

Economic Security in Emerging Markets

A Look at India, Vietnam, and Indonesia

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THE ISSUE

With the outbreak of the Covid-19 pandemic, supply chain resilience has emerged as a policy priority of the United States and its allies. The issue of supply chains has also raised the profile of emerging economies that offer possible alternatives to China as production platforms for multinational firms. This report surveys economic security policy developments in three major emerging economies: India, Vietnam, and Indonesia. It finds that all are attempting to take advantage of this new focus on supply chain resilience, while (to varying degrees) balancing the economic security risks posed by China's rise. The United States and its allies have an opportunity to work with these emerging economies to shape their decisions about trade, investment, and technology policies in ways that promote mutual economic security and enhance international economic rules and norms.

INTRODUCTION

“Economic security” is an amorphous concept. It can refer to a **wide range** of policies that promote economic growth and competitiveness, protect national security, and shape the international economic environment. It is beyond the scope of this report to adjudicate the precise definition of economic security; instead, this report will focus on how the concept is being operationalized in practice, skewing the analysis more toward the “protect” aspect of economic security. Specifically, these protective policies have taken the form of investment screening mechanisms, which review inbound foreign investments for their impact on national security; export controls, which seek to prevent the leakage of critical technologies to adversaries; and supply chain resilience initiatives, which aim to identify and reduce dependencies on an adversarial nation for critical commodities, components, and products.

With the release of the Biden administration’s **100-day** and **one-year** supply chain reviews as well as the European Union’s **analysis** of strategic dependencies,

supply chain resilience has become the economic security issue du jour in the post-Covid world. Advanced economies will **increasingly** look to an array of emerging economies as alternatives to China in the complex supply chains that span the globe. However, these emerging economies have their own national security and economic interests, distinct from those of more developed economies. Whereas much **attention** has been paid to recent **economic security** policy developments within **advanced** economies, much less attention has been paid to the perspective of emerging markets.

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This report seeks to rectify this knowledge gap by summarizing recent economic security developments in

three important emerging markets: India, Vietnam, and Indonesia. Not only do these three countries account for one-fifth of the global population, they also represent three of the world's fastest-growing economies. Each is economically intertwined with China. Both **Vietnam** and **India** have fought wars with China in the past 60 years and have seen their relations with Beijing sour with the latter's aggressive turn. While all three nations have **territorial and maritime disputes** with China, Indonesia has in recent years begun to take a more **conciliatory** approach to Beijing in its foreign and international economic policies. India, Vietnam, and Indonesia are therefore representative case studies from which the United States and its allies can infer trends in economic security policy and identify where and how engagement between advanced and emerging economies can best uphold the principles of the international rules-based order while also advancing legitimate national security interests.

THE PROLIFERATION OF ECONOMIC SECURITY POLICIES

In recent years, it has become evident that the distinction between economic and national security is rapidly blurring. The United States, beginning in 2018 with the Foreign Investment Risk Review Modernization Act (FIRRMA) and the Export Control Reform Act, has expanded—and continues to expand and refine—its export control and investment screening toolkits. Congress seems poised to establish a new outbound investment screening mechanism, a policy position **endorsed** by high-level officials in the White House. The Biden administration has **overseen** a review of strategic supply chains, while Congress is **considering legislation** aimed at enhancing domestic innovation and providing funding for the reshoring and nearshoring strategic supply chains.

Key allies have followed suit. **The United Kingdom's** new investment screening mechanism came online at the beginning of the year, while the **European Union's** investment screening framework just celebrated its one-year anniversary. As of April 2022, all but **three** EU members have implemented, or are in the process of implementing, investment screening systems. In the Pacific, Japan has created a **new economic security minister position**, while

Australia has led among allied countries in the identification of emerging technologies warranting enhanced screening and control. **South Korea** has stood up an economic security task force to review strategic supply chains.

A primary impetus for these policy developments has been China's rise and aggressive turn. It has become clear that whichever nation (or more likely, group of nations) can master and control a handful of critical emerging technologies—especially those in the fields of artificial intelligence, quantum computing, and biotechnology—will reap enormous economic and strategic advantages. A new technological "**space race**" has been launched, and a winning strategy will properly balance policies aimed at protecting national security with those that promote innovation—aims which can at times work in contradiction with each other.

The Covid-19 pandemic and its enduring supply chain shocks have acted as a catalyst, forcing many nations to reconsider the single-minded focus on efficiency that led to the dizzying array of supply chains that have come to crisscross the globe. The recent Russian invasion of Ukraine has also highlighted the **central role** that economic statecraft has come to play in geopolitics. The United States and allies have responded to Putin's action with a sanctions package unprecedented in scope and severity, while European **dependence** on Russian energy sources has further exposed the national security risks embedded in supply chains.

The structural forces driving the adoption of economic security policy, combined with the global focus on building resilient supply chains, not only portend the dissemination of such policies from advanced economies to emerging ones, but also mean that the position of emerging economies in global supply chains will be a central component of any advanced economies' comprehensive economic security strategy. It is therefore worth taking a closer look at regional emerging economies in the Indo-Pacific to better understand how they are sharpening their own economic security toolkits while leveraging their position in global supply chains to advance their national interests.

COUNTRY SURVEYS

INDIA

Following its independence in 1947, India pursued state-led planned economic growth until rapid **liberalization, privatization, and globalization** began in the 1990s. Since then, India has become the world's **sixth-largest economy**. In recent years, it has also developed a burgeoning tech industry. The nation has produced about 100 "**unicorns**"—young tech companies valued at over \$1 billion—and the city of Bangalore has emerged as the "**Silicon Valley of India**."

China and the United States are both **important economic partners** of India, with the former being its primary source of imports and the latter its primary export destination. The United States is also its **second-largest** official source of foreign direct investment (FDI), though informally, the United States is by far the largest individual source of FDI. China, although **ranking** only eighteenth, accounts for 99 percent of FDI coming from bordering states. India's service sector makes up **53 percent** of India's GDP. The country plays an **important** role in the global pharmaceutical supply chain and is the world's **fifth-largest** exporter of refined petroleum.

India's security situation is complex. During the Cold War, India pursued a foreign policy of nonalignment, but in recent years China's rise has led India's interests in the Indo-Pacific to **increasingly** align with those of the United States and its allies. However, New Delhi's historic ties to Moscow—especially its continued purchases of **Russian military** kit—complicate the bilateral relationship with the United States. Meanwhile, India's relations with its historic geopolitical rival, Pakistan, remain at a **low** point.

Investment Screening

Rising tensions with China have led India to expand its investment screening regime in recent years. India's foreign investment inflows are sorted into one of **two routes**—automatic or government—depending on the business sector and ownership share. Investments qualifying for the automatic route do not require government approval, whereas investments in sensitive or protected sectors must apply for government approval through the relevant approving authority, **typically** the concerned government department. Under Prime Minister Modi, India has nominally made some progress toward **liberalizing** its foreign investment regime—on paper **prohibiting** investment in just eight business categories—but in practice, India's rules governing FDI remain **restrictive**.

India has historically maintained additional targeted security measures for sensitive partners such as Pakistan and Bangladesh. However, in 2020, this policy was **broadened** to mandate that any investor or beneficial owner from a neighboring country invest only through the government route, regardless of sector or ownership share. The new, more expansive screening measures were justified by the Modi government on the grounds that Covid-19, and the ensuing economic disruptions, made Indian firms vulnerable to "**opportunistic takeovers**" by foreign entities. The subsequent restrictions imposed on **public procurement**, likewise requiring bidders from neighboring countries to register with and obtain clearance from the government before bidding, hint at a more salient national security justification.

The national security justification is lent further credence by the fact that China represents the vast majority of FDI inflows originating from neighboring states, making **China** the likely target of the new policy. Indeed, the **majority** of investment currently under review due to the new policy is Chinese in origin. In addition, it has been reported that the new FDI policy was "**in the pipeline**" prior to the outbreak of the Covid-19 pandemic, undermining the argument that the pandemic was the sole justification for its implementation.

Increased scrutiny of Chinese investments is not without economic cost. As of January **2022**, the proposals pending scrutiny stood at \$6 billion, equal in value to **about 10.3 percent** of India's total FDI inflow during FY 2020–2021. This has prompted the Modi government to consider easing reviews on Chinese investment by exempting proposals where the beneficial ownership is less than 10 percent. This reversal highlights the often-unavoidable trade-offs that accompany the implementation of economic security policies.

Strategic Trade Controls

India's strategic trade controls have similarly expanded in response to the national and economic security threats posed by both China and the Covid-19 pandemic. India places export controls on a list of dual-use items in line with guidance set forth by the **four** multilateral export-control regimes (MECRs), of which it is a **member**. India's control list is referred to as **SCOMET**, short for the Special Chemicals, Organisms, Materials, Equipment, and Technologies List. In addition to dual-use items, India also maintains prohibitions and restrictions on the export of items to **specific countries**. If not completely prohibited,

authorization is needed from the government—specifically from the Directorate General of Foreign Trade, Department of Defense Production, or Department of Atomic Energy—to export a listed item.

The outbreak of Covid-19 saw India institute a number of national security-justified export controls on items not listed on SCOMET. These included a de facto ban on the export of vaccines, in order to **protect** domestic supplies. Similarly, early in the pandemic, before vaccines were available, India moved quickly to **block** the export of personal protective equipment. As the virus spread, this ban was **expanded** to include medical equipment such as ventilators and sanitizers. Most recently, India has **banned** the export of syringes to ensure sufficient supply to meet the needs of its domestic vaccine drive.

Concurrently, the national security threat posed by China's rise and aggressive turn has also prompted India to begin implementing certain bans on Chinese products. Following the deadly border clash of June 2020, India enacted "**emergency measures**" granted under its extensive **Information Technology Act** to prohibit domestic usage of **59** apps belonging to Chinese tech giants such as Alibaba, Baidu, and Tencent. Justified on national security grounds, India has continued to ban Chinese apps, bringing the total count to **321**. India also implemented a **de facto import ban** on power equipment from China on cybersecurity grounds and cautioned its state-owned telecommunications companies to exclude Chinese telecom firms from its network upgrading process. In 2021, given concerns about access to sensitive data, India began 5G trials that **excluded** Chinese technology. However, India has so far stopped **short** of banning China's telecom firms.

Other Indian strategic trade controls aimed at China appear motivated as much by protectionism as security. In 2021, India **delayed** approval for imports of Chinese Wi-Fi modules contained in finished electronic devices, underscoring its strategy to undercut China's influence and stimulate its domestic smartphone industry. In February 2022, India announced an import ban on **drones**. Although the United States has **blocked** exports of parts to, and banned investment in, China's largest drone manufacturer—the Shenzhen-based DJI—on national security grounds, India's announcement seems to be at least in part aimed at promoting its own domestic drone industry rather than protecting sensitive data. Not only did India's import ban include a **carve-out** for defense, but this ban also comes in the wake of India's January 2022 **licensure relaxations** and September 2021 **Production-**

Linked Incentives for drones, both policies aimed at spurring domestic production of drones.

Supply Chains

Covid-19 made alarmingly evident the degree to which many developed and developing nations alike had become unsustainably dependent on Chinese supply chains. India has sought to position itself as an alternative. At the same time, rising tensions between New Delhi and Beijing highlighted the vulnerabilities of India's own supply chains and domestic economy. The pandemic has since offered an opportunity for the Modi government to launch initiatives, both domestic and multilateral, aimed at building supply chain resiliency, attracting foreign production, and promoting self-sufficiency.

It has long been an objective of the Modi government to boost India's manufacturing capability. The "**Make in India**" initiative was launched in 2014 to increase investment in and grow over 20 industries, bolstering India's ascent as a manufacturing hub. However, returns on investments in manufacturing proved **disappointing**, even before the disruptions caused by the global pandemic. In response to Covid-19, Prime Minister Modi launched the "**Self-Reliant India Scheme**" in May 2020. The scheme, seen by some as a repackaging of "Make in India," promises \$265 billion to promote domestic production. In announcing the new government support, Prime Minister Modi **emphasized** "the importance of local manufacturing, local market and local supply chains." In addition to the Self-Reliant India Scheme, India has also rolled out production-linked incentives, which are likewise aimed at boosting manufacturing. Originally targeting **three** critical sectors, these incentives have now been expanded to include 13 high-priority industries, **with \$20 billion** made available to entice foreign firms to shift production to India.

Since the pandemic, India has also looked to multilateral agreements to secure its own critical supply chains as well as to leverage growing international anxiety about overdependence on China. Launched along with Australia and Japan, the trilateral **Supply Chain Resilience Initiative** aims to coordinate and incentivize the diversification of supply chains away from China toward the three countries and like-minded partners. Likewise, at the September 2021 Leaders' Summit of the Quadrilateral Security Forum (Quad), it was agreed that the four members—India, Australia, Japan, and the United States—would launch a **Semiconductor Supply Chain Initiative** to map and secure semiconductor supply chains. India and the United

States also relaunched the **U.S.-India Trade Policy Forum**, in which building “resilient and secure supply chains” was identified as a priority, and India’s centrality in the pharmaceutical industry was specifically referenced as a possible synergy. The **India-Japan Industrial Competitiveness Partnership** likewise emphasizes **cooperation** between the two nations in the area of supply chain resilience.

VIETNAM

In just 50 years, Vietnam has emerged from war and poverty to become one of the fastest-growing economies in the Indo-Pacific region. The Southeast Asian nation’s remarkable growth has been **propelled** by its openness to trade and investment. Its comparative advantage in low-cost labor has enabled Vietnam to emerge as a key manufacturing node in global supply chains. However, as Vietnam’s labor costs rise along with wages, the Communist Party of Vietnam will have to develop its own domestic **services sector**, **high-skilled** workforce, and capital-intensive manufacturing if it is to escape the middle-income trap and reach its goal of becoming a high-income country by 2045.

For **decades**, Vietnam has adhered to the dictum of having “fewer enemies, more friends.” It plays a delicate balancing act between China and the United States, two large partners it has had complicated historical relationships with. Confounding the balancing act further, Hanoi, like New Delhi, maintains close relations with Russia, likewise **purchasing** much of its military kit from Moscow. Even as it grows **closer** and bolder in its relationship with the United States—being named a **leading partner** in the nascent Indo-Pacific Strategy and **engaging** in Quad dialogues—Vietnam’s **largest** trading partner and **fifth-largest source** of FDI remains China. Hanoi is therefore careful to manage tensions with China to preserve its investment and trade relationship, which bolsters domestic competitiveness. That said, Vietnam has been **vocal** in its criticism of China’s violations of Vietnam’s **sovereignty** in the South China Sea. In Hanoi’s 2019 National Defense White Paper, China is **implied**—but not named—as the main security challenge and focus of the document.

Investment Screening

Eager to capitalize on its proximity to China amid the exodus of manufacturing companies to nearby countries, Vietnam has established more open investment laws and incentives over the last few years. Approved in 2020 and effective as of January 2021, Vietnam’s updated Law

on Investment **clarified** sectors prohibited for foreign investment and **reduced** the number of “conditional” sectors subject to additional criteria meant to maintain national defense, social order, and security. Priority sectors—such as research and development centers and innovative startups—were granted **incentives** such as reduced corporate taxes and exemption from import taxes on inputs. The year prior, Vietnam **established** separate incentives targeted toward small and medium-sized enterprises.

Notably, this legislation gives the government prerogative to **terminate** or suspend investment activities based on national security concerns. However, national security is not **defined** in the bill, leaving the government room to interpret security concerns in a potentially expansive manner. In addition, the National Assembly maintains authority over **large-scale and sensitive projects**. Other projects, such as those pertaining to airports or requiring extensive population relocations, are subject to the prime minister’s authority. Any project not falling under the domain of the National Assembly or prime minister is **instead** subject to the approval of the relevant province’s People’s Committee.

Vietnam’s investment screening is as much rooted in boosting the quality of investments as in ferreting out security concerns. Screened investments that fall under the jurisdiction of the National Assembly and prime minister are subject to an approval process that involves **reviews** of the investor’s financial capacities, a detailed investment proposal including an assessment of socioeconomic impacts from the project, and an assessment of how the project aligns with national and regional development plans. These criteria complement the objectives of the 2021 Politburo resolution, which establishes a strategy to shift foreign investments to high-tech industries while also monitoring investments for environmental impact. The resolution **prioritizes** projects with multinational corporations, in advanced sectors, and with possible positive spillover effects.

Strategic Trade Controls

Vietnam is not a **party** to any of the four multilateral export control regimes. However, the Southeast Asian nation maintains **minimum** export controls on items such as **military equipment** and encrypted products used for the protection of state secrets and maintaining national security. It also maintains controls on wildlife and plants in accordance with Vietnam’s **obligations** under international agreements. As Vietnam develops, Hanoi has been seeking

to modernize its export control system to bring it in line with its **commitments in the Asia-Pacific Economic Cooperation (APEC) forum**.

While not as active as India in this policy space, Vietnam has also implemented de facto and de jure controls in response to both the Covid-19 pandemic and China's aggressive turn. Early in the pandemic, for example, Hanoi moved to ban the export of certain **Covid-19 medications** as well as **rice**, fearing shortages of both. Out of security concerns, Vietnam's telecommunications companies have also **avoided** collaboration with Shenzhen-based Huawei. However, Hanoi has resisted implementing an official ban, likely in order to avoid angering its northern neighbor. Instead, Vietnam's military-owned domestic telecom firm, Viettel, has worked to develop its own fifth-generation (5G) equipment. Ostensibly manufactured with at least **80 percent** indigenously sourced components, the Hanoi-based firm rolled out its first 5G stations in January 2019. Viettel's success may reveal an additional economic motivation, which may also be behind Hanoi's aversion to Huawei; in fact, a 2019 ban on the import of **used machinery** is more directly linked to bolstering Vietnam's manufacturing sector, rather than countering any immediate national security threat, even if China is the nation most impacted by it.

Supply Chains

As an expanding manufacturing hub, Vietnam has emerged as a central node in regional and global supply chains. A "tiger cub" economy, the Southeast Asian nation has crafted its policies to encourage foreign investment, value-added production, and export-oriented growth. In addition to Vietnam's robust textile and footwear sectors, its electronics industry has achieved strong growth, with exports in that sector **doubling** between 2015 and 2019. Low labor costs, tax incentives, proximity to China, a strong network of trade agreements, and external factors such as the global push to diversify supply chains away from China have all attracted investors to Vietnam, including major tech giants like **Apple** and **Intel**. Around **half** of the South Korean firm Samsung's production occurs in Vietnam, and that one firm accounts for nearly 25 percent of Vietnam's total exports. **Chinese firms** have also flocked to neighboring Vietnam in an effort to circumvent U.S. tariffs on China-originating goods.

In recent years, Vietnam has strengthened its position in global supply chains by joining several bilateral and multilateral free trade agreements (FTAs). Vietnam **signed**

onto the Trans-Pacific Partnership (TPP) in 2016 and ratified its successor agreement in **2018**. The EU-Vietnam FTA entered into force in 2020 and includes **commitments** to open the government procurement process, enhance intellectual property protections, and promote sustainable development alongside increased market access. Vietnam augmented the EU FTA in 2021 with a **trade agreement with the United Kingdom**, while the Regional Comprehensive Economic Partnership—the multilateral trade agreement to which 15 Asia-Pacific nations including China and Vietnam are signatories—came into **effect** at the beginning of this year. In addition, U.S.-China strategic competition has also benefited Vietnam. In a trade diversion study conducted by the Centre for Policy Research, Vietnam's **gains** from the U.S.-China trade war are estimated at \$8.5 billion, compared to \$1.2 billion for India.

INDONESIA

The largest archipelago nation in the world, Indonesia boasts a **strategic geographic position** with access to the Strait of Malacca and the South China Sea. It is **rich in natural resources**, including palm oil; petroleum; and metals such as bauxite, nickel, copper, gold, and silver. Indonesia's geography and resources have defined its development, which has flourished since its contraction during the Asian Financial Crisis of 1997. Today, Indonesia is the **largest** economy in Southeast Asia and the **16th** largest economy in the world.

One of the **founding members** of the nonaligned movement during the Cold War, Indonesia finds itself once again in the middle of a great power contest, this time between the United States and China. Just as Indonesia did during that last era of great power competition, it seeks to maintain a level of **strategic autonomy**, playing off both great powers to its advantage. Moreover, much of Indonesia's foreign policy has historically been driven by concerns centering around the **domestic legitimacy** of the government. These traits of Indonesian foreign policy and strategic thinking are evident in its interactions and relations with both Washington and Beijing. When tensions are high between Jakarta and Beijing over maritime disputes—such as during the Natuna Sea dispute—Indonesia has looked to **enhance military cooperation** with the United States. However, to spur economic growth, Jakarta looks north to China, its largest trading partner and its **second-largest** investment partner. Indonesia also is a key node in the maritime component of Beijing's Belt and Road Initiative (BRI), receiving funds for **projects** including the construction of a high-speed rail line and a hydropower plant.

Investment Screening

An active participant in international forums, Indonesia is nevertheless **prone** to protectionism and uncertain rule of law. Specifically, foreign investors have long complained about Indonesia's **weak enforcement** of contracts, which have complicated the business environment and undermined investment. When President Joko "Jokowi" Widodo, a political outsider, came to power in 2014, he **promised** reforms that would boost investment and hasten **infrastructure** development. To achieve this end, President Jokowi has pursued a deregulatory agenda. The most recent iteration of this was the **2020 Omnibus Law**, which among other provisions eliminated Indonesia's negative investment list, reformed labor laws, and made it easier to register businesses. According to the now-discontinued World Bank ease of doing business index, Indonesia has **jumped** 42 places in the world ranking—from number 114 to 72—during Jokowi's tenure, but many observers have been **disappointed** in the slow pace of reforms and the authoritarian **backsliding** that has also occurred under Jokowi's presidency.

Indonesia **does not** have in place a formal mechanism to screen foreign investments for their impact on national security. Instead, foreign investment is barred **in seven sectors** and certain defense-related investments are restricted to the Indonesian government. In 2020, Indonesia moved to simplify the business licensing process by creating an online application and moving to a "**risk-based approach**." However, the simplified licensing procedure does not screen for national security risks. Instead, business activities are sorted into either high-, medium-, or low-risk categories based on their impact on **health, safety, the environment, and utilization or management of resources**. Nonetheless, there are hints that Indonesia is concerned about the impact that Chinese investment could have on its national security. For example, the 2020 Omnibus Law **established** Indonesia's sovereign wealth fund, the Indonesian Investment Authority (INA). With a mission of investing in infrastructure projects, the INA has received commitments from several foreign investors, including the Japan Bank for International Cooperation. China, however, is noticeably **absent**, likely due to fear about China gaining control over critical infrastructure.

China nevertheless views Indonesia as an important economic partner, and investment between the two Indo-Pacific nations has only continued **to climb** in recent years, despite maritime disagreements and the security concerns

Indonesia may harbor. Chinese investors are particularly interested in Indonesia's **nickel** deposits, which are used in the manufacture of lithium-ion batteries. A top **destination** for BRI projects, Indonesia has attempted to write **conditions** into contracts that would safeguard against China's abusive lending practices. However, the effectiveness of these safeguards is suspect. For example, the Indonesian government promised that no public funds would be used to fund the Jakarta-Bandung High-Speed Railway, a BRI project, but cost overruns prompted the government to **reverse** its position.

Strategic Trade Controls

Compared to India and Vietnam, Indonesia's export control measures are the least aligned with global norms. Indonesia is **not a member** of any multilateral export control regime, nor does it **maintain** a list of dual-use items for control. Jakarta's resistance to strategic trade controls is **borne out** of concern that dual-use controls developed by developed nations are discriminatory toward developing countries and may inhibit Indonesia's access to dual-use technology. Further, Jakarta believes that its **adherence** to nonproliferation treaties governing weapons of mass destruction (WMDs), such as the Nuclear Non-Proliferation Treaty, adequately addresses the concerns of the international community regarding the proliferation of WMDs.

Indonesia instead has made use of trade controls to further domestic economic goals. Export controls on commodities, for example, have been used to incentivize the development of a downstream commodity processing sector. This strategy can be dated to 2009, when Indonesia adopted a new **export policy** incentivizing mining firms to build smelters domestically by prohibiting the export of certain unprocessed metal ores after 2014. The export ban was relaxed in 2017, due to domestic pressure from the mining industry, but **reimposed** in 2020. President Jokowi believes that Indonesia's resource abundance provides the archipelago nation with the **leverage** necessary to entice foreign firms to move manufacturing to Indonesia to gain access to its mineral and metal deposits, enabling Indonesia to move up the manufacturing value chain in a way reminiscent of the East Asian tigers.

In addition to using export controls to push Indonesia up the value chain, President Jokowi, who **champions** himself as a resource nationalist, also views trade controls as a means to attain self-sufficiency, especially in the **agriculture sector**. To this end, his government has **previously** placed an import ban on rice to drive up

domestic prices and spur production. Likewise, earlier this year, fearing potential blackouts, the Indonesian government moved to **ban** the export of coal to shore up domestic supply. In the midst of the Covid-19 outbreak, Indonesia, like India and Vietnam, also **placed** temporary export bans on certain personal protective equipment.

Supply Chains

Despite being Southeast Asia's largest economy, Indonesia's global value chain participation has **been underwhelming** compared to surrounding economies, particularly Vietnam. Like Vietnam and India, Indonesia had aimed to take advantage of the U.S.-China trade war and the ensuing effort by multinational firms to derisk their supply chains by diversifying away from China, and Indonesia's supply chain participation has been growing. However, Indonesia's onerous investment and labor regulations **initially** frustrated the government's efforts to attract relocating businesses. After the government 2020 efforts to **streamline** the foreign investment approval process, Indonesia has had more success persuading firms from the United States, Japan, and South Korea to shift some production out of China and to the archipelago.

Looking ahead, Indonesia's nickel reserves—the **largest** in the world—portend a central position in battery supply chains. Indeed, the Indonesian government is aiming to become a **leading producer** of electric vehicle batteries by 2030. It has set up a **state-owned holding company**, the Indonesia Battery Corporation, to oversee and manage industry development, including coordination with foreign investors. So far, Indonesia has **secured** investment from firms such as Japan's Toyota, South Korea's Hyundai and LG Energy Solution, and China's CATL and GEM. Although Indonesia has also hinted about a possible U.S. investment from Tesla, so far it has failed to materialize.

CONCLUSION AND POLICY RECOMMENDATIONS

India, Vietnam, and Indonesia—by virtue of their size, location, and rapid economic growth—represent key players in this new era of great power competition. Engagement with these three countries, based on an informed understanding of recent economic security developments in each, will better position the United States and its allies to secure their supply chains, prevent the leakage of critical technologies to adversaries, and promote international norms and rules.

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CROSS-CUTTING RECOMMENDATIONS

Concerns about overdependence on China for critical materials have led many advanced countries, including the United States, to consider providing incentives for firms to shift some or all of their production out of the mainland. When considering such policies, the United States and its allies should **avoid providing regional and country-specific incentives**. Such targeted incentives may have political appeal, but they risk subsidizing protectionist policies in emerging markets and engendering resentment among allies and partners as winners and losers are picked. As this report highlights, each of the three major emerging markets surveyed are already taking steps to make their markets more attractive to foreign investors. By providing incentives that are agnostic to country or region, advanced countries can incentivize the continued liberalization of these markets by promoting healthy competition among countries seeking to attract firms and investors relocating from mainland China.

Relatedly, this report highlights the limits of supply chain diversification. Each of the countries surveyed—all of which represent possible partial alternative manufacturing hubs to China—enacted some sort of ban on the export of Covid-related supplies. This should serve as warning to policymakers that supply chain diversification will not solve all the supply chain woes experienced during the Covid-19 pandemic. At some threshold of disaster or emergency, countries will prioritize their own populations over their international commercial obligations. Since countries will face the next Covid-19 (or worse) with the supplies they have, not the supplies they wish they had, the United States and its allies would be wise to **combine any supply chain diversification strategy with the strategic stockpiling of some limited number of items deemed critical** in a time of a global emergency or disaster.

INDIA RECOMMENDATIONS

Of the three countries surveyed, India has in place the most robust investment screening regime and, as a member of the four MECRs, the most comprehensive set

of export controls. India has also awakened to the national security threat posed by China, banning hundreds of Chinese apps and excluding Huawei from the country's 5G trials. In addition, India has sought to attract foreign firms seeking to relocate their operations out of mainland China. The convergence of India and advanced countries on these economic security issues offers several opportunities. First, the app ban and exclusion of Huawei from India's 5G trials on data security grounds signal an increasing alignment on digital issues. Advanced countries should take advantage of this opportunity to **engage with India to develop multilateral norms and standards on a plethora of digital issues ranging from data security to artificial intelligence.**

India's desire to attract foreign firms and build resilient supply chains can be leveraged to **encourage India to make further liberalizing reforms to its restrictive foreign investment regime.** On the other hand, under Prime Minister Modi, India has taken a **protectionist** turn, shunning free trade deals. This is misguided. It is in part due to its free trade orientation that Vietnam has been the most successful at attracting foreign firms diversifying away from China. The United States and its allies should encourage India to do the same. Indeed, there is **evidence** that Prime Minister Modi is warming to new FTAs, recently signing one with the United Arab Emirates, concluding another with Australia, and negotiating others with Canada, Israel, the United Kingdom, and the European Union.

Despite the positive momentum, some of India's economic security policies still raise concerns about protectionism. Specifically, the moves to ban Chinese drones and Wi-Fi modules contained in finished electronic devices have protectionist undertones. Even if these bans do represent real national security concerns and are justified, advanced countries should still seek to **share information and best practices with India, so that strategic trade controls are implemented in a way that uphold international norms and do not undermine legitimate commerce.**

VIETNAM RECOMMENDATIONS

Vietnam's openness to trade and tilt away from China, both economically and politically, has been a welcome development for the United States and its allies. They should **continue to encourage Vietnam's negotiation of FTAs and look to shift production to the Southeast Asian nation where possible to diversify critical supply chains away from China.** Allies should also **help Vietnam improve its export control regime as Hanoi seeks to meet its APEC**

commitments. In addition, allies can **nudge Vietnam to continue to liberalize its foreign investment regime and clarify what constitutes a national security threat.** This will provide foreign investors with greater certainty and opportunity, potentially helping Vietnam fund the additional critical infrastructure and industrial park space it requires to sustain the influx of foreign businesses.

INDONESIA RECOMMENDATIONS

Indonesia poses the greatest challenge for the United States and its allies with regard to the policies discussed in this report. Jakarta's skepticism toward controls on dual-use technology presents a risk that sensitive items will fall into the wrong hands, especially as Indonesia is projected to **move up** the value chain in several dual-use sectors. However, given the country's commitment to a nonaligned foreign policy, appeals to prevent the leakage of dual-use technologies to China are unlikely to resonate. Instead, allies should **make the case to Jakarta that stronger economic security policies will address concerns about non-state actors and domestic and regional security. In addition, more robust export controls may attract the FDI that Indonesia is currently losing out on to countries like Vietnam and India.**

Indonesia's lack of export controls on dual-use technology also has the potential to advantage Chinese firms over those from allied countries, as Chinese firms will have less compunction about potential leakage of dual-use technology to nefarious actors. A similar dynamic is at play with Indonesia's protectionist use of export controls to advance its manufacturing sector. Allied country firms may balk at the environmental, social, and governance (ESG) **concerns** raised by policies that require ores to be refined in Indonesia. Chinese firms, again, may not be so restrained.

Indonesia's desire to attract foreign firms away from China should be seen as a positive development. Allied countries should **encourage the Jokowi government to continue its deregulatory agenda, making it easier for foreign investment to enter the market.** While Indonesia's decision to exclude Chinese investors from its newly created sovereign wealth fund reveals that officials are at least somewhat wary of China gaining control over critical infrastructure, Indonesia continues to **solicit** BRI funds from Beijing, raising concerns about predatory lending practices and Chinese firms controlling critical mineral supplies. Advanced countries should **continue to focus on offering alternative, high-standard infrastructure investments where possible.**

CONCLUSION

The proliferation of economic security policies in emerging economies presents both risks and opportunities for the United States and its allies. If poorly implemented, economic security policies risk stifling investment and innovation and may promote corruption and crony capitalism. Worryingly, they may also advantage Chinese firms over those of developed democracies. On the other hand, allied nations have the opportunity to disseminate best practices—and in doing so, to foster more resilient supply chains, mitigate Chinese economic coercion and predatory investment, and enhance their control over critical technology. Engagement will be most effective when it is based on a sound understanding of the economic and national security context unique to each emerging market. ■

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