

FT BIG READ. GLOBAL TRADE

New Delhi's severe restrictions on investment, parts and personnel from its larger neighbour risk stifling its ambitions to become a manufacturing superpower on its own terms.

By Chris Kay and John Reed

At a testing facility near the town of Cheyyar in India's southern Tamil Nadu state, a new generation of Mahindra Group vehicles are being put through their paces.

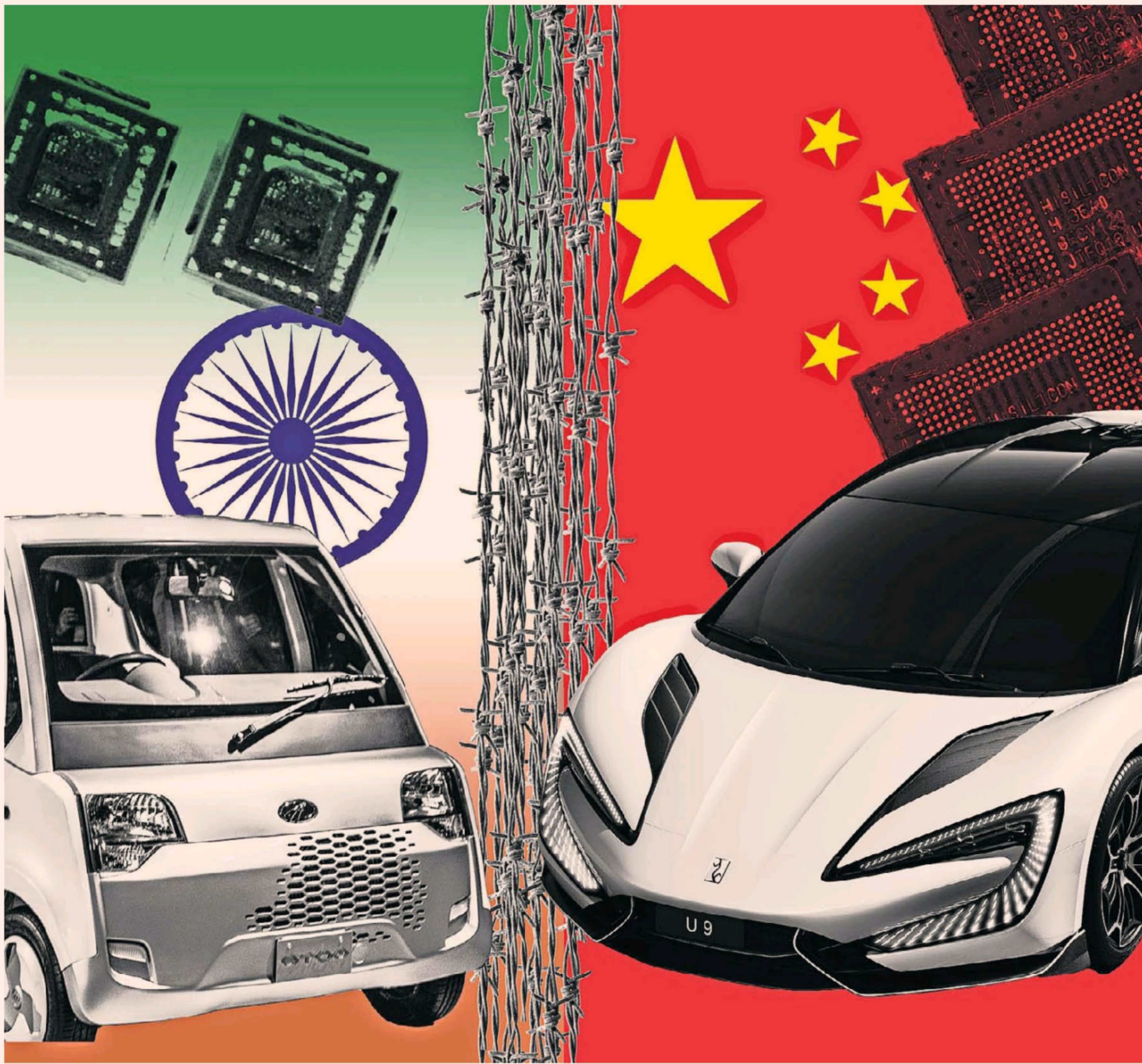
The carmaker's latest flagship sport utility vehicles whizz around a high-speed racetrack with sheer banking slopes, muddy off-road courses, and potholed lanes designed to simulate Indian roads. At the company's nearby research centre, electric vehicle prototypes due to be released early next year are being fine tuned and equipped with the latest digital technology.

Mahindra's futuristic fleet attests not only to a rising automotive sector in India, but to Prime Minister Narendra Modi's Atmanirbhar Bharat Abhiyaan, or "Self-reliant India", campaign.

EVs are one of the industrial sectors, alongside advanced batteries and microchips, to which the Modi government has devoted billions of dollars of "production-linked incentives" or PLIs — sweeteners for companies that pledge to "Make in India", in the words of one of the leader's top slogans.

After missing out on the export-led growth spurt that lifted China's economy over the past three decades, India is determined to catch up with its neighbour and rival — but strictly on its own terms. That has translated to some of the harshest restrictions on Chinese inward investment of any major world economy.

Since 2020, companies with Chinese shareholders have needed to apply for permission from New Delhi to invest



months fast-tracked the provision of visas for Chinese citizens whose work falls under the rubric of India's PLIs.

According to a second government official, there is a split within the establishment. The ministries of foreign and home affairs support a more hawkish stance, while economic technocrats argue for more flexibility.

"Over time we have convinced them we would not be doing ourselves any favours if they didn't provide visas for engineers," the bureaucrat says. "It would be self-harm on our part."

With perhaps more success, New Delhi appears to have been pushing some Chinese investors that want to work in India into joint ventures with local interests — an echo of Beijing's own past policy of demanding tie-ups in sectors like carmaking to ensure a transfer of skills and intellectual property.

In March, China's SAIC Motor, which owns the MG brand, announced a partnership with Indian steelmaker JWS to produce and sell cars in India. A number of the mainland Chinese companies that supply Apple via its Taiwanese contract manufacturers have also formed JVs with Indian partners and received government approval, Indian government officials told the FT, although it is unclear how many are actually operating.

But, at the end of July, India's commerce minister Piyush Goyal told reporters that the government was not rethinking its overall hawkish stance on Chinese investment.

"India will probably make exceptions, but there is unlikely to be a blanket lifting of restrictions," says Madan at Brookings.

"India's competition with and concerns about China will persist."

Meanwhile, some companies are quietly working to extricate themselves from Chinese supply chains.

Tata Power is manufacturing some of the core building blocks for Indian green power at a solar panel factory that opened in March. While the cells that go into the modules are mostly still made in China, that is about to change. Tata is opening its own solar cell unit in Tirunelveli this month, after which it will be relying on made-in-India cells only.

"We will stop importing the cells," Praveer Sinha, Tata Power's chief executive, tells the FT. "We need the security of supply."

In its push to create new supply chains not reliant on China, New Delhi has allies — notably in Washington, which is working more closely than ever with India to develop alternatives: The US International Development Finance Corporation last year approved \$425mn in financing for the Tirunelveli plant.

India's government extended PLI subsidies to support the factory, which also won incentives from Tamil Nadu, one of India's most business-friendly states. Those ramp-ups will aid India's goals to become domestically self-sufficient in the coming years, according to the National Solar Energy Federation of India.

"Undoubtedly India is headed towards a position where in the next two to three years we will be decreasing our dependence on China to a larger extent," says Subrahmanyam Pulipaka, chief executive of the lobby group.

India's economic survey also pointed to other manufacturing growth in areas such as toys, with Chinese imports falling from \$214mn to \$41.6mn in the past decade.

Yet in other industries, the subsidies do not appear to be working their magic. Shipments of bulk drugs and precursors from China for finished pharmaceuticals grew 5.9 per cent in the most recent financial year.

Even those that import little or nothing from China, such as the Serum Institute of India — the world's largest vaccine producer — believe local manufacturers in the short term will remain dependent on cheaper raw materials from across the border.

"Whether they're in vaccines or pharmaceuticals, they need to be conscious of their margins," Adar Poonawalla, Serum's billionaire scion and chief executive, tells the FT.

However, he adds, "over time I see a major shift coming. In five years' time, if you were to ask me the same question, you're maybe going to see half the dependency at least."

That transformation is already being actively pursued at major Indian companies, including the Mahindra Group, whose executives are contemplating setting up a domestic EV battery plant.

"The goal is very clear," says Anand Mahindra. "We will have to try to become a more value-added player in the global supply chain, particularly in areas where China has a stranglehold."

# Can India's economy thrive without China's help?

'China is not a market economy and yet the world has given it the benefits of one. They have flooded our market with their goods'

India, so the expertise has to come from somewhere," says one executive.

Anand Mahindra, the billionaire chair of the eponymous conglomerate, acknowledges it is "not going to be easy" for India to go it alone. "There's going to be an enormous pull for India, an enormous call for India to move much more swiftly on trying to become a substitute for China," he tells the Financial Times.

Inside India's government, a debate is under way about whether or not the restrictions are an own goal for a country that aspires to build an export-driven manufacturing sector to rival other Asian powerhouses. Officials privately acknowledge that to become a credible "China plus one" manufacturing destination, India — paradoxically — needs key inputs from China.

The government's annual economic survey released in July argued it was "inevitable" that India would have to plug itself into China's supply chains to meet that aim.

But even amid a growing corporate clamour to loosen the restrictions on Chinese capital, anti-China sentiment remains high in New Delhi, which has refused to reset relations with Beijing until normality is restored at their frontier.

As India's foreign secretary S Jaishankar asked a corporate audience in May, "would you do business with someone who has barged into your turf?"

India's rethink of its relationship with China dates back to 2020, when its economic and security circumstances altered dramatically.

The Covid-19 pandemic was then laying bare India's reliance on China for about 70 per cent of its bulk drugs — such as paracetamol — and ingredients, after shortfalls from its neighbour caused a drop in medicine supplies.

At around the same time, bilateral relations deteriorated after Indian and Chinese troops clashed on the disputed border in the Himalayan region of Ladakh, killing at least 24.

Even before the Ladakh skirmishes, New Delhi had sought to "curb opportunistic takeovers/acquisitions of Indian companies" due to the pandemic. In a measure dubbed Press Note 3, India made all investments by "land border-sharing countries" subject to government approval and introduced a bureaucratic process that Indian policymakers themselves privately acknowledge is opaque.

While the measure made explicit reference only to Bangladesh and India's arch-enemy Pakistan, it was widely understood as primarily a defence against China. "China's Covid-era actions and the border crisis have been an inflection point in how Delhi saw economic ties with China," says Tanvi Madan, senior fellow at the Brookings Institution in Washington.

"The goal hasn't been decoupling but de-risking, with the idea being to

identify and reduce or mitigate India's vulnerabilities, particularly in critical sectors and build a more resilient economy."

Yet officials acknowledge the moves are not only about Indian weaknesses but also Chinese strengths. "China is not a market economy and yet the world has given it the benefits of a market economy," one senior Indian official told the FT last year. "They have flooded our markets with their goods."

India's soaring import bill is indeed in part due to Chinese dumping as its economy slows, says Nandita Rajhansa, economist at Marcellus Investment Managers in Mumbai. "They have a lot of capacity, but no one to consume within the country," she says. Indian companies should "take that as an opportunity, get raw materials really cheap . . . then obviously they gain benefits from scale."

New Delhi's hawkishness seems prescient at a time when the EU, US and others are also taking measures to build resilience against China in areas such as chips and EVs. But inside the Indian establishment, doubts are increasingly being voiced about the wisdom of the government's anti-China stance.

"There is a general discussion going on whether Press Note 3 should be done away with, whether it's harming the setting up of manufacturing here," one government bureaucrat says. "If you want Apple here and you don't get suppliers here, value addition will always be low."

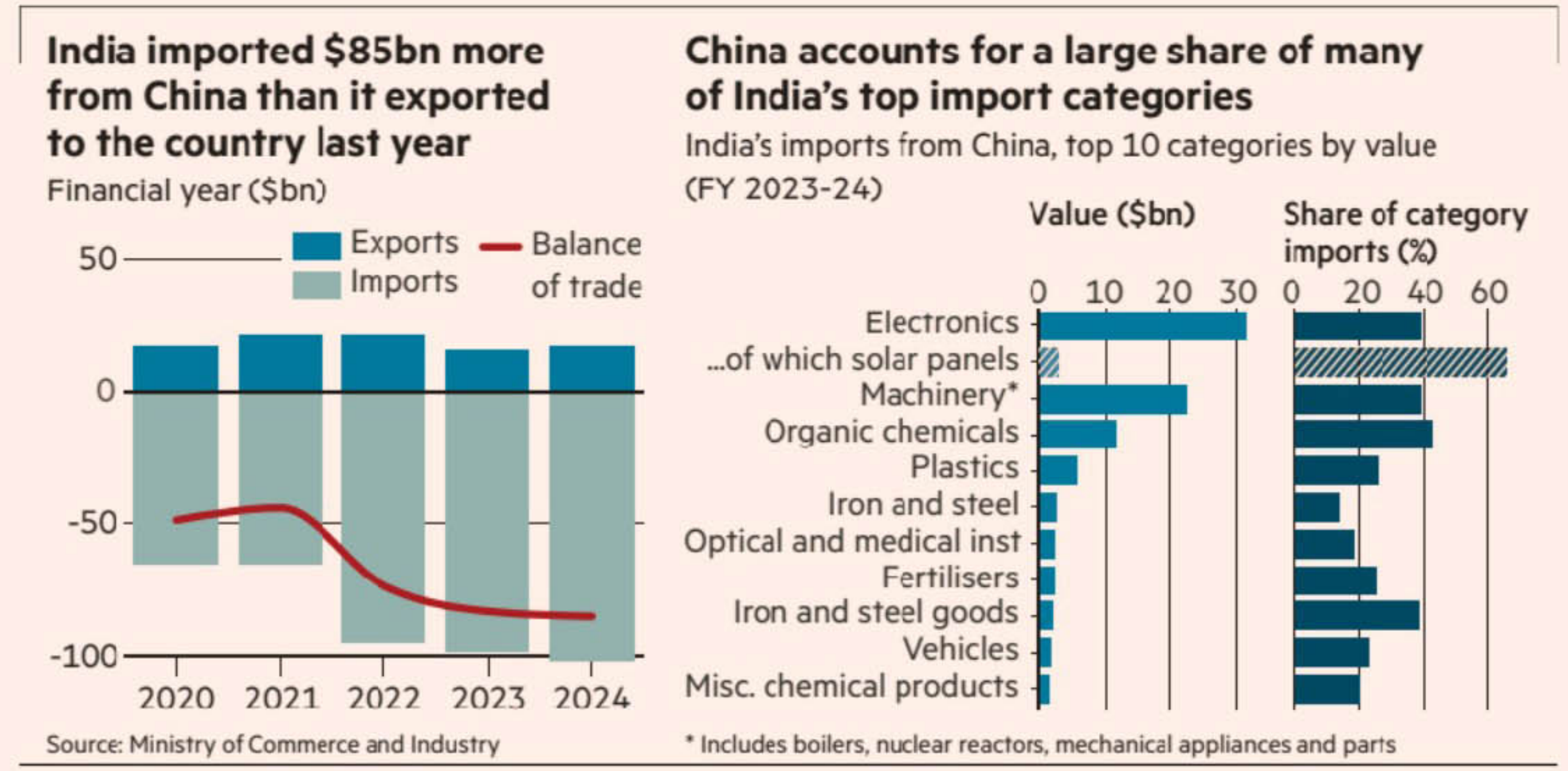
In June the electronics industry complained about a backlog of thousands of visas for Chinese engineers and technicians. Pankaj Mohindroo, chair of the Indian Cellular and Electronics Association, told the FT that the bottleneck was hitting not only Chinese companies, but American, British, Taiwanese, Japanese and domestic firms that are building capabilities in India and need Chinese experts to set up or run their lines.

According to three government officials, Luxshare, the Chinese manufacturer that supplies Apple, was thwarted by Press Note 3 in its attempt to expand its operations in India, and instead shifted its planned investment to Vietnam. In a partial course correction, Modi's government has in recent

Indian carmaker Mahindra's futuristic fleet, left, attests to Prime Minister Narendra Modi's 'Self-reliant India' campaign. The nation has refused China's dominant EV carmaker BYD, right, permission to build a factory, as well as taking protectionist steps in such fields as advanced batteries and microchips

FT montage/Getty

'The political messaging contradicts economic demands. Eventually, India cannot do without economic ties with Beijing'



in India — and this has rarely been granted. BYD, the Chinese EV behemoth that increasingly dominates world markets, is among the companies the Modi government has refused permission to build a factory.

At the same time, India has outlawed dozens of Chinese apps, while launching a tax and legal crackdown on Chinese mobile phone producers. Indian officials boast of being the world's first country to have banned the China-owned social media app TikTok. India has also cut back visas for Chinese nationals, making it one of Asia's few countries where they are a rare sight.

These moves come against the backdrop of a long-standing Indian penchant for protectionism, a toxic border dispute with China in the Himalayas, and mounting paranoia over the security risks of allowing Beijing a free hand in its consumer markets, companies, and high tech.

But some critics are warning that India's tough line on China could stave it of the capital, components and know-how needed to realise its ambition of becoming a major manufacturing power.

Even as the Modi government strives to restrict the flow of Chinese investment and visitors, Indian companies remain heavily dependent on Chinese imports. Mahindra's EVs — for all their localised ingenuity — use battery cells made by BYD and imported from China.

Chinese goods dominate other industries too, from solar panels to the active pharmaceutical ingredients that go into drugs. In the latest financial year, India's imports from China hit a record \$101.7bn, a 66 per cent rise since the same period seven years ago. China has now supplanted the US as the country's top trading partner.

"The shrill rhetoric against China has created a situation where there is an incongruence between political messaging and economic requirements, and this contradiction is placing New Delhi under stress," says Sushant Singh, lecturer in South Asian studies at Yale University. "Eventually, India cannot do without close economic ties with Beijing."

A backlash is forming in the business community. Some argue the Modi administration's Sinophobia is working at cross purposes with its industrial ambitions in sectors such as consumer electronics. They say tough rules are keeping out suppliers and technicians serving companies like Apple, who have faced long delays in obtaining visas.

Top conglomerates from Adani Group to Tata Sons are among those pushing for visa access for Chinese workers needed to install machinery or design plants. "This [industry] never existed in