

The Implications of Noda's Visit to India

Rajaram Panda and Shamshad A. Khan

Dr. Rajaram Panda is Senior Fellow and Shamshad A Khan is Research Assistant at the Institute for Defence Studies and Analyses (IDSA), New Delhi.

January 13, 2012

Summary

The visit of Japan's Prime Minister Noda Yoshihiko to India in late December 2011 and his summit meeting with Prime Minister Manmohan Singh, served as a good opportunity for both sides to enhance mutual trust and consolidate cooperation. This was Noda's first visit to India after assuming the office of Prime Minister in September 2011. The last Prime Ministerial visit from Japan to India was that by Hatoyama Yukio in December 2009, which was followed by Singh's return visit to Japan in October 2010. The broad spectrum of talks between the two sides clearly demonstrated the fact that they are strategically important to each other. The talks centered on issues such as infrastructure, energy and industry, nuclear and currency swap, the last with a view to stabilize their respective currencies. The purpose of Noda's visit was to tap potential synergies between the two countries. He stressed the fact that the marriage between India's young workforce and Japan's capital and technology could help build better infrastructure to sustain long-term growth. The talks also covered the prospects for a pact on civil nuclear cooperation.

The visit of Japan's Prime Minister Noda Yoshihiko to India in late December 2011 and his summit meeting with Prime Minister Manmohan Singh, served as a good opportunity for both sides to enhance mutual trust and consolidate cooperation. This was Noda's first visit to India after assuming the office of Prime Minister in September 2011. The last Prime Ministerial visit from Japan to India was that by Hatoyama Yukio in December 2009, which was followed by Singh's return visit to Japan in October 2010. The broad spectrum of talks between the two sides clearly demonstrated the fact that they are strategically important to each other. The talks centered on issues such as infrastructure, energy and industry, nuclear and currency swap, the last with a view to stabilize their respective currencies. The purpose of Noda's visit was to tap potential synergies between the two countries. He stressed the fact that the marriage between India's young workforce and Japan's capital and technology could help build better infrastructure to sustain long-term growth. The talks also covered the prospects for a pact on civil nuclear cooperation.

Economic Issues

The highlight of the economic component of bilateral ties during Noda's visit was a currency swap deal to address the shortage of US dollars in the wake of increasing concerns linked to the sovereign debt crisis in the Eurozone, which has also led to the rise of risk aversion among foreign investors. The swap agreement allows a country faced with short-term liquidity problems to borrow from the other's foreign reserves in order to absorb heavy selling pressure on its own currency.

India and Japan agreed to upgrade their currency swap arrangement from the previous \$3 billion (a three year deal agreed upon in June 2008) to \$15 billion (¥1.3 trillion). Japan realizes that India has emerged as the third largest economy in Asia after China; hence, the importance of upgrading the swap that would allow the Indian government to better respond to the financial crisis and address the continuing fall of the Indian rupee. Japan has similar currency-swap accords with other Asian countries, including China, South Korea (signed in October 2011), Indonesia, and the Philippines.

As per the agreement, Japan will accept rupees and give dollars to India for up to \$7.5 billion; similarly India will take the Yen and send dollars for the corresponding amount to Japan if speculators seek to thrash down the respective currencies. The agreement opens up a new window for Indian corporates to raise Yen-denominated loans at extremely cheap rates. This is a cost-effective tool for regional cooperation. Japan's foreign reserves hit an all-time high of \$1.3 trillion in November 2011, and the swap arrangement is now expected to help support the Indian rupee, which has been Asia's worst performing currency in 2011. The rupee's depreciating value has led to the country's reserves declining substantially. The deal 'aims at preventing adverse contagion effects during crises fuelled by speculative investment'.¹

¹ 'Japan PM in Delhi, currency pact soon', *The Hindustan Times*, December 28, 2011.

The Japanese government and some of its agencies are funding several large Indian infrastructure projects, including the Rs 1 lakh crore Delhi-Mumbai Industrial Corridor (DMIC) and the third phase of the Delhi Metro. Japan has funded several infrastructural projects in India over the past few decades. Top Japanese companies have made their presence in the Indian market, which they have found lucrative. The currency swap deal is a signal that Japan is serious about deepening its economic engagement with India. It was, therefore, appropriate that Prime Minister Noda emphasized the importance of the emergence of a large middle class, which could be the driving force for growth in the manufacturing sector. Addressing the business forum organized by the CII, ASSOCHAM and FICCI, Noda said that the development of India's manufacturing sector would facilitate the achievement of greater trade volumes.

The signing of the Comprehensive Economic Partnership Agreement (CEPA) between the two countries in February 2011, which took effect in August that year, has placed India-Japan economic ties on a high trajectory. The CEPA will facilitate increase in bilateral trade significantly. Both countries have set a target of \$25 billion in bilateral trade by 2014. Addressing the India-Japan Business Forum on December 28, 2011, Commerce, Industry and Textile Minister Anand Sharma observed: 'The signing of CEPA has begun a whole new chapter in our economic partnership, unlocking the true potential of trade between our two countries. I am hopeful that CEPA will further deepen economic engagement in terms of trade in goods, services, and investment.'² India hopes that the CEPA will jumpstart greater investment in India. Under the CEPA, India will abolish tariffs on 90 per cent of items imported from Japan; this will eclipse the 70 per cent items covered by the India-South Korea free trade agreement.

There are already over 800 Japanese companies doing business in India and the number is increasing every year. However, compared to the 84,000-odd Japanese companies doing business in China (about 8,400 in Shanghai alone), this number is very small. The CEPA and the DMIC project will go a long way in correcting this imbalance in the near future. Both countries also agreed to invest \$4.5 billion (¥ 350 billion) in India over the next five years through the Japan Bank for International Cooperation, which will promote the DMIC project and thus help develop an industrial zone that spans six states in India.

The DMIC project, which started in 2006, would involve the development of freight railways, roads, and power plants between Delhi and Mumbai. The total project cost will be \$90 billion (¥7 trillion), the largest project, in terms of cost, ever undertaken in India. It is expected that this huge project will dramatically transform the character of India-Japan economic relations in a few years' time. Japanese companies hope to receive orders to build large industrial complexes and other facilities, although many of the

² 'India, Japan sign \$15 bn currency swap deal', *The Times of India*, December 29, 2011.

related projects will be built on the PPP (public-private partnership) model based on a competitive international bidding process.

The Indian government has also drawn up a blueprint to build a high-speed railway system, and Japan has requested India to adopt its *Shinkansen* (bullet train) technology. Both countries also discussed cooperation over natural resources, and expressed the hope that Indian and Japanese companies will promote joint businesses on production and trade in rare earths, which are vital for a wide range of green energy technologies as well as military applications. It also transpired that Japan wants to grab a bigger slice of the market in India, whose population is expected to become the world's largest as early as 2030.

Nuclear Issue

India and Japan also revived the hope of civil nuclear cooperation by urging their negotiators to 'exert further efforts'³ for an early conclusion of the agreement. This development took place during the Japanese Premier's visit with both sides making a commitment in this regard in the joint statement issued on December 28. Prime Minister Noda's announcement of the resumption of negotiations on nuclear cooperation must be seen as a departure from the policy of his predecessor Naoto Kan, who had suspended talks with all prospective buyers of Japanese nuclear reactors, including India. Speaking at a function organized by the Indian Council of World Affairs on December 29, 2011, Noda put a positive spin on the nuclear deal. He said that at the working level, 'discussions on the civil nuclear deal have proceeded in right direction' and welcomed this progress.⁴ Stressing Japan's unique nuclear history, he reminded the gathering that 'Japan is the only country attacked by a nuclear weapon'.⁵ It transpires that Prime Minister Noda faces lots of internal political challenges in this regard, and that it would be difficult for him to take the negotiation to a logical conclusion in a very short time.

Given this, what are the factors that put the possibility of exporting nuclear technology to India back on the Japanese agenda? The issue was actually put on the backburner following the Fukushima incident. Japan's pursuit to export nuclear reactors is driven by various internal factors, including an entrepreneurial interest. Prime Minister Noda, a graduate from Matsushita Institute of Government and Management, aims at creating an overseas infrastructure market by selling Japanese technology, including nuclear

³ 'Vision for enhancement of India-Japan strategic and Global Partnership upon entering the year of the 60th anniversary of the establishment of diplomatic relations' (India Japan Joint statement), available at <http://www.mea.gov.in/mystart.php?id=100518843> (accessed on December 29, 2011).

⁴ Indrani Bagchi, 'India, Japan move to end deadlock on N-deal', *The Times of India*, December 29, 2011.

⁵ Quoted in *Ibid.*

technology, and eventually reviving the Japanese economy. At home, Noda faces the daunting task of reviving the Japanese economy. In 2011, multiple factors, including the earthquake, tsunami and the nuclear meltdown at Fukushima Daiichi Nuclear Plant caused an estimated loss of \$300 billion to the Japanese exchequer. His effort to impose a 20 per cent consumption tax has been opposed by his own colleagues in the ruling party, and Noda has put that decision in abeyance till 2013. With few options available, the Noda administration is pinning hopes on nuclear exports.

The announcement about reviving negotiations with India comes against the backdrop of the Japanese Diet's approval of erstwhile bilateral civilian agreements signed with Jordan, Vietnam, South Korea, and Russia. These agreements will come into effect in January 2012, paving the way for the export of Japanese nuclear technology and nuclear reactors to these countries. Apart from India, Japan is also negotiating similar civilian nuclear agreements with Turkey, Saudi Arabia, South Africa, Brazil, and the UAE. Considering the fact that former Premier Naoto Kan had stated that Japan should 're-examine' its nuclear reactor's export policy following Fukushima and even suspended further negotiations, the Diet's approval of the agreement signed before the March 2011 crisis is a big departure from those policy pronouncements. The developments at the Japanese domestic level suggest a better prospect for the conclusion of an India-Japan nuclear agreement. However, a lot will depend on whether the agreement is approved by the Democratic Party of Japan (DPJ) and the Japanese Diet. Noda is already drawing flak from his colleagues for getting the agreements approved by the Diet. Many of his own party colleagues find the nuclear export policy to be 'problematic'. Two DPJ parliamentarians voted against the bill, while 15 others abstained during the voting in the Lower House. People in Japan have also been questioning the government's pursuit of export of nuclear reactors. They question why Japan wants benefits from selling something which it thinks is dangerous for itself. An aggrieved Japanese recently wrote in *The Japan Times*'s 'Readers in Council' section opining that 'selling nuclear power plants is like selling opium or deadly weapons. Japan should stop selling nuclear power plants overseas before it is called a merchant of death.'⁶ Similarly, an opinion poll conducted in November 2011 by Japan's *Mainichi Daily* revealed that 65 per cent of respondents were against exporting nuclear reactors following the Fukushima incident. The country's leading daily, *The Japan Times*, in an editorial termed the nuclear export policy as 'unprincipled'. It added: 'Although the countries that signed the agreements and Japanese makers are certain to welcome the Diet approval of the agreements, the international community would regard Japan's policy as hypocritical.'⁷

⁶ Hiroshi Matsuoka, 'Do not export what you won't use' (Readers In Council), *The Japan Times*, August 28, 2011.

⁷ 'Unprincipled nuclear power policy' (editorial), *The Japan Times*, December 16, 2011.

With respect to civilian nuclear cooperation with India, Japan has been treading cautiously. To assuage the Japanese nuclear-allergic public, a majority of whom remain unaware of India's 'unilateral moratorium on nuclear testing', Japan has been demanding the inclusion of a clause in the pact stating that 'Tokyo would halt nuclear energy cooperation if New Delhi conducts a nuclear test'. The Japanese continued with this demand over three rounds of negotiations, the last being in November 2010. However, post-Fukushima, Japan has urged India more emphatically to join the CTBT. A joint statement signed during Noda's visit notes in this regard: 'Prime Minister Noda stressed the importance of bringing into force the CTBT at an early date.'⁸

Japan is in a better bargaining position than India, since it enjoys monopoly over certain key components including 'reactor vessels' required in nuclear reactors. American and French companies also depend on reactor vessels made by Japan Steel Works Limited. A Japanese media report states: 'Japan Steel Works Limited produces nearly 80 per cent of global supplies of forged nuclear reactor parts.'⁹ Since General Electric and Areva SA also depend on Japanese components, they cannot start new nuclear power generation projects they have bagged contracts for, in order to set up nuclear reactors in India. Thus Japan has 'considerable leverage' over the Indian civil nuclear programme. However, a group of Japanese, especially from the nuclear industry, worries that more suppliers would surface in the future, and that there could be a 'global supply chain without Japanese makers'. This would put the Japanese nuclear power industry at a disadvantage. Therefore, they do not want to prolong negotiations with India. A close look at Japanese thinking on nuclear cooperation with India suggests that Japan faces a dilemma. It is unable to decide between economic gains and the idealistic principle of not selling nuclear technology to a non-NPT member.

The new Centre-Left DPJ is praised in India for initiating negotiations for civil nuclear cooperation, something which the nationalist Liberal Democratic Party (LDP) could not do officially. However, the DPJ has not made significant efforts to convince the anti-nuclear lobbies at home. It stressed the inclusion of a clause in the pact that would enable Japan to nullify the agreement if India conducts another nuclear test. Contrary to the DPJ, the LDP was successful in assuaging domestic opposition when it voted in India's favour during the NSG debate. At that time, the LDP justified its decision by arguing that the provision of nuclear technology to India will help lower carbon emissions, an issue which was closer to the heart of common Japanese then. The DPJ should also make similar efforts to convince the masses from its party platform if it wants to take the negotiations to a logical conclusion.

⁸ See India Japan Joint statement available at <http://www.mea.gov.in/mystart.php?id=100518843> (accessed on December 29, 2011) n. 4.

⁹ 'Uncertainty over test stymies India nuclear pact', *Kyodo News/Japan Times*, October 26, 2010.

Security Cooperation

Both countries are of the opinion that security in the Indian Ocean zone is important as it is a major sea lane connecting East Asia with the Middle East. Japan imports a large amount of crude oil from this region. Both leaders agreed on the following:

- Japan's Maritime Self-Defense Forces (MSDF) and the Indian Navy will conduct joint exercises in 2012.
- Both countries will move ahead with discussions on resuming negotiations over a bilateral pact on peaceful nuclear energy cooperation.

Indeed, closer naval cooperation between India and Japan will be determined by events principally in East Asia and the Indian Ocean.¹⁰ Since maritime commerce is vital for both India and Japan, it is necessary for both to agree to build a stable, liberal, rule-based order in Asia. As much as 97 per cent of India's international trade by volume and almost all of Japan's international trade is sea-borne. This calls for both countries to work together for unimpeded freedom of navigation, which is critical to their security and economic well-being. The decision to start holding joint naval exercises from 2012 is a sign that both countries have graduated from emphasizing shared values to seeking to jointly protect shared interests.¹¹

Two aspects of the India-Japan strategic cooperation may be highlighted here. The first is to build interoperability between their naval forces, which, along with cooperation with other friendly countries, can secure peace and stability in the Asia-Pacific region. A few months ago, former Japanese Prime Minister Abe Shinzo expressed hope that 'sooner rather than later, Japan's Navy and the Indian Navy are seamlessly interconnected'. Presently, Japan has naval interoperability only with US forces. The other aspect is to jointly develop defence systems and cooperation on related technologies for mutual security.

In his address to the Indian Council of World Affairs on December 28, 2011, Noda also underscored the importance of cooperation between the MSDF and the Indian Navy in confronting pirates in the Gulf of Aden off Somalia. In this respect, the decision to hold joint naval exercises is a step forward in the right direction. Through a stronger partnership with India, Japan hopes to put pressure on China, which has intensified its activities in the high seas recently.¹²

¹⁰ Brahma Chellaney, 'Build Japan-India naval ties', *The Japan Times*, December 28, 2011, available at www.japantimes.co.jp/text/eo20111228bc.html (accessed on December 29, 2011).

¹¹ Ibid.

¹² 'Japan, India agree to boost maritime security cooperation', *The Yimouri Shimbun*, December 30, 2011, available at <http://www.yomiuri.co.jp/dy/national/T111229005248.htm> (accessed on December 31, 2011).

China Factor

There are reports that Noda's India visit to boost bilateral ties was part of Tokyo's attempt to strengthen its alliances with Asia-Pacific nations to 'contain' a rising China. According to Lu Yaodong, director of the department of Japanese diplomacy at the Institute of Japanese Studies of the Chinese Academy of Social Sciences, the summit meeting is a continuation of Japan's 'Arc of Freedom and Prosperity' strategy, widely interpreted as an effort to contain China.¹³

China has noted with apprehension that both India and Japan have comprehensively boosted regional cooperation in recent years in the economic and security realms. Relations between the two countries have moved to a multilateral level and have become much more broad-based by including the US and Australia. China sees the Arc of Freedom and Prosperity concept, initiated in 2007 by former foreign minister Aso Taro and seen in Japan as the pillar of its diplomacy, as the latter's strategy to join its allies to contain China's rise in the Asia-Pacific region. China sees this game plan by both India and Japan as Noda's visit to New Delhi came soon after the first round of India-Japan-US trilateral talks in Washington on December 19, and the India-Japan Defence Ministers' meeting in Tokyo in November 2011.

China's assumption reflects its rather paranoid attitude towards other powers' perceptions of its rise. In an interdependent, globalised world where every country is trying to reach out to others, China appears to want to redefine and rewrite the rules of the world on its own terms; Beijing tends to perceive any contrary view as targeting China. In fact, China should take note that there has been a veritable renaissance in India-Japan relations since India embarked on market reforms, and Japan, in turn, has found in India a large, new market. It is only during the past five years or so that both started seeing each other as potential strategic partners, and China's rise more or less has coincided with this.

As Japan strives to move out of a long economic slump, its leadership is under immense pressure to look for measures that might resuscitate its flagging economy. In this regard, Japan has lifted the ban on arms exports thus paving the way for its air and marine forces to upgrade their hardware capability. China views this as a threat. It interprets Japan's decision as possibly reshuffling the international arms trade, and feels that the latter's competitiveness in electrical equipment for military use may squeeze out the market shares of other countries. As Japan now breaks into a politically restricted area, China feels that Japan's move would create uncertainties in the Asia-Pacific region. China also fears that Japan sought and obtained Washington's approval to relax the ban on

¹³ Quoted in 'Japanese Premier Noda's India trip, part of Japan's strategy to contain China', December 28, 2011, available at http://articles.economictimes.indiatimes.com/2011-12-28/news/30564973_1_japan-india-japan-and-india-freedom-and-prosperity (accessed on December 29, 2011).

arms exports as a part of their joint Asia-Pacific strategy to 'contain' China. That India is a possible market for Japanese arms manufacturers also concerns China.

Conclusion

The joint statement issued by Prime Ministers Noda and Singh at the end of the former's visit spoke of bolstering cooperation on security and economic issues. The decision to conduct joint naval exercises in 2012 – to beef up maritime security in the Indian Ocean and to protect sea lanes of communication with a view to secure maritime commerce – is a landmark development. Coming ahead of the 60th anniversary, in 2012, of the establishment of diplomatic ties between the two countries, and amid China's growing military and economic might in the region, Noda's India visit was extremely significant. The agreement to boost trade and investment based on the CEPA and the decision to invest \$4.5 billion over the next five years to promote the DMIC were significant agreements. Japan's summit diplomacy to boost its exports of high-speed railways and nuclear power plants constitute key pillars of its infrastructure export line-up.

In November 2010, India had made a set of proposals to accommodate Japan's concerns on civil nuclear cooperation. The decision to resume talks and break the deadlock on a bilateral pact on civil nuclear energy cooperation, following the Fukushima nuclear accident, is, therefore, a significant achievement. By putting a positive spin on the nuclear deal, Noda welcomed the progress made on the civil nuclear deal at the working level. Given the sensitivities in Japan over the nuclear issue, further heightened by the Fukushima incident, it would perhaps have been too optimistic to expect much in the nuclear field this time around. It is possible that in 2012, when both India and Japan have digested the implications of Fukushima further, an agreement could be reached. It is more a question of 'when' that will happen, rather than 'if'. Noda's visit to India is a demonstration of Japan's long-term commitment to scale up India-Japan bilateral ties to a higher trajectory. The China factor contributes indirectly to bring both countries together, to put the strategic dimension in perspective.