**Speech by Amb. Sujan R. Chinoy,**
**Director General, Manohar Parrikar Institute for Defence Studies and Analyses (MP-IDSA)**
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**On**
**'India's Prospects in Resilient Supply Chains: Challenges and Opportunities'**

Mr. Tetsuya Watanabe, Vice President, Research Institute for Economy, Trade and Industry (RIETI),

Mr. Noriyoshi Fukuoka, Director, South West Asia Office, Trade Policy Bureau, Ministry of Economy, Trade and Industry (METI),

Good morning.

It is an honour for me to be invited today to deliver a talk on "India's Prospects in Resilient Supply Chains: Challenges and Opportunities". I had the pleasure of informally exchanging views with Mr. Watanabe. We both felt that think-tanks in India and Japan should engage with one another to develop research and support the efforts of the two Governments and industry to enhance cooperation in the field of resilient supply chains.

**What is Resilience in Supply Chains?**

In my view, resilience in supply chain management relates to the ability to create supply chains and invest in ensuring that the effects of costly disruptions are delayed or avoided altogether, and, in the event that disruption cannot be avoided, to ensure the capability to respond appropriately and recover in the shortest possible time.

Disruptions in supply chains can be natural or man-made, or sometimes both together. Permit me to explain this with examples. Disruptions caused by natural calamities are commonly experienced around the world. Japan has seen the unfortunate effects of the Great Tohoku Earthquake of 2011, followed by the Tsunami which led to a nuclear disaster. The economic disruption caused by power outages, breakdown in infrastructure and non-availability of labour and raw materials resulted in a major setback. For example, it led to a sharp drop in Japanese automobile exports to the US.

Man-made disruptions in supply chains are also a part of the globalised economy. For example, terrorist drone attacks on ARAMCO's oil refineries at Abqaiq and Khurais in Saudi Arabia in September 2019 suddenly resulted in a drop of 5.7 million barrels of oil per day, amounting to nearly fifty percent of its production capacity. It led to a steep plunge in Saudi Arabia's stock market, besides leading to a sharp spike in global oil prices. Apart from terrorism, there are other man-made disruptions such as wars. You are all aware how global oil supplies were disrupted during the Fourth Arab-Israel War, better known as the Yom Kippur War in October 1973, when the Arab countries imposed an oil embargo on many countries for their support of Israel.

As a major trading nation that is reliant on imports of virtually every raw material, including energy, Japan is no stranger to the vagaries of supply chain disruptions. As the world's second-largest developed economy, with cutting edge technologies and large outlays on R&D, Japan has mitigated the impact of disruption through innovation.

**Supply Chain Politics**

Today, globalisation is being redefined. Not every country has fully benefited from the rapid integration of the global economy. Some have taken greater than their fair share, by gaming the system. China has utilised the liberal global trading system to create monopolies and dependencies. Without being a market economy, China has exploited its membership of the World Trading Organisation since 2001 to become a factory for the world. It has hollowed out domestic manufacturing capacities in many countries by exporting cheaper products, with hidden subsidies. It practices its own brand of “state capitalism”.

China has long practiced “supply chain politics”. Japanese entrepreneurs are fully aware of how detention of a Chinese fishing trawler captain in 2010 near the Senkaku Islands resulted in the Chinese government blocking exports to Japan of rare earths used in the production of electronics, hybrid cars, wind turbines and guided missiles.

Friends, the entire world is reeling from the widespread effects of the COVID-19 pandemic. The global economy has suffered a major downturn, just as multilateralism has also suffered retrenchment on account of the politics of the pandemic. The priority in every country is to stimulate economic recovery.

An inadequately prepared global community was taken by surprise by the pandemic. Likewise, the global economy was also taken by surprise when the pandemic-related lockdowns in China at the start of the year caused major disruptions in global supply chains. The adverse effect was felt across the board, not only in the supply chains emanating from China but also elsewhere. In India, the Japanese companies felt the disruption in the automotive, electronics and white goods sector, including for components such as a/c compressors and motors for washing machines. Globally, the temporary trade restrictions and shortages of pharmaceuticals and critical medical supplies such as ventilators and personal protective equipment enhanced vulnerabilities.

The disruptions, already being felt due to the US-China trade war, were compounded by the politics of the pandemic, economic nationalism and trade protectionism. Suddenly, it felt as if the world was moving in an opposite direction from free trade and the liberal global trading order.

Taking into account China’s unacceptable trade practices, unilateralism, assertive behaviour and its militarisation, the US government has imposed restrictions on export of microchips to China's biggest semiconductor manufacturer, SMIC, following assessment that there was an "unacceptable risk" that equipment supplied to it could be used for military purposes. Leading Chinese companies such as Huawei and ZTE have not been spared.

The trend towards greater weaponisation of trade and technology is likely to continue in future. The incoming Biden administration in the US, in my view, is unlikely to be in a position to roll back the export control restrictions already in place without compromising on US security considerations.

It is in this milieu that India, Japan and Australia agreed in September this year to work together to achieve supply chain resilience in the Indo-Pacific. This is a great initiative which is expected to look at possibilities to reduce undue reliance on any one country or geography for sourcing products or materials. Automobiles and parts, petroleum, steel, textiles, financial services and IT are some of the focus sectors identified under the Supply Chain Resilience Initiative (SCRI). This initiative is expected to contribute to the global risk mitigation strategies of not only companies of Japan, Australia and India but also other nations operating in the Indo-Pacific.

Friends, geo-politics and geo-economics can never be truly separated. It is a myth to imagine that one can have truly stable economic relations with any nation in the absence of stable political ties. It is worse still to base a nation's strategic calculus on the presumption that trade and economic ties can remain normal in the face of territorial and geostrategic contestation. This is what Henry Kissinger called the "principle of linkage" in his analysis of US relations with the Soviet Union. When the Nixon administration came to power in 1969, the Soviet Union was keen on some trading arrangements with the US and western economies. The Soviet Union wanted access to certain technologies too, such as computing. Yet, it was unwilling to relent on strategic and military issues, whether in terms of the arms race or its interventions in places as distant as Vietnam or Angola. Kissinger clearly pointed out that to 'separate issues into distinct compartments would encourage the Soviet leaders to believe that they could use cooperation as a safety valve while striving for unilateral advantages elsewhere'.

Over the last several decades, China has also been using this very policy, of trying to maintain normal trade and economic engagement to its advantage, without moderating its behaviour on political, strategic and territorial issues. In fact, China has developed into a fine art the ability to use deeper economic engagement with countries like Japan and Australia to weaken their resolve on political and strategic issues.

**Japan's Strategy For Ameliorating Supply Chain Disruption**

Recently, both on account of the US-China trade war and the supply chain disruptions occasioned by the pandemic, Japan has earmarked US $2.2 billion for an economic stimulus package to help Japanese companies shift production out of China. As you all know, US $ 2 billion has been earmarked for companies to shift production to Japan and another US $ 200 million for those moving production to ASEAN, India and Bangladesh.

Since the normalisation of diplomatic ties, Japan's economic ties with China have deepened tremendously. Japan has invested hundreds of billions of dollars in the Chinese economy. Much of the growth of Japanese companies comes from their manufacturing facilities and supply chains in China, whether for export of parts to their facilities in third countries or exports to markets around the world. In such a situation, it is difficult to achieve decoupling in a short span of time. It may not be entirely feasible in some sectors either. However, a pragmatic global risk mitigation strategy requires that entrepreneurs must not “put all their eggs in one basket”. This means that supply chain disruption can be reduced, or even avoided altogether by creating new supply chains through active relocation of manufacturing facilities, investing in transfer of technology and skilling manpower in alternative destinations. A certain amount of planned redundancy, or overlap in supply chains, may also be necessary as insurance against disruption.

Japanese companies have shown a capacity to pursue such a strategy for quite some time now. Japan has pursued the China Plus One, also known simply as Plus One, as a business strategy to avoid investing only in China and to diversify investments to other countries, particularly to ASEAN. In recent years, this strategy has been expanded to include South Asia, notably India.

In Phase-1 of the Relocation Package, which was worth US $ 653 million, one notices that 89 Japanese companies/projects availed subsidies to shift out of China. Of these, 57 companies relocated to Japan, 30 moved their manufacturing to Southeast Asia and 2 companies transferred manufacturing to India. These two are Sumida Corporation, a large company in the auto components sector, and Toyota Tsusho Co. Ltd., which is also a large company in the rare earths sector. This is a good decision, but I also noticed that a very large number of small and medium enterprises (SMEs) went to Southeast Asian countries such as Vietnam, Thailand and Malaysia. I am not surprised that Japanese companies should look favourably at Southeast Asia. After all, Japanese entrepreneurs are more familiar with these countries and also find the business environment quite welcoming. But I do feel that companies in the field of healthcare and medical devices, especially those manufacturing PPEs, such as Plus Co. Ltd, Yokoi Sada Co. Ltd would have benefitted more by shifting to India, which offers a much larger local market, as well as lower labour costs for manufacturing for exports to global markets.

Over the years, Japan has emerged as one of the largest investors in the Indian economy, with cumulative investments of US $ 33 billion. Japan is present in every large infrastructure project and is a key player in every flagship programme in India. Its contributions are especially valued in the automotive sector, skill development and the digital and start-up space. A panoply of agreements has facilitated a growing relationship in electronics, healthcare, agriculture and food processing.

**India’s Case**

In the aftermath of the pandemic, India has taken several measures to support investors. India has announced production-linked incentive schemes in 11 key sectors: these are advance chemistry cell battery, telecom and networking products, textile products, pharmaceuticals, medical devices, food products, high efficiency solar PV modules, automobiles and auto components, electronics and technology products, speciality steel and white goods such as air-conditioners and LEDs. India’s Foreign Trade Policy for 2015-2020 has also been extended, to continue incentives under various export promotion schemes under the existing provisions for one more year. India has given particular emphasis to boosting these 11 sectors.

I also believe that India offers many new opportunities in EDTECH, FINTECH and remote working tools as we all make a transition to the new normal created by the pandemic, such as working from home. EDTECH will see millions of young people across the world, about 770 million according to an estimate by the United Nations, turn to companies that offer online learning. India has one of the world’s largest populations of young people, with 60 percent below the age of 35 years. Indians can offer online English language classes to Japanese students and vice-versa. FINTECH, likewise, is likely to rely even more on the digital space in the future. Even healthcare will have to adapt to the new digital norm for conducting online consultations and treatment.

## Opportunities Await Japanese Entrepreneurs

I wish to say a few words about some of these key sectors in India in which opportunities await Japanese entrepreneurs.

## Automotive Sector

India is the 4th largest automotive market as well as the 5th largest producer of automobiles in the world. The Indian automotive industry contributes about 7.5 percent to India's GDP. The Indian auto components sector accounted for 2.3 percent of India's GDP and 25 percent of its manufacturing GDP. It employs about 5 million people in India. The pandemic caused a breakdown in global supply chains in the automotive sector since most manufacturers had concentrated their facilities in China which suddenly went offline earlier this year. China also accounts for 27 percent of India's imports of automotive parts, and this also includes some components required by Japanese auto companies based in India. This was definitely a wake-up call for all, given the sudden shortage of parts, especially braking components, electrical components, interiors and lighting fixtures.

Japanese companies such as Suzuki have achieved global recognition as a brand due to their presence in India. Suzuki contributed greatly to the development of vendor supply chains in the automotive sector in India. Overall, the setback due to the pandemic is expected to be short-lived. The Indian automobile industry is set to grow stronger, once the growth rate of 18.3 per cent achieved two years ago is regained. Moreover, the market is also expected to grow with the rapid expansion in the road network across India.

## Healthcare Sector

The medical device industry in India is currently worth US $ 11 billion with an estimated growth rate of 15.8 percent. India currently has about 800 medical device manufacturers. What is noteworthy is that despite being the 4th largest market in Asia, India has an import dependency of 80 percent. Among the biggest exporters to India in this field are China, US, Germany, Singapore and Japan. I believe this is not sustainable. I believe this is the right time for Japanese companies to ramp up their presence in India to fill this gap through local manufacturing. There are many Japanese SMEs which can no longer sell their medical devices in Japan due to changing standards and regulations. They can no longer make fresh investments to compete for the market in Japan. Such SMEs should be encouraged to relocate to Japanese townships, special investment parks and plug-and-play facilities in India. Overall, by investing in supply chains in India in the field of medical devices, I am confident that Japan can increase its share of the global market, which currently stands at about 4 percent, as compared to 29 percent for the US, 13 percent for France, 12 percent for UK, 11 percent for Germany and 8 percent for China.

**ESDM Sector**

One of the most important sectors for building resilient supply chains is the ESDM industry, short for Electronic System Design and Manufacturing industry. India's electronics industry was worth US $112 billion in 2017-2018. Its size is forecast to grow to US $ 400 billion by 2024, at a rate of 26.7 percent. Moreover, India's consumer electronics industry is huge and fast-growing, with many opportunities for Japanese companies to expand their presence in India. India currently produces consumer electronics, medical electronics, industrial electronics, automotive electronics, telecom products and related IT hardware.

The government of India has taken additional measures to ensure India's emergence as a major global manufacturing hub for ESDM. Today, India is poised to increase its presence substantially in the global supply chains by attracting the semiconductor components and packaging industry to the country, while building a robust ecosystem of domestic companies engaged in the manufacturing of printed circuit boards (PCBs), active and passive components, electromechanical and wound components. As Indian electronics manufacturing moves from completely knocked down (CKD) assembly to high value addition, components and semiconductors are being targeted through a slew of policy measures in the National Policy on Electronics of 2019, including capex and production linked incentives, conformance to standards, trusted value chains, etc.

We should make greater efforts to take advantage of the MoU concluded between India Electronics and Semiconductor Association (IESA) and Japan's Asia Semiconductor Trading Support Association (ASTSA).

## Steel Sector

The steel sector is also important. India is the world's second largest producer of steel with an output of 112 million tons of crude steel in 2019. It accounts for 2 percent of India's GDP. With major thrust on infrastructure and the housing sector, the demand for steel is only going to rise further.

## Atma Nirbhar Bharat (Self-Reliant India)

Friends, Prime Minister Mr. Narendra Modi announced in his address to the nation on 13 May 2020 the theme of "*Atma Nirbhar Bharat*". It literally means "Self-reliant India". Under this scheme, India has provided a robust framework for combining reforms with plans for long-term development. The five main pillars of the scheme are Economy, Infrastructure, System, Demography and Demand. A special economic stimulus package of about US $ 268 billion, equivalent to 10 percent of India's GDP, has been announced to mitigate the adverse impact of the pandemic and lockdown. This will dovetail into the effort for imparting a renewed impetus to Make In India 2.0.

## Defence Sector

Our defence and security cooperation is also a crucial pillar of our bilateral engagement. Today, the Indian government is seeking to provide a big boost to defence manufacturing in India under the Make in India programme. It has identified 101 items of which it will not permit imports, covering a vast range of defence items and equipment including important weapons systems. There is a tremendous opportunity for Japanese companies to enter into JVs and tie-ups with reputable Indian defence manufacturers. A second list may also be put out soon for even more sophisticated items. The key question is whether Japanese companies are ready to risk entering into JVs or 100 per cent investments in India in this sector without any guarantee of contracts beforehand. They will have to bid like any other company in a tendering process and prototypes made in India will have to pass the tests. They will be competing against companies from US, UK, France, Israel and other places which are very familiar with the Indian defence sector. Japanese companies need to think big and out of the box. They cannot be in this space if they always expect G2G contracts of the type they are used to in the protected Japanese environment. Most Indian majors would prefer to have the Japanese as partners provided the costs of technology and production in India can remain competitive. We already have a Defence Industry Forum to advance mutual understanding between defence industries of Japan and India. This Forum can be activated for this purpose.

I must make it clear that the push for self-reliance in India is not an autarkic policy. It does not imply foreclosure of the Indian economy to foreign trade and participation in the global economy. On the contrary, it is aimed at strengthening India's capacities to participate more vigorously without being prey to supply chain disruptions.

India has the capacity and the potential to become one of the world's largest destinations for investments, and one of the world's largest manufacturing hubs, in the aftermath of the pandemic. Pharmaceuticals is one such area in which India is clearly a major global player.

Friends, due to lack of time, it will not be possible for me to take a deep dive into every sector. Suffice it to say, the time is ripe for India and Japan to work together to create new, reliable and durable supply chains. We can make modest beginnings in a few sectors that are mutually beneficial.

Two years ago, when I was still there in Japan as Ambassador, the CEO of Sushi Zanmai chain of restaurants Mr. Kiyoshi Kimura had met me and spoke of the depleting Tuna reserves around Japan. We had discussed the advantages of Sushi Zanmai collaborating with the fisheries department in the State of Tamil Nadu in India to equip local fishermen with Japanese fishing equipment and preservation technologies to augment their Tuna catch for consumption in Japan. This is an example of creating resilient supply chains for Japanese consumers for something very close to their heart, i.e., Sushi and Sashimi.

As a former ambassador of India to Japan, I remain deeply committed to the promotion of our ties in every field, especially our economic engagement. Forging a new partnership in the creation of resilient supply chains will add a new dimension to our Special Strategic and Global Partnership.

Thank you.

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