Business Standard

Shyam Saran: Revisiting India's growth strategy

The world cannot accommodate another China, so India will need to find another growth model to emulate

Shyam Saran May 12, 2015 Last Updated at 21:50 IST

Will India be able to replicate the remarkable Chinese growth story in the coming decades? In the next 30 years, is it feasible for India to grow at an average annual rate of 10 per cent, just as China did between 1980 and 2010, thereby closing the widening gap between the two largest emerging economies? China's spectacular growth record is seen as validation of the investment- and export-led strategy, broadly similar to that pursued earlier by East Asian economies with focus on low-cost and employment-intensive manufacturing. India, it is argued, must traverse a similar path, if it is to join the ranks of successful Asian economies.

China's emergence as the world's leading merchandise exporter has been associated with a relatively extended period, when unusually favourable international economic factors prevailed at least up until the global financial and economic crisis in 2007-08. The major consuming markets of the United States, the European Union (EU) and Japan were relatively open and expanding. Global trade, on an average, grew at six per cent a year, double the rate of global gross domestic product (GDP) growth. Furthermore, over 50 per cent of China's merchandise exports were generated by wholly owned subsidiaries of multinationals or joint ventures between Chinese and foreign companies. More recently, China has become increasingly integrated into global supply chains of multinational companies. Thus, foreign investment has come to China, less to seek local markets, than to use China as a low-cost processing base for products that would be sold in Western markets. Since China joined the World Trade Organization in 2001, its share of the combined US, EU and Japanese import market has risen to 18 per cent. This supportive international economic environment, which China could leverage to its advantage, is no longer available since the global financial and economic crisis. Some of the unfavourable environment is the direct consequence of the crisis and may be ameliorated as the global economy recovers. But there are also longer-term factors that may be transforming the global economic and trade order in a manner that renders the investment- and export-led strategy less efficacious.

Despite the global economic slowdown, the United States, the EU and Japan remain the most significant export markets, but global trade overall is growing at the rate of a little over two per cent. The long-term trend of trade growing at twice the rate of global GDP has now been interrupted. China is now the second largest economy in the world, but plays only a small role as an importer of consumer goods. It accounts for only two per cent of global consumer goods imports.

It should also be noted that for an economy of its size, China's personal consumption as proportion of GDP is only 36 per cent and still declining. In the larger Western economies, the proportion is higher but stagnant at around 60 per cent.

Therefore, precisely at a time when India may be looking for significantly increasing its exports as a driver of accelerated growth the global marketplace is likely to be less welcoming. Furthermore, global supply chains, centred upon China, are now deeply entrenched. It has been and will continue to be difficult for Indian industry to become integrated into them. In addition, thanks to technological changes, such as 3-D printing, there is an incipient trend towards re-localisation of manufacture, which, too, may dampen prospects for increased exports.

China experienced rapid growth in its exports - from $17 billion in 1980 to $1.7 trillion in 2010, during a period of steady globalisation with diminishing trade barriers. Capital flows from and among major economies also grew at a rapid pace. For example, foreign direct investment (FDI) from the United States grew from $19 billion in 1980 to $338 billion in 2013. Japanese FDI rose from $2.3 billion in 1980 to $135.7 billion in 2013. Outward investment from the EU rose from $21 billion in 1980 to reach a peak of $809 billion in 2000, but declined to $250 billion in 2013. These large capital outflows generated larger trade flows and this was clearly the case with China. However, since the global financial and economic crisis, there is a trend towards fragmentation of the global economy, with protectionist trends on the rise. The pursuit of new trade and investment arrangements, such as the Trans-Pacific Partnership and the Transatlantic Trade and Investment Partnership, may create an even more fragmented global economy, reversing the trend towards a progressively integrated global market. Entry into the world's largest markets of the United States, the EU and Japan may become more challenging particularly since the proposed trade blocs will be creating non-tariff barriers in the form of a new and more rigorous set of norms and standards, which we may be unable to meet in the foreseeable future. These may also bias investment within the blocs rather than in countries outside, like India. India is likely to be pushed to the margins of the emerging economic and trade order, precisely when it is seeking enhanced participation.

This is not to argue that India should not promote exports or seek foreign investment. These will continue to be significant - indeed indispensable - components in any growth strategy. However, it is necessary to review our current strategies to determine what other drivers we should leverage in order to accelerate our economic growth. The Indian market, for example, offers scale second only to China. How can this be leveraged? In the past, we have talked about "making poverty pay" or using the "bottom of the pyramid" to trigger and sustain growth. No serious effort has been made to articulate a credible growth story around these concepts that would also promote inclusive growth. Technology has emerged as a major driver of growth, but in India, there has been no conscious effort to leverage high-technology capabilities, such as those in space, atomic energy or information technology, to create an ecosystem of innovation and marketisation. These capabilities are instead being leveraged by foreign entities, several of whom have set up large research and development centres in India, to generate cutting-edge technologies, innovations and products, which are then patented and commercialised outside.

China has pursued a highly energy- and resource-intensive strategy of growth and is already a major consumer of both fossil fuels and raw materials from across the globe. India may find it much more difficult to compete with China and globally for these same resources. Would India be able to sustain a similar growth pattern as China in what is becoming an increasingly resource-constrained world? We will also have to contend with pressures on account of concerns over fossil fuel-induced climate change. Though we have used concepts such as resource-frugal manufacture and are committed to expanding the use of renewable energy, these are often pursued as disconnected and *ad hoc* initiatives and not incorporated into a credible and coherent growth strategy.

The world cannot accommodate another China. India will have to traverse a different economic trajectory if it wishes to emerge as a front-ranking economic power in the next couple of decades. We should begin to explore alternative strategies sooner rather than later.

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