

▶ Chapter 4

US–Indian Relations

—A Multifaced Partnership Under Construction

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1. The history of US–Indian relations

1.1 1947-1990: The Cold War era

US–Indian economic relations were never insignificant following India’s independence, but mutual understanding was lost during the Cold War system, resulting in suppressed progress in the bilateral economic relationship. As a result of India’s adoption of a parliamentary democracy after independence, the US assumed that as a country with the same values, India would naturally adopt an economic policy encouraging free development of corporate activities. As a result, the US had high hopes that India would be one of the powerful countries of the free world under the Cold War system, and provided India with generous support.

By contrast, India was concerned about the intensification of tensions under the Cold War system, and upheld the banner of non-alignment outside of both the Eastern and Western blocs, in addition to domestically adopting a state-led development model. To the US mindset, which believes in clearly defining black and white, India’s external posture of accepting aid from both the US and the USSR as well as its economic policy that was rather controlled were very difficult to understand. From India’s point of view, by contrast, US foreign policy was very intrusive and American capitalism valued materialism above all else, and thus they were not easily assented to.

The Indo–Pakistani hostility led to a still wider gap between India and the US. The US deployed an equidistant diplomacy to India and Pakistan, and at the same time leveraged Pakistan as an anti-Communist bastion. When the Indo–Pakistani War of 1965 broke out, the US, which had maintained amicable relations with Pakistan, temporarily suspended aid to India. Furthermore, at the time of the Indo–Pakistani War of 1971, the US deployed the USS Enterprise, a nuclear-powered aircraft carrier, to the Bay of Bengal to check India. Amidst the Sino-Soviet split and Sino-Indian hostility, the US position of proximity to Pakistan inevitably tilted India towards the USSR. In 1971, the Indo-Soviet Treaty of Friendship and Cooperation was signed, which strayed far from the principles of non-aligned diplomacy. Furthermore, when India set boldly forth with its first nuclear test in 1974, the US formed the Nuclear Suppliers Group (NSG), implementing measures restricting the export of nuclear technology and related equipment to non-signatories to the Nuclear

Non-Proliferation Treaty (NPT), exemplified by India.

1.2 The shift towards closer US-Indian relations

The geopolitical tectonic shift accompanying the collapse of the Cold War system had a large effect on US-Indian relations. To the US, as the sole superpower following the breakup of the Soviet Union, Indo-Russian relations ceased to be a concerning diplomatic issue, and the importance of Pakistan as part of the anti-Soviet alliance dropped. In the post-Cold War world, predicted to be uncertain, the US came to hold higher hopes for India as a regional power indispensable for maintaining stability and balance. An improvement in US-Indian relations was brought about by a number of factors simultaneously even aside from the geopolitical shift. India introduced economic reforms in 1991 as if to match the timing of the end of the Cold War. As a result, India put an end to the closed policies of import substitution and protectionism of domestic industries that had been in place for many years, and made great strides towards economic liberalization with an eye towards global competition. Up until then, the American industrial sector had largely been ignoring India, but as economic liberalization progressed, it has begun seeking large opportunities as a business deployment destination in India, the world's second most populous country.

The IT revolution that began in the 1990s was even more deeply related to closer US-Indian relations. After independence, India adopted an educational policy emphasizing higher education and the natural sciences, as exemplified by the founding of the Indian Institutes of Technology (IITs). As a result, it was possible to produce abundant human resources able to be successful in the software industry.

1.3 Building a strategic partnership

As a result of India going forward with nuclear tests, the US immediately imposed economic sanctions on India, but it is noteworthy that after these sanctions were implemented, high-level strategic dialogue between the two countries continued without pause in an active effort towards mutual communication.

President Bill Clinton's trip to India in March 2000 as the first US president to visit in 22 years was a watershed moment in US-Indian relations. It can be said that the aim of President Clinton's visit was to indicate that US diplomacy in South Asia would be very different from what it had been during the Cold War era. The fact that he stayed for only five hours in Pakistan while visiting India for a period of five days truly indicates a clear stance by the US government of placing importance on India.

The sanctions on India did not have any effect on India's GDP growth rate, and were abandoned in 2001.

The following three points can be noted as lying in the backdrop to the US leaning closer towards

India. First, in addition to the importance of economic relations with India rising through IT outsourcing, India has a middle class that rivals that of the US, and it is predicted that its population and economic growth will surpass those of China in the long term; there is a high likelihood that it will provide the most important market to the US. Second, both India and the US are at the front lines of the war against Islamic extremism, and cooperation with India has been becoming indispensable in waging the war against terror since 9/11. Third, with an eye towards a rising China, strengthening ties to India as large democracy alongside the US has been kept firmly in mind as a shared fundamental interest for maintaining and reinforcing an international order backed by open, democratic values.¹

1.4 Signing the US-India Civil Nuclear Agreement

Restrictions on access to cutting-edge technology that were more strict than those on China had been placed on India with respect to atomic power. This was particularly the case in the field of atomic energy, which the US hoped was a potential new market.² As it became clear that India's exclusion from the international nuclear order would be an obstacle towards progress for a US-Indian strategic cooperative relationship, President Bush reversed the Western policy up to that point and deployed a bold campaign, bringing India into the nuclear club and working hard to make India have responsibilities and duties.³

On the other hand, India had established the Atomic Energy Commission immediately after independence, treading its own path towards atomic development. India had consistently objected to the NPT (Non Proliferation Treaty), which only approved the five permanent members of the US Security Council (including China) as “nuclear-weapon states,” and so after its nuclear test in 1974, it was cut off from relationships of nuclear cooperation with other countries. In order to meet burgeoning electricity demand, the Indian government had high hopes for nuclear power, establishing the goal of expanding capacity to 20,000 megawatts by 2020 and 63,000 megawatts by 2032, and supplying 25% of total power generation by 2050. Building more domestically-produced reactors (heavy water reactors) would not be sufficient to expand nuclear power generation, and so there was the awareness that obtaining higher performance large uranium-fueled reactors (light water reactors) from overseas was indispensable.⁴

The US-India Civil Nuclear Agreement was announced by Prime Minister Manmohan Singh and President Bush in July 2005. Thereafter, vigorous activities were deployed in both countries towards its implementation aiming for obtaining domestic agreements and international

¹ Twining (2011)

² Pacific Council on International Policy and Observer Research Foundation (2005)

³ Twining, *op.cit.*.

⁴ Kaneko (2009).

recognition. In the US, new legislative measures were necessary to allow the exception of nuclear cooperation with India as a non-signatory to the NPT. As a result, the United States-India Peaceful Atomic Energy Cooperation Act (the Hyde Act), which included a revision to the US Atomic Energy Act, was submitted, and passed into law in December 2006. When the contents of the proposed US-India Civil Nuclear Agreement were publicized in August 2007, strong opposition was expressed by the opposition parties as well as the Communist Party, which had been cooperating with the government from outside the cabinet. In response, Prime Minister Manmohan Singh bet the survival of his administration, facing a confidence vote in the parliament in July 2008, and succeeded in attaching confidence to the nuclear agreement negotiations.

Later, the agreement was approved by the International Atomic Energy Agency (IAEA) Board of Governors in August of the same year, and in September, a waiver for India was unanimously approved at a special NSG meeting due to the vigorous lobbying by both India and the US. In response, both houses of Congress in the US approved the agreement, and it came into force in November of the same year.

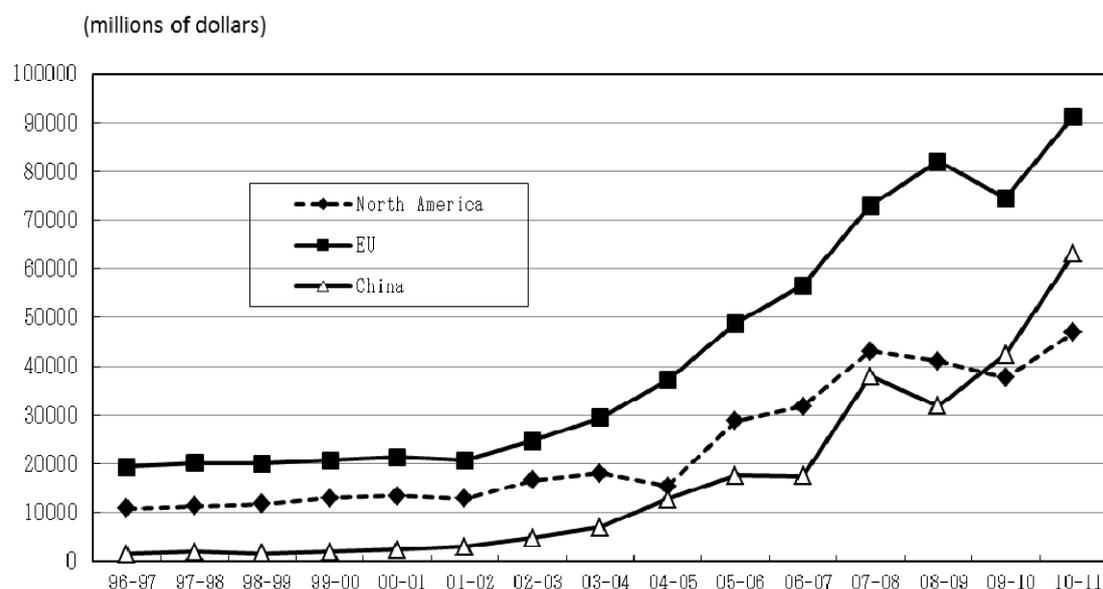
2. Trade and investment

2.1 The direction of trade

After independence, India's most important trade partner by country was the US for many years. India's trade with the US amounted to \$10.2 billion in fiscal year 1996, but expanded to \$45.6 billion in 2010. When looking by region, the EU was India's largest trade partner through the 1990s, exceeding Asia. However, with the sequence of events from the Look East policy, East Asia's share gradually expanded, surpassing that of the EU in fiscal year 2001. Although the pace of expansion of trade with North America has been quickening since the dawn of the 21st century, its share of India's overall trade has been trending downwards in relative terms (see Figure 4.1). Traditionally, US-India trade greatly surpassed India-ASEAN trade, but since 2004, the latter has passed the former.

India's service exports to North America are very large, and IT-BPO exports easily exceeded \$35 billion in 2010. The US is still the largest trade partner for India when looking at trade in products and services overall.

Figure 4.1: India's Primary Trade Partners



Source: Ministry of Commerce and Industry, Export and Import Data Bank.

Amidst a chronic deficit in India's balance of trade (trade in goods), trade with the US has consistently been a surplus for the Indian side. In fiscal year 2010 as well, imports from the US amounted to \$20,050.72 million, while exports totaled \$25,548.30 million (see table 4.1).

Particularly notable among the items exported to the US are pharmaceuticals. Previously, foreign corporations had been crushing Indian firms in the pharmaceuticals market, but the Patent Act was established in 1970, recognizing process patents instead of the usual substance patents. As a result, a number of manufacturers emerged producing copied drugs based on reverse engineering, and the drug manufacturing abilities of India as a whole were raised greatly. Meanwhile, India became the dominant country for the low-cost manufacture of generic drugs, for which patent protection has expired, and has enjoyed this advantage. In 2007, Indian production facilities approved by the US Food and Drug Administration (FDA) reached 119, the greatest number overseas. The US is the most important export destination for Indian pharmaceuticals, making up 19.1% of total pharmaceutical exports in 2007.⁵

⁵ Ministry of Commerce and Industry (2008)

Table 4.1: Breakdown of Primary Products in Indian Trade with the US (FY 2010)

Exports to the US					Imports from the US				
Rank	Item Name	Value (\$ millions)	YOY Growth (%)	Share (%)	Rank	Item Name	Value (\$ millions)	YOY Growth (%)	Share (%)
1	Precious Stones and Jewelry	5,284	11.5	20.7	1	Precious Stones and Jewelry	2,792	85.5	13.9
2	Apparel related articles	4,282	13.0	16.4	2	Machinery	2,564	-0.5	12.8
3	Steel and Steel Products	2,348	31.4	9.2	3	Aircraft	1,594	-32.9	7.9
4	Pharmaceuticals	1,771	41.7	6.9	4	Electronic Machinery	12,662	6.0	6.3
5	Electronic Machinery	1,333	32.7	5.2	5	Optical Equipment and Fixtures	1,157	15.4	5.8
6	Organic Chemicals	1,231	13.4	4.8	6	Oil and Petroleum Products	1,133	36.2	5.6
7	Machinery	1,177	32.7	4.6	7	Fertilizers	901.8	-10.2	4.5
	Total	25,549	30.8	100.0		Total	20,051	18.2	100.0

Source: Ministry of Commerce and Industry, Export Import Data Bank.

Currently, problems such as expanded access to the agricultural market, child labor problems, and anti-dumping are frequently discussed as trade problems between India and the US.

2.2 The direction of investment

Looking at foreign direct investment (FDI), the US was the greatest supplier of FDI to India since the economic reforms were introduced in 1991, excepting Mauritius which is used as a tax haven. Cumulative US FDI in India totaled \$12.3 billion from April 1991 to March 2007. Since 2007, although US FDI in India has continued to expand except for fiscal year 2010, Singapore's FDI in India skyrocketed, resulting in US FDI ranking third behind Mauritius and Singapore (see table 4.2).

Portfolio investment in stocks, bonds, and the like began flowing into India in fiscal year 1993. Portfolio investment in India is limited solely to foreign institutional investors (FII). While experiencing large fluctuations, portfolio investment inflows have been at the level of FDI since 2003. The US share of portfolio investment in India decreased from above 50% in the 1990s to the 30% level in the 21st century, but there has been no change in the US consistently being the largest investor.

Table 4.2: Breakdown by country of FDI to India (in millions of dollars)

Rank	Country	FY2005	2006	2007	2008	2009	2010	2011 (April- August)	Share of Total (4/00- 8/11)
1	Mauritius	2,570	6,363	11,096	11,208	10,376	6,987	5,945	41%
2	Singapore	275	578	3,083	3,454	2,379	1,705	3,028	10%
3	US	502	856	1,089	1,802	1,943	1,170	402	7%
4	UK	296	1,878	1,176	864	657	755	2,519	6%
5	Japan	208	85	815	405	1,183	1,562	1,743	5%
Total Inflow		5,546	15,726	24,579	27,309	25,834	19,427	17,370	

Source: Ministry of Commerce and Industry, Fact Sheet of Foreign Direct Investment (FDI).

Meanwhile, alongside progress in regulatory easing, outward FDI by Indian corporations has been gradually increasing since the year 2000, and FDI in the US began in 2002. A characteristic of India's outward FDI is that it does not only include greenfield investment in new factory construction, but also involves much investment through M&A. During the period of 2004-2009, FDI in the US by Indian corporations included 127 cases of greenfield investment totaling \$5.5 billion and leading to 16,576 jobs.⁶

3. IT outsourcing

3.1 US corporations and the progress of offshoring to India

The use of India by US corporations goes back to the 1970s. It all started when US mainframe manufacturer Burroughs made a request of Tata Consultancy Services (TCS, founded in 1968), which was handling their Indian sales, to send Indian programmers to install system software for a US client company. Following that, many Indian IT vendors followed TCS and entered the programming business. The Indian engineers dispatched to the US were able to learn about much cutting-edge technology. Initially, it was mainly short-term low-added-value work that ended within a year, but many Indian technicians elected to remain in the US after completion of their duties. The presence of high-level Indian human resources in the US contributes to the progress of the IT industry in the country, and has come to play a very important role in expanding offshoring by US firms to India.

As a result of digitalization, modularization, and technological revolutions such as the internet and

⁶ Jain and Jain (2010)

telecommunications revolutions from the 1980s through the 1990s, services came to be provided at a low cost remotely from India instead of dispatching engineers to the US. At the same time, the shift from onsite to offshore progressed in a spurt. In the technological background to the acceleration of offshoring, it was important that that due to Unix workstations becoming a de facto international standard in the 1980s and the C programming language rapidly coming into widespread use, the modularization of programming became possible, and it became easy to subcontract to remote areas. As a result, it became possible for software vendors to use standardized tools to develop programs compatible with various operating systems and applications. Thereafter, the situation was that the Windows OS rapidly became widely used in place of Unix workstations and applications started to be able to take advantage of the beginning of internet evolution, enabling dispersed software development in distant regions. A variety of IT technology innovations were turned out from the 1980s through the 1990s, such as the provision of services divided into components, the standardization of hard and soft platforms, the development of new programming languages, and the standardization of the foundation for data transmission through the internet. These spurred offshoring.

Another factor that was a tailwind for offshoring to India was the progress of regulatory easing in the 1980s, particularly the adoption of policies favorable to the IT industry. A “Computer Policy” was announced under the Rajiv Gandhi administration in 1984, and import tariffs on both hardware and software were reduced to 60%. Also, the software industry became a “delicensed industry,” allowing foreign capitalized firms to establish wholly owned subsidiaries when they are export-oriented. Many Software Parks were established across the country as earth stations capable of low-cost satellite communication, and various preferential measures were implemented such as an exemption from the corporate tax for software exports.

3.2 A new direction for India’s IT industry

The movements of US corporations in the Indian domestic market are quite interesting. Traditionally, since the major Indian IT companies were consistent in their policy of emphasizing exports, the share of the domestic market in sales was only around 10%. Having taken advantage of this situation, currently IBM is the top corporation in the Indian domestic IT services market, with a 12% market share, followed by HP in the number three spot. IBM greatly expanded its market share as an outsourcing destination from the dominant telecommunications carriers in India. In the future, it is predicted that the competition between firms both domestic and foreign will heat up in the expanding domestic IT services market.

3.3 IT Offshoring and US employment problems

In terms of employment, while offshoring gives rise to new work, in exchange certain existing

work is unfailingly lost. Although it is difficult to accurately grasp what impact IT outsourcing is having on US employment, the increasing momentum of offshoring is a large threat to US IT-related professionals. When the US employment situation worsens as a result, the anti-offshoring movement grows in certain cases.

Although the IT industry made it out of the economic downturn and recovered in 2003, employment in the IT industry did not grow in a “recovery without employment.” As a result, the argument arose that outsourcing exclusively to places abroad with low personnel costs like India was stealing the jobs of US IT workers, and furthermore, arguments arose fearing the hollowing-out of the IT industry, which was even taken up as an important point of dispute during the 2004 presidential election.

In the US, the H-1B visa is granted to foreigners who have a high level of specialized knowledge or skills. It is a working visa limited to a three-year period (with renewals permitted), and was introduced on the basis of the 1990 Immigration Act based on predictions that there would be a deficiency in engineers, scientists, and other high-level experts. Incidentally, Indians hold the most H-1B visas, and in 2010, the proportion of Indians among all H-1B visa holders is 65%. The issuance limit for H-1B visas was raised from 65,000 in 1992 to 115,000 in 1999-2000 and 195,000 in 2000-2001, but with a growing anti-offshoring movement, it was lowered back to 65,000 in 2004-2005. Furthermore, with the headwinds of the slowdown in the US economy, the increase in unemployment, and also the “Employ American Workers Act” (enacted in February 2009), the actual number of H-1B visas issued has at times fallen below the limit.

4. US-India human exchanges

4.1 The expansion in Indian-Americans

Immigration of Indians to the US began at the beginning of the 20th century, but feeling the ripples from the Immigration Act of 1924, immigration of people from Asia essentially was not permitted before WWII. Indians were finally able to legally become Americans in 1946. From the 1950s onwards, immigration of Indians to the US gradually came to be seen, centered on international students and professionals. Then, an increase in Indian immigration was triggered by the 1965 reform of the Immigration Act, which had favored European immigration, and the quotas by country for Asian immigrants were abolished. Afterwards, Indian immigration accelerated from the end of the 1970s to the beginning of the 1980s.

Amidst the technology boom that surged in the US through the 1990s, large numbers of Indians were attracted to the country, particularly in the latter half of the decade. With the start of the 21st century, Indian immigration increased yet again. The increase in Indian immigration was 352,278 from 1990-1999, but reached 421,006 from 2000-2006. The number of Indian immigrants was

behind those from China and the Philippines among the Asian countries. Incidentally, roughly 60% of Indian immigrants have acquired US citizenship.

Indian-Americans comprise the following two groups. The first group is that of businesspeople who work in existing industries such as imports/exports, jewelry, and precious stones, and who are largely concentrated in the east coast. The second group is that of successful professionals such as doctors, scholars, and engineers. There are also many Indian engineers working in high-tech fields such as software development, the aviation industry, and telecommunications, many of whom are concentrated in Silicon Valley, Washington, Boston, and the like.

4.2 Indian-Americans active in each sector

Overall, Indian immigrants in the US have a high educational level. According to the 2000 census, the proportion of those with at least a college degree is 29% among Americans, 40% among Asian immigrants, and 58% among Indian immigrants. Also, a majority of Indian immigrants work in high-income managerial or professional positions. Thus, the per capita income of Indian immigrants exceeds the average US income by 50%. In 2002, there were 230,000 businesses owned by Indian immigrants, employing 610,000 people.⁷

A third of the engineers working in Silicon Valley and 7% of the CEOs of high-tech firms are of Indian descent. Indian immigrants are conspicuously dominant in terms of founding engineering and technology companies. TiE (The Indus Entrepreneurs), which is an organization of Indian entrepreneurs, was organized in Silicon Valley in 1992, and has been playing the role of supporting NRI businesses in the US.

Among the Indian immigrants, there is no small number of successful top executives of leading companies. With Vinod Khosla, one of the founders of Sun Microsystems, Intra Nooyi, the (female) CEO and Chairperson of PepsiCo, Vikram Pandit, the CEO of Citigroup, Shantanu Narayen, CEO of Adobe Systems, and Sanjay Jha, co-CEO of Motorola, there are too many to list everyone.

Indian immigration is producing leading human resources not only in business administration, but also in academia, the cultural arena such as film, and politics, and has a rapidly rising presence in US society. Many scholars of Indian descent are active in universities and research centers, their numbers easily exceeding 5000 people. It is well known that there are many leading Indian scholars who are active not only in the field of science and engineering, but also in economics, such as Amartya Sen, who was awarded the Nobel Prize in Economics. It is notable that in recent years, the same could be said about the leading edge fields within business theory. The late C.K. Prahalad, who was a Professor at the University of Michigan, is known for proposing the concepts of Core

⁷ Indian-Americans have a large presence in hotel administration, and there are 21,000 hotels owned by Indian-Americans, employing about 580,000 employees.

Competency and the Bottom of the Pyramid. At Harvard University and the University of Chicago, Nitin Nohria and Sunil Kumar are the respective deans of the business schools of their institutions, and each is a scholar of Indian descent.

Nevertheless, as India's IT industry achieved tremendous growth through outsourcing and started providing favorable employment opportunities, the phenomenon arose around 2003 of people newly returning to India (called the newly returned Indians, or NRI). They are the successor to the other conventional meaning of the same acronym (non-resident Indians).

5. Conclusion

Under the Cold War system and amidst continuing Indo-Pakistani hostility, the US deployed diplomacy placing importance on Pakistan as a bastion against communism, while India approached the USSR while advocating non-aligned diplomacy. Also, under a mixed system, India's economy leaned towards closed policies. As a result, US and Indian diplomacy did not mesh, and awkward relations continued.

With the end of the Cold War, the once-chilly relations between the US and India thawed. To the US, as the sole superpower, Indo-Russian relations ceased to be a concerning diplomatic issue, and the importance of Pakistan as an anti-communist bastion decreased. Furthermore, with the opening of the Indian economy alongside the introduction of economic reforms, the Indian economy came to draw high hopes from the US as a regional power. Since the 1990s, US-Indian relations greatly expanded in terms of both trade and investment, and the importance of the US as an economic partner to India rose rapidly.

The expansion in human exchanges between the US and India must not be overlooked. The IT industry was the driver of Indian economic expansion as the new face of the Indian economy, but the presence of people of Indian descent in the US has played an indispensable role in the rise of this industry. Indian-Americans encountered the IT revolution in the US, and in addition to making valuable contributions, were able to act as an important bridge for when US corporations have expanded IT offshoring to India.

When India conducted nuclear tests in 1998, the US imposed economic sanctions, but strategic dialogue continued energetically, and Indian-Americans deployed active lobbying activities for easing of the sanctions. Since the dawn of the 21st century, India and the US have had shared interests in counterterrorism against Islamic extremism and in checking a rising China, and are further strengthening a strategic partnership. The signing of the US-India Civil Nuclear Agreement was also proof that a firm strategic and economic partnership had been built between the two countries. Based on an omnidirectional, practical diplomacy, India has quickly expanded trade in products with China, and in recent years, China has become one of its largest trade partners.

Nevertheless, when looking at trade in products and services as a whole, there has been no change in the fact that India's biggest economic partner has remained the US.

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