



Delhi Policy Group

Advancing India's Rise as a Leading Power



ECONOMIC SECURITY AND RESILIENCE REVIEW

JULY 2023

Author

V.S. Seshadri

Volume I, Issue 7



Delhi Policy Group

Core 5A, 1st Floor, India Habitat Centre, Lodhi Road, New Delhi- 110003

www.delhipolicygroup.org



Delhi Policy Group

Advancing India's Rise as a Leading Power

Economic Security and Resilience Review

Vol. I, Issue 7

July 2023

ABOUT US

Founded in 1994, the Delhi Policy Group (DPG) is among India's oldest think tanks with its primary focus on strategic and international issues of critical national interest. DPG is a non-partisan institution and is independently funded by a non-profit Trust. Over past decades, DPG has established itself in both domestic and international circles and is widely recognised today among the top security think tanks of India and of Asia's major powers.

Since 2016, in keeping with India's increasing global profile, DPG has expanded its focus areas to include India's regional and global role and its policies in the Indo-Pacific. In a realist environment, DPG remains mindful of the need to align India's ambitions with matching strategies and capabilities, from diplomatic initiatives to security policy and military modernisation.

At a time of disruptive change in the global order, DPG aims to deliver research based, relevant, reliable and realist policy perspectives to an actively engaged public, both at home and abroad. DPG is deeply committed to the growth of India's national power and purpose, the security and prosperity of the people of India and India's contributions to the global public good. We remain firmly anchored within these foundational principles which have defined DPG since its inception.

Author

Dr. V.S. Seshadri, I.F.S (Retd.), Senior Fellow for Economic Security, Delhi Policy Group

The views expressed in this publication are those of the author and should not be attributed to the Delhi Policy Group as an Institution.

Cover Image:

PM Narendra Modi at the inauguration of Semicon India 2023 at Gandhinagar, Gujrat on July 28, 2023. (Source: [PM India Website](#))

Secretary of the Treasury Janet L. Yellen met with Vice Premier of the People's Republic of China He Lifeng in Beijing on July 8, 2023. (Source: [U.S. Embassy & Consulates In China](#))

© 2023 by the Delhi Policy Group

Delhi Policy Group

Core 5A, 1st Floor,
India Habitat Centre,
Lodhi Road, New Delhi- 110003.
www.delhipolicygroup.org

Economic Security and Resilience Review

Vol. I, Issue 7

July 2023

Contents

Introduction	1
China Foreign Relations Law Adopted	2
China places restrictions on export of gallium and germanium	3
Janet Yellen sounds conciliatory but says premature to end tariffs on China	4
Germany releases its strategy paper on China	5
NATO's Vilnius communique pronounces on China's policies	6
Inflation Reduction Act spurs investment surge in the US	6
PM Modi inaugurates Fourth Semicon India conference: More investors show interest	7
Japan and India agree to boost cooperation on semiconductor development	8
India rejects BYDU investment proposal for electric vehicles	8
South Korea hosts fourth Round of IPEF negotiations in Busan	8
Eleventh Round of India-UK FTA negotiations held	8
Rupee trade gains traction with some initiatives	9

Economic Security and Resilience Review

by

V. S. Seshadri

Introduction

China's adoption of its new Foreign Relations Law that has come into force on July 1, 2023 could henceforth sharpen its actions on economic security matters. The law gives China wide latitude with what are regarded as acts detrimental to its interests. The key economic security relevant provisions under this new basic law are highlighted in this month's review. Also covered in this review are export restrictions placed by China on gallium and germanium, with effect from August 1, 2023, that could perhaps affect Indian industry interests. These two critical minerals have applications in the semiconductor making and renewable energy sectors.

US Treasury Secretary Janet Yellen travelled to Beijing adopting a somewhat conciliatory tone and met several of China's top economic leaders. While she said at the end of her visit that her discussions served a step forward to put the US-China relationship on a surer footing, she did not indicate any specific steps that will be taken in this regard. Meanwhile, Germany issued a strategy paper outlining its approach to China on trade and economic issues, which stated that derisking was urgently needed. The joint communique of the NATO Vilnius summit had a couple of critical paras on China, which again pointed to how China sought to control key technological and industrial sectors, critical infrastructure, and strategic materials and supply chains.

Among developments related to India covered in this issue, the foremost is the increasing interest among global semiconductor majors in setting up manufacturing and allied facilities in India in this strategic sector. The memorandum of cooperation signed with Japan on semiconductor development also marked an important step. Significant progress on the IPEF and the India-UK FTA negotiations were also reported, with prospects for their conclusion before the end of this year appearing brighter now.

Finally, India is also seen to be making some progress in its initiative to undertake local currency trade with select partners.

China Foreign Relations Law Adopted

China's National People's Congress (NPC) adopted a new Foreign Relations Law on June 28, 2023 that came into effect from July 1. Conceived as a comprehensive and basic law on its conduct of foreign relations and comprising six chapters and 45 articles, it also deals with any harmful actions against China's interests. The very first article indicates it was drafted inter alia to 'preserve national sovereignty, security and developmental interests' and 'to preserve and develop the people's interests'. Wang Yi, member of the Politburo and Director of the Office of the Foreign Affairs Commission of the Communist Party's Central Committee and now also the Foreign Minister, is reported to have stated that the formulation of the Law will help to expand China's legal tool box and provide a legal basis for opposing hegemonism and power politics, unilateralism, protectionism, and bullying, with a preventive and deterrent effect¹.

Economic commentators have particularly flagged Article 8 of the law, which stipulates that any organisation or individual who committed acts that are detrimental to China's national interests in violation of this law, and other applicable laws, in the course of engaging in international exchanges, shall be held accountable by law. The provision uses broad declaratory language and could be subject to wide interpretation, such as the term 'detrimental to China's interests'.

Article 33 of the new law restates existing legislation on 'counter measures and restrictive measures' and declares that China has the right to take such measures against acts that harmed its sovereignty and developmental interests in violation of international law and fundamental norms of international relations. This could be seen as an enabling provision to take action against export controls, investment screening or other restrictive measures.

Article 32 of the law is regarded by commentators as providing potential for extra territorial application in case of perceived harm against its interests. It stipulates that that China shall, in compliance with fundamental principles of international law and fundamental norms governing international relations, strengthen the perceived implementation and application of its laws and regulations in foreign related fields as well as take law enforcement and judicial measures in accordance with the law.

¹ <https://www.wilmerhale.com/en/insights/client-alerts/20230705-china-rolls-out-foreign-relations-law>

It may be recalled that China had earlier in the year also put into effect an expanded anti-espionage law that introduced the possibility of criminal action against the sharing of information deemed sensitive. There were also some raids on US consultancy companies, including Bain & Co and the Mintz group, and restrictions placed on US semiconductor company Micron Technologies. As per a recent news report,² the revised law and raids have 'businesses scrambling to understand their current compliance footing,' and is driving multinationals in China to separate their technology systems dealing with Chinese data from those covering the rest of the world.

China places restrictions on export of gallium and germanium

In a notice issued on July 3, the Ministry of Commerce of China (MOFCOM) said that starting on August 1, its exporters are required to apply for permission before exporting items related to gallium and germanium. In the application, exporters must provide relevant export contracts, proof of the end users and end uses, as well as information on the importers and the end users. Gallium is used in making semiconductor wafers, in integrated circuits of LEDs, in advanced circuitry, and in solar cells. Germanium is used to produce silicon alloys for high speed devices in electronics, solar applications and fibre optics.

Noting that the move is aimed at safeguarding China's national security and interests, the notice said that for exports of listed items that have a major impact on national security, MOFCOM and other departments will report to the State Council for approval. Asked about the move, Mao Ning, a spokesperson for the Chinese Foreign Ministry, said that it was a common international common practice to implement export controls on relevant items in accordance with the law, and it did not target any specific country.

In an editorial on the issue, the 'Global Times', regarded a voice of the Chinese government, said³ that China's decision was a clear message that it will not passively accept being excluded from the global chips supply chain. It was a practical way to communicate to the US and its allies that their attempts to limit China's access to high technology were a miscalculation. It questioned why China should not make necessary adjustments and exercise caution in depleting its limited resources of rare earths to support those who have aligned themselves with the US-led 'decoupling agenda'. At the same time, the editorial also said that China's imposition of export controls on gallium and germanium products did not necessarily mean a ban on exports of relevant items. The only difference is that China will meet the needs of the international market under

² 'Multinationals in China accelerate push to decouple data' Financial Times 16 July 2023

³ <https://www.globaltimes.cn/page/202307/1293723.shtml>

the provisions of the Export Control Law. If the relevant exports involved military use or are used in scenarios that may undermine China's national security and interests, then the relevant authorities have the right to reject the export application.

For India, the Ministry of Mines has identified both gallium and germanium as among the 30 critical minerals that were announced recently (see ESRR June 2023). India is 100% import dependent on germanium and the Ministry's report puts it as of high supply risk. Its main sources are China, South Africa, Australia, France and the US. As for gallium, the main sources are China, Russia and Ukraine and the metal, obtained as a byproduct of alumina, is regarded as both of high economic importance and of high supply risk.

As per one news report⁴, Japan, Korea and India were the largest importers of the two metals from China amounting to approximately US\$ 200 m, US\$ 170 m and US\$ 165 m respectively in the year 2022. Taiwan (\$ 85 m), Germany (US\$ 75 m) and the US (US\$ 60 m) came next. India's own import figures, however, do not corroborate this.

Janet Yellen sounds conciliatory but says premature to end tariffs on China

The US Treasury Secretary paid a four day visit to China from July 6-9, 2023 when she met with Prime Minister Li Keqiang, Vice Premier He Lifeng, Finance Minister Liu Kun and the Chinese Central Bank head Pan Gongsheng. At the conclusion of her visit, she said that she believed that these discussions served a step forward to put the US-China relationship on a surer footing. In her remarks to the Press,⁵ she also said she communicated to her Chinese counterparts the US desire to have a future of healthy economic competition between the two countries. She further made it clear that the US was not seeking to decouple from China, which will be disastrous for both countries. She drew a distinction between decoupling and diversifying critical supply chains, or taking targeted national security actions. She also pressed US's serious concerns about China's unfair economic practices, including non-market policies, along with barriers to market access for foreign firms and issues involving intellectual property. She further expressed her concern about the recent uptick in coercive actions against US firms. At the same time, she also reportedly told the Chinese leaders that the two sides can work together to

⁴ See 'China's curbs on metal exports reverberates across chip sectors', Financial Times, 4 July 2023

⁵ <https://china.usembassy-china.org.cn/remarks-by-secretary-of-the-treasury-janet-l-yellen-at-press-conference-in-beijing-the-peoples-republic-of-china/>

make sure businesses understand there is a wide swath of economic interactions that are uncontroversial to both sides. When queried about removing the additional tariffs in force on Chinese imports, she said while this was an area in which they could make progress, it was premature to use this as an area of de-escalation at the present time.

Germany releases its strategy paper on China

Germany released its 'Strategy on China' on July 13, 2023, which outlined its future approach towards the country, including on issues pertaining to economic security and resilience⁶. It stated that 'China has changed' adding 'As a result of this and China's political decisions we need to change our approach to China'. The document affirmed that China was leveraging the political, military and economic weight it had gained to pursue its interests on all continents and in international organisations, and was working to reshape the existing rules-based order according to its preferences. It further assessed that China's economic strategy was aimed at making it less dependent on other countries while making international supply chains more dependent on China.

As for how Germany proposes to deal with China, the strategy indicated that the federal government will promote diversification of economic relations so that while Germany continued to participate in China's economic development, there will be a reduction in dependence in critical sectors. The strategy also talked about using market economy instruments to change the incentive structure of German companies in order to make removing unilateral dependencies attractive. It also talks of how state extended investment or export guarantees may be used, investment screening can be strengthened, export controls made more effective, and reciprocal measures at the bilateral and European levels can be used to reduce asymmetries. Derisking, the document makes clear, was urgently needed.

While the approach is somewhat generally worded, perhaps because on trade and investment related issues it is the EU Commission that takes the lead, the document also stated that Germany will align its policy on China with that of the EU and coordinate it more closely with EU partners.

In response, China's foreign ministry has called the strategy counterproductive and accused the German government of protectionism and exacerbating

⁶ <https://www.auswaertiges-amt.de/blob/2608580/49d50fecc479304c3da2e2079c55e106/china-strategie-en-data.pdf>

global divisions. It hoped that Germany will take a comprehensive and objective view of China's development.

NATO's Vilnius communique pronounces on China's policies

The summit meeting of the North Atlantic Council held on July 11, 2023, addressed China's stated ambitions and coercive policies, including on economic security related issues. It said that China sought to control key technological and industrial sectors, critical infrastructure, and strategic materials and supply chains. It used its economic leverage to create strategic dependencies and enhance its influence. It also strived to subvert the rules-based international order including in the space, cyber and maritime domains.

As for the response of the Alliance partners, the communiqué said they were boosting their shared awareness, enhancing their resilience and preparedness, and protecting against China's coercive tactics and efforts to divide the Alliance.

China's Mission to the EU, in its response,⁷ characterised the communiqué as arbitrarily distorting China's stance and policies and deliberately smearing China. It also firmly opposed NATO's eastward movement into the Asia Pacific region, and warned any action that jeopardised China's legitimate rights and interests will be met with a resolute response.

Inflation Reduction Act spurs investment surge in the US

As per a news report⁸, the Inflation Reduction Act (IRA) of the US, which incentivises climate related investments, has spurred nearly US\$ 110 bn in clean energy projects in that country since the Act was passed almost a year ago. Companies from South Korea, Japan and China account for over 60% of those investments. Fifteen of the twenty such large investments are also related to battery factories set up by foreign businesses. It may be recalled here that the India-US Joint Statement released at the conclusion of PM Modi's June visit to the US, also referred to three Indian companies investing over US\$ 2 bn in the US in solar and other energy related sectors.

While Chinese companies, or companies with substantial links to China, account for nearly US\$ 8 bn of such investments in the US, it is not clear how the IRA rules will deal with their products. The US Department of Treasury has proposed that electric vehicles using battery materials that were produced by a

⁷ http://eu.china-mission.gov.cn/eng/fyrjh/202307/t20230712_11112008.htm

⁸ <https://www.wsj.com/articles/the-biggest-winners-in-americas-climate-law-foreign-companies-c672e09d>

'foreign entity of concern' (including China) would not qualify for tax credits beginning from 2025.

PM Modi inaugurates Fourth Semicon India conference: More investors show interest

Flanked by several industry leaders and experts drawn from across the globe, Prime Minister Modi made a strong pitch for global semi-conductor companies to set up manufacturing and allied facilities in India in this strategically important sector. Inaugurating SemiconIndia 2023 on July 28 at Gandhinagar in Gujarat, he conveyed India's commitment to build a semiconductor manufacturing ecosystem. Participating companies included Micron Technology, Applied Materials, Foxconn, Cadence, AMD and Vedanta Group, each of which have indicated keen interest in participation.

While Micron Technology and Applied Materials Inc. had already announced their plans during PM Modi's visit to the US in June (see ESRR June 2023), another US chipmaker Advanced Micro Devices (AMD), which specialises in graphics and high performance computing, announced that it would invest US\$ 400 m in the next five years and will build its largest design centre in Bengaluru. Foxconn, the Taiwanese major which recently pulled out of a chip making venture with Vedanta, said that it will apply for incentives under the government's semiconductor production scheme. Its chairman, Young Liu, said that he was optimistic about the direction and the roadmap of India's semiconductor plan. The Chairman of the Vedanta Group, Anil Agarwal, indicated that the first phase of his group's semiconductor project involving US\$ 5 bn of investment will be ready with made-in-India chips in two and a half years.

In a Press interview⁹, the Minister of State for Electronics and IT, Rajeev Chandrasekhar said that as the first mover, Micron has sent an important signal to other companies, and its announcement is also creating awareness and visibility in the supply chain of fabs and ATMPs (assembly, testing, marking and packaging), be it providers of gas, minerals, equipment or logistics, that they should also explore.

⁹ https://www.business-standard.com/industry/news/chip-makers-in-talks-to-invest-in-india-after-micron-s-announcement-mos-it-123073000433_1.html

Japan and India agree to boost cooperation on semiconductor development

A memorandum of cooperation (MOC) was signed on July 20, between Minister of Electronics and IT, Ashwini Vaishnaw, and the Minister of Economy Trade and Industry of Japan, Nishimura Yasutoshi, covering semiconductor development, manufacturing, research, design and talent development. Under the MOC, an implementation organisation will be created which will present government to government and industry to industry collaborations. Japan has companies which do not just manufacture chips but also provide raw materials such as ingots, wafers, gases and other items.

India rejects BYDU investment proposal for electric vehicles

The Government of India has reportedly rejected¹⁰ a USD 1 billion investment proposal of Chinese electric car maker BYD and its Hyderabad-based partner Megha Engineering and Infrastructures Ltd. (MEIL) to set up an electric vehicle manufacturing plant in Telangana state. The proposal was apparently examined under Press Note 3 of FDI rules, that requires any proposal having investments from countries which share land border with India, to secure government approval. BYD is currently a technology partner to MEIL's Olektra.

South Korea hosts fourth Round of IPEF negotiations in Busan

Republic of Korea hosted the fourth round of the Indo-Pacific Economic Framework (IPEF) negotiations in Busan from July 9-15, 2023. Press statements about the meeting noted that the IPEF partners continued to make progress on the negotiations towards high standard outcomes under Pillar I (Trade), Pillar III (Clean economy) and Pillar IV (Fair economy). The fourth round also advanced the legal review of the supply chain pillar whose negotiations have already substantially concluded. It is learnt that the informal deadline set towards final agreement on all pillars is the November 2023 APEC summit.

Eleventh Round of India-UK FTA negotiations held

The eleventh round of the India-UK FTA negotiations was held in the UK from July 10-18, 2023. It was reported that technical discussions were held across 9 policy areas over 42 separate sessions (including some in a hybrid online manner), which included detailed discussions on the draft treaty text. While earlier reports had indicated that 14 chapters had been substantially closed after

¹⁰ <https://www.livemint.com/politics/policy/govt-rejects-chinese-byd-megha-engineerings-1-billion-proposal-to-set-up-ev-plant-11690200288132.html>

the tenth round, it has now been reported that five more chapters may have been substantially closed following the eleventh round, including those relating to environment, labour and digital trade.

Meanwhile, the twelfth round is to be held from the second week of August, and some reports suggest that the two sides are trying to build consensus on three key topics¹¹ - rules of origin, intellectual property rights and investment treaty. The investment treaty itself will, however, be a separate agreement to be concluded simultaneously with the FTA. The rapid rise in momentum in the negotiations with successive rounds taking place almost every month brightens the prospects for signing the deal before the end of this year.

Rupee trade gains traction with some initiatives

India's new trade policy, that came into effect from April 1 this year, had sought to promote the settlement of international trade in Indian rupees, which can reduce the country's dependence on the US dollar, thus enhancing resilience. Initiatives moving this approach forward have now been taken. Bangladesh and India have started some trade transactions in rupees during the month of July. "The new trading mechanism will increase exports and reduce pressure on the forex market," said Bangladesh Bank Governor Abdur Rouf Talukder. Bangladesh's central bank had also said¹² the transaction costs during trade with India would reduce with the introduction of the Taka-Rupee dual currency card, which was "almost ready to be launched from September."

India and the UAE have also taken some steps¹³ to use the Indian rupee and the UAE dirham for their bilateral trade. During the visit of PM Modi to the UAE on July 15, two MOUs were signed in this regard by the governors of the two central banks:

1. An MOU for the establishment of a framework to promote the use of local currencies for cross-border transactions; and
2. An MOU on interlinking payments and messaging systems.

News reports further indicate that India and Indonesia are discussing a proposal to settle bilateral trade in domestic currencies. The related issues were apparently discussed between India's Finance Minister Nirmala Sitharaman

¹¹ https://www.business-standard.com/economy/news/india-uk-fta-aim-to-build-consensus-on-investment-pact-ipr-in-next-meet-123072800716_1.html

¹² <https://www.theweek.in/wire-updates/business/2023/07/25/ccm3-biz-rupee-trade.html>

¹³ <https://www.mea.gov.in/bilateral-documents.htm?dtl/36813/IndiaUAE+Joint+Statement+during+the+visit+of+Prime+Minister+Shri+Narendra+Modi+to+UAE#:~:text=The%20leaders%20reaffirmed%20their%20joint,%2C%20terrorist%20financing%2C%20and%20extremism.>

and her Indonesian counterpart Sri Mulyani Indrawati on the sidelines of the G-20 Finance Ministers meeting on July 17. An India-Indonesia Economic and Financial dialogue was also launched on the occasion.



Delhi Policy Group
Core 5A, 1st Floor,
India Habitat Centre, Lodhi Road
New Delhi - 110003
India

www.delhipolicygroup.org