Turning Tariffs into Trade Opportunity

This editorial, based on "The Opportunity in Tariff War" published on 31/07/2025, in Financial Express, examines how the 25% tariff on Indian goods and penalties imposed by the US, linked to India's dealings with Russia, present both challenges and opportunities for India.

For Prelims: **Foreign Direct Investment (FDI)**, **Production Linked Incentive Scheme (PLI), Make in India**, **ASEAN**, **free trade agreements (FTAs)**.

For Mains: Impacts of US Tariffs on India, Strategic Opportunities that India can Derive from US Tariff Policies.

The **imposition of 25% tariffs by the United States on Indian imports**, along with penalties linked to India's defense and energy dealings with Russia, represents a significant shift in **India-US trade relations**. These measures not only strain bilateral economic ties but also have a ripple effect on India's export competitiveness, investment climate, and **broader geo-economic positioning in a multipolar world**. While they pose immediate challenges, they also offer India a strategic opportunity to **reassess and strengthen its manufacturing, trade diversification, and long-term economic growth strategies**.

How do US Tariffs Affect India's Economy and Trade Dynamics?

- **Weakened Export Edge and Potential Growth Strain:** The 25% tariff on Indian exports to the US **threatens India's competitiveness**, particularly in labor-intensive sectors like textiles, seafood, and gems.
  - **The US was India's largest trading partner for the fourth consecutive year** in 2024-25, with bilateral trade valued at USD 131.84 billion.
  - Estimates suggest that if half of the US demand disappears, **India's exports could decline by USD 40 billion**, reducing GDP growth by 1% in FY26.
    - The imposition of tariffs **can lead to the depreciation of the Indian rupee** as well.
    - Also, lower US tariffs on ASEAN countries like Vietnam and Indonesia **divert export orders away from India**, further reducing its market share.
- **Risks to Small and Medium Enterprises (SMEs):** SMEs, often operating with limited working capital and small margins in labour-intensive sectors like garments, leather, and handicrafts, are **particularly vulnerable to tariff hikes**.
  - These businesses could face challenges in managing the increased costs, resulting in potential job losses **as they lack the financial and logistical bandwidth** to absorb cost increases or explore alternate markets quickly.
  - Simultaneously, tariff-driven restrictions on Chinese goods in the US push **China to dump surplus inventory into alternative markets like India**, leading to price suppression and increased pressure on domestic industries.

- **Potential Vulnerability in High-Growth Sectors:** Though high growth sectors like **electronics and pharma** are currently not subject to reciprocal tariffs, both sectors could face a larger impact later, particularly when the US introduces **sectoral tariffs**.
    - This could diminish India's competitive edge in electronics and other high-value sectors, even though these industries have seen rapid growth due to [Foreign Direct Investment (FDI)] and [Production Linked Incentive Scheme (PLI)] schemes.
- **Compromised Scope for Value Chain Upgradation:** India is trying to shift from being a **low-value exporter** (e.g., raw materials, intermediates) **to high-value manufacturing** and design-based exports.
    - US tariffs, particularly if applied on high-tech or precision engineering goods, may freeze India's movement up the value chain. This **risks keeping India stuck in low-margin segments**, limiting its ability to compete in the advanced manufacturing race.

What Strategic Opportunities Can India Derive from US Tariff Policies?

- **Enhancing Position in Global Supply Chains:** Amid US **"friend-shoring" and "China+1" strategies**, India has a chance to become a trusted node in global value chains (GVCs). Sectors like electronics, [semiconductors], and defence manufacturing are ripe for integration.
    - Additionally, India **can capitalize on sunrise sectors such as Active Pharmaceutical Ingredients (APIs)** and technical textiles, further expanding its role in global supply chains and driving long-term economic growth.
    - The impact of tariffs can push **Indian industries to upgrade** their quality, technology readiness, and scale, **moving away from only seeking temporary protection** to building robust, long-term global capabilities.
- **Strategic Opening for Services and Data Trade Diplomacy:** While US tariffs largely target goods, they offer India a strategic window to recalibrate trade diplomacy toward services, digital commerce, and cross-border data flows—domains where India holds a clear competitive edge.
    - **India can leverage platforms like [iCET (Initiative on Critical and Emerging Technology)]** to shape norms around data sovereignty, fintech interoperability, and digital taxation. This **allows India to transition from a tariff-reactive posture to a rule-shaping partner** in the digital domain.
- **Boost to Domestic Manufacturing and Export Diversification:** The US decision to impose tariffs provides India with an opportunity to strengthen its domestic manufacturing, **particularly in sectors like auto components, electronics, and industrial machinery**, where tariffs on China's exports have created new competitive openings.
    - Indian manufacturers can benefit from the **USD 20 billion in China's exports** to the US that are at risk because of the [tariff war].
    - For example, India's auto components sector could grow by **establishing operations in tariff-neutral regions** or increasing direct exports.
- **Deepening Economic Ties with Alternative Partners:** The unpredictability of US tariffs pushes India to accelerate trade with alternative partners, such as the **European Union (EU), ASEAN nations, and Latin American and Caribbean (LAC)** countries.
    - This strategy aims to diversify India's export markets, **reducing reliance on the US** and insulating its economy from US-centric risks.
    - By strengthening these trade relations, **India can safeguard its economic growth and open new avenues for investment** and market access, ensuring long-term stability amid global trade uncertainties.

What Measures Can India Adopt to Maximize Trade Gains Amid Global Tariff Shifts?

- **Strengthening Domestic Manufacturing and Innovation:** India must continue focusing on advanced manufacturing technologies and improving product quality to make its industries globally competitive.
    - Key sectors like electronics, pharma, auto components, and textiles **must ramp up R&D, compliance, and innovation** to meet global standards.

        - Strengthen **Production Linked Incentive Schemes** and **Make in India** in semiconductors, electronics, APIs, and solar modules to curb overdependence on imports.
- **Enhancing Trade Diplomacy and FTAs:** India must expedite negotiations for **free trade agreements (FTAs)** with the European Union and ASEAN countries to mitigate the impact of tariffs. These agreements can offer market access and tariff cuts that can offset the burden of US tariffs.
    - Strengthening sectors like **renewable energy, electric vehicles, and high-tech manufacturing** should be a priority, as these areas align with global sustainability trends and offer long-term growth potential.
    - Additionally, a **reformed India-US trade pact should be prioritized**, aiming for comprehensive, long-term alignment that goes beyond temporary tariff negotiations to address non-tariff barriers, investment flows, and policy flexibility.
    - Also, instead of expanding volume in a few sectors, **India should prioritise horizontal diversification (new sectors) and vertical upgrading (high-value stages).**
        - For example, rather than exporting raw textiles, India must aim for branded garments or smart fabrics.
- **Supporting SMEs and Protecting Vulnerable Sectors:** SMEs, especially in textiles and seafood, should receive targeted financial support through measures like **interest rate subventions and export incentives.**
    - A sector-specific response could help ease the burden for SMEs, including **support for industries** like marine food products, gems, and jewelry, where India has a significant market share in the US.
    - At the same time, the **private sector must step up as a key partner to invest in R&D**, enhance quality standards, and develop a future-ready workforce. This **synergy between state and industry** will be critical to drive productivity and attract global investors.
- **Strategic Resilience Against China's Dumping:** India needs to deploy stringent anti-dumping policies in line with the **WTO's Anti-Dumping Agreement** to counter the risk of Chinese overproduction in sectors like steel, chemicals, and electronics.
    - India should **deploy a real-time tariff monitoring system** to ensure that domestic industries are shielded from aggressive pricing strategies by Chinese producers.
        - India imposes import duties on solar panels to promote domestic manufacturing and reduce reliance on foreign imports, it serves as a useful precedent.
- **Policy Reform and Structural Changes:** India must focus on improving its infrastructure, logistics, and energy reliability to lower factor costs and improve the **ease of doing business**. This can help ensure that **Indian goods remain competitive despite tariff hikes.**
    - Structural reforms, including land acquisition modernization, credit access for MSMEs, and regulatory efficiency, are essential for creating a **business-friendly environment conducive to long-term manufacturing growth**.

Conclusion

India has a unique opportunity to optimize trade relations and enhance economic resilience in the face of global uncertainties amid rising tariffs. By focusing on **sectoral growth, technological advancements, and regional trade partnerships,** India can capitalize on the shifting global landscape. With a strategic emphasis on sustainable development, capacity building, and innovation-driven growth, **India can position itself as a key player in the global economy**.

Drishti Mains Question

Analyze the impact of US tariffs on India's manufacturing sector and suggest measures to strengthen its position in global supply chains.

UPSC Civil Services Examination, Previous Year Questions (PYQs)

Mains

Q. 'What introduces friction into the ties between India and the United States is that Washington is still unable to find for India a position in its global strategy, which would satisfy India's National self-esteem and ambitions'. Explain with suitable examples. **(2019)**
