INDIA NEWS

The 13-Year Divide: India's Economy Looks Much Like China's in 2001

Delhi Hopes to Emulate Beijing's Success, but Will Delay in Liberalizing Prove Too Costly?

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Updated Sept. 14, 2014 9:21 p.m. ET

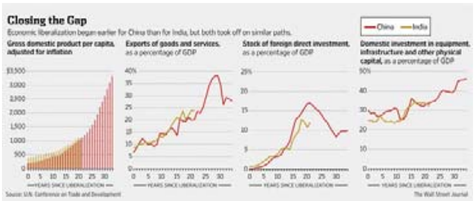
Indian Prime Minister Narendra Modi, left, shakes hands with Chinese President Xi Jinping during the 6th BRICS Summit in Brazil in July. *Agence France-Presse/Getty Images*

NEW DELHI—India today doesn't look quite like the economic dynamo that, just a few years ago, some predicted would overtake China as emerging-markets champion.

But the race looks a lot closer if you account for one key fact: China got a 13-year head start on India in opening its economy and giving companies greater freedom to invest and produce. In exports, capital spending and foreign investment, India today is remarkably similar to China circa 2001.

That should both console and concern India as it gets back on its feet after three years of weak growth and high inflation. Console, since it suggests the country's economy could remain on a China-like trajectory for years to come. But concern, because India's delay could mean that the country has missed out on some big advantages that catalyzed China's boom.

The latter point is especially worth considering given how assiduously India's recently elected prime minister, Narendra Modi, is working to follow the blueprint for China's export- and investment-driven success.



When Chinese President Xi Jinping visits the Indian capital this week he will encounter a recipe for economic revival that ought to look very familiar. Delhi is aiming to boost exports and raise India's share in world trade by 50% over the next five years. "Sell anywhere," Mr. Modi said in an Independence Day exhortation to global business last month. "But manufacture here."

The prime minister is promising Indians bullet trains and "smart cities." He is rolling out more "special economic zones" in which companies get tax benefits and zip through India's bureaucratic thickets.

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He also appears to be taking cues from a certain northern neighbor about how industry can benefit from strong state direction and support. Trade Minister Nirmala Sitharaman said last week that the government will "ensure that we do enough hand-holding with our manufacturers so that 'Made in India' becomes a brand which all of us can be proud of."

But does the same lightning really strike twice? Here's where the matter of head starts and late arrivals potentially becomes important. The seeds of China's growth spurt were planted in 1978, when Deng Xiaoping decollectivized agriculture and started welcoming foreign investment. For India, economic takeoff can be traced to 1991, when a foreign-exchange crisis forced Delhi to scrap controls on firms' production and imports in exchange for an international bailout.

Roadside vegetable sellers wait for customers in Amritsar, India. *Agence France-Presse/Getty Images*

If you start the clocks at those respective openings, then the two countries' paths look strikingly similar. In the years after liberalization, exports, foreign investment and spending on equipment, infrastructure and other ingredients for future growth, all grew at similar rates in the two nations. India's per capita output last year, adjusted for inflation, was slightly above China's in 2000.

There are differences, too. China's economy, even in 2001, was much more manufacturing-oriented than India's is today. India's growth has been fueled more by services such as software and business outsourcing.

Continuing on a China-like path, however, may require India to do more than simply re-enact China's recent playbook.

Low-cost manufacturing is less of a sure bet today.

"The growth in global demand is now being driven less by rich, advanced economies than it is by other middle-income economies, which themselves are still relying on exports to maintain growth," said Eswar Prasad, an economist at Cornell University.

India, in other words, is arriving late to what has become a very crowded party. Bangladesh makes garments; the Philippines, electronics; Thailand and Vietnam, machines and computer parts.

Saon Ray, an economist at the Indian Council for Research on International Economic Relations, says India still has opportunities in the "very high-tech but very niche segments" in which it already has a foothold, such as pharmaceutical development and semiconductor design. (India doesn't manufacture chips, however.)

"It is never too late" to become an industrial hub, Ms. Ray said. "Because the good thing about technology is that it evolves all the time."

Another issue, Mr. Prasad says, is that India today can't boost its exports by weakening its currency. Unlike China and other Asian success stories in the past, India's capital account today is fairly open, and the rupee, for better or worse, moves at the whim of global markets.

Also absent today: easy money from the U.S. Federal Reserve, which many economists say was the driving force behind the emerging-market booms of the 2000s, including China's and India's.

Morgan Stanley economist Chetan Ahya emphasizes the economic advantage of India's young population. In 2000, the median Chinese person was 30 years old. The median Indian person today is 27. Educating India's younger generation and creating enough decent jobs for them will be the key. "Where you peak out depends upon how well you have been able to use the working-age population," Mr. Ahya said.

In that department, however, China's lead over India is even greater. India in 2011 still hadn't achieved the literacy rate that China had in 1990. In terms of the number of years the average adult has spent in school, India in 2013 was comparable to China in 1985. India is similarly decades behind on indicators of health, sanitation and longevity.

Economic powerhouses aren't often built on foundations like these.

—R. Jai Krishna contributed to this article.