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# Is India 'the Next China'?

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*India is currently the fifth country in the world in terms of GDP, after the USA, China, Japan and Germany, and on track to become the world's third-largest economy by 2030, according to S&P Global. The key investments that the country has made in technology and energy together with the global offshoring after the COVID-19 pandemic, made the country one of the fastest-growing economies in the world. In this article, I want to present the stages that India went through to develop and become the world's 5$^{th}$ largest economy, and answer the question: Is India 'the next China'? Can India, in the near future, reach and even surpass the economic performance recorded by China and become a more attractive country for foreign investors?*

***Keywords:*** *India, China, economic growth, FDI inflow*

***JEL Classification****: O53, I10, F21*

## 1. Introduction

The process of transition of poorly developed countries to the stage of medium-developed countries started in the 70s, along two alternative paths: (1) exploitation of natural resources, especially oil reserves; (2) exploitation of other types of factors (intelligence, entrepreneurial spirit, social capital, etc.) in order to create a national competitive advantage. India and China are included in the second category of countries, whose development was due, to an important extent, to their own venture capital effort, supported by inflows of foreign investments.

The way India has developed over the years and the challenges the country has faced in this process have been intensively studied by many economists over time. Dreze and Sen showed in 1999 the limits that public authorities had in reducing deprivation since Independence, due to inadequate public involvement in the provision of basic education, health care and social security (Dreze and Sen, 1999). Das pointed out that in India, the most important factors for the overall development process relate to basic needs. In this sense, he requests the involvement of the government to improve elementary education, safe drinking water facilities and health care, and to remove barriers against social minorities, especially women (Das, 1999, p. 313-345). In explaining the economic development of India, the specialized literature presents the role played by the software industry (Ashish and Suma, 2002, p. 253-273), by physical and social infrastructure (Kumari and Sharma, 2017, p. 30-33), as well as by financial inclusion and ICT development (Pradhan et al., 2021). Moreover, the economists went further by studying the economic growth of India in comparison to the

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economic growth of the biggest economic power in Asia, the rival China (Saccone and Valli, 2009, p.1-29), (Fan, 2011, p. 49–73).

The remarkable development of India's economy in the last decade made the world wonder if India is Asia's next emerging giant and if it will succeed in the near future to surpass China's economic performance and become a more attractive country for foreign investors. Considering the relevance of this topic today, the article aims to provide an answer to this question, in the context of the new events taking place at a global level. In order to accomplish this goal, I have elaborated quantitative research, by collecting information and data from India and China's national statistics, international statistics, and from specialized literature. The research hypothesis is that despite being the world's 5th largest economy, with great potential, India has no chance, in the nearer future to surpass China's economic performance and become the preferred country for global investors.

## 2. The economic development of India and China over the years

India is currently the fifth country in the world in terms of GDP, after the USA, China, Japan and Germany. As in China's case, the GDP growth occurred after 1991 (Figure 1). Until then, India's economy was a combination between the planned economy of the Union of Soviet Socialist Republics (USSR) and the market economy left behind by British colonialism. Agriculture and heavy industry were organized according to a 5-year plan, with the private industry still able to exist but under heavy regulations. Large industries were dominated by big state-owned companies that benefited from subsidies, so it was very difficult for private companies to enter. On the other side, in the small markets, undersized enterprises had serious difficulties in starting a business as they needed to comply with many licensing, regulations, and red tape imposed by the government. In this context, large international companies were discouraged to invest in India as it was too difficult to work with.

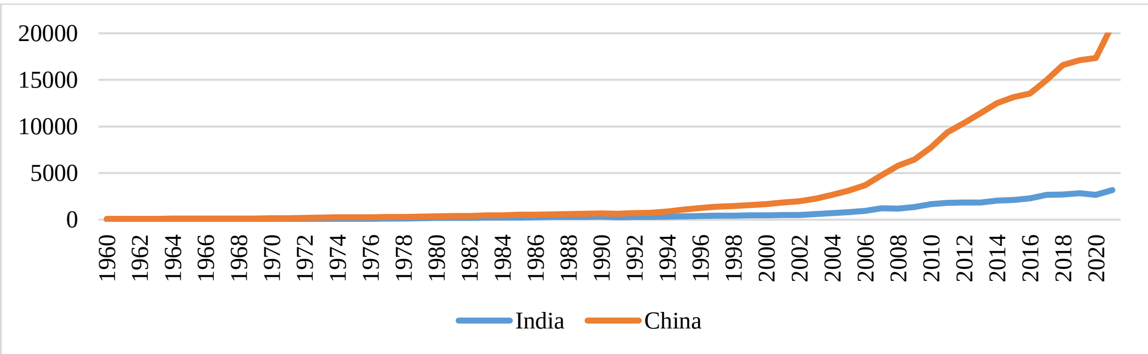


*Figure 1. India and China GDP (current US$)*
Source: The World Bank, Data, 2022a

The collapse of the USSR, which was an essential trade partner of India, combined with the country's internal problems, generated a huge international debt problem which was overcome with the help of the International Monetary Fund (IMF). The aid came in certain terms that implied the implementation of the Washington Consensus, a list of policies that open up the economy to trade and private business. For example, in 1990 India recorded an average import tariff of 80.9%, the highest in the world, in second place Brazil with 33.5%. This percentage decreased during the years, reaching 9.4% in 2020, still above rival China, which registered an average import tariff of 5.3% (World Bank, 2022b). With the abandonment of protectionist policies and of the complicated system of licenses and restrictions that all businesses needed to adhere to, India revealed its real potential, attracting more foreign investors. As a consequence, in the last 15 years, India achieved a historic performance, lifting 415 million people out of poverty (United Nations, 2022).

China, the world's second-largest power by GDP, adopted market-oriented reforms much earlier. In 1978, after 11 years of central planning that destroyed agriculture and industrial productivity, the country opened its market to the world and instituted the Law of Joint Ventures Using Chinese and Foreign Investment. China's incorporation into the world capitalist economy has resulted in 800 million people being lifted out of poverty (The World Bank, 2022), and a large growth in the middle class. If in 1987 the GDP of China and

India was almost equal, in 2021 China's GDP became 5.58 times higher (The World Bank, Data, 2022a). China's measures taken to eliminate the government restrictions contributed to this spectacular increase in GDP. Starting with 2005, China began removing quota and licensing requirements from most imports, having at the beginning of 2022, only 14 categories of commodities subject to import licensing control. (Poon C. H., 2022)

## 3. India's advantage in relation to China

Currently, India is the second most populated country in the world, after China, about to become the world's most populous nation. Its large and fast-growing middle class is helping to drive consumer spending. Unlike China, where the majority of the population does not speak English, India is the second largest English-speaking country in the world, after the US. Along with the parliamentary democracy that India inherited from the British Empire, the English language proved to be a very important legacy in the country's development. With over 129 million English speakers, India had the opportunity to benefit from an increasingly globalized world, becoming a favorite destination for multinationals to outsource their operations, especially services like accounting, engineering, design and even legal services. Advanced English speakers have significantly higher wages, and have the opportunity to have access to scientific and academic knowledge from across the world, which has generated innovation and led to the increase in the quality of the country's human capital. The large number of English speakers together with the government's incentives to boost the development of the country's IT industry, offers India the opportunity of becoming the 'world's office'.

In both countries economic growth is supported by low-wage workers, however the price of labor in India is 4.8 times lower than in China. Benefiting from this competitive advantage, India can steal manufacturing jobs from China as companies seek to reduce labor costs. In 2020 India introduced the Production Linked Incentive Schemes (PLIS), meant to boost domestic manufacturing, attract large investments, facilitate large-scale job creation, and reduce imports. The government offers incentives to domestic and foreign investors, actions intended to support the major national program 'Make in India'.

India's intense manpower has contributed significantly to making it a big force on the economic stage. If other countries face an aging population: Japan (median age 48.6 years), Germany (median age 47.8 years), and India has a very young workforce, with a median age of 28,7 years, almost 10 years younger in comparison to China (median age of 38.4 years) (The World Factbook, 2020a). Analyzing the age distribution (Figure 2), we notice that in comparison to China, India has a much younger population, with almost 48% of the entire population having less than 24 years old. This young and dynamic population, which grew up in a market economy, will be the largest consumer and labor source in the knowledge-based economy.

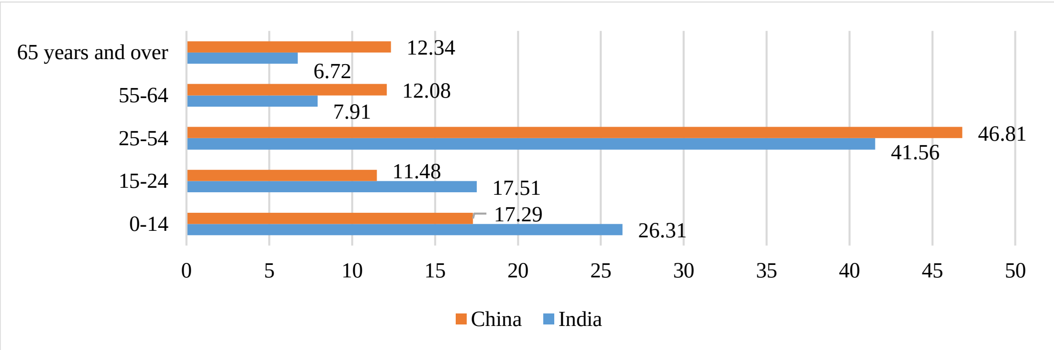


*Figure 2. Age distribution in India and China (% of the total population)*
Source: The World Factbook, 2020b

India registers a new advantage over China regarding the old-age dependency ratio which measures the ratio of the population aged 65 years or over to the population aged 15–64. In China, the elderly dependency ratio is almost double (19%) compared to the level recorded in India (10%) (The World Factbook, 2020c), a gap that is expected to deepen in the coming years. This means that in China, the working-age population, and the overall economy, will face a greater burden in supporting the aging population in the following years.

In terms of foreign direct investment (FDI), India has attracted a record amount of US $64 billion in 2020, a 27% increase in comparison to the previous year, being ranked as the eighth-largest recipient of FDI in the world (UNCTAD, 2022). This was the result of a long effort to ease the country's investment policies and introduce favorable initiatives. The government has recently taken action in easing FDI regulations in various industries, such as telecommunication, oil refineries, and defense. The country's relatively lower wages, special investment privileges, and fast-growing consumer base are also important factors that attract foreign investors. As companies are considering relocating part of their operation from China to lessen the risk of disruption in their supply, India can be the winner. China's political system, the trade war with the US, rising geopolitical tensions, and COVID-19 lockdowns, made companies diversify supply chains away from China, a trend that is likely to continue. India, the world's largest democracy and the second largest English-speaking country in the world is about to pick up more manufacturing business that moves away from China.

India's large and growing domestic market, low-cost and abundant labor, increasingly transparent policies, and the improvement of the tax regime have put the country on the investors' radar, making it impossible to ignore. If the government wants to make the country 'the next China', it must prove to the investors that India is a cheaper and easier place to do business.

## 4. India's limits in relation to China

Despite the impressive level of India's GDP, it should not be forgotten that this value is spread out against a huge population of 1.41 billion (Worldometer, 2022), which is in rapid growth. Thus, the GDP per capita provides a much better determination of the living standards of the average person as compared to GDP alone. Until 1990, the GDP per capita of India and China recorded similar values, but afterward, China visibly distanced itself, the difference deepening every year (Figure 3). In 2021 the GDP per capita in India was $2,257, 5.6 times lower than China, highlighting India's low economic productivity.

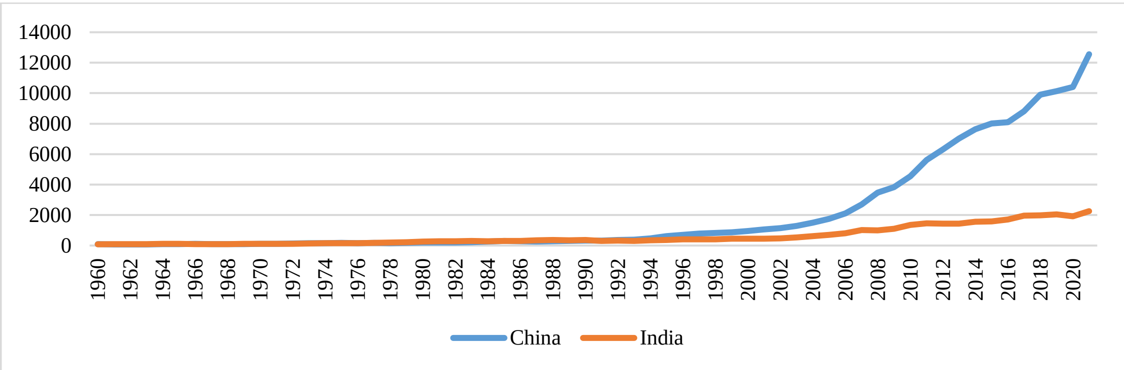


*Figure 3. India and China's GDP per capita (current US$)*
Source: The World Bank, Data, 2022c

India's small GDP per capita is diminished by farm households, whose average income is much smaller. In India, 47% of the total labor force is employed in the agricultural sector, double that of China, where only 27.7% of the population works in this sector (The World Factbook, 2020d). The population's low living standard and the vulnerability of education and health in India are also reflected in the low level of the Human Development Index (HDI). In 2021, the HDI value in India was 0.633, placing the country in 132nd place worldwide, in the Medium human development category. Starting with 2018, the level of this indicator is in a continuous decrease, highlighting the limits of the Indian economy in these key sectors. On the other hand, China's HDI value increased since 1990, reaching 0.768 in 2021, placing the country in the 79$^{th}$ place worldwide, in the High human development category (Human Development Reports, 2022).

According to Global Hunger Index, India is ranked 107 out of 121 developing countries emphasizing the seriousness of the prevailing hunger situation in the country. China, despite its very large population, is positioned among the countries with a low level of hunger, registering significantly higher scores than India for undernourishment, child stunting, child wasting, and child mortality (Global Hunger Index, 2022). Moreover, despite lifting 415 million people out of poverty, India still has the highest number of poor children in the world (97 million) and the largest number of poor people worldwide (228.9 million). About 16.4 percent of India's population lives in poverty, and approximately 4.2 percent of the population lives in severe poverty (OPHI, 2022). This data should be a wake-up call for India, a country that wants to be considered an emerging global power. Rather than seeking rapid economic growth, India should solve its internal problems.

Despite the impressive level of the GDP, what really matters are the living conditions of the population and their level of satisfaction. According to The World Happiness Report 2022, India is in 136 places out of 146 countries in The Happiness ranking, the scores being based on a survey in which respondents evaluate the quality of their current lives on a scale of 0 to 10. Chinese people declared themselves to be much happier than their Asian neighbors, placing the country in the middle of the ranking, in 72nd place (World Happiness Report, 2022). India's growing population can be a great advantage over China, but it can also be a curse if the government doesn't pay more attention to region, caste, and gender inequality.

Both India and China have adopted the Doing Business indicators as a core component of their reform strategies. In 2020, out of the 10 areas of the Ease of Doing Business Indicator (Table 1), India improved 4 of them, respectively starting a business, dealing with construction permits, trading across borders, and resolving insolvency. Despite the country's efforts, China has shown more eagerness to reform, so out of the 10 areas of the Ease of doing business indicator it improved 8 of them. The effect of these measures is the fact that China managed to surpass India and many other democracies and even developed countries, ranking 31st out of 190 countries analyzed.

*Table 1. Ease of Doing Business Ranking, 2020*

| | **India – 63rd place** | **China – 31st place** |
|---|---|---|
| Starting a business | 136 | 27 |
| Dealing with construction permits | 27 | 33 |
| Getting electricity | 22 | 12 |
| Registering property | 154 | 28 |
| Getting credit | 25 | 80 |
| Protecting minority investors | 13 | 28 |
| Paying taxes | 115 | 105 |
| Trading across borders | 68 | 56 |
| Enforcing contracts | 163 | 5 |
| Resolving insolvency | 52 | 51 |

Source: Doing Business, 2020

Due to the high regulations that are still in place in India, the informal economy is at a very high level, as many businesses decided to operate outside the official government control to save more money. Also, much more must be done for the small and medium-sized enterprises (SMEs), the backbone of India's economy, which continue to find it hard to start a business in the country's heavy bureaucracy.

Analyzing the competitiveness of the two countries, using The World Competitiveness Ranking (Table 2), we notice that out of 63 analyzed countries, India is in the lower half of the ranking, in position 37, while China is in position 17. The World Competitiveness Ranking is based on 333 competitiveness criteria selected as a result of comprehensive research using economic literature, international, national, and regional sources, and feedback from the business community, government agencies, and academics (IMD World Competitiveness Center, 2022).

*Table 2. World Competitiveness Ranking 2022*

| | **India – 37th place** | **China – 17th place** |
|---|---|---|
| Economic Performance | 28 | 4 |
| Government Efficiency | 45 | 29 |
| Business Efficiency | 23 | 15 |
| Infrastructure | 49 | 21 |

Source: IMD World Competitiveness Center, 2022

From the table above, it should be noted that India has the greatest vulnerabilities in the following sectors: government efficiency (public finance, tax policy, institutional framework, business legislation, and societal framework) and infrastructure (basic infrastructure, technological infrastructure, scientific infrastructure, health and environment, education). India's government should provide an environment characterized by efficient institutions and policies and efficient infrastructure to encourage sustainable value creation by enterprises.

India’s weak infrastructure, underinvestment in human capital, corruption, and bureaucracy remain the main barriers to attracting more foreign investors. Analyzing the FDI inflows from 1979 to 2021, it can be seen (Figure 4) that starting with 1990, the difference between the two countries has deepened, reaching 2021 to be 4 times greater in China than in India.

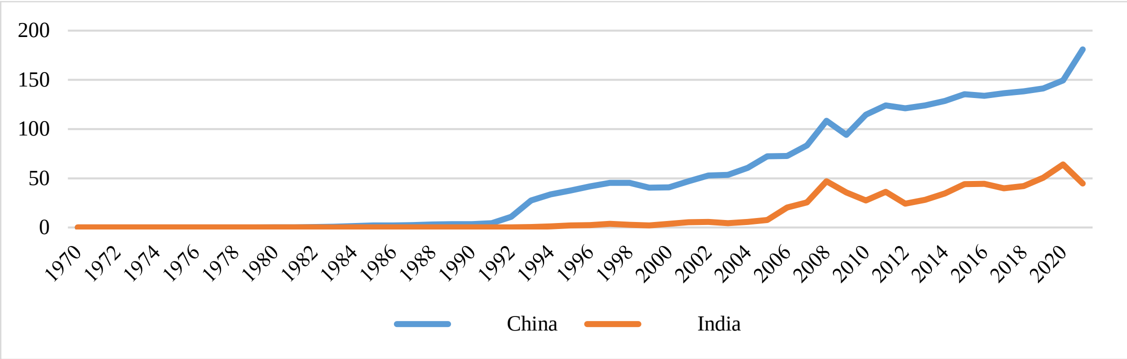


*Figure 4. Inward foreign direct investment in China and India (billion US$)*
Source: UNCTAD STAT, 2022

The ‘Make in India’ initiative did not fulfill its objective, to transform the country into a global design and manufacturing hub. In 2021 the manufacturing sector’s contribution to GDP in India was only 17%, in comparison to China, where the manufacturing sector’s contribution to GDP represented 27% (The World Bank, Data, 2022d). The technology sector has attracted foreign direct investments in India, but this type of manufacturing requires highly skilled workers, a resource that is largely absent in India’s economy. On the other side, India seems to have abandoned the light industries to countries like Vietnam, where manufacturing represents 25% of GDP, thus losing many jobs. Given that the unemployment rate in India is quite high, over 7%, increasing the employment rate should be a priority. New jobs imply higher incomes which boost consumption and attract more businesses to invest and create more jobs, thus creating a virtuous economic circle.

If India wants to become a globally competitive manufacturing hub it must grow its manufacturing sector, invest in its hard infrastructure and continue policy liberalization. India has enormous potential in the industry field, and the rescue can come primarily from the private sector, which must be supported and encouraged through business-friendly policies.

## 5. Conclusion

India has made remarkable progress from being the tenth-largest economy a decade ago, to the fifth-largest today. However, the gross domestic product alone is not sufficient in determining a country’s economic progress. Indeed, India is slowly emerging out of China’s shadow but if we take into consideration other social indices such as education, health services, housing, and environment, India remains far behind.

India may be an attractive potential alternative to China, but we cannot say that we have reached the ‘Make in India’ era. The companies’ dependency on China is a result of decades and cannot change very soon. Companies are trying to add diversity to their supply base, in case something goes wrong in China, and India is one of the best alternatives. However, India’s poor infrastructure, still excessive regulations, and lack of skilled labor prevents it from replacing China as the world’s factory soon.

The answer to the question ‘Is India the next China? it is definitely no. It is not, and in the near future, there are no chances that it will even reach, let alone surpass, the economic performances recorded by China. Compared to India, China registers superior performances in almost all fields, making remarkable progress over the years in reducing poverty, improving the educational standard, and making affordable healthcare services available to most of its citizens. Without sustained investments in infrastructure, efforts in the qualification of the labor force, and more business-friendly policies, India will not succeed in becoming a more attractive country for foreign investors and implicitly in improving the standard of living of its citizens. Even if it still has a long time to catch up with China, India is a strong economy that should not be missed.

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