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Why China has overtaken the Indian economy

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Abstract

In Asia there are two counties India and China who share the two largest population of the world. Chinese and Indians alike, economic life is hard despite the fact that reforms and globalization have created various new opportunities and as such both countries have witnessed an emerging middle class with Americanized tastes and preferences, irrespective of this however, both countries remain very poor. In 1995 for the first time trade had exceeded US$1 billion between them. They have lately received a lot of international attention being viewed as emerging giant economies as they both play key roles at the international level. For example China has been a permanent member of the Security Council at the UN, while India who has leads the Non-Aligned Movement for years and is still vying for a similar position. Furthermore, India has been one of the founding members of the WTO and has played a prominent role as one of the developing nations whereas China has had to fight for decades to obtain its admission into this international organization. They have lately received a lot of international attention being viewed as emerging giant economies as they both play key roles at the international level. While both China and India have an extended history of international trade going back centuries ago, both their economies were until recently highly protected and controlled to a large extent albeit that their political systems are very different. China is still a very unique case in the sense that while it has allowed its economy to be opened to Capitalists MNCs, it is still governed by the Communist Party with a strong leadership not giving away state power. The phenomenon of globalization has however affected both these countries. Given their large populations, big land mass and abundant resource bases, they have both relied on indigenous capabilities to a large extent to develop a wide range of goods for their internal markets. With the Japanese economy facing intense macroeconomic challenges and its Prime Minister publicly apologizing for Japanese misbehaviors towards China and South Korea in order not to close its doors for business opportunities in that region, and America after the 11th of September rallying support from India and China who until recently were particularly highly critical of American Foreign Policy, the importance of these two nations in world politics and in the globalization process are not to be neglected. In this paper I tried to discussed differences and similarities of these two countries and furthermore to know the reasons why China has overtaken the Indian economy is highlighted.

Keywords: Globalization, Political, Macroeconomic, Economy.

1. Introduction

What is globalization? Globalization or (globalization) is the process by which the people of the world are unified into a single society and function together. Globalization is often used to refer to economic globalization: the integration of national economies into the international economy through trade, foreign direct investment, capital flows, migration, and the spread of technology. This process is usually recognized as being driven by a combination of economic, technological, socio-cultural, political and biological factors. The term can also refer to the transnational dissemination of ideas, languages, or popular culture.

The world's national economies are being redefined and interconnected at an unprecedented rate due to an increase in the mobility of capital as a consequence of deregulation, new communications and information technology. India became independent in 1947 from the British and its population grew from 340 million to exceed one billion in 2000.

"Indian economy will become a $5.6 trillion economy by fiscal 2020, at current market price, from the $1.73 trillion in fiscal 2010-11," Dun & Bradstreet India Senior Economist Arun Singh.

"Total public spending on transport and water infrastructure has fallen steadily since the 1960s and now stands at 2.4% of GDP," the article says. "Europe, by contrast, invests 5% of GDP in its infrastructure, while China is racing into the future at 9%." For data on India, Ryan's office cited a July 21 Economist piece titled "India's economy, the half-finished revolution." It quotes Morgan Stanley economist Chetan Ahya predicting that India's infrastructure spending will "still be an adequate 8% of GDP this fiscal year." The article goes on to say that India's government what is that share to rise to 10 percent over the next five year. For India's statistics, we found a January 2011 report from the Indian government's Secretariat for Infrastructure, which said that the India wants investment in its physical infrastructure to reach about 9 percent of GDP by 2011-2012. Tables in the report projected the number would actually be 8.37. The report estimated that India spent nearly 8 percent of its gross domestic product on infrastructure in 2010-2011, and 7.51 percent in 2009-2010. The number was 5.71 in 2006-2007 and 6.44 percent in 2007-2008. Those numbers approximate The Economist's statistics, though they don't reach the 10 percent cited by Ryan. Its per capita GDP is US $475 making it one of the poorest countries, although paradoxically it has had nuclear capabilities since 1974 and is one of the few countries in the world which has its own satellite in orbit due to an indigenous space program. India has always faced internal problems connected to caste and wealth, religion and language issues amongst others and as a democracy it has survived and can boast to have a free press, regular elections and an independent judiciary. It has definitely opened itself to globalization especially as a result of changes in economic policies in the early 90's

China is the world's most populated country with 1.3 billion people. The GDP per head is US$ 870 and had a total GDP of US$1.1trn in 2000 as compared to India's total GDP of US$2233 billion for the same period. In 2003 China's GDP hit 11.694 trillion yuan (US$1.414 trillion), According to the National bureau of statististics, China's growth rate in the previous five years have been 8.8 percent with a revenue of 3 trillion yuan.China's economy grew 10.3 percent in 2010, official data showed last week. Plagued by a series of civil wars and invaded by Japan until the end of World War II, China then experienced communism under Chairman Mao. Relying strongly on autarky to achieve about-intensive industrialization which subsequently failed, China suffered from a severe setback during the cultural revolution which saw several cadres being taken to the countryside to work as peasants. Deng Xiao Ping however recognized the backwardness of China and realized the suffering done to their own people. He then steered the country towards a progressively open economy under the control of the Communist party whereby in the 1980s various special economic zones were established to attract for capital.

1.1 *Encounter with Globalization*

The race is on in earnest. It's a fiscal showdown with two of the fastest growing economies in the world. The Red Dragon and the Four Lions are locked in trade and industry combat. From **competing to be the best in the outsourcing industry to capturing the utility manufacturing** industries, this face-off is enacted on a global stage. Some of the major impacts feared by nations due to globalisation are:-

- The giving away of national sovereignty and some new forms of colonialism by MNCs.
- The decline of the State as a protector of individuals and groups and the rise of virtual states depending on investment and production abroad, not to mention the fact that due to the size of the the top forty MNCs having GDPs bigger than a country like Turkey for example, this creates an impression that governments have surrendered their power to capitalism.

This sort of argument is very common in India today and has been used to attract a lot of support from nationalist parties (swadeshi philosophy) and trade unions specially because they associate the presence of MNCs with colonialism.

This research paper outlines some of the factors that have influenced the globalization process in China and India, while analysing commonalities and differences in their approaches. While this research paper centers on the globalization process in China and India, around economic reforms it also highlights the cultural element of globalization as well. It encompasses new avenues developing with increasing human migration and communication which favour economic and technological change in a way which is described by Appadurai as 'the complex ways in which culture and nation are refracted and reinvented through the disjointed social, economic, technological and ideological dimensions of the contemporary world .

This paper shows the impact of globalization on the formulation of two different styles of the management and implementation of public policy in relation to issues like privatization of State Owned Enterprises, government approaches to deal with FDI and technology policy and development. Opposers of globalization in India emphasise the link between promotion of FDI and the international institutions like the World Bank, the International Monetary Fund and the World Trade Organisation who all support economic liberalism and reduction of government intervention while fully supporting privatization.

In the case of China, in the absence of democracy has meant that socio-political tendencies which may be latent but are invisible, do not hinder the march to globalization. However the Chinese government will fairly soon have to change a series of policies when adhering to

WTO rules and regulations, in other words, the State will have to give away some of its sovereignty on economic matters and international trade. Although it can be argued that these two giant economies have to face a different set of challenges because of the major differences in their political systems, they are both attracting a significant volume of foreign direct investment due to their size and low level of capital intensity.

Foreign direct investment is the locomotive of globalization and because both China and India unlike many other third world countries have a sizeable number of highly skilled workers as well as an enormous supply of low unskilled labour, their development are closely linked to similar sectors in which they have comparative advantage and therefore face similar challenges.

Given the capacity of China and India to be competitive in both labour intensive sectors as well as in capital intensive product lines, this particularity has reduced the dependence of the region on trade with industrial countries and open up further opportunities for intra-asian trade and will be reinforced furthermore by the flow of direct investment from Japan and other industrial countries.

They both have a substantial number of people who have migrated all around the world for various reasons and while this migrating process was very common at the time colonization had just started many are still emigrating to countries having higher standards of living and the days of migration of cheap labour are over. Most of the migrants are now highly demanded professionals.

While the Chinese overseas network has played a major role in bringing FDI into China, India has tried promoting a similar policy towards its Non Resident Indian(NRI) and the Global Organisation of People of Indian Origin(GOPIO) is also actively engaged in the promotion of International business.

However once in the United States and in other countries of the OECD, those very same Indian talents participated in the creation of intellectual capital and it is a fact that technical knowledge is vital as a central factor of production. Also many of them became entrepreneurs setting up their own businesses. The Silicon Valley is a very good example of this phenomenon and according to various IT sources and reports, Indian scientists and entrepreneurs are in decisive numbers in most of the major companies and in fifty per cent of start-ups. In this field India has the advantage of having the second largest pool of English- speaking scientific labour in the world, and the cost of that labour in India is among the lowest[1] . One Silicon Valley joke is that the I in IC (Integrated Circuits) stands for Indian and C for Chinese as a sizeable number of

Chinese Scientists are also present in the Valley except that they do not have as much linkages with the home industry because of the disadvantage of English language.

Despite the brain-drain effect the positive side of the story is that due to a lack of trained personnel in the industrialised world, and given the Indian connection a lot of linkages have been developed with India in this field, so much so that according to India Today many of the final year students of the famous Indian Institutes of Technology have already become software entrepreneurs running projects and research and development for many of their senior college fellows now in the USA. While in 1999, Indians received 47% of the 100,000 high-skill visas issued by the USA, an interesting development in India lately has been

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the massive investment made by Indian based in America in ploughing back some US$300million into more technology education in India.Based on the US Silicon Valley model, India has created its own cyber city in Bangalore and Microsoft giant made sure it is present in India by locating itself there. According to Business Asia, India has 250,000 software workers which makes about 30%of the world total IT workforce and in the past ten years, they have been involved in developing half of the world software programs through export contracts. Indian IT companies are now listed on the NASDAQ. The IT sector in India has not only become one of the leading players in software development but another factor which is closely linked to this is the fact that the movement of labour even in IT has become unnecessary at times as data are transferred electronically

1.1.1 Economic Reforms in China and India 3

One of the most important political events of the late twentieth century, has been a world shift towards more liberal policies and free trade with reduction of protectionism and it has happened in most regions of the world with remarkably few exceptions . In many countries, the public debt became unbearable and the ideology of promoting import substitution and capital controls were replaced by policies in favour of pro-market and pro-foreign investment. Earlier on a combination of nationalism and sick home economies made it difficult for China and India to take advantage of globalization.

At the very outset , it must be emphasised that in the case of both China and India, reforms were initiated more as a result of compulsion rather than due to any other reasons albeit that both countries initiated the reform process at different times with **Deng Xiao Ping** in 1979 and Dr. **Manmohan Singh** Indian Finance Minister in 1991.

In fact the shift towards economic liberalism and to a more and more free-market economy has been noted worldwide specially after the demise of the Soviet bloc and the consequence of the latter was instrumental in the shift of the Indian economy towards liberal reforms. That was due to an excessive dependency of exports from India to the USSR. With the collapse of the USSR, India had to face a severe economic downturn coupled with the reaction of the Gulf War in 1991 where again India lost considerable businesses as Iraq was not only an important importer of Indian goods and services, but was also a major provider of oil.

In both countries, it would be right to say that economic reforms did not take place because entrenched political and business leaders suddenly discovered the virtues of a capitalist economy but rather, it became apparent that a certain historical approach of running centrally planned economies became bankrupt after forty years of growing state intervention through state owned enterprises and this state-led development finally ran out of steam as argued by **Bryanetal** . China had the advantage of having started economic reforms much earlier ie in 1979 as compared to India, and this can be judged by looking at the economic progress of China during the last two decades and the reasons as to why it continues to be the largest destination of FDI outside the US, Europe and Japan.

Despite the reforms and the continued economic growth in India, a team of leading American economists from Harvard and Columbia have lead a comparative study with Chinese economic growth during the same period and have noted that India did not succeed in linking foreign investors, capital and expertise with a large and low-cost labour force by assuring investors of the basic quality infrastructure, physical security, adequate power, decent logistics and other key conditions for profitability. While China did provide same to investors as far back as the early 80’s, India did not provide them with adequate infrastructure and logistical support and links to airports coupled with government red-tape thus failing in basic policy strategy. The centralization of power with New Delhi, a highly regulated labour market and government approval for exit policy even for loss-making firms and regulations against full foreign ownership are further impediments which discourage FDI despite the government’s effort to promote foreign investment. As in China, there are similar problems whereby State Enterprises that have borrowed heavily from creditors mainly public sector banks finally default on debt repayment and government many a times have to rescue such Public bodies by providing them subsidies.

According to **Sachset** al as compared to China, the tax and tariff structures in India remain to a large extent

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anti-export

This analysis is further confirmed by **Swami Nathan** when he argues that the reforms are half-baked and not achieving the targets due to reasons put forth above. In addition corruption in India in the banking sector leads to a lot of efficiencies and similarly China's industrial strategy of holding on large-scale reforms towards the privatization of SOEs whereby some cronies from the Communist Party manage the State Owned enterprises. Corruption income hinders economic expansion due to misallocation of subsidies.

1.1.2 Is the Overseas Chinese Business Network a model for India in the globalization process?

It would be good to mention that at the time China had started economic reforms there were some set of objective conditions which coincided with the stages of development in Hong Kong, Taiwan and Singapore when they had in fact shifted their economies from labour-intensive import-substitution policies to export promotion. Subsequently when Communist China opened its doors, china benefited enormously from Overseas Chinese investors living in Hong Kong, Taiwan and Singapore. Due to the globalised economies of the Asian Tigers, a corridor to China was swifly established whereby the latter benefited from technology transfer at a rapid pace.

The cultural affinity of the Overseas Chinese network definitely became a strength and according to studies conducted by the Nomura research institute an economic synergy developed as a result of the Chinese overseas Network specially from Hong Kong which for years had been the main investor in China mostly in the manufacturing sector. Sharing a similar language with mainland China very often, training Chinese workers, conducting research and labour management turned out to be fairly straightforward for the overseas Chinese.

While the aim of the Chinese government was to induce linkages in the economy, it inversely used Hong Kong as a middleman between China and the global economy in networking formation in the services sector. Just like in India, the overseas Indian based in America, contributed to considerable extent to the globalization of the economy, China similarly benefited from overseas Chinese business networks with the exception that this particular link had started much earlier.

It would have been interesting to know whether without this cultural affinity and the objective conditions present at the beginning of the 80's, whether the globalization of the Chinese economy would have taken place? Had the Asian Tigers been culturally different from China, would they have diverted investment into India had they been offered similar facilities? recently a group of people of Indian Origin around the world have created an organisation known as GOPIO to promote international Business with India and the Indian Government is banking on the Nonresident Indian to attract investment into India in a similar way with the Chinese overseas Business network. While the diaspora of Chinese origin people approximate some 55 million, according to GOPIO there are some 21million people of Indian origin residing outside India .

Moreover despite the bitterness and sustained political divergence between China and Taiwan, a substantial amount of FDI from the latter, finds its way into China through Hong Kong. Likewise although in general there is a mistrust and animosity between Chinese and Japanese as a result of the Japanese Invasion of China, Japanese are nowadays investing more and more in China given the severe economic climate in Japan and the net advantage of Chinese cost of labour . It is not fortuitous, that early this month Prime minister of Japan, Junichiro koizumi visited Beijing and publicly apologised for Japanese aggression against China during World War II.

1.1.3 Challenges, futures and conclusion

To better understand what India is and what it is not, lets compare it to China. First, forget the hype about both China and India. Keep in mind that despite all the talk of China or India's rising status, both China and India are still desperately poor countries with large disparities in incomes across each country. In China nearly half of the country's labor force remains in agriculture (about 60 percent in India). Also, despite all the talk about Indian software engineers and Nobel laureates and Chinese engineering whizzes, India has the largest number of illiterate people in the world and China also is burdened with a large number of rural poorly educated who will offer continued challenges for economic development. (India's illiteracy rate is nearly 40 percent and China's is nearly 10 percent according to World Bank statistics.) Of the total of 2.3 billion people in these two countries, nearly 1.5 billion earn less than US$2 a day, according to World Bank calculations. The opportunities in both countries are substantial; the challenges are also large.

With this in mind, lets compare the two countries by size: China is the world's third-largest country after Russia and Canada and is the second largest country by land area. India is about a third of China's size. In terms of population, China tops India at 1.3 billion people compared to India at just over 1 billion but India is growing at a faster rate and has a younger population. In terms of political systems, China is a communist country which economically is following market reforms that encourage free trade and capitalist-based business models. India, by comparison, is the world's largest democracy, but with a system of commerce that until the 1980s was based on the Soviet model and has since been reforming itself to follow more free trade and capitalist-based models. China has been reforming its economy since 1978; India has been working since 1991 but at a faster rate of speed. Given the limitation of this essay, other aspects which are no less important impacting on the respective political economies of China and India like regionalism, international environmental laws, the effect of terrorism on the Indian economy and the huge military expenditure that mobilise financial resources from these two countries have not been discussed amongst other points.

According to **HelingShi**, a consultant to the ADB and specialist on the Chinese economy, the great challenges which China will have to face in the coming years are leadership in politics with economic freedom. In addition the government will to adjust to a new macroeconomic environment where both fiscal policies as well as monetary policies will have to be managed effectively but at present the Chinese governments are not used to such instruments for policy coordination.

While on the issue of democracy, India is well anchored in that tradition on the other hand it can be said that China is doing economically better than India. However according to the Economist[2] , it will have to face the foreseeable demand from the Chinese people for democratic values and a thirst for information specially with the advent of the internet; China's communists will have to loosen their political grip or see their authority increasingly challenged, as others have done before them.

Secondly as the Chinese economy get more and more reformed specially after its accession to the WTO, a sizeable number of state Owned enterprises will slowly disappear paving the way for more and more international firms to enter the market and compete openly for projects thus reducing considerably the state power to influence the market while diminishing some sort of shady revenue for corrupt officials and party activists. Both countries will have to reshape governance issues as a result of the globalization process and their banking sectors will definitely have to be revitalized to face foreign competition as a result of which the productive sectors of their respective economies will greatly benefit. an acceleration of industrialization and the flow of foreign capital, automatically development will have a spillover effect in the rural areas as the main industrial areas will be too congested and for expansion and also due to higher costs of labour in cities, some industries will have to delocalize while leaving important business areas, to shift into the service sector, a phenomenon already happening in India. Critics of globalization suggest that an equitable distribution of benefits should become a reality for according to the Economist social uprising may be the response if growth in GDP's are not matched by a corresponding sense of well-being and security among ordinary citizens. This argument is applicable to both China and India.

The combination of trade and technology in the integration of world economies follows the flying goose pattern and in such a dynamic environment the development of human resources and training are of paramount importance for these two economies to further their development however much emphasis and effort have to be put in the rural areas as well in order not to increase the existing income disparity but also in preparation for the delocalization of certain industries in the rural regions.

China is also gearing itself up to take development to the rural regions with its massive plan to develop the Western region. This particular project will be financed by the ADB to the tune of some $20 billion. The important element attached to this financing agreement is that the private sector will have to participate actively while institutional reforms like the modernization of the government services are also part of the package.

Although India has emerged within the last decade as one of the leaders in the IT world, the effects of computerization in eradicating poverty and raising the standard of living in typical Indian villages is yet to be seen, however since it has a very large population and a consequent business sector which is still in need of modernization, the potential for further development at an accelerated pace in this sector is quite promising. Indian competitiveness and success has been possible due to the process of globalization with both mobility of capital and labour illustrating the benefit of forward and backward linkages in various areas of the economy not limited to India only.

As compared to China, India does not have enough quality infrastructure and labour productivity but on the other hand it has a good judicial system and that is very important for international investment and also in areas where intellectual property rights are at stake as compared to China. India will find it next to impossible to boot out a multi-national like Coca Cola now, as it had happened some two decades ago under Swadeshi pressure due to international bodies like them WTO. The changes brought by globalization are now considered to be irreversible in both countries as the process continues to unfold.

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