEP, another initiative known as BIMST-EC (the Bangladesh, India, Myanmar, Sri Lanka, Thailand-Economic Cooperation group) also officially came into existence in June 1997.[33] This grouping had been brewing some time and came to fruition as a result of Thailand's initiative.[34] It was interested in creating a Bay of Bengal-based economic cooperation agreement in keeping with its "look west" policy. For India, BIMST-EC also provided an additional stepping-stone to ASEAN through Thailand and created a grouping that excluded Pakistan.

Despite these various efforts, commentators were skeptical about the progress of the LEP even before the Asian financial crisis had fully manifested itself. As *The Hindu* noted in an editorial on July 25, 1997:

> If the investors from Southeast Asia are disappointed that economic reforms are not extended to the critical areas such as financial services in the non-banking sector or aviation, Indian businessmen and officials realize that their expectations from ASEAN were pegged too high. South East Asia may be a major trading partner, but not yet a leading investor.[35]

Thus, despite significant reform and liberalization in India, problems in implementing the LEP still remained.

8.3.2 Looking for Alternatives: the LEP in Flux and the Turn to Sri Lanka

As the Asian financial crisis struck hard in much of East Asia, India's LEP faced a major challenge. Many began to question whether the eastward turn was wise while others questioned a policy of globalization in view of the vulnerabilities of the East Asian economies to financial speculation and capital movements. Of greatest impact was the disillusionment in East Asia with the aid provided by the IMF and the U.S., leading them to turn increasingly toward attempting to develop their own regional trade and financial arrangements. India was relatively unprepared for the dramatic shift toward preferential trading arrangements that took root and accelerated thereafter. It did, however, manage to undertake an accord with Sri Lanka in the context of a continued difficult relationship with Pakistan

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32 Grare and Mathoo (2003:13-14)

33 BIMST-EC's name was changed to the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC) in 2004 to preserve the acronym but to address the entry of Nepal and Bhutan.

34 Saint-Mezard (2003:39-41)

35 "The Hindu-Editorial: Consolidate the partnership". The Hindu (Chennai), 7/25/1997, 20

and little progress in SAARC. Both its relationship with Pakistan and East Asia were, of course, sharply affected by the Indian and Pakistani nuclear tests in 1998.

Shocks: The Asian Financial Crisis and Nuclear Tests in South Asia[36]

When the Thai baht began to falter in June 1997, few analysts foresaw the financial crisis that it would create. In December 1996, the IMF's report, *Thailand: The Road to Sustained Growth,* raised no concerns. By April 1997, when speculative pressures against the baht began to rise, the IMF and the U.S. government were openly urging the Thai government to force banks to declare their bad debts and begin to clean up the financial system. Even after Thailand was forced in early July to announce a managed float of the baht, devaluing it by about 20 percent, it refused to apply new economic measures or openly seek IMF assistance. For their part, however, the IMF and the United States did not treat Thailand's currency crisis as a serious problem.

Thailand finally requested IMF assistance in August 1997. On August 20, it signed a letter of intent with the IMF in Tokyo, after which the IMF authorized $17 billion to rescue the Thai economy. In return, Thailand agreed to a series of economic and financial reforms. Yet the IMF's medicine only exacerbated financial troubles. The abrupt announcements of bank closures only served to inflame the panic rather than instill confidence and added to the ongoing liquidity squeeze, making it more difficult for existing banks to continue normal lending operations.[37] Credit all but dried up. Meanwhile, by August, the United States had dropped out of the process, being conspicuously absent during the loan negotiations. The United States strategy appeared to backfire almost immediately as the currency crisis continued to spread beyond Thailand. Despite the IMF's intervention, the financial crisis, largely driven by currency speculation, continued to spread to the Philippines, Malaysia, Indonesia, and most importantly, South Korea. The IMF eventually promised the Philippines $1.1 billion in aid, Indonesia up to $40 billion, and South Korea up to $60 billion.

With the U.S. failing to financially participate in the Thai rescue package, the Japanese took the lead in September 1998 with a proposal for an Asian Monetary Fund (AMF) to be backed by $100 billion that they had lined up in commitments in the region. But the IMF and U.S. attempted almost immediately to quash this initiative, with the Treasury leading the charge. Instead of directly confronting American opposition, the APT

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36 This subsection draws on Aggarwal (2000).

37 Bresnan (1998:4)

countries set up a currency swap scheme in Chiang Mai, Thailand, in 2000 as a "firewall" against future financial crises.[38]

In addition to these trends in finance, East Asian countries also began to consider the negotiation of preferential trading arrangements with each other. The Asia Pacific Economic Cooperation (APEC) forum, the pan-Pacific agreement that included North American countries, Chile, Peru and most East Asian countries, had proved ineffectual in dealing with the Asian financial crisis and in advancing trade liberalization. In this context, East Asian countries began to show a strong interest in securing their trade position, initially through the negotiation of bilateral preferential trading arrangements. The most active state was Singapore, which negotiated agreements with New Zealand (2000) and then with Japan (2002). Meanwhile, the ASEAN group held its first meeting with China, Japan, and South Korea, creating the ASEAN Plus Three grouping in 1997. By 2000, the ASEAN Plus Three was making plans to create a free trade agreement.

With respect to the second "shock", soon after the Bharatiya Janata Party (BJP) came to power for the second time on March 19, 1998, India tested several nuclear devices in May 1998. This decision also threw India's LEP into further turmoil as ASEAN countries (and most Western countries) expressed their dismay at the tests (which were soon followed by Pakistani tests). Yet in this case, Indian diplomacy, through a series of meetings with key players in the region and working through ARF, appears to have prevented the Philippines and Thailand from promoting a hard-line position to condemn India.

Factors Affecting India's Response

We next turn to India's changing policies in the post-1997 period. Turning first to goods, the altered security environment with the end of the Cold War created a need for India to seek new alignments and ensure its security. In the absence of any club goods or public goods that would guarantee India's security, India sought to pursue "private" goods through the Pokhran II tests in May 1998. In the trade realm, the Asian financial crisis was followed by an increasingly regionalizing club and the pursuit of bilateral club goods by key players in the region.

In terms of its evolving international situation, India had moved forward with cooperation with the U.S., but still had not positioned itself clearly in either security or trade. In security, the U.S. perceived India a regional player that was primarily focused on Pakistan. At the same time, it aspired to a larger global role, but its military position did not put it in that role. Similarly, in the economic realm, India had begun to grow relatively rapidly, and its trade was increasing. Still, despite a significant push

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[38] See Amyx (2003) for details.

toward an export-oriented model, its share of global trade had only crept up to 0.6 percent in 1995-96, up from 0.41 percent in 1992-93.[39] By contrast, China already accounted for 1.9 percent of world exports in 1990, increasing to 4 percent by 2000.[40]

India's domestic coalition also faced difficulties with fluctuating governments and anti-liberalization pressures. Reforms had slowed and there was considerable concern about India's ability to sustain a continued liberalization policy. In terms of elite views, there still appeared to be a strong commitment to a multilateral approach to trade liberalization, albeit with exceptions for developing countries and pressure to keep some restrictions on trade. With respect to nuclear weaponization, as Amitabh Mattoo notes, there was a strong shift among elites in support of India moving to develop nuclear weapons between the 1974 test and 1994 (before the tests).[41]

Finally, in terms of institutional context, India faced the challenge of an indefinite extension of the Non-Proliferation Treaty in 1995 and the conclusion of the Comprehensive Test Ban Treaty in 1997.[42] This led to concern about growing institutional constraints on India's efforts to move toward great power status and increasing freedom of maneuver. With respect to trade, as we have seen, the primary context in which India operated was the WTO. The LEP had not resulted in any significant institutionalization beyond creation of BIMST-EC while SAARC's 1993 decision to create a free trade agreement had yielded little growth in intra-regional trade or significant institutionalization.

India's LEP in Flux and the Turn to Sri Lanka

With the East Asian crisis in full bloom in 1997-98 and India's nuclear tests, economic cooperation with Southeast Asia was hindered significantly. Merchandise exports to ASEAN declined from $2.349 billion to $1.835 billion between 1995 and 1998, and as a percentage of India's total exports from 7.69 percent to 5.45 percent. Meanwhile, as ASEAN countries' currencies underwent rapid devaluation in the crisis, imports to India from the region simultaneously surged from $2.3 billion to $4.1 billion, growing from 6.7 percent of India's total imports to 9.8 percent during the same three-year period.

Concern about India's LEP was nicely expressed with the phrase "India Looks East But Asia Looks Away," in an article in *The Hindu* on December 1, 1999. Raja Mohan, whose perspective appeared to be widely

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39 http://www.wto.org/english/tratop_e/tpr_e/tp71_e.htm.

40 http://www.imf.org/external/np/speeches/2005/011005.htm

41 Mattoo (2001:102)

42 RAND (2001) based on Tellis 2001.

shared, argued that "India is increasingly seen in the region as the "Middle Kingdom", obsessed with its own domestic political wrangling and unprepared for a serious regional engagement." He went on to note that the LEP appeared to be in trouble, arguing "The mild 'India fever' that gripped South East Asia in the mid-1990s has long evaporated." And he pointed out that "India's nuclear tests followed by increased political tensions with the U.S., Japan and China put it in a difficult position vis-à-vis the rest of Asia. Renewed hostilities with Pakistan have reinforced the traditional image of a perennially squabbling subcontinent, that few in South East Asia have the desire to get entangled in."

Even as East Asia's states recovered economically, India still appeared to be facing difficulties in implementing its LEP and pursuing economic liberalization more generally. As *The Straits Times* (Singapore) reported on January 20, 2000 on the occasion of Singaporean Prime Minister Goh Chok Tong's visit to India:

> Visiting Prime Minister Goh Chok Tong said yesterday that the government in India had to try and change its mindset to fully capitalize on its 10-year-old "Look East" policy. He also said that the private sector should pressure the government to change its mindset in support of globalization.[43]

Yet all was not lost. India continued to play catch up with the LEP and invigorate the general rhetoric with actual policy changes. It moved to set up an economic cooperation agreement with Singapore, links to Myanmar, and cooperation agreements with Laos in late 2000. Jaswant Singh colorfully described the state of the LEP when he noted, "We have been talking about looking east but so far it has been a bit like the Delhi water supply. You turn on the tap and there is the sound of the promise of water but it's usually air. This has to change."[44] At the same time, India faced a perception of South Asia as being outside of "Asia" with its efforts to join APEC coming to naught. Indeed, despite significant efforts, India had been unable to join APEC and a moratorium on membership had come into effect in 1997 for 10 years, thus impinging on the LEP and India's efforts to insert itself firmly into the East Asia institutional context. Meanwhile, India continued various efforts to link its economy to Southeast Asia. One effort, the Mekong-Ganga Cooperation (MGC) initiative, attempted to give more substance to the LEP, which was clearly by this time seen to be in trouble. India also continued to press forward with BIMSTEC.

In short, the changes wrought by the Asian financial crisis, which led East Asian states to increasingly focus on regional and bilateral efforts

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43 "India gov't. 'should try to change its mindset'", Straits Times (Singapore), 1/20/2000, 17.

44 Straits Times (Singapore), November 15, 2000, 27.

amongst themselves, seemed to have created difficulties for India's LEP. Indian policymakers clearly recognized this and made a strenuous effort to play catch-up. One of the most significant of these catch-up efforts was the decision to pursue India's first preferential agreement with Sri Lanka. The treaty was signed in 1998 and became operational in 2000. Improvements in security relations and interdependence concerns aided this process. Sri Lanka–India trade was ridden with vulnerability concerns before 1998. These vulnerability concerns had impeded the progress of Joint Commissions since 1968. There had been fears that Sri Lanka would be flooded with Indian products.

The end of the Cold War was a background condition. Sri Lanka was considered too pro-West during the J.R. Jayawardane presidency. The significant event that pushed the countries toward friendlier relations was the assassination of Rajiv Gandhi and India's withdrawal of support for the Liberation Tigers of Tamil Eelam (LTTE), an anti-government force in Sri Lanka that was responsible for the assassination. Indo-Lanka relations improved dramatically after Narasimha Rao became Prime Minister. Subsequently, Prime Ministers Gujral, Vajpayee and Singh have continued the positive momentum in Indo-Lanka relations. The departure of the Indian Peace Keeping Force was followed by an unprecedented level of activity within the Joint Commissions and subsequent High Commissioners were viewed as being sympathetic to Sri Lankan concerns.[45]

The removal of the security irritant was accompanied by India's quest to increase its trade. The U.S. trade sanctions in the aftermath of the Indian nuclear and the Asian financial crisis increased India's resolve to have a successful sub-regional trade agreement with Sri Lanka. India was willing to grant more than reciprocal concessions to Sri Lanka.

Given India's growing commercial might it was in Sri Lanka's interest to lock India into a preferential trade relationship. Aided by an excellent study of the World Institute of Development Economics Research (WIDER) and ably complemented by technocratic activism of the Presidential Advisor Lal Jayawardane, Sri Lanka found good reason to lock a willing India into a trade relationship. The success of India's economic liberalization program saw India surpassing Japan as Sri Lanka's leading exporter in 1996. India supplied 10.4 percent of Sri Lanka's imports compared with 9.2 percent coming from Japan. In 1997, out of a total trade of $560 million Sri Lanka's exports to India were a paltry $ 42.7

[45] Personal interview by Rahul Mukherji with Saman Kelegama, April 9, 2003. Kelegama is the Director of the Institute of Policy Studies, Colombo. See also Kelegama (1999:91-92)

million. Sri Lanka's exports to India as a share of its total exports declined from 1.1 percent in 1990 to 1.0 percent in 1996.[46]

There was much opposition to the agreement from small industrialists, farmers and trade unions in Sri Lanka. An agreement could be reached after a number of asymmetrical and favorable concessions were made by India. India granted zero-duty concessions on 1,000 items compared with Sri
Lanka's 300. India's negative list covered 24 percent of the goods while Sri Lanka's covered 49 percent of its products, ably protecting competing producers. The adjustment period for India was three years while that for Sri Lanka was eight years.[47]

Table 8.5: Trade flows between Sri Lanka and India[48]

Year	India's imports from Sri Lanka (millions of Rupees)	India's exports to Sri Lanka (millions of Rupees)	Import-Export Ratio
1998	35,837.7	2,279.4	16.1
1999	36,012.9	3,320.3	11.1
2000	45,477.1	4,217.3	11.1
2001	53,750.0	6,265.7	8.61
2002	79,847.1	16,152.9	5.1

The results of these asymmetrical concessions were favorable for Sri Lanka. Between 1998 and 2002, the ratio of Sri Lanka's imports from India to its exports to India declined from 16:1 to 5:1 (Table 8.5). The preferential exports of Sri Lanka had grown by 620 percent in 2002.[49] India is the biggest foreign investor in Sri Lanka, and at the time of this writing the two countries were negotiating to broaden the Comprehensive Economic Partnership Agreement to include services by late 2007.[50]

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46 See WIDER (1991); WIDER (1993); Jayawardane (2001); Kelegama (1999). The technocratic activism was explained to Rahul Mukherji by Lal Jayawardane in a personal interview in Colombo in April 2003. He was the most powerful technocratic force within Sri Lanka that pushed this agreement.

47 The opposition to the Indo-Lanka Agreement is clear from Sri Lankan newspaper articles of 1998 and 1999. Only big business supported the agreement. On this, we benefited from Mukherji's interviews with Saman Kelegama, Lal Jayawardane, Jayanta Kelegama, Ken Balendra, Stanley Jayawardane, and Patrick Amarsinghe in April 2003.

48 Kelegama (2003: 3153)

49 Kelegama (2003:3153-3154)

50 "Sri-Lanka India Comprehensive Economic Partnership Agreement in early 2007", Colombo Page 11/18/2006. See http://www.colombopage.com/archive/November18140900SL.html

The Indo-Lanka Free Trade Agreement (ILFTA), which reflected growing sub-regional interdependence within South Asia, was aided by the end of the Cold War and India's trade potential resulting from the economic liberalization program. The nuclear sanctions and the Asian financial crisis made India desperate to look for partners within the region. It was only when security relations warmed after the assassination of Rajiv Gandhi that commercial considerations drove Sri Lanka toward a preferential trading relationship.

8.3.3 Post-9/11: A New Security and Trade Environment

The third set of shocks and its aftermath for India's trade policy are the attacks of September 11, 2001, the U.S. and East Asian shift to preferential trading arrangements, and the collapse of the Doha Round in 2006. These attacks dramatically altered both the security and economic environment in which India operated as the U.S. dislodged the Taliban in Afghanistan and invaded Iraq to remove Saddam Hussein. In the case of Afghanistan, closer relations between the U.S. and Pakistan were a natural result of this need for a frontline ally. Yet here, the outcome was not as detrimental to India's interests as might have been feared in view of the aftermath of the Soviet invasion of Afghanistan in 1979 and the installation of Babrak Karmal that led to massive U.S. aid to Pakistan.

As the U.S. turned its trade policy in a more bilateral direction and began to use institutions such as APEC and ARF to promote an anti-terrorist agenda, East Asian countries responded with an acceleration of bilateral and regional trade efforts. In this case, unlike India's response to the Asian financial crisis of 1997-1998, when it was caught flat-footed, India responded more aggressively and has made significant inroads in successfully pursuing its "East Asian" agenda as well as new initiatives such as a possible bilateral trade agreement with the European Union.

New Shocks: 9/11, Kargil and Parakram, and Trade Promotion Authority

The most dramatic event in the transformation of U.S. foreign policy after the end of the Cold War is undoubtedly the aftermath of the 9/11 attacks on New York and Washington D.C. The invasion of Afghanistan, intended to destroy the al-Qaeda terrorist network and remove its Taliban sponsors from political power, had proven to be a relative success. In March 2003, the anti-terrorist effort was carried to Iraq, with the deposing of Saddam Hussein. The controversy over Saddam's links to al-Qaeda and the question of weapons of mass destruction are clearly beyond the scope of this paper. Suffice it to say that the ensuing debacle in which the U.S. now finds itself has yet to be resolved, with calls for American troop withdrawals being criticized by Bush administration officials.

Two other crises influenced India's policies. First, the Kargil invasion by Pakistani forces, in which forces crossed over the Line of Control in Jammu and Kashmir, led to a flurry of activity by the United States. President Clinton brokered an agreement that led to Pakistani withdrawal of its troops from the region. But soon thereafter, India's Operation Parakram, a large scale Indian mobilization of troops from January through November 2002, dramatically increased tensions. India launched this mobilization as an effort to engage in coercive diplomacy to deter Pakistan from further support of cross-border terrorist activities. The immediate precipitant was the attack on the Indian parliament in December 2001 that was attributed to Lashkar-e-Taiyaba and Jaish-e-Mohammad, which India argued had been allowed by Pakistan to operate freely. Yet this mobilization effort did not lead to significant reductions in Pakistani support for such groups, and raised the prospects of a major war between India and Pakistan that once again led to U.S. diplomatic efforts to prevent further conflict.

Another key event was the passage of Trade Promotion Authority by the U.S. House of Representatives in December 2001. This was soon followed by Senate passage of the trade bill in May 2002, and final passage of the jointly agreed House-Senate Trade Promotion bill in August 2002. Even as the House passed the bill, U.S. Trade Representative Robert Zoellick was gearing up for the U.S. emphasis on a multipronged trade liberalization effort. As the press release commented, "The United States will press ahead with negotiations on a Free Trade Area of the Americas, free trade agreements with Chile and Singapore, and global trade negotiations under the auspices of the WTO."[51]

Finally, in July 2006, the Doha Round of the WTO was suspended. The major issues of contention concerned reciprocal concessions in agriculture and manufacturing. The developing countries called for sharp cuts in agricultural subsidies in both the U.S. and the EU, which in turn pressed developing countries to lower and bind their manufacturing tariffs. At the time of this writing in the summer of 2007, although the round has resumed, its outcome is uncertain. Yet in the aftermath of the Doha Round many key players have moved toward negotiating bilateral trade negotiations, posing a challenge to India to follow this trend.

Factors Affecting India's Response

With respect to goods, security still remained in flux. In the aftermath of 9/11, the U.S. began to reorient its focus away from its previous concern with ensuring that China's rise would not pose a threat to the U.S. to a policy of pursuing specific private goods. The U.S. was less concerned with the provision of Asian security and playing a balancing role in the

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51 U.S. Mission Geneva, Press Release, 12/6/2001

region, and more concerned with pursuing terrorists and working with states who perceived the terrorist threat to be paramount.

In terms of trade "goods", although the U.S. continued to work with other WTO members, it was increasingly interested in securing bilateral and minilateral trade agreements. East Asian states had already begun to negotiate trade agreements, with Singapore taking a leading negotiating role in the region following the 1997-98 crisis, but this trend toward the conclusion of such bilateral accords sharply accelerated. Singapore continued to enter into trade accords with many other countries, including the European Free Trade Agreement (EFTA) countries, Australia, the U.S., Jordan, South Korea, Panama, and India (discussed below) and had a host of other negotiations underway.

China, Japan, South Korea, and other states in East Asia also joined the FTA bandwagon. At the APT meeting in Brunei in 2001, China proposed an ASEAN-China FTA and signed a surprise agreement in November 2002 with the 10 ASEAN countries pledging free trade. The proposed FTA is scheduled to take effect in 2010 for the six original members of ASEAN (ASEAN-6), and in 2015 for the less developed members (Cambodia, Laos, Vietnam and Myanmar). Under the agreement, China has accorded Most Favored Nation treatment to Cambodia, Laos, and Vietnam (which are not members of the WTO), has written off $220 million of debt, and promised an "early harvest" of tariff reductions on hundreds of agricultural products, with discussions on goods, services, and investments to be held sooner rather than later.

Challenged to do the same and to demonstrate a continued Japanese capability to lead within East Asia, Japan proposed a Japan-ASEAN FTA at the ASEAN summit in 2002. It also hosted the ASEAN-Japan Commemorative Summit in December 2003, confirming its enthusiasm for promoting collaboration with ASEAN members. Japan also had agreements or was in negotiations with Mexico, South Korea, Malaysia, Thailand and the Philippines. Meanwhile, South Korea signed its first FTA with Chile, proceeded to conclude negotiations with Singapore, EFTA, and ASEAN, and held discussions with Japan, Mexico, Israel, the U.S. and others. Clearly, bilateral club goods was the name of the new game.

In terms of India's individual situation, as we have seen, the conflict with Pakistan continued to be high on the agenda. India also found itself in a rapidly changing dynamic. With its economic position as a key player in the software industry and rapid economic growth, the security-economic dynamic involving China, Russia, the U.S., Pakistan, ASEAN countries, and others was in tremendous flux.

With respect to India's domestic coalition, liberalization over the years since 1991 has created an increasingly outward-oriented focus, although protectionist elements still remain strong. With respect to interest groups, it is quite clear that the emergence of a service sector, with a high-tech focus in part of it, has been an important factor supporting the global turn.

Services now account for over 46 percent of India's GDP, up from 40 percent prior to the reform.[52] The service sector also provides a nice complement for India's manufacturing sector, thus providing a good fit and strong incentive for trade cooperation. And as Christophe Jaffrelot has noted, "India's capacity in the high-tech sector was also an important element in the relaunching of relations between India and the Southeast Asian countries after the peak of the Asian crisis was over."[53] And in contrast to the earlier opposition that the liberalization policy faced from the so-called "Bombay Club", one of its leading members, Rahul Bajaj, "has finally realized that he needs to diversify his manufacturing base globally to compete effectively in the international market. He has decided to set up two assembly operations in Indonesia and Brazil."[54] In particular, the banking industry has argued that FTAs had helped Indian banks to expand globally.[55]

Still, free trade agreements or the prospects of them are seen by some industries in India as a threat to their viability. Discussing the FTA that India negotiated with Thailand, the head of the auto manufacturers association in India worried that: "…perhaps without intending to, the Thai FTA could end up hurting India's manufacturing industry."[56] A powerful lobbying group, the Federation of Indian Chambers of Commerce and Industry (FICCI) has also raised concerns about India's current bilateral trade agreement strategy. As Chetan Bijesure noted in a recent interview, "bilateral agreements with which Indian industry faces strict competition in strategic sectors should be minimized."[57] He went on to note that the Thai FTA had failed because of the increased competition that Indian industry faced in autos and electronics. In the context of negotiations with ASEAN, he called on the government to continue to protect weak sectors from competition.

More generally, with respect to trade liberalization, other lobbying groups have also expressed doubts. The Associated Chambers of Commerce and Industry (ASSOCHAM) has also been critical of liberalization, arguing that the FTAs signed with Sri Lanka and Thailand have not benefited India and that other countries have used Sri Lanka and

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[52] Virmani and Batra (2004:6)

[53] Jaffrelot (2003:63)

[54] Bajaj Report, The India Express, 7/25/2005

[55] "Consolidation of banks imperative to compete globally: FICCI". The Press Trust of India, 9/24/2006

[56] Asia Times Online, 2/13/2004

[57] Interview, November 2006.

Thailand to dump products in India.[58] Yet ASSOCHAM has not been entirely opposed to trade liberalization; they conducted a survey of Indian industry about an FTA with the EU and concluded that a specialized FTA in services, targeting knowledge sectors like IT, bio-tech, and pharmaceuticals would be of great benefit.[59] ASSOCHAM's concerns are primarily about the costs of short-run adjustment problems that FTAs bring. They still believe that in the long run FTAs will bring gains for Indian industry, provided that the agreements are drafted carefully, particularly in areas like rules of origin.[60] ASSOCHAM has come out in favor of standardizing the format of rules of origin for all future FTA negotiations, in effect pushing for stringent guidelines in the ASEAN negotiations to avoid weakening India's bargaining position on such issues in the future.[61]

In terms of multinational corporations' incentives, a large number of Indian multinational corporations have begun to look eastward already, thus helping to push India to focus on the east. The information technology sector, which has companies with operations in Southeast Asia are the major proponents of free trade with Southeast Asia. These would include large companies like the Tata Consultancy Services and the powerful industry organization—National Software and Service Companies (NASSCOM). There interests were taken into consideration in the Comprehensive Economic Cooperation Agreement (CECA) with Singapore, which allows for the easy movement of natural persons and recognition of professional standards.

And for their part, elites have been increasingly pushing the need to not only see India as a global player, but also to more firmly "insert" India into Asia. In calculating where to turn for India's prospective FTA partners, elites focused in part on the balance of trade. Thus, in the case of Thailand, it appears that the Government of India decided on Thailand in view of India's balance of trade surplus. Yet, as noted in terms of the reaction of domestic coalitions, the rapid reversal in the balance of trade with Thailand in the 82 liberalized products created a panic, and Thailand has responded by suggesting that additional items be liberalized to improve India's trade balance in liberalized goods.

Finally, with security institutions such as ARF relatively ineffective, security remains relatively uninstitutionalized in the region. Still, ASEAN

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[58] "FTA With Sri Lanka, Thailand Not Benefiting India: ASSOCHAM". Asia Pulse, 2/6/2006

[59] "India Inc for Services FTA". Indian Express, 9/6/2005

[60] "FTAs Will Create Adjustment Problems in Short Term: ASSOCHAM". Hindustan Times, 10/19/2005

[61] "Do Not Tamper With RORs Already in Place for ASEAN: ASSOCHAM". Hindustan Times, 6/17/2005

has shown a willingness to involve India in regional maritime activities and the U.S. has conducted exercises with India.[62]

8.3.4 Toward a New Trade Policy?

With the security context and economic context rapidly in flux since 2001, how has India's trade policy evolved? We can examine its new orientation by briefly examining its approach to negotiations at the multilateral, minilateral, and bilateral level.

Global Negotiations

With respect to global multilateral negotiations, India played a highly active role in the Doha Round of the WTO. It has become a key member of the informal Group of 4 that includes U.S., the EU, and Brazil. Throughout the negotiations, Kamal Nath, India's chief negotiator and the commerce and industry minister, has argued vociferously for sharp cuts in agricultural tariffs by the U.S. and EU. When the latter responded by calling for India and other major developing countries to bind their industrial tariffs to no more than 16 percent, India responded by arguing that "India had already made it clear that the rich nations cannot seek a price from developing countries for scrapping farm subsidies since it was a correction of a historic imbalance."[63]

The standoff on the tradeoff between industries tariff cuts by developing countries and cuts in agricultural tariffs and subsidies by the rich countries has continued to this day. The U.S. government has responded to the stalemate with hints that India will lose its position as a preferential trading partner if its actions continue.[64] Indian rhetoric has become confrontational as well. In October of 2006, Indian Prime Minister Manmohan Singh accused developed countries of obstructing the Doha Round, "hit out at developed countries for their 'myopia' and asked them not to allow their 'short-term national interests' to prevail at the cost of promoting free trade and combating poverty."[65] As of this writing, negotiations have been revived in the WTO, but the fate of the Doha Round still remains uncertain.

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[62] See Chapter Nine of this volume by Eswaran Sridharan.

[63] Global News Wire, Financial Times Information, 4/6/2006

[64] "India May Lose U.S. Preferential Trade". The Statesman Ltd., Source: Financial Times Information Limited – Asia. 8/9/2006

[65] "India PM criticized developed countries on trade in Cambridge speech". British Broadcasting Corporation, 10/11/2006

Minilateral Negotiations

India also secured an invitation to the December 2005 East Asia Summit meeting and is now one of 16 participants (ASEAN plus South Korea, Japan, and China; Australia, New Zealand, and India). The EAS finds its roots in conceptions of creating an East Asian regional bloc to counter the regionalism in North American and Europe. Although China prefers an even more restricted membership that follows the ASEAN +3 format, Japan has pushed for the inclusion of Australia, New Zealand, and India.

On a narrower minilateral basis, India and ASEAN continue to pursue negotiations on a proposed FTA. The Indians have given the ASEAN negotiators a negative list of 490 items, down from the initial number of around 1400 items that they proposed in 2005.[66] This concession has still been met with protest by ASEAN countries, which say it covers too many goods of interest to them. Agricultural products, followed by textiles, appear to be the main points of contention on the Indian list.[67] Palm oil in particular is of major interest to Malaysia and Indonesia; India has offered to negotiate a separate agreement for palm oil, cutting tariffs to about 50 percent, in order to speed negotiations along.[68] Talks on services and investment are expected to occur once substantial progress has been made in the talks on trade in goods.[69] Unlike the Thai agreement that has led to concerns about the impact of the FTA, these same concerns appear less applicable to the potential ASEAN FTA because India's exports to ASEAN have been growing faster than ASEAN's exports to India.[70] Joint Secretary of the Union External Affairs Ministry Mukta Tomar has expressed the hope that the ASEAN FTA framework could begin to be implemented in 2007, and also related that the "thrust in India's foreign policy in the last 15 years was to increase connectivity with the neighboring countries and groups like BIMSTEC, ASEAN and SAARC

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66 "Monday, India, ASEAN to meet next month for FTA talk," The Press Trust of India, 10/16/2006

67 "Doha Talks Failure Giving the India-ASEAN FTA a New Thrust," Business Line, 8/24/2006. See also, M K Venu, "India, ASEAN set negative list cap at 5 percent of trade," The Economic Times, 1/15/2007.

68 Damodaran, Rupa, "India Proposes Separate Agreements on Palm Oil," Business Times (Malaysia), 8/26/2006

69 "ASEAN, India agree to resume free trade talks; more tariff cuts demanded," BBC Worldwide Monitoring, 8/24/2006

70 "Doha Talks Failure Giving the India-ASEAN FTA a New Thrust," Business Line, 8/24/2006

with the northeast so that the region could become a hub in trade and commerce."[71]

The India-ASEAN FTA negotiations have gained momentum but the Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation (BIMSTEC), which was supposed to be signed by July 2006, may now be delayed. The initiative involves Bangladesh, India, Myanmar, Sri Lanka, Thailand, Nepal and Bhutan. Negotiations have been bogged down by debates over rules of origin, negative lists and the non-tariff barriers of developing countries. BIMSTEC involves all the countries of South Asia except Pakistan and India's neighbors in Southeast Asia. If successful, this agreement will bring South Asia closer to Southeast Asia. Given that BIMSTEC's FTA essentially duplicates the regional FTAs that India will have with ASEAN and the South Asia Free Trade Agreement (SAFTA), it may be that India's interest in BIMSTEC is due to a desire to hedge its bets against potential problems with Pakistan in SAFTA.

The talks between India and the Gulf Cooperation Council (GCC)—composed of Qatar, Oman, Bahrain, Kuwait, UAE and Saudi Arabia—to develop a FTA stalled in late 2006. Concerns over weak enforcement of IPR laws in GCC countries, different legal systems among the various GCC members, and the costs of standards compliance in GCC countries have held up the FTA talks; this has led members of the GCC to seek individual FTAs with India.[72] Moreover, the Indian petrochemicals and plastics industry with an investment of 500 billion Rupees is feeling the threat from this FTA. In particular, Oman, with which India has the strongest economic ties, would like to conclude an FTA with India immediately, while India would like to wait and enter into agreements jointly with the 6 GCC countries.[73] India has already begun discussions for individual FTAs at the ambassadorial level, though the pace of talks is currently undisclosed.[74] An FTA with the GCC members is expected to boost India's pharmaceutical and chemical industries.[75] The articles covering India-GCC interaction repeatedly emphasize the importance of joint ventures. The India-GCC negotiations for an FTA got underway after

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71 "FTA likely with ASEAN, BIMSTEC nations: official," The Press Trust of India, 9/19/2006

72 "Weak IPR Makes GCC-6 Seek Individual FTAs with India", Financial Express, 9/15/2006

73 Ibid. For opposition from Indian industry see, "Now FTA with Gulf runs into trouble", Times of India, June 9, 2006; "India-GCC FTA Talks in April: Nath", The Hindu, March 27, 2007; and, for lack of political will on India's side, see N Janardhan, "India-UAE ties: Time to pull no punches", Gulf in the Media, March 25, 2007.

74 Ibid.

75 Ibid.

a Framework Agreement on Economic Cooperation was signed in 2004; the talks proceeded with the expectation that trade in goods, services, and investment would be covered.[76] Oman especially was trying to expedite the trade talks by pushing for a fast-track mechanism.[77] In addition to IPR and standards compliance cost concerns, Indian industry and agriculture expressed reservations about the impact that the proposed FTA might have on vegetable oils, tobacco, and polymers.[78]

Bilateral Agreements

Finally, on a purely bilateral basis, India has concluded trade agreements with Thailand (2003) and a Comprehensive Economic Cooperation Agreement with Singapore in 2005. It has also been involved in talks with Japan and there is some movement on a possible accord with the EU.

The Indo-Thai Free Trade Agreement was an example of political strategy rather than careful trade policy driving India's Look East policy. An Indo-Thai Free Trade Agreement was signed in October 2003 with 82 items earmarked for duty reduction within the early harvest scheme. Within months Thailand's trade surplus was 400:1, with Thailand's comparative advantage emerging in auto components and consumer durables. Subsequently, a study by the Indian Credit Rating Agency (ICRA) found that Thailand had a comparative advantage in these areas owing largely to the duty structure in India. The result was that truck makers like Ashok Leland were trying to set up factories in Thailand. Industrialists hurt by the agreement worried that the government, even if it needed to conduct trade agreements for strategic and political reasons, should have conducted consultations with business. Indo-Thai trade is faced with issues concerning rules of origin. India wants restrictive rules that ensure that products manufactured in other countries do not receive easy access to India via Thailand.

The Comprehensive Economic Cooperation Agreement between India and Singapore was signed on June 29, 2005 to bind more firmly India's commercial relations with Singapore. This was a way of rewarding Singapore's initiatives to bring India closer to Southeast and East Asia. Since Singapore is an open economy there was limited scope for preferential market access available to India via this initiative. The quid pro quo was to allow Singapore greater access to the Indian market in return for Singaporean investment and easier entry of Indian skilled

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76 "IT, energy and ICT, new focus areas for India-Gulf cooperation", Hindustan Times, May 17, 2006

77 "Oman Seeks Fast-Track Mechanism for India-GCC FTA", Asia Pulse, 9/5/2006

78 "Industry For Change in Gulf FTA", Financial Express, 6/2/2006

professionals into Singapore. The CECA also provided for service sector liberalization and mutual recognition of degrees in various professions. Singapore accepted a restrictive rule of origin criteria that required 40 percent value addition and a change in tariff heading under the harmonized system code for a product to be considered as one originating from Singapore. India was keen on such a definition after it found that Sri Lanka was being used as a base from which to sell the products of other countries, taking advantage of less restrictive rules of origin for Sri Lankan goods.[79] The CECA needed negotiations with domestic industry in sectors such as automobiles, chemicals, banking and textiles, which felt threatened by competition. By subjecting Indian industry to greater levels of competition in a graduated way, CECA was also likely to make it more competitive.

Lastly, starting in July 2005, Japan and India convened a bilateral joint study group to explore the possibility of signing an FTA between the two countries. It issued a report that was adopted in July 2006 by then-Japanese Prime Minister Koizumi and Prime Minister Singh, following the G8 summit.[80] The report recognizes the potential for further economic engagement and paves the way for the launch of official FTA negotiations later in 2006.[81] In September 2006, Singh expressed a desire to launch bilateral trade agreement negotiations with the new Abe administration.[82] Comprehensive Economic Partnership Agreement (CEPA) negotiations are likely to get underway in the fall of 2007, with the Japanese hopeful for a conclusion by the end of 2008.[83] The bilateral joint report says that sensitive sectors, industrial imports into India and agricultural imports into Japan, should be treated flexibly, but it is hoped that the FTA will cover goods, services and investment.[84] India's strategy with these talks seems to be an attempt to spur greater Japanese investment, particularly in infrastructure,[85] and to leverage its complementarities in software with the

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79 Mukherji is grateful to Aparna Shivpuri Singh for pointing this out to him.

80 "Japan, India adopt FTA report to pave way for negotiation", BBC Worldwide Monitoring, 7/17/2006

81 Ibid.

82 "India wants to start FTA talks with Japan: Singh", Japan Economic Newswire, 9/26/2006

83 "CEPA Agreement Beneficial for India, Japan: Japanese Ambassador", Asia Pulse, 8/9/2006

84 "Japan, India adopt FTA report to pave way for negotiations", BBC Worldwide Monitoring, 7/17/2006

85 "India wants to start FTA talks with Japan: Singh", Japan Economic Newswire, 9/26/2006

Japanese hardware industry.[86] The non-state electronics industry associations of Japan and India have signed an agreement in an attempt to bring more Japanese investment to India; these domestic Indian actors appear to be in favor of greater liberalization.[87]

Indian and Japanese views on Asian trade seem to converge to a greater extent than the views of China and India. While China is keen to develop a free trade area in Asia that would involve itself and the ASEAN countries along with South Korea and Japan, Japan wants a larger area that would also include India, Australia and New Zealand. While India is not enthusiastic about promoting a free trade area with China, it is taking measures to increase its trade with Japan.

In sum, in the post-9/11 era, India has coped remarkably well and has successfully been "catching up" with the flurry of bilateral and minilateral East Asian-based economic cooperation initiatives. Its liberalization project also appears to be moving relatively well. Whether these trends are likely to continue are, of course, unknown, but we can examine these questions in a speculative manner, a task we take up in the next section.

8.4 The Future of India's Trade Policy: Scenarios

How is India's trade policy likely to evolve over time? Clearly, making predictions is not easy as some significant shocks could once again dramatically alter both the security and economic context in which India is operating. What we have seen to this point is that India's trade policy has been a product of dramatic changes in the security and economic environment. In terms of the driving force behind policy changes, in all three post-shock periods (Cold War/Balance of Payments crisis; Asian financial crisis; and 9/11, U.S. TPA, and Indo-Pakistan security issues) the primary combination of factors has been India's changing economic and security position, combined with elite-led strategies. What is most striking in view of the research described here is the *absence* of a significant pro-trade coalition. The sectors with some weight that are in favor of liberalization are the ones such as the software and services sector and the pharmaceuticals sector. The National Association of Software and Services Companies is one example of pro-trade industry association. Given the greater weight of protectionist propensities in Indian industry, any changes in the trade balance that adversely affects Indian industry leads to protectionist pressures. This absence of a deep-seated commitment to

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86 "Japan, India adopt FTA report to pave way for negotiations," BBC Worldwide Monitoring, 7/17/2006

87 "Japan, India sign electronic goods treaty Bilateral Trade", Financial Times (Asia Edition), 9/7/2006

market opening and elite-led bilateral strategies that are often focused on security casts doubt on the long-run ability of India to conclude and implement strong bilateral and minilateral trade liberalization.

In looking at the future of India's trade policy, we cannot predict major shocks that might radically alter its path, but we can consider several factors that might influence future outcomes. First, it is likely that the U.S. focus on fighting terrorism will continue, leading to stronger links between security and trade issues. With respect to economic institutions, the Doha Round of the WTO remains troubled, while U.S. trade promotion authority will expire in the summer of 2007. APEC is unlikely to be dramatically revived as a trade forum, and thus the bilateral and regional focus looks to be well entrenched. Given India's interest in the U.S. for security and trade, it is likely that it will forge closer trading ties with the U.S. even though a free trade agreement may not be politically feasible.

From a security perspective, the nuclearization of the subcontinent has led to a standoff that may increase the willingness of both India and Pakistan to work out their outstanding conflicts. Indeed, the recent overtures toward reconciliation between India and Pakistan appear to have advanced and India was confident enough to not oppose Pakistan's admission to ARF in 1994. India still seeks to become a UN Security Council member, along with other contenders, but this does not appear to be the most important factor driving its security strategy. And in its relations with the U.S., the American interest in fostering a power to balance China leads it to look favorably on India's rise. Moreover, with India's own longstanding battle against terrorists, the U.S. and India have a strong alignment of interests on this dimension. Improved Indo-U.S. relations have had a positive impact on Indo-Pakistan relations.

From an economic perspective, India maintains a strong position and is increasingly seen to be a driver of regional growth in Asia and possibly the global economy as well. There has been some backlash against job outsourcing in the U.S. and a corresponding fear that high-paying American jobs will shift to high-paying industries to India, but with American multinationals rushing to enter the Indian (and Chinese) market, there is a strong countervailing force in the U.S. against anti-Indian protectionist pressures.

In terms of India's own domestic liberalization strategy and elite commitment, its focus on becoming a global power, increasing its economic weight in world affairs, and continuing on its rapid growth path has prevented the formation of a significant counter-liberal coalition. Despite changes in government, there have been few changes with respect to the overall economic strategy and the strategy of major firms in India except at the margins. Yet while there is little pressure for a return to the policies that created the "Hindu" rate of growth, the drive to liberalize has been primarily elite-led. It remains to be seen if a powerful business coalition will continue to grow and sustain an activist outward trade orientation that goes beyond framework arrangements to real trade liberalization.

While India's globalization, aided by a small pro-trade coalition, is likely to push the technocratic elite toward agreements with ASEAN, BIMSTEC, and Japan, opposition from protectionist lobbies could delay the process. India's trade surplus with neighbors such as Sri Lanka and Bangladesh is becoming significant.[88] The recent unilateral concessions made by India for the least developed SAARC countries will benefit Bangladesh. This could be a way of wooing Bangladesh toward closer trade ties with India in light of improved security relations between the two countries in recent times. Despite some warming of Indo-Pakistani relations, substantially improved trade ties between the two countries will probably need to wait for further improvement in security relations.

Finally, in terms of institutional architecture and trade, India is likely to continue its strong focus on East Asia and continued effort to become an integral part of the dynamic Asian economy. Its relations with China on this score are surprisingly good, and there is increasing talk of a China-India FTA. For now, the trade figures on both the export and import side suggests that continued exchange and economic cooperation is likely to continue. If this is the case, Pakistan will potentially be further marginalized in this new economic dynamic relationship, particularly if the U.S. reduces its anti-terrorist activities in that region. Of course, security concerns between India and China, and between the U.S. and China, have by no means abated and thus for the foreseeable future, an India-China FTA is unlikely.

8.5 Conclusion

We have argued that the shift in India's trade policy from import substitution toward trade promotion resulted in part due to changes in the external context and in part due to domestic changes in elite views about the need for export orientation for India's development. The paper suggests that trade and security concerns are intimately connected. External shocks may alter security considerations, which affect the trade potential; they may also directly alter expectations about the need for a preferential trading engagement. These variables explain the persistence of the autarkic phase, the drive to export orientation, and subsequently greater dependence on bilateral and minilateral trade promotion measures. The nature of goods provided by the bipolar or unipolar world orders in the realm of security and trade generated the international context within which India strategized its trade. For example, multilateralism may lead to

[88] Mukherji (2006:103-115)

the provision of club or public goods such as trade rules within the WTO but its failure to contribute to trade promotion could lead to the proliferation of minilateralism or bilateralism.

The Cold War balance and India's import substitution reflected the convergence of India's security and economic needs. Strategic relations with the USSR and the lack of need to pursue trade as a route to development complemented themselves well. For example, India's trade with the USSR was substantial, and its need for markets in countries with ties to the U.S. such as the ones in Southeast and East Asia was not significant. India's trade within South Asia with neighbors with closer ties to the U.S. was insignificant during the Cold War.

External shocks such as the end of Cold War created a situation where India could not depend on the security benefits derived from the Cold War balance of power. By this time, there had occurred enough internal thinking within the Government of India to convince the technocrats that import substitution was no longer a viable development strategy. Moreover, the Gulf War-driven oil shock, which brought India very close to a balance of payment default, drove home this point in a very telling manner. In the changed scenario, when the USSR as a security and trading partner became much less important, India was drawn closer to the U.S. and its allies in both security and trade. India was offered dialogue partner status in ASEAN and membership in the ASEAN Regional Forum, neither of which had materialized during the Cold War years.

The Asian financial crisis and India's nuclear tests were drivers for the search for bilateral trade agreements within South Asia, culminating in the Indo-Lanka Free Trade Agreement. The crisis hurt India's exports to Southeast and East Asia because of economic decline coupled with the devaluation of currencies of the countries in the region. The nuclear tests and consequent U.S. trade sanctions increased India's resolve to conclude a preferential trade agreement with Sri Lanka. Indo-Lanka relations had improved considerably after the assassination of Rajiv Gandhi by the LTTE. The ILFTA was a model of asymmetrical concessions that India was willing to make in search of markets at a time when the markets for Indian exports seemed restricted elsewhere.

The post-Cold War security and trade context did not change but the global trend toward bilateral and minilateral agreements in the context of the failure of the multilateral negotiations pushed India toward bilateral and minilateral agreements. This coincided with the post-9/11 period when U.S. security concerns focused more on combating terrorism than containing China. India successfully signed its most comprehensive preferential trade agreement with Singapore (CECA) in 2005 and another with Thailand in 2003. India was actively negotiating an agreement with ASEAN and had participated in the East Asia summit. It was also working toward preferential agreements with Japan and New Zealand, while its trade relations with China had become cordial. India was negotiating an agreement along with other BIMSTEC countries, comprising countries in the Bay of Bengal region, Bhutan and Nepal.

External shocks have helped changed the strategic and economic context. The domestic context also changed with a technocratic view in favor of trade promotion supported by export-oriented sectors like services, software and pharmaceuticals. The interests of these sectors were in opposition to the majority view within Indian industry, used to years to import substitution. The changed international and domestic context first pushed India toward trade promotion with the U.S. and countries friendly to the U.S. Subsequently, when the multilateral system seemed inadequate for India's trade promotion, it pushed for bilateral and minilateral agreements. External shocks and the changed domestic political economy favoring trade promotion will remain important considerations for understanding the trajectory of India's trade policy given the complementarity between strategic and economic considerations.

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