

India in the Post COVID-19 World Order

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*An agenda for India to prosper
in a post-COVID world*

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Executive Summary

COVID-19 is likely to accelerate the competition and confrontation between the US and China, and simultaneously reduce the global authority of both by eroding their absolute power and legitimacy. The relative power scale can tilt in either direction.

India and other middle powers are likely to enjoy greater bargaining capabilities with both US and China. Smaller powers are likely to fall in line with any side that provides them the required capital.

India's geopolitical stance depends on actioning key domestic reforms, failing which India's leverage will reduce and it will be forced to ally with a major power on less favourable terms.

If India's relative power vis-a-vis China and the US improves, India can become a swing power for both the US and China led groupings. If India's relative power declines, India will have to align itself more closely with the US.

How will the world change?



Emergent Geopolitical Trends

COVID-19 is likely to accelerate the competition and confrontation between the US and China, and simultaneously reduce the global authority of both by eroding their absolute power and legitimacy. The relative power scale can tilt in either direction.

The “decline” of the Superpowers

This situation may be similar in some respects to the Cold War era in that both major powers may engage in confrontation and competition but stop short of fighting wars. And it is different from the Cold War in that both poles would be facing an absolute decline in power because of COVID-19. US legitimacy could decline due to its response to the pandemic and recent isolationist stances. China’s economic power will be hit significantly because of COVID-19.

The Rise of the Rest

Middle powers such as France, Germany, Brazil, India, and Russia are likely to have more leeway in engaging with both the US and China and forming their own interest-based multilateral groups. On the other hand, Iran will be ravaged by COVID-19, leaving a power vacuum in West Asia that may be filled by Saudi Arabia and Turkey.

Some old political projects may fall out of favour

Nationalist movements across the world may accelerate, and states will likely play larger roles in citizens’ lives. The European Union may weaken as a political project, though economic ties will remain important. ASEAN might also become less relevant, as each ASEAN nation will likely bandwagon with either China or the US. The UN could become even more irrelevant.



Emergent Geoeconomic Trends

COVID-19 is likely to alter the economic order significantly. The recession will give way to a secular stagnation. Rising economic nationalism may lead to a “gated” globalisation.

Global recession in the short run, secular stagnation in the medium-term

Even after the public health crisis is managed, a quick V-shaped economic recovery seems unlikely. Global economy will settle into a secular stagnation over the medium-term, with sluggish consumption and low growth.

The liberal economic order will suffer a setback

International labour mobility may drop precipitously as nationalism continues to rise. Large capital flows are likely to be restricted to relatively high-performing developing countries. The goods and services trade between many countries, especially the US and China, will contract.

Economic nationalism will be back in fashion

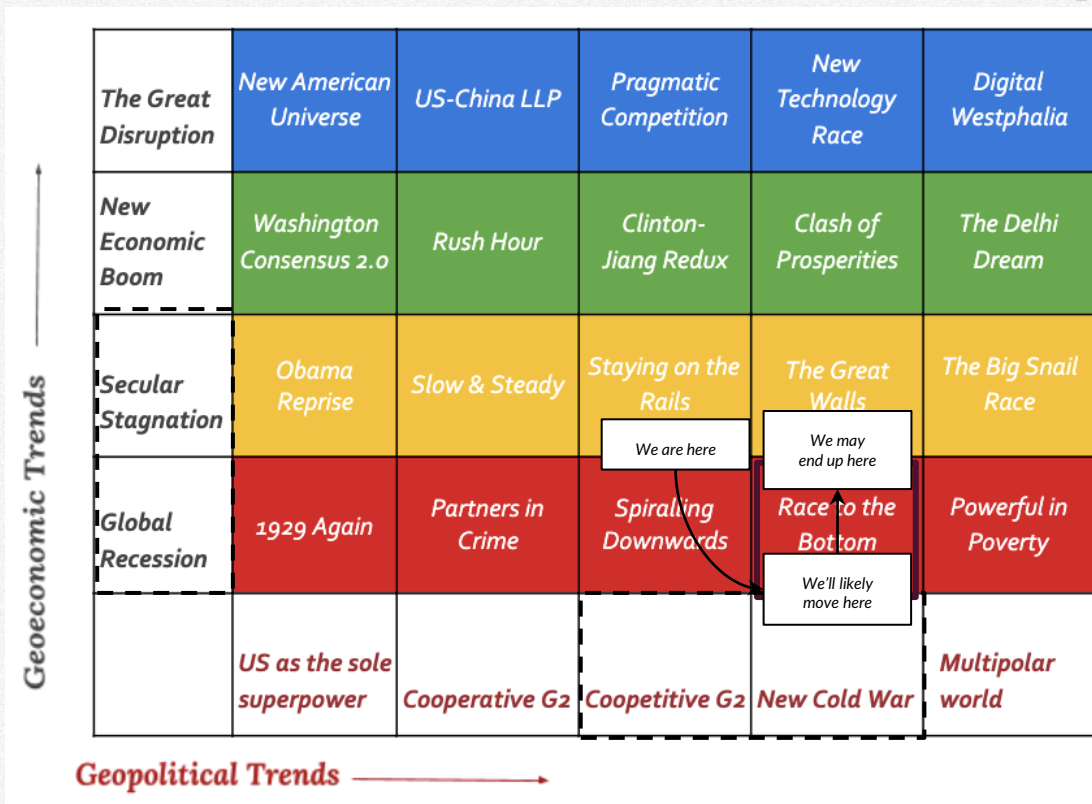
Supply chains are likely to be shaped by industrial policy regimes, tariff regimes, and restrictive trade agreements. The globalisation project will change as a result of economic nationalism, leading to the emergence of “webs” of trade – blocs grouped around major poles in a form of “gated globalisation”. Hitherto highly-optimised global supply chains will change to include multiple sourcing and the removal of supply chain bottlenecks.



The post COVID-19 World Order: A Framework

In 2018, we proposed a framework to imagine New World Order scenarios at the intersection of key geopolitical and geoeconomic trends.

After COVID-19, some world order scenarios become more likely than others. Overall, we are heading towards a “Race to the Bottom” scenario in the short term, at the intersection of a ‘Global Recession’ in geoeconomics and a ‘New Cold War’ in geopolitics.



Source: [India's Strategies for a New World Order](#)

“Race to the Bottom” = Global Recession + New Cold War [1/2]

The US-China confrontation will increase. The middle powers will enjoy greater bargaining with both the US and China. The smaller powers are likely to fall in line with any side that provides them capital.



From One to Many Economic Webs

In the post COVID-19 world, many ‘Great Walls of China’ may come up – a new version of the Iron Curtain, where the world is split into three economic webs - one dominated by US markets and investments, one by Chinese markets and investments, and a more diffused collection of middle powers (such as Russia, India etc.) who independently strike bargains with the US and China-led economic webs, and form their own networks of trade with friendly countries.

The US-led economic web may take the shape of a Dollar bloc, perhaps underpinned by the US Fed as a lender of the last resort for all central banks. The economic web will be underpinned by the US running high trade deficits and acting as a consumer market with low trade barriers for allies, and possibly even unlimited currency swap lines with its allies to provide dollars on demand, similar to its response to the 2007-8 GFC and the current COVID-19 crisis.

The Chinese web would be anchored on China as the investor, with possibly an enhanced BRI++ to build infrastructure in many countries. That will mean China will still run high current account surpluses and export to other countries. However, as it would still need large markets to fuel its growth, it may concede a lot more to construct this alliance, adopting a less belligerent stance than it has in recent years. It may look to Russia, India and some European countries as partners to keep its economy from falling into a debt-driven collapse.



“Race to the Bottom” = Global Recession + New Cold War [2/2]

The US-China confrontation will increase. The middle powers would enjoy greater bargaining with both the US and China. The smaller powers are likely to fall in line with any side that provides them capital.

The swing powers would interact with both webs - they may export to the US (even with tariff barriers in place) and receive access to technology, while also being beneficiaries of Chinese investment. India, Russia, Vietnam, South Korea, and some European and South East Asian powers will likely adopt this strategy.

Stable geopolitics, dynamic geoeconomics

In the post COVID-19 world, the US will likely see countering China as an overriding national priority. Reorienting supply chains to reduce dependence on China will be an important priority. As a result, the post COVID-19 global recession won't be easily solved as global trade and investment flows are reoriented, leading to a period of secular stagnation for quite some time. We are likely to migrate from the “Race to the Bottom” scenario in the short term to the “Great Walls” scenario (Secular Stagnation + New Cold War) in the medium term (5-10 years).

A New Age of Multilateralism

Every facet of policy will be affected by the New Cold War. Like the global economy, the Internet may splinter into multiple interacting webs with unprecedented State oversight, especially outside the old Western liberal democracies. Global bodies would become far less important, and multilateral institutions organised around powerful nation-states become far more important for transnational cooperation.

How does this “Race to the Bottom” world affect India?



Impact on India

As a middle power with a large market, India's bargaining power with both China and the USA will increase. However, India will face significant economic and social challenges.

In our 2017-18 analysis, discussing a “Race to the Bottom” scenario, we wrote:

‘High inequality and unemployment [may] lead to demands for social justice. Populism and security are the dominant themes of discourse. Simultaneously, India is wooed by both superpowers to join their blocs or provide market access. If handled delicately, there could be major payoffs by playing off the superpowers.’

These are likely to hold true in a post COVID-19 world, though much depends on how India responds to the pandemic and what welfare and healthcare systems will be put into place in the coming years. Rebuilding broken social harmony will be a key imperative for building strength.

An extremely cautious approach will need to be adopted to interact with the superpowers, and bold reforms will be needed to improve all citizens’ quality of life in the midst of a recession.

The India growth story will continue to require free flows of capital, labour, goods and services. In this world where distrust over China increases, India can be a part of multiple economic webs and gain from them.



India's interests in the post COVID-19 world

India will need an engine of growth in a changed world. As a middle power with a large market, large-scale manufacturing for the world can be that engine.

Global flows of labour and capital were key determinants of India's economic power in the pre COVID-19 world.

In a "Race to the Bottom" world, global labour flows will become restricted. Capital flows are likely to thin out.

India needs another engine of growth in such a world. Large-scale manufacturing offers one such opportunity. China beat India in this game in the pre COVID-19 world. But in a new world where China is distrusted, India can be part of more economic webs and build its own strength.

The next section outlines what India should do domestically to increase its leverage. Subsequently, we discuss two possible geopolitical pathways for India. The last section deals with small bets India can take under the changed circumstances.

Domestic Policy Reforms for the post COVID-19 world



Domestic Policy Reforms for a post COVID-19 world

India's policy responses can be categorised into three phases.

Phase 1: Responding to the pandemic : focus on public health and provide livelihood support

Phase 2: Reconstruction: with a fiscal and monetary stimulus

Phase 3: Towards a post COVID-19 world: build an industrial economy with structural reforms

India's geopolitical stance depends on actioning key domestic reforms, failing which its leverage will reduce and it will be forced to ally with a major power on far less favourable terms.

Phase 1: Responding to the Pandemic (2020-21)

The limited economic policy objectives in this phase are (i) to help low-income groups tide over lockdowns with cash and food support through existing schemes leveraging DBT through JAM; and (ii) Keep enterprises alive through a mix of monetary actions (greater regulatory forbearance, etc.) and fiscal actions (tax support for maintaining employment, etc.). For details of the Phase 1 response, check our work [here](#).

Phase 2: Reconstruction (2021-24)

The focus should be on a large-scale fiscal stimulus, coordinated with a monetary stimulus, focused on infrastructure building.

Phase 3: Towards a post COVID-19 world (2024 and beyond)

The Government should focus on building an industrial economy i.e., India as the factory of the world, with high quality infrastructure, and a deep economic integration with the US-led web, as well as possibly the China-led web.



Phase 2: Reconstruction [1/2]

Focus should be on a large-scale fiscal stimulus, coordinated with a monetary stimulus, focused on infrastructure building.

Fiscal stimulus to create a big new source of demand through infrastructure and other capital expenditure and to support private investment revival.

Focus on infrastructure

1. Deliver the infrastructure pipeline of ₹ 100 lakh crores.
2. Undertake financial sector reforms to attract infra financing, including developing the bond-currency-derivatives market, increasing the depth of markets for InVITS, TOT etc.
3. Ensure that bottlenecks to infrastructure are removed easily. Create special tribunals, build regulatory judicial capacity and undertake judicial reforms to ensure that dispute resolution on infrastructure (e.g., in land acquisition, environmental clearances etc.) are completed in a timely way.
4. Build new cities centred around universities and medical centres. Invite some of the best foreign players in these markets to set up for the Indian market.
5. Build large scale transport and logistics hubs that can also cater to India's immediate neighbours.



Phase 2: Reconstruction [2/2]

Focus should be on a large-scale fiscal stimulus, coordinated with a monetary stimulus, focused on infrastructure building.

Provide support for a private sector investment revival

1. Recapitalise and reform banks and NBFCs including a TARP/ bad bank for stressed assets
2. Create credit guarantees for MSMEs to revive investment

Provide a large-scale monetary stimulus

1. Keep monetary policy stance accommodative across interest rates. The RBI should be advised to reduce CRR, SLR and the repo rate.
2. The RBI should inject liquidity in the system by pursuing an aggressive asset purchasing strategy through open market operations.
3. Transfer RBI reserves to the government as per the norms of the Bimal Jalan committee.

Complement with non-traditional external financing

1. Create a government-guaranteed special purpose vehicle (SPV) for long-term large infrastructure expenditure that is equity-funded by sovereign and pension funds around the world. Target sovereign wealth funds of countries which want to diversify from oil, like Saudi Arabia and Norway.
2. This can be further leveraged by low interest rate development capital from countries like Japan.



Phase 3: Towards a Post COVID-19 World [1/2]

Build an industrial economy with structural reforms, focussing on attracting global manufacturing away from China.

Transition to a low import duty regime

Reduction in import duties will allow manufacturers moving away from China to continue buying from across the world while manufacturing in India. To Make in India, we need not restrain buying from abroad. Signing a trade agreement with the US, Japan, and ASEAN can be another way to lower import tariffs.

Create a Free Trading Zone with Bangladesh

Bangladesh is a fast-growing economy and a potentially big market for Indian manufacturing. A free trading zone with Bangladesh can create wealth on both sides. Opening up can imply cheaper textiles and other goods into India, but it would also give an opportunity to export higher value goods. In time, extend the Free Trading Agreement to other economies in the subcontinent.

Reduce the risks of investments

Arbitrary judicial interventions and failure to protect corporate interests deters global companies from investing in India. Setting up special tribunals for projects moving out of China will assure companies that grievance redressal is faster.



Phase 3: Towards a Post COVID-19 World [2/2]

Build an industrial economy with structural reforms, focussing on attracting global manufacturing away from China.

Follow the Global In-house Centre Approach (GIC 2.0)

In IT/BPO sectors, India has allowed global MNCs to set up Global Inhouse Centres that follow the insourcing model. This model can be replicated in manufacturing: create a ring-fenced zone where global manufacturing companies can easily acquire land, build plants, and send expats to work in India etc.

Grab new opportunities in the services sector

With the norms of social distancing, the demand for services that can be delivered remotely will increase. India can play an important role in providing telemedicine services. There should be a push to export complementary and supplementary services to school and college education that can be delivered online.

Business consultation, data processing and data analytics, marketing, and even accounting can be done remotely and India can offer these services competitively in the world. A stable, reliable, and economically viable telecommunication sector is key to achieving these goals.

Foreign Policy Outlook for the post COVID-19 world



Geopolitical Pathways for India

[1/2]

US-China competition will influence both India's choice of economic partners as well as the security decisions it must take. It must make some moves to ensure strategic autonomy nevertheless.

Increasing India's Geopolitical Leverage

Increasing India's economic power can help ensure favourable relations with many other poles of the dynamic post COVID-19 global economic landscape. However, US-China competition will continue, and this will influence India's choice of economic partners as well as the security decisions it needs to make. The following actions can help ensure a degree of strategic autonomy irrespective of the actions of other players:

1. Reform defence to shift focus from Manpower to Firepower, Continental to Maritime, Conventional to Sub-Conventional, and Kinetic to Non-Kinetic. Expand technological capacity especially in the new domains such as cyber & space. Reduce dependence on other powers for key defence equipment.
2. Create parallel multilateral institutions and strengthen presence in select existing ones. e.g., a new FTA in the Indian subcontinent; expanded presence in the IMF; a world body for governing the internet; coordinating global capital flows and monetary policy; reforming the WHO for global public health.
3. Strengthen the Quad grouping. If India remains as a swing power, then strengthen the Quad *without* explicitly making it a military alliance. Convert it to a formal military alliance and expand it, if India chooses to align with the US.



Geopolitical Pathways for India [2/2]

India might still need to choose a geopolitical pathway depending on the actions of other powers.

Choosing a Pathway

Some choices, however, depend on the actions of other powers. Some potential pathways, and the conditions under which India should embark on them, are outlined below.

Two potential geopolitical stances for India are:

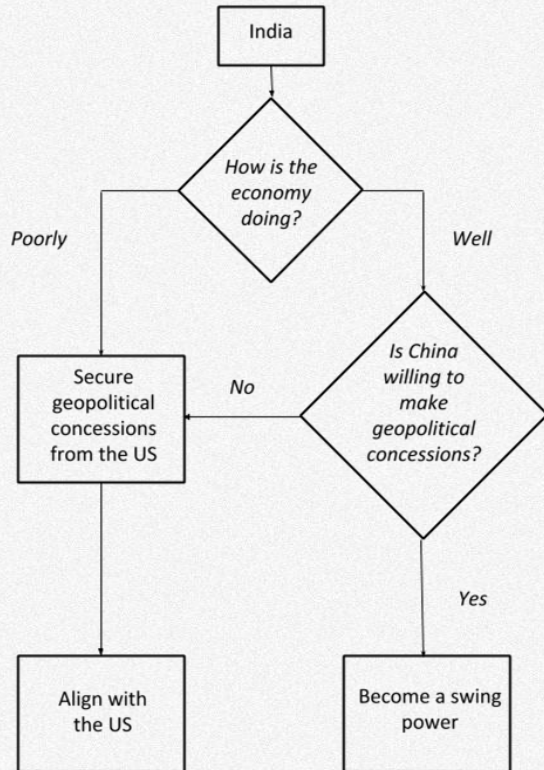
1. To be a swing power for both the US and China-led groupings
2. To align itself with the US

The choice between these two stances depends upon:

1. India's relative power vis-a-vis both the US and China
2. Willingness of the US and of China to make concessions to India on both geopolitics and economics



Choosing a Geopolitical Pathway



When should India choose to be a swing power?

- India's economy does well, and is an attractive investment and trade partner for both China and the US
- China shows willingness to make the following concessions:
 - Settle the border dispute with India
 - Cede the subcontinent to the Indian sphere of influence in exchange for India agreeing to not balance China
 - China opens up its own consumer market for India
 - China invests significantly in a rebooted BRI in India

When should India choose to align with the US?

- India's economy slows, and it lacks the power to balance China
- China is unwilling to make the concessions above, while the US is willing to do the following:
 - Free trade agreement with India, and actively invest in shifting supply chains to India, and providing currency swap lines
 - Formal military alliance with India, and military support to emerge as the predominant power of the Indo-Pacific.

Small Bets for an Uncertain World



Small Bets for an Uncertain World [1/2]

Given the uncertainty, India should also invest in small bets, which when doubled down on could yield big benefits, should some currently unlikely scenarios emerge

Small bet #1:

Military cooperation with the littoral Indian Ocean States at low cost e.g., listening posts; deepening intelligence cooperation; training of military; arms supplies.

Scenario when it would help: Indian Ocean becomes a global centre of gravity; and Indian power differential vis-a-vis China narrows significantly.

How this small bet could be doubled down on: In this scenario, this bet could lead to India asserting dominance on the Indian Ocean Region (with an Indian 'Monroe doctrine'), with a formal military alliance, and military bases in the IOR and Central Asia, and co-opting the island nations of the IOR as protectorates, or even annexing them.



Small Bets for an Uncertain World [2/2]

Given the uncertainty, India should also invest in small bets, which when doubled down on could yield big benefits, should some currently unlikely scenarios emerge

Small bet #2:

Invest in vocational education in select sectors and expand visa programs with developed countries.

Scenario when it would help: India's domestic economic growth stagnates; Europe and Japan continue to be ageing societies.

How this small bet could be doubled down on: In this scenario, the best route may be to become a large-scale exporter of people. At that stage, creating the right bilateral and multilateral institutions for free movement of people, supported by the diplomatic corps focused on overseas Indian affairs, and a safety net and health and vocational education in India funded in part by tapping into remittances, may be the best option for India.

Small bet #3:

Cultivate a deeper relationship with Tibetan and Uighur separatists, and the Taiwanese government.

Scenario when it would help: China is wracked by internal instability

How this small bet could be doubled down on: If this scenario materialises, then India can double down by supporting separatist movements and revolutionary movements to split and cause regime change in China.

/end