Trends and Prospects of India’s Trade with Japan: A Study for the Period 2002-2019

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Abstract

With the fast-growing economics and political synergies between India and Japan, the opportunities for both nations in terms of businesses and commerce are bound to contribute meaningfully in shaping Indo-Japan’s international business story. Since India has opted out of RCEP, engagement with Japan became more important to remain relevant in the international business scenario. The development of a relationship with Japan is also aligned with India’s Act East Policy objectives. This paper is intended to examine the trade trends, intensities and complementarities between India and Japan. For this purpose, different indices have been calculated using secondary data collected from a database maintained by international institutions. The indices and the trends calculated reveals the trade intensity and complementarities between the two nation. As indicated by the trade complementarity index, more economic engagements by India-Japan will not only accelerate India’s growth trajectory but also increase economic gains for enterprises of Japan.

Keywords: Look East, Export-Import, Free Trade Agreement (FTA), Regional Comprehensive Economic Partnership (RCEP), Trade Intensity.

Introduction

Japan and India are the second and the third largest economies in Asia. Japan is one of the few trade surplus economies in the world. The emergence of Japan as one of the top economic power and a trade surplus nation in the world has been possible due to the interaction at economic, political and social levels with different countries. The worldwide role of Japan in the global economy has become of considerable interest to India. India and Japan have made significant progress in their bilateral economic and political relationships in the last two decades. Globally, Free Trade Agreements have become significant in building partnerships for enhancing trade and investment cooperation. On similar lines, India and Japan have taken many initiatives to enhance the bilateral strategic relationship. The governments of Japan and India started negotiating a Comprehensive Economic Partnership Agreement (CEPA) in January 2007. In February 2011, the Comprehensive Economic Partnership Agreement (CEPA) was signed between India and Japan. The agreement came into effect on 1 August 2011. The CEPA with Japan is only one of the two Free Trade Agreements (FTA) that India has signed with OECD (Organisation for Economic Co-operation and Development) economies. The other FTA was signed with South Korea.

The FTA with Japan has its significance as it covers the widest range of goods and services compared with the other FTAs that India has been part of. The FTA with Japan includes comprehensive measures on trade in goods, trade in services and investments. The agreement also ensures that the sensitive
sectors for India, such as agriculture which includes fruits, spices, wheat, rice, edible oils, wines and spirits, are fully protected under the agreement. The signing of the CEPA resulted in the elimination and reduction of tariffs on approximately 90 percent of merchandise traded between India-Japan. The FTA between India and Japan was entered into based on the existence of mutual complementarities and intensities in the respective economies. More amicable political relationships and new policy initiatives have further strengthened the association. However, as we can see from our analysis of data that even after eight years of the signing of the CEPA, the trade and economic engagement between India-Japan is still on the lower side given the size and potential of both economies. Total bilateral trade volume between India and Japan was worth US$3.9 billion in 2002, which has multiplied into US$ 17.6 billion in the year 2019. As per the estimation of the Ministry of Foreign Affairs of Japan, total bilateral trade between India and Japan is expected to reach US$ 50 billion by 2050. Japan is also the fifth largest investor in the Indian economy in FDI. The amount of Japan’s cumulative FDI in India from 2000 to 2020 has been US$ 34 billion, contributing 7% to India’s total FDI inflows during the same period. Investment of Japan in India has been majorly in automobiles, electrical equipment, telecommunications, chemical and pharmaceuticals. As the Government of India has decided to opt-out of the Regional Comprehensive Economic Partnership (RCEP) agreement, more engagement with Japan and other nations became necessary to remain relevant in the Asia-pacific region, economically as well as politically.

Review of Literature

Rajamohan et al. (2008) present an overview of the Indo-Japan relationship over the past several years and analyses the opportunities and challenges for cooperation. He finds that India and Japan have undergone a paradigm shift in their relations and argues that while there are still problems between the countries in the form of distance and communication, the rise of China etc. but the current and future dynamics in macroeconomic fundamental in both the nation mean that India-Japan relations will continue to experience significant development not just politically but also in Economic terms. Subhash Bera (2012) analyses the trade and investment relations between Japan and India. According to him, India’s export and FDI outflow to Japan are yet to gain momentum. However, India’s imports and FDI from Japan show an upward trend. Implementing CEPA between India and Japan is expected to improve the bilateral trade, thereby bridging the knowledge and information gap between the two countries. Khan(2013) observes that the trade flows between India and Japan have experienced a boost after signing CEPA in 2011. However, the flow of Japanese manufacturers in India remains slow mainly because of the poor infrastructure and the increasing presence of China in India. He suggests that India aim to ease the economic overdependence with China, whose presence in India is growing. Ram Upendra Das (2014) argues that bilateral trade between India and Japan is below potential, which sets the basis for harnessing the full benefit of India-Japan CEPA of its trade and investment augmenting potential. Besides, the implementation of CEPA has played an important role in providing leadership in EAS, and it will help build consensus on various economic issues. Karnik and Burangle (2018) find a boost in Intra Industry Trade with Japan, especially in manufacturing products. Narsapur (2018) attempts to study the mutual benefit claim of international economics between Japan and India. He highlights that both Japan and India are highly benefitted from the strengthening trade and diplomatic ties between them. India’s Look East Policy has gained better trade ties for India, and the Investments are benefitting the Indian Economy by providing it with better resources, development projects and improved infrastructure. India’s Trade Agreements (2018) observed that the share of the regional grouping in India’s trade has increased. India can harvest immense business opportunities through bilateral trade, and it will foster the development of India as a manufacturing hub and lead to the expansion of infrastructure. B.P.Sarath Chandran (2018) argues that the RCEP agreement will result in the influx of cheaper commodities to India, especially from China, which may affect the manufacturing sector. He believes that India’s advantage lies primarily in the services sector. Thus comprehensive agreement
must include trade, services and other investments. Chand and Tokas (2020) examine the prospect for expanding trade and investment between India and Japan in the service sector. Japan’s potential to provide us with a new untapped market and its technological expertise makes it an attractive trading partner. Thus, linguistic and cultural gaps, lack of understanding and awareness of each other’s market should be bridged to realise the benefits of bilateral trade between India and Japan and CEPA. Radha Raghuramatrumi (2020) has assessed the bilateral trade relations between India and Japan and tried to understand the commodity trade potential between the two countries. According to him, the bilateral ties between the two countries are strengthening, and they have export complementarities between them, thus making trade feasible. Besides, Japan’s investment in India’s core and heavy industries, its role in India’s high-end infrastructural development and its decision to have defence relations with India are the signs of the rising strong bilateral ties between the two countries. India and Japan: Entering a New Era of Economic Relationship identifies that some areas of bilateral trade between Japan and India are still weak. Although India’s trade with the rest of the globe is increasing with Japan, the pace is not up to the mark. Japan’s FDI flow to India in 2008 was lesser than its investment in smaller economies like Vietnam. India and Japan have the potential to double their trade in the coming years if issues like trade facilitation and trade barriers are addressed amicably in the coming years.

**Research Gap**

The existing literature has theoretically and empirically examined the India-Japan relationship from a need for India’s economic development. The above literature on the bilateral trade between India and Japan suggests that India’s intention of greater regional economic integration resulted from the Look East policy only. India’s relationship with Japan has been amicable. Because of such positivity in the relationship, India has benefited from Japan’s financial aid. The existing research has highlighted economic and security engagements between India and Japan; There are fewer studies that focus on examining the trade intensity, especially after the signing of CEPA in 2011 and mutual trade complementarity. In the endeavour of enhancing on those findings, this paper is an attempt to examine the changes in the trade intensity which might have changed because of the signing of the Free Trade Agreement by India and Japan. Additionally, the paper tries to examine trends in bilateral trade but with the relative importance of changes in quantity and price in the value of India’s exports to Japan and imports from Japan.

**Objectives of the Study**

- To examine the trends and trade patterns of India and Japan.
- To examine the trade intensity between India and Japan.
- To examine the trade complementarities between India and Japan.

**The Hypothesis of the Study**

H1: India’s trade with Japan during the period (2002-2019) has witnessed a rising trend.
H2: India’s exports to Japan (2002-2019) have witnessed significant growth.
H3: India’s imports from Japan (2002-2019) have not gone up significantly.
H4: India’s has experienced a strong trade intensity with Japan (2002-2019).

**Period of the Study**

The study covers 18 years, i.e. from 2002 to 2019. The choice of the initial year was made keeping in view the time of expansion of India’s Look East Policy in which the ‘Extended neighbourhood’ concept was introduced. India wanted to widen its area under the Look East Policy by including Japan and other Asia-Pacific countries in the second phase. The cut-off year for the study has been decided to keep in view the data-availability factor.

**Methodology of the Study**

The study is mainly based on secondary data. Secondary data were collected from literature and reports, bulletins, statistics published by various government organisations. The secondary data collected has been tabulated in a systematic manner for the purpose of examining the trend of
Trade between India and Japan during the period mentioned. Different indices are being developed by many prominent researchers to examine the international trade patterns and prospects. Indices suggested by World Bank and other international institutions are used in this paper to assess whether greater economic cooperation is possible between India and Japan. Indices used in the paper to study trade are Trade Intensity Index (TII) and Trade Complementarity Index (TCI).

**Trade Intensity Index**

The Trade Intensity Index was proposed by Brown in 1949. It was further augmented by Kojima in 1964. The Trade Intensity index is the ratio of two export shares. The trade intensity index (TII) is used to determine whether the volume of mutual bilateral trade between two nations engaged is larger or smaller than that is expected based on those countries relevance in the world’s total trade volume. The index may take any value between 0 and +∞. Values greater than 1 indicate an ‘intense’ trade relationship, and less than 1 indicate that the trade relationship is ‘passive’. It is calculated as:

\[
TII = \frac{\frac{X_{ij}}{X_{it}}}{\frac{X_{wj}}{X_{wt}}}
\]

Where \(x_{ij}\) = the values of country i’s exports to country j.

\(x_{wj}\) = world exports to country j.

\(X_{it}\) = country i’s total exports and

\(X_{wt}\) = total world exports.

**Trade Complementarity Index**

Michaely introduced the trade complementarity indices (TCIs) in 1996. The range of the trade complementarity index lies between 0 and 100. When the trade complementarity index is 0, no goods are exported by the particular country to the partner country. When the index is 100, it implies that the export share of one country and import shares of the partner country exactly match. A high trade complementarity index may indicate that two countries are expected to benefit from increased trade volume and vice-versa. The Trade Complementarity index between country k and country j is calculated as follows:

\[
TC_{ij} = 100(1 - \sum (\frac{m_{ik} - x_{ij}}{2}))
\]

Where \(x_{ij}\) = the share of good i in the global exports of country j

\(m_{ik}\) = the share of good i in total imports of country k

**Trade Relationship between India and Japan**

Japan and India are amongst the most prominent economies in Asia as well as the world, with GDP sizes of US$5 trillion and US$ 2.9 trillion, respectively. India has been one of the fastest-growing economies globally, clocking to a growth rate of 5.02% in 2019. The population size of 1.2 billion provides a large potential market in India. Also, the young population of India provide a large demographic dividend. India’s relationship with Japan has been cordial in politics and economics. The cordial relationship has been going on since the pre-independence era. India is on the path of becoming a strong and stable nation with consistent GDP growth and higher forex reserve. (as of 2019, the forex reserve of India is US$ 463.47). More economic engagement with countries like Japan would further strengthen India growth story.

| Items                              | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|------------------------------------|------|------|------|------|------|------|------|------|------|------|
| GDP growth (%)                     | 4.19 | -0.115 | 1.5 | 2 | 0.3 | 1.2 | 1 | 2.17 | 0.323 | 0.654 |
| GDP current prices (US$ bn)        | 5700 | 6157 | 6203 | 5156 | 4849 | 4383 | 4939 | 4867 | 4955 | 5082 |
| GDP per capita, current prices (US$) | 44,508 | 48,168 | 49,480 | 48,280 | 43,940 | 38,780 | 38,000 | 38,387 | 39,159 | 40,247 |
| Inflation, average consumer prices (%) | -1.895 | -1.674 | -0.03 | 0.35 | 2.76 | 0.8 | -0.12 | -0.229 | -0.098 | 0.592 |

Table 1: Macroeconomic Snapshot of Japan
Table 2: Macroeconomic Snapshot of India

| Items                                | 2010     | 2011     | 2012     | 2013     | 2014     | 2015     | 2016     | 2017     | 2018     | 2019     |
|--------------------------------------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| GDP growth (%)                       | 8.5      | 5.24     | 5.48     | 6.54     | 7.18     | 7.93     | 7.11     | 7.04     | 6.12     | 5.02     |
| GDP current prices (US$ bn)          | 1676     | 1823     | 1827.6   | 1856.7   | 2035.4   | 2111.8   | 2263.5   | 2653     | 2713     | 2875     |
| GDP per capita, current prices (US$) | 1357.6   | 1458.1   | 1475     | 1550.1   | 1646.8   | 1758     | 1861.5   | 1981.7   | 2005.9   | 2104.1   |
| Inflation, average consumer prices (%)| 10.53    | 8.73     | 9.3      | 10.93    | 6.37     | 5.88     | 4.97     | 3.78     | 4.56     | 2.31     |
| Population (mn)                      | 1234     | 1250     | 1213.4   | 1223     | 1267     | 1283     | 1299     | 1339     | 1353     | 1366     |
| Current account balance (% of GDP)   | -3.253   | -3.429   | -4.8     | -1.74    | -1.31    | -1.058   | -0.7     | -1.439   | -2.418   | -1.035   |
| Foreign Exchange Reserves, (US$ bn)  | 300.48   | 298.74   | 294.4    | 292.05   | 304.22   | 341.64   | 371.27   | 412.61   | 399.17   | 463.47   |
| Foreign Exchange Reserves (US$ bn)   | 1105     | 1296     | 1268.1   | 1266.8   | 1260.6   | 1233.2   | 1216.9   | 1264     | 1270     | 1322     |

(Source: http://www.worldbank.org)

Results and Analysis

Trends in Trade

In merchandise trade, there has been no significant change in market shares. India’s trade with Japan during 2002-19 has witnessed a rising trend. The average growth rate in total trade has been 9.68% during the period. The signing of the Free Trade Agreement helped increase the trade volume between India and Japan. The total trade growth figure of 31.96% in 2010 substantiates the fact. But the trade figures eventually stabilised during the course.

Exports - India’s exports to Japan were US$1787 million in 2002, representing an export share of 3.57%. The figure has increased to US$4953 million in 2019, but the share of India’s exports has decreased to 1.53%. During the period, the average share of India’s exports was 2.09%.

Imports - India’s imports from Japan were US$2140 million in 2002, representing an import share of 3.72%. The figure has increased to US$12,656 million in 2019. The share in India’s imports has decreased to 2.64%. India’s import share from Japan has been consistently over 2%. During the said period, the average share was 2.63%.

Trade Balance - India has a consistent trade deficit balance with Japan. During the said period, the trade deficit went up from US$353 million in 2002 to US$7702 million in 2019. The average trade deficit has been US$3917 million during the period.

India and Japan signed a Free Trade Agreement viz. Comprehensive Economic Partnership Agreement (CEPA) in February 2011 and implemented in August 2011. The agreement is one
of India’s most comprehensive trade agreements to date. The FTA was signed keeping in mind the liberalisation of trade in goods, services as well as investment flows between the two countries. However, trends in bilateral trade suggest that the trade potential remains untapped. With the synergies of both India and Japan, there is a huge prospect to enhance bilateral trade.

### Table 3: Trends in India-Japan Trade (U.S. $ million)

| Year | India's export to Japan | Share in India's total export (%) | India's import from Japan | Share in India's total import (%) | Total trade | Growth rate (%) |
|------|------------------------|----------------------------------|---------------------------|----------------------------------|-------------|-----------------|
| 2002 | 1787                   | 3.57                             | 2140                      | 3.72                             | 3927        | --              |
| 2003 | 1710                   | 2.88                             | 2333                      | 3.22                             | 4043        | 2.96            |
| 2004 | 1848                   | 2.43                             | 2962                      | 2.99                             | 4810        | 18.97           |
| 2005 | 2455                   | 2.45                             | 3679                      | 2.61                             | 6134        | 27.53           |
| 2006 | 2804                   | 2.31                             | 4743                      | 2.66                             | 7548        | 23.05           |
| 2007 | 3263                   | 2.24                             | 5833                      | 2.67                             | 9096        | 20.52           |
| 2008 | 3624                   | 1.99                             | 7784                      | 2.47                             | 11409       | 25.42           |
| 2009 | 3216                   | 1.82                             | 6689                      | 2.51                             | 9905        | -13.18          |
| 2010 | 4805                   | 2.18                             | 8265                      | 2.36                             | 13070       | 31.96           |
| 2011 | 5593                   | 1.86                             | 11218                     | 2.43                             | 16811       | 28.62           |
| 2012 | 6416                   | 2.22                             | 12363                     | 2.53                             | 18779       | 11.70           |
| 2013 | 7325                   | 2.18                             | 10490                     | 2.25                             | 17815       | -5.13           |
| 2014 | 5757                   | 1.81                             | 9964                      | 2.17                             | 15721       | -11.76          |
| 2015 | 4454                   | 1.69                             | 9628                      | 2.46                             | 14082       | -10.42          |
| 2016 | 3827                   | 1.47                             | 9808                      | 2.75                             | 13635       | -3.18           |
| 2017 | 4499                   | 1.52                             | 10465                     | 2.36                             | 14964       | 9.75            |
| 2018 | 4751                   | 1.47                             | 12578                     | 2.47                             | 17329       | 15.80           |
| 2019 | 4953                   | 1.53                             | 12656                     | 2.64                             | 17609       | 1.62            |
| Average | 4060                   | 2.09                             | 7978                      | 2.63                             | ---         | 9.68            |

(Source: International trade statistics)

### Table 4: India’s Trade Balance with Japan (U.S. $ million)

| Year | India's export to Japan | India's import from Japan | Total trade | Trade balance |
|------|------------------------|---------------------------|-------------|---------------|
| 2002 | 1787                   | 2140                      | 3927        | -353          |
| 2003 | 1710                   | 2333                      | 4043        | -623          |
| 2004 | 1848                   | 2962                      | 4810        | -1114         |
| 2005 | 2455                   | 3679                      | 6134        | -1223         |
| 2006 | 2804                   | 4743                      | 7548        | -1939         |
| 2007 | 3263                   | 5833                      | 9096        | -2569         |
| 2008 | 3624                   | 7784                      | 11409       | -4160         |
| 2009 | 3216                   | 6689                      | 9905        | -3473         |
| 2010 | 4805                   | 8265                      | 13070       | -3460         |
| 2011 | 5593                   | 11218                     | 16811       | -5626         |
| 2012 | 6416                   | 12363                     | 18779       | -5947         |

(Source: International trade statistics)
World trade. From the index calculated, it is revealed that India’s trade intensity index with Japan has been less than 1 in every year considered. Similarly, Japan’s trade intensity index with India is less consistently below 1. The average of India’s trade intensity index and Japan’s index are .46 and .24, respectively. The index implies that trade intensity between India and Japan is less than expected. More notably, India’s trade intensity with Japan has decreased from 0.679 in 2002 to 0.398 in 2019. The same is the case in Japan’s index with India. Even though the FTA has lifted the volume of trade between India and Japan, it could not intensify the trade in respect of world trade. Therefore we can safely assume that the volume in trade has gone up not only with India but also with the rest of the world. There is scope for further improvement in the mutual trade between India and Japan. In this context, Free Trade Agreement between India and Japan can be reviewed and incorporate policies that would intensify the mutual trade.

### Table 5: Trade Intensity Index between India and Japan (2002-2019)

| Year | India’s TII with Japan | Japan’s TII with India |
|------|------------------------|------------------------|
| 2002 | 0.679                  | 0.085                  |
| 2003 | 0.562                  | 0.099                  |
| 2004 | 0.487                  | 0.108                  |
| 2005 | 0.491                  | 0.119                  |
| 2006 | 0.478                  | 0.142                  |
| 2007 | 0.496                  | 0.191                  |
| 2008 | 0.417                  | 0.212                  |
| 2009 | 0.407                  | 0.244                  |
| 2010 | 0.474                  | 0.255                  |
| 2011 | 0.393                  | 0.285                  |
| 2012 | 0.460                  | 0.275                  |
| 2013 | 0.493                  | 0.272                  |
| 2014 | 0.421                  | 0.273                  |
| 2015 | 0.427                  | 0.328                  |
| 2016 | 0.384                  | 0.333                  |
| 2017 | 0.397                  | 0.331                  |
| 2018 | 0.378                  | 0.384                  |
| 2019 | 0.398                  | 0.404                  |
| Mean | 0.460                  | 0.241                  |

(Source: Author’s calculation from WITS and ITC)
The Trade Complementarity Index between India and Japan has been calculated for 99 product groups classification based on HS-2 from 2002 to 2019. The index indicates a possibility of mutual trade gain from increased trade between the two countries. The index was lowest in 2002 with 49.84 and increased gradually with an average of 59.08 in the said period. The index has reached its highest in 2019, with the index measuring 64.59. The higher Trade Complementarity Index indicates that the exports and imports of India and Japan have been complementing each other. But as we have seen, that trade intensity index was not significant enough. In contrast, the Trade Complementarity Index, with an average of 59.08, indicates a very significant scope to intensify the trade between India and Japan.

**Table 6: Trade Complementarity Index between India and Japan (2002-2019)**

| Year | TCI  |
|------|------|
| 2002 | 49.84|
| 2003 | 50.38|
| 2004 | 52.08|
| 2005 | 53.59|
| 2006 | 57.83|
| 2007 | 60.25|
| 2008 | 61.54|
| 2009 | 60.69|
| 2010 | 62.5 |
| 2011 | 61.29|
| 2012 | 60.56|
| 2013 | 62.49|

**Summary**

India’s trade with Japan during 2002-19 has witnessed a rising trend. The average growth rate in total trade has been 9.68% during the period. Therefore hypothesis, India’s trade with Japan during the period has witnessed a rising trend is accepted. During the period, the average share in India’s export was 2.09%. The export share has been consistently under 2% in every year considered. Therefore hypothesis, India’s exports to Japan during the period have witnessed significant growth is rejected. On the regard can be rejected. India’s import share from Japan has been consistently over 2%. The highest import was 3.72% in 2002, and the lowest share was 2.17% in 2014. During the said period, the average share was 2.63%. Therefore hypothesis, India’s imports from Japan during the period have not gone up significantly is accepted. The revision and correction of the free trade agreement between India and Japan would further enhance the volume of bilateral trade. From the trade intensity index table, we can safely conclude that trade between India and Japan has not been intense w.r.t. trade with the rest of the world. The intensity index was highest in 2002 with 0.679 and gradually declined and
reached the lowest in 2018 with 0.378. The average trade intensity index between India and Japan was 0.460, which indicates great trends. Therefore, the hypothesis, India has experienced a strong trade intensity with Japan during the period is rejected. But there is a lot of potential for enhancing the mutual trade between the two countries, as indicated by the trade complementarity index. (average 59.08).

Conclusion
Since the 1990s, the regional economic integration process has been growing rapidly. In line with the objectives of more economic integration and endeavour of India’s Act East Policy, the Government of India has been focusing on deepening the relationship with Japan. Japan’s government has expressed interest in aligning with the Indian Government’s growth visions. Most of India’s population is under 35 years of age which would certainly provide demographic dividends to the nation. The availability of a largely young and dynamic workforce is an attractive opportunity for global companies looking to invest in India. Several Japanese big multinational companies have been already accelerating their plans for setting up or expanding their operations in India. With the fast-growing economics and political synergies between India and Japan, the opportunities for both nations in terms of businesses and commerce are bound to contribute meaningfully in shaping Indo-Japan’s international business story. More economic engagements by India-Japan will not only accelerate India’s growth trajectory but also increase economic gains for enterprises of Japan. As Japan’s Prime Minister Shinzo Abe had said - “A strong India benefits Japan, and a strong Japan benefits India.”

Limitations of the Study
Research work cannot be completed without any limitations. Despite the best efforts, the study suffers from certain limitations. Limitations of our study are described as follows:

The study is based on secondary data, which were collected from the data maintained by international organisations. The limitations in the collection and maintenance of data by the concerned organisation are likely to pass into our analysis.

The study covers 18 years, i.e. from 2002 to 2019. However, the longer period of study could have been considered for analysing the trends of trade and investment, which could reveal a different picture.

The used only Trade Intensity Index to assess the intensity of trade between India and Japan. A deeper study could be done using other indices like Export Intensity Index, Import Intensity Index, and Export Diversification (or concentration) index along with the Trade Intensity Index.

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