

# **Problematic Pivot**

*C.P. Chandrasekhar*

When US President Donald Trump announced in early August that imports from India to the US would be taxed at the rate of 25 per cent (with few exceptions), many were taken by surprise. Given the bonhomie on display between Prime Minister Narendra Modi and Trump, and the willingness of India to align with the US on many international issues, the expectation was that India would quickly secure a trade deal and be let off lightly.

However, India's inability to accede to all demands for market access prevented a deal and precipitated the announcement of a higher 25 per cent tariff on its exports compared with the 10-15 per cent imposed on most countries.

But matters did not end there. A few days later, Trump announced an additional 25 per cent impost on imports from India on the grounds that it was helping finance Russia's war in Ukraine by purchasing Russian crude at low prices. That came as a shock since India is hardly the only country importing crude from Russia.

If it is being singled out, the reasons must go beyond just oil. Imports of military equipment and India's refusal to accept the trade deal offered may have peeved the US President. Whatever the explanation, the Indian government has chosen to stick by its position on crude imports from Russia, possibly because of the powerful business interests any restriction would affect.

The hugely discriminatory tariff imposed on India will have a significant impact on sectors such as textiles and apparel, gems and jewellery, and leather goods as the US accounts for a lion's share of their exports. Their relative competitiveness under a tariff rate that is 30-40 per cent higher than what the competing nations attract would be eroded to such a degree that it would be impossible to compensate for with cost adjustments.

## **For New Markets**

Shocked by Trump's move, India is going all out not just to find new markets but also to send a signal to the US. Besides dropping its reticence on joining more assertive and critical voices in global or regional coalitions, especially BRICS, India is accelerating efforts to normalise and improve relations with China that had weakened and almost broken down after the conflict in the Galwan river valley in Ladakh in 2020. Modi travelled to China after seven years and met President Xi Jinping at the Shanghai Cooperation Organisation summit. Talks on the border dispute, normalisation of diplomatic relations, enhanced people-to-people contacts, and trade are under way between the two countries at multiple levels.

What is unclear is whether this belated turn away from the US towards what could be considered India's natural allies will help. There are four issues here. The first is that most low- and middle-income countries (LMICs) would be looking to diversify away from the US to other markets irrespective of the level of tariff they have been subjected to. In addition, they may turn protectionist to manage any likely deterioration in the balance of payments situation because of a fall in exports to the US. So, replacing the lost US market with exports to those

countries would be difficult. If exports are to recover enough to offset the US shock, the gains will have to come from developed markets such as the EU, Canada, Japan, and Australia.

Second, if India's exports to the LMICs are to increase significantly, a large part of that increase must come from the largest of these markets: China. India's effort at improving trade relations with China is clearly motivated by that objective. However, past trends and indicators of relative competitiveness suggest that India is positioned to be a recipient of Chinese exports rather than a provider of goods and services to that country.

Increased aggregate trade between the two countries could widen the already large deficit in China's favour, with imports outpacing exports. It could also displace some domestic production, compounding the strain on the economy already caused by Trump's tariffs.

Third, the fact that India's first response to the Trump tariff threat was to push for a deal with some concessions baked in could be read as weakness. It is this perception of weakness that probably explains the Trump administration's decision to impose additional tariffs. Trump seems upset with India and, given its weak response, wants to make an example of it. So, the expectation that a pivot on the diplomatic front, especially towards China, would force retraction on the part of the US may be misplaced.

Finally, India's real weakness is its excessive dependence on the US market for exports of software. The US accounted for 54 per cent of the exports of software and IT-enabled services in 2023-24. If Trump is further peeved by India's response to the 50 per cent tariff he has imposed on imports from the country, he could choose to target these exports as well. That could be hugely damaging and hit some very influential companies in the country and India's large youth population that sees finance and IT as preferred avenues of employment and as routes to upward mobility.

In sum, there are no easy solutions here. Not yielding to Trump's demands risks further action that cannot be avoided. But succumbing will only increase the scale and scope of his demands.

It is best to think of ways in which India can leverage its geographical and demographic size to build domestic markets as the basis for growth. The policy should not focus on protecting local manufacturers and increasing exports but concentrate on expanding domestic demand and production for the domestic market. That, however, does not seem to be on the Modi government's agenda.

**\* This article was originally published in The Frontline on September 4, 2025.**