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BILATERAL TRADE BETWEEN INDIA AND CHINA: ISSUES AND CHALLENGES

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Abstract: *The present study is an attempt to identify the areas which may be targeted to fill the gaps between the bilateral trade of India and China. The study is planned to be subdivided into six sections. Section 1 deals with the general features of bilateral trade between these economies along with the brief review of literature. Section 2 presents an overview of Indian and Chinese economy. Section 3 deals methodology and data sources. Section 4 is associated with bilateral trade status between India and China. Section 5 deals with the analysis of Revealed Comparative Advantage between India and China for the selected commodities. The last section deals with the findings and suggestions.*

Keywords: *Bilateral Trade, Revealed Comparative Advantage, Export*

JEL Classification: *F14, F15, F17*

1. INTRODUCTION

As a result of the leading economic dynamism in India and China, the literature comparing the two Asian giants has expanded substantially. The most dramatic success story in India-China relations is in the economic area. Both economies are growing fast. The gap between China's explosive growth and India's has narrowed, but it appears unlikely that India will overtake China's economic size in the next few decades. India and China continue to attract high rates of investment. This paper attempts to analysis the bilateral trade with the help of RCA via using the Comtrade Database published by UNCTAD. The selected literature reviewed for this study includes the study conducted by Anjali Tandon (March 2012),B.P. Sarath Chandra (2010), Balassa, Bala (1959), Kumar, N (2002), NCAER (2005), S. K. Mohanty (2013). These studies examines the significance of trade between India and China through trade intensity, competitiveness, trade elasticity, trade complementarities and trade similarities.

In this paper, the basic objectives are to understand the trade structure and trade policies in India and China and to examine the revealed comparative advantage (RCA) in terms of the selected commodities for India and China over the period 1999 to 2012. Following this introduction, Section 2 presents an overview

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of Indian & Chinese economy. Section 3 deals with research methodology and estimation procedure. Section 4 is related with bilateral trade relationship between India and China. Section 5 examines the analysis of Revealed Comparative Advantage (RCA) for India over China and for China over India during the period for the selected five commodities. The selection of the commodities is done on the basis of the trade performance between India and China during 2012. The conclusions and suggestions are presented in the last section.

2. AN OVERVIEW OF INDIAN AND CHINESE ECONOMY:

Growth momentum of the Indian economy has been susceptive to the global business cycle as shown. During the periods 2001-2002 and 2008-09, India's growth performance was limping as compared to the years of buoyancy from in the global economy. Average GDP growth declined to 6.5 per cent during 2008-09 from 9.5 per cent during 2005-07. The speed of recovery in India was slow in comparison with China, though both countries revived from the global recession in 2010. With a rebounding of the economy, India could post a robust GDP growth of 10.1 per cent in 2010, allowing per capita income to rise from $1077 in 2009 to $1371 in 2010. During the last decade, India increased its global share in World Gross Product from 3.7 per cent in 2000 to 5.5 per cent in 2010. Simultaneously, exports and imports picked up, registering double digit growth rates in this year.

However, the surge in the external sector performance of India is considerably below its potential. Strong inflationary pressure grappled the Indian economy during 2008-10, leading to a surfacing of numerous macro-economic imbalances in the domestic economy. Until 2005, India's rate of inflation was under the permissible macro-economic ceiling of 4 per cent. With the onslaught of recession in 2008, the current imbalance as a percentage of GDP went up to -2.6 per cent in 2010 from -1.0 per cent in 2006. In value terms, current imbalance grew from $8.1 billion in 2007 to $44.3 billion 2012, registering a CAGR of 75.1 per cent during the period 2007-12. Therefore, India's recovery in 2012 is coupled with macro-economic instability, which is reflected in the macro-economic indicators as showed in Table 1.

China has increasingly attracted the attention of the global economic community during the last three decades due to its excellent track record in maintaining a high growth rate unparallel in the annals of the world economy. Since 1980, China has been maintaining an average GDP growth of about 9 per cent per annum and has taken major strides in elevating large sections of its population above the poverty line. During the period of global buoyancy which spanned the year 2003 to 2010, its GDP growth rate accelerated to more than 10 per cent per year, while its highest growth rate in recent time was recorded in 2007 as shown in Table 1. The reoccurrence of the Global Financial Crisis in 2008 tapered global economic activities substantially. However,

Table 1
Selected Economic and Social Indicators for India and China

Macroeconomic Indicators	*2000*	*2001*	*2002*	*2003*	*2004*	*2005*	*2006*	*2007*	*2008*	*2009*	*2010*	*2011*	*2012*
						China							
Growth Rate, GDP (%)	8.4	8.3	9.1	10.0	10.1	11.3	12.7	14.2	9.6	9.2	10.3	9.5	9.0
GDP per capita PPP, (In $)	2379	2616	2882	3217	3614	4102	4748	5550	6187	6794	7544	8394	9204
GDP, current prices (US$ Billion)	1198	1325	1454	1641	1932	2257	2713	3494	4520	4991	5878	6988	7744
GDP per capita, current prices (US$)	946	1038	1132	1270	1486	1726	2064	2645	3404	3739	4382	5184	5716
Population (Million)	1267	1276	1285	1292	1300	1308	1314	1321	1328	1335	1341	1348	1355
GDP share of world total, PPP (%)	7.1	7.6	8.0	8.5	8.9	9.5	10.1	11.0	11.7	12.9	13.6	14.4	15.1
Inflation, average CPI (%)	0.4	0.7	-0.8	1.2	3.9	1.8	1.5	4.8	5.9	-0.7	3.3	5.5	3.3
Export volume of goods (%chg)	26.6	8.5	21.7	27.8	28.6	23.7	20.8	18.1	8.3	-10.7	24.2	15.6	12.2
Import volume of goods (%chg)	27.9	11.7	20.7	31.5	23.1	11.8	11.8	8.0	3.4	2.1	22.0	16.5	12.4
Current account balance (% GDP)	1.7	1.3	2.4	2.8	3.6	5.9	8.6	10.1	9.1	5.2	5.2	5.2	5.6
Current account balance (US$ Bill)	20.5	17.4	35.4	45.9	68.7	134.1	232.8	353.9	412.4	261.0	305.3	360.5	431.6
GDP based on PPP (Billion Int $)	3015	3339	3702	4158	4698	5364	6241	7334	8216	9068	10120	11316	12470
GDP, constant prices (LC Billion)	5216	5649	6163	6779	7464	8307	9362	10691	11718	12798	14120	15457	16855
						India							
Growth Rate, GDP (%)	5.8	3.9	4.6	6.9	7.6	9.0	9.5	10.0	6.2	6.8	10.1	7.8	7.5
GDP per capita PPP, (Int $)	1534	1599	1673	1798	1973	2190	2441	2724	2916	3104	3408	3703	3971
GDP, current prices (US$ Billion)	476	488	510	591	689	809	908	1153	1251	1265	1632	1843	2013
GDP per capita, current prices (US$)	465	467	481	549	630	729	807	1009	1081	1077	1371	1527	1646
Population (Million)	1024	1044	1060	1076	1093	1110	1126	1142	1158	1174	1191	1207	1223
GDP share of world total, PPP (%)	3.7	3.8	3.8	4.0	4.1	4.3	4.5	4.7	4.8	5.2	5.5	5.7	5.9
Inflation, average CPI (%)	3.9	3.7	4.5	3.7	3.9	4.0	6.3	6.4	8.3	10.9	12.0	10.6	8.6
Export volume of goods (%chg)	13.5	5.9	14.1	12.4	12.9	10.8	6.5	14.8	6.5	5.5	19.9	15.4	14.5
Import volume of goods (%chg)	-3.4	-0.1	8.0	9.4	22.8	15.4	4.9	16.6	14.0	7.6	10.7	11.2	10.2
Current account balance (% GDP)	-1.0	0.3	1.4	1.5	0.1	-1.3	-1.0	-0.7	-2.0	-2.8	-2.6	-2.2	-2.2
Current account balance (US$ Bill)	-4.6	1.4	7.1	8.8	0.8	-10.3	-9.3	-8.1	-24.9	-35.8	-42.8	-40.3	-44.0
GDP based on PPP (Billion Int $)	1571	1669	1774	1935	2157	2431	2749	3111	3377	3644	4058	4470	4857
GDP, constant prices (LC Billion)	25331	26315	27515	29400	31632	34489	37776	41550	44120	47108	51863	55929	60142

Source: RIS based on World Economic Outlook, April 2012, World Bank

China continued to maintain higher growth despite the persistence of a global economic downturn. In the Post-Asian Financial Crisis period, the external sector has emerged as the key source of China's growth, and its exports and imports grew at the rate of 28.1 per cent and 25.4 per cent, respectively during 2003-08 and declined significantly during 2009-10.1

According to the Ministry of Commerce of China (MoCC, 2011), trade in services, which grew at a modest rate earlier, has registered a high growth in the recent years. Foreign direct investment added up to $378 billion cumulatively with about $108 billion in 2008. Rising current account surpluses combined with strong capital flows brought the net international reserves to about $1.55 trillion in 2007, surpassing those of Japan in the present decade.

The resilient Chinese economy dealt with intermittent occurrences of external shocks in recent years. It has effectively coped with shocks for example like the Asian Financial Crisis; the SARs epidemic; several major natural disasters including floods, earthquake, etc. and current episode of global recession, among others.

Therefore, both the economies have performed strongly and competitively in the changing structure of trade at national and international level. Their bilateral trade is growing at a better pace especially since last more than two decades.

3. ESTIMATION: METHODOLOGY AND DATA

3.1. Methodology

There mainly exist two prominent theories of trade based on comparative advantage: the Ricardian theory and the Heckscher-Ohlin (H-O) theory. The Ricardian theory assumes that comparative advantage arises from differences in technology across countries while the H-O theory suggests that technologies are the same across countries. Instead, the H-O theory attributes comparative advantage to cost differences resulting from differences in factor prices across countries. In brief, the predictions of orthodox trade theories are based on the principle of comparative advantage which derives from relative price determination, i.e. differences in pre-trade relative prices across countries, underlined by supply and demand factors. According to the H-O theory, a country's comparative advantage is determined by its relative factor scarcity (i.e. its factor endowment ratios, relative to the rest of the world or a set of countries). However, it is well known that measuring comparative advantage and testing the Hecksher-Ohlin (H-O) theory have some difficulties (Balassa, 1989: 42-4) since relative prices under autarky are not observable. Given this fact, Balassa (1965) proposes that it may not be necessary to include all constituents effecting country's comparative advantage. Instead, he suggests that comparative advantage is "revealed" by observed trade patterns, and in line with the theory, one needs pre-trade relative

prices which are not observable. Thus, inferring comparative advantage from observed data is named "revealed" comparative advantage (RCA). In practice, this is a commonly accepted method to analysing trade data. Balassa (1965) derives an index (called the Balassa Index) that measures a country's comparative advantage. The Balassa index tries to identify whether a country has a "revealed" comparative advantage rather than to determine the underlying sources of comparative advantage. To compare India's and China's competitiveness in world trade, the Revealed Comparative Advantage (RCA) index of the selected commodities has been computed using the Balassa formula. The following formula for the calculation of Revealed Comparative Advantage Index of India over China and China over India has been employed-

$$\mathbf{RCAic = (Xijc / Xitc)/(Xwjc / Xwtc)}$$

Where,

RCAic = Revealed Comparative Advantage Index of India over China in jth commodity

Xijc = Total exports of jth commodity by India to China

Xitc = Total exports by India to China

Xwjc = Total exports of jth commodity by world to China

Xwtc = Total exports of world to China

Simailarly

$$\mathbf{RCAci = (Xcji / Xcti) / (Xwji / Xwti)}$$

Where,

RCAci = Revealed Comparative Advantage Index of China over India in jth commodity

Xcji = Total exports of jth commodity by China to India

Xcti = Total exports by China to India

Xwji = Total exports of jth commodity by world to India

Xwti = Total exports of world to India

RCA is the index which shows the comparative advantage of a country in a particular commodity in world market. Generally, RCA index is taking a value less than one when the commodity's share in a country's exports is less than its share in world trade. This indicates that the country has a revealed comparative disadvantage in that commodity. But, if the index is greater than one, the country has a revealed comparative advantage in the commodity.

RCAab shows comparative advantage of "country a" in a particular commodity in market of "country b". Here we are talking about bilateral trade, so if RCAab

index is less than one we cannot conclude that "country a" has comparative disadvantage in particular commodity in the market of "country b" unless we know the value of RCAba index.

Under the bilateral trade, if RCAab is less than RCAba then "country a" has disadvantage in that commodity in the market of "country b" and if RCAab is greater than RCAba then "country a" has advantage in that commodity in the market of "country b".

3.2. Data Description

In the present study, secondary data have been collected. Major sources of data are online database of World Bank, Database of People's Bank of China, Database of Department of Commerce, India and Database of UN Comtrade. The study is based on the data basically collected from UN Comtrade database.

4. INDIA-CHINA BILATERAL TRADE

4.1. Trends of Bilateral Trade in India

Bilateral trade between India-China has grown rapidly in the past few years and picked up significantly after Chinese accession to WTO. During the period 2001-2009, bilateral trade turnover jumped by nearly twelve and a half times from US$ 3.6 billion to nearly US$ 45.1 billion as presented in Table 4.2. With a conservative estimate, the India-China trade turnover is expected to cross US$ 60 billion in 2010 and further to 125 billion in 2012. China has now emerged as the largest trade partner of India30 since 2008-09.

During the last nine years, exports of India to China have grown at annual rate of 29.8 per cent and by 2009, they formed 7.7 per cent of the total exports. In 2001, China was lagging behind several countries including Belgium and Singapore so far as its share in the total trade of India is concerned. In the same year, China shared 3.5 per cent of India's total trade whereas the US shared 14.4 per cent, the UK 5.1 per cent and Belgium 4.1 per cent of total India's trade. The trade scenario changed significantly in 2009 with a sizable increase in India's bilateral imports. China not only jumped up in its ranking among India's lead bilateral trade partners but also splashed the Indian market with its exports, causing serious bilateral trade imbalances. It is now sharing nearly 9 per cent of India's total trade in 2009. Its current bilateral trade is larger than the combined bilateral trade of Germany, the UK and Japan with India.

4.2. Trends of Chinese Trade with the World

The global business cycle has had a profound impact on the performance of the Chinese external sector. During the slums period of 2001-2003, the average

Table 2
India's Bilateral Trade with China

(In Percent)

Year	*India's Bilateral Export*		*India's Bilateral Imports*		*Total Bilateral Trade*
	Growth Rate	*Share in Total Exports*	*Growth Rate*	*Share in Total Exports*	*Growth*
1999	2.2	1.4	12.5	2.6	9.3
2000	48.4	1.8	16.8	2.9	26.0
2001	103.8	3.4	44.5	3.5	64.9
2002	11.3	3.4	24.3	4.4	18.8
2003	57.6	4.4	43.6	5.0	49.2
2004	54.2	5.5	62.5	6.1	59.0
2005	54.9	6.6	63.4	7.1	60.0
2006	22.2	6.6	59.3	9.0	44.7
2007	28.9	6.6	56.2	10.5	47.1
2008	-5.2	5.4	22.6	10.8	14.5
2009	5.1	6.1	-4.7	11.2	-2.4
2010	74.3	8.1	52.6	12.4	58.3
Average					
1999-2001	51.5	2.2	24.6	3.0	33.4
2001-03	57.6	3.7	37.5	4.3	44.3
2004-07	40.0	6.3	60.3	8.2	52.7
2007-10	25.8	6.6	31.7	11.2	29.4

Source: Direction of Trade Statistics CD, September 2011, IMF, Washington DC.

growth rate of the trade sector was 22.1 per cent per annum on an average, and revived during 2004-07 with an average annual growth rate of 26.5 per cent with global recovery. In the recent episode of recession (2007-2009), the average annual growth rate remained positive, but remained lowest in recent years owing to the negative external sector growth recorded in 2009. The experience shows that the revival of the Chinese trade sector in the post-recessionary period has been very swift in recent years.

One of the important features of the Chinese export sector has been its persistent creation of trade surplus over a period of time despite global recession. The size of trade surplus from merchandise trade was growing at the CAGR of 101.4 per cent during 2004-07. The growth trajectory of trade surplus was so stiff that a negative growth rate was recorded in 2009 after five years of persistently positive growth performance. Though the recession engulfed the world economy in 2009, China continued to generate a trade surplus of US$ 200 billion, covering 16.6 per cent of its exports.

China has impressively integrated itself with the world economy, particularly after its accession to the WTO in 2001. During 1998-2009, world trade grew by 2.3 times, but trade by China grew three times more than that of the global trade. Sparks of such growth performances were felt in both exports and imports of the country. China has gradually improved its global share in exports and imports since the post Asian Financial crisis. In 1998, the country's share in global exports and imports were 3.4 per cent and 2.5 per cent respectively, but these shares increased to 9.7 per cent and 7.8 per cent respectively, in 2009. Interestingly, Chinese share in global trade improved significantly during the period of recession. Chinese exports have been dependent on its imports and opportunities in the import sector have to be explored strategically to have a wider market access in China.

Table 3
China's Trade with the World Economy

(US $ Million)

Year	*Imports*	*Growth*	*Exports*	*Growth*	*Trade Surplus*	*Share of trade surplus to exports*
1998	140358		183751		43366	23.6
1999	165718	18	194941	6.1	29223	15
2000	225175	35.9	249223	27.8	24048	9.6
2001	243567	8.2	266723	7	23156	8.7
2002	295440	21.3	325783	22.1	30343	9.3
2003	412837	39.7	438486	34.6	25649	5.8
2004	560811	35.8	593770	35.4	32959	5.6
2005	660224	17.7	762648	28.4	102424	13.4
2006	791795	19.9	969698	27.1	177903	18.3
2007	956264	20.8	1218700	25.7	262436	21.5
2008	1131920	18.4	1429340	17.3	297420	20.8
2009	1003910	-11.3	120320	-15.8	199510	16.6
2010	1393920	38.8	1580400	31.3	186480	11.8
			Average for the period			
1999-2001	211487	20.7	236962	13.7	25476	11.1
2001-2003	317281	23.1	343664	21.3	26383	7.9
2004-2007	742274	23.6	886204	29.2	143931	14.7
2007-2010	1121504	16.7	1357965	14.6	236462	17.7

Source: Direction of Trade Statistics CD, April 2012, IMF, Washington DC.

5. ANALYSIS OF REVEALED COMPARATIVE ADVANTAGE

In the present study an attempt has been done to examine the RCA of India over China and vice –versa for the period from 1999 to 2012 for the five selected commodities i.e Organic Chemical (HS Code 29), Plastic and articles (HS Code 39), Pearls, precious stones, metals, coins etc (HS Code 71), Iron and Steel (HS Code 72) and Electrical, electronic equipment (HS Code 85).

Table 4
Revealed Comparative Advantage of India over China for the Selected Industries (RCAic)

Year	*Organic Chemical (29)*	*Plastic & Articles (39)*	*Pearls, Precious Stones, Metals, Coins etc (71)*	*Iron & steal (72)*	*Electrical, Electronic Equipment (85)*
1999	3.725003364	0.406855518	0.136835347	0.177252541	0.06652238
2000	3.466037829	1.171340107	0.076304404	0.412725925	0.07892162
2001	2.940742682	1.977050828	0.135573535	0.603161982	0.04210565
2002	2.733414306	1.609995892	0.089871338	3.124193135	0.03163143
2003	1.942551672	1.53476653	0.854519686	5.371829845	0.03758543
2004	1.780853647	1.849451607	0.906398207	2.571425282	0.03341871
2005	1.427721941	0.932944519	0.28219678	2.563964191	0.02492558
2006	1.755482434	1.078100202	0.327027727	2.043127639	0.03116308
2007	1.602415189	0.616436218	0.486689759	1.489338678	0.03457934
2008	1.304121002	0.381107469	0.37715697	0.940278228	0.04211182
2009	1.224364902	0.407328327	16.45107862	1.466191482	0.09918263
2010	1.257132232	0.465780421	0.636615957	2.338179251	0.05253516
2011	1.421618381	0.918219054	0.726105083	2.371275354	0.09724835
2012	2.07464484	1.081106995	0.877141104	1.740322201	0.08116894

Source: Author's own calculation based on Comtrade Database

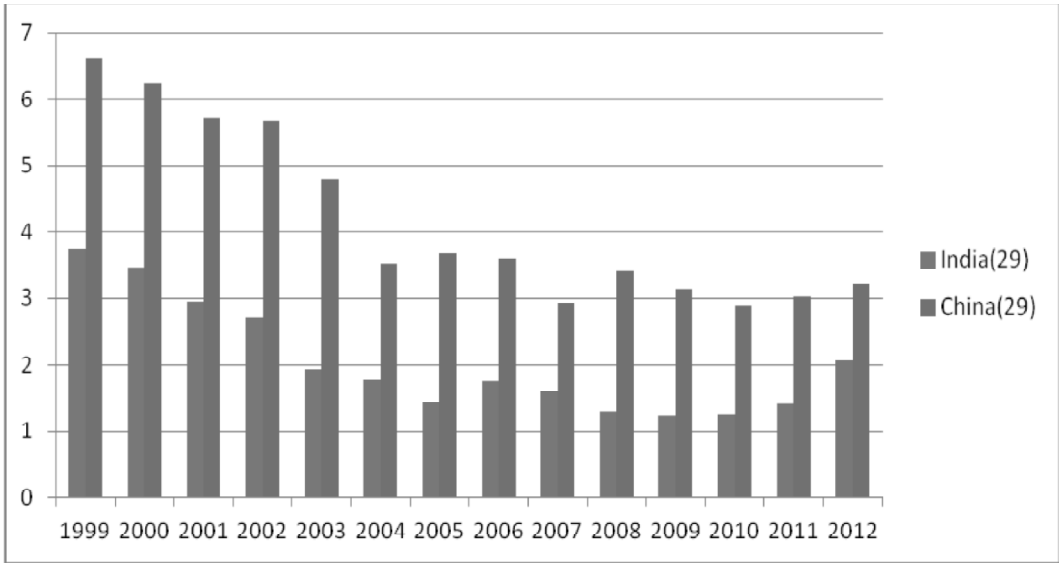
Table 5
Revealed Comparative Advantage of China over India for the Selected Industries (RCAci)

Year	*Organic Chemical (29)*	*Plastic & articles (39)*	*Pearls, Precious stones, metals, coins etc (71)*	*Iron & steal (72)*	*Electrical, electronic equipment (85)*
1999	6.627228756	0.319739229	0.045299746	0.330381	1.796321
2000	6.240264603	0.46354274	0.019334183	0.221864	2.086325
2001	5.705631205	0.468900837	0.093416992	0.164519	2.250181
2002	5.667851349	0.666600713	0.069201764	0.114489	2.792181
2003	4.789129726	1.059218892	0.057706836	0.305872	2.267543
2004	3.535252291	1.310121494	0.028678474	0.529722	2.894357
2005	3.673783497	1.269620463	0.061279382	0.769248	2.564729
2006	3.602662957	1.357150476	0.064895029	1.338827	3.164274
2007	2.929863039	1.501912289	0.048930071	1.586826	3.443616
2008	3.421838322	1.361653303	0.032743253	1.60849	3.728298
2009	3.137890073	0.89668052	0.02070255	0.630159	3.214946
2010	2.883409285	0.984377712	0.009595924	1.622312	3.263694
2011	3.016045271	1.314655724	0.009851227	1.303757	3.049437
2012	3.201006352	1.507892728	0.005709423	1.072126	3.474224

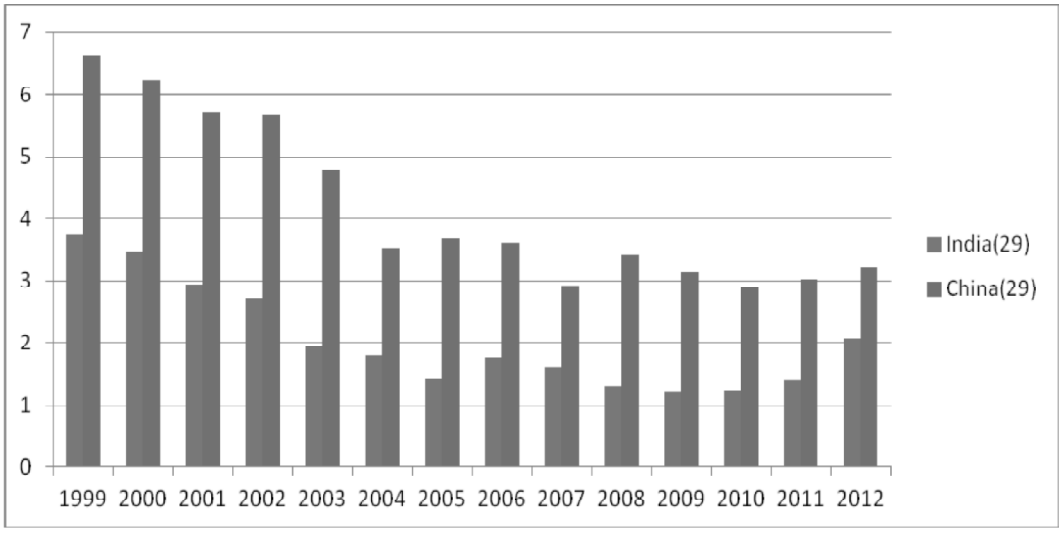
Source: Author's own calculation based on Comtrade Database

As per the Balassa's interpretation of RCA, Under the bilateral trade if the index of RCAic is lesser than the RCAci then "country I" has disadvantages in that commodity in the market of "county c" and if RCAic is higher than RCAci , then "country I" has advantage in that commodity in the market of "country b". On this basis, the interpretation derived from the observation of the Table 3 & 4 along with the above mentioned graphs, the following inferences can be drawn-

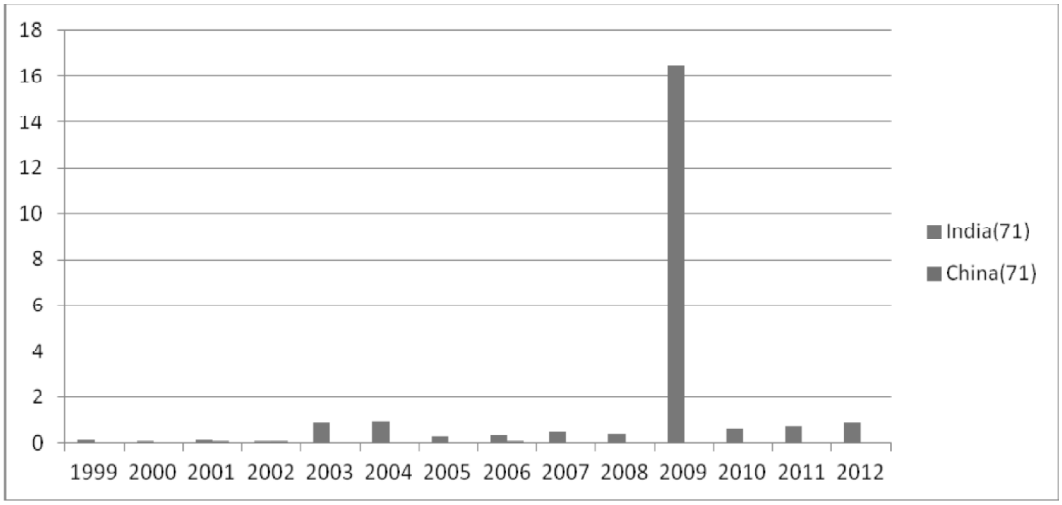
Graph 1: Organic Chemical (HS Code 29)



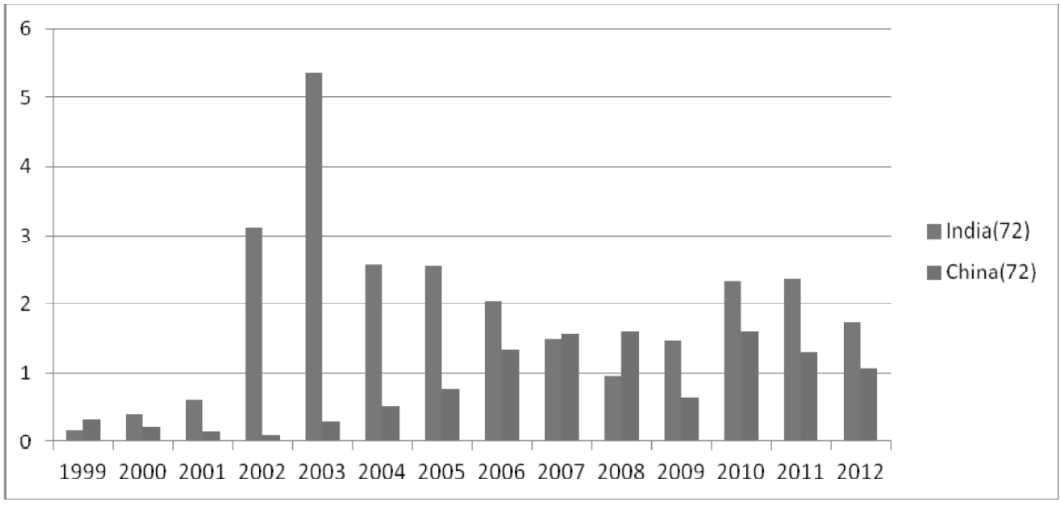
Graph 2: Organic Chemical (HS Code 29)



Graph 3: Pearls, Precious stones, Metals, Coins etc (HS Code 71)



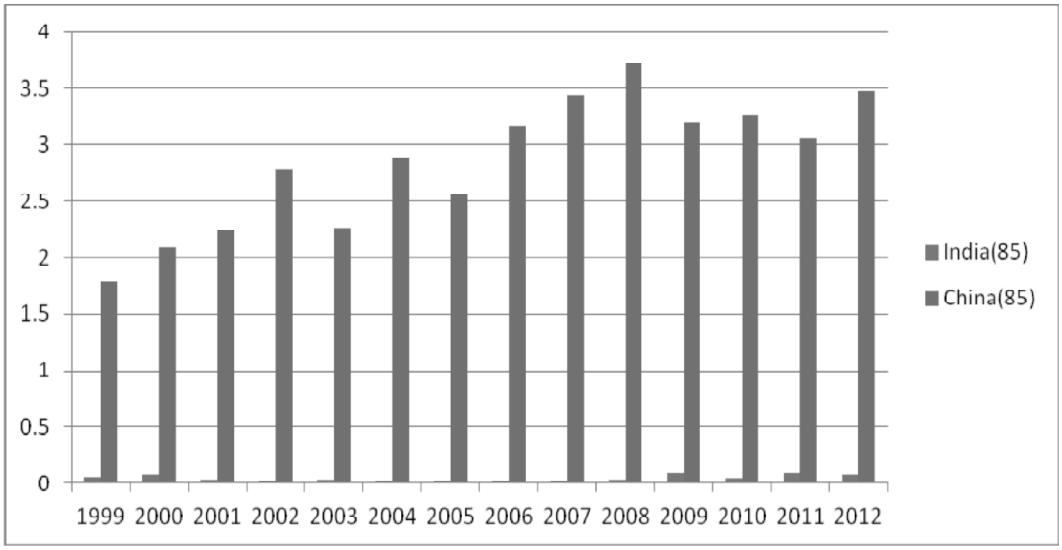
Graph 4: Iron and Steel (HS Code 72)



(i) In case of bilateral trade of Organic Chemical (H S code 29), the RCA index of India over China is regularly lower during 1999 to 2012 than RCA index of the same commodity for China over India which implies that India is having the regular disadvantage in the bilateral trade of Organic Chemicals in the market of China.

(ii) In case of Plastic and Articles (H S code 39), the RCA index of India over China during 1999 to 2004 was performing better. It was higher than the RCA index of China over India. But it is after 2004, the RCA index of China

Graph 5: Electrical, Electronic equipment (HS Code 85)



over India shows some better results resulting the disadvantages to India on regular basis in the market of China.

(iii) In case of Pearl, Precious Stones, Metals, Coins etc (H S code 71), India is having the marginally advantages over China during the period 1999 to 2012 and China is facing the disadvantages in the bilateral trade in Indian market.

(iv) In the bilateral trade of Iron & Steel (H S code 72), the performance of India's bilateral trade is showing better results. The RCA index of India over China is higher that the RCA index of China over India which explain the picture in favor of India.

(v) In case of Electrical & Electronic equipments (H S code 85) the RCA index of India over China is regularly lower that the RCA index of China over India which indicates that for this commodity, in bilateral trade , India is facing the regular disadvantages in the market of China and at the same time China is regularly exploiting the market of India in its favor regularly during the selected period.

CONCLUSION AND SUGGESTION

To sum up, China and India have enjoyed unprecedented economic growth in the past decade. A rapid expansion of bilateral trade has been associated with this growth. A further increase in bilateral trade could be determined by other factors. First, the estimated revealed comparative indices show that India and China are not still trading at as high a level as could be expected.

There is therefore scope for growth in bilateral trade. Second, growth in bilateral trade is also possible if each country exploits its own comparative advantages. There is an overlap only in some commodities, so the two countries can still expand trade in the areas where there is no overlap in comparative advantage. It can be sum up with these words that out of the five selected commodities for this study in which the volume of trade is very high in both the countries, there is need to be more concentration so that maximum advantage can be exploited for both the economics in alternative market.

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