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When might India rival China as the world's workshop?
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We're on the verge of great things, but we cannot assume we're there.

> Raghuram Rajan Unplugged: RBI Governor Answers 12 Qs in Rapid-Fire Round. New Delhi: NDTV. 30 November 2015.

The task

The presenter has been asked to speak about India's economic progress, 18 months after Mr Modi was elected to office, and to address the question: 'When might India rival China as the world's workshop?' The question came up after India's growth rate of the economy has been reported to be higher than that of the People's Republic of China.

Before trying to answer the questions, it needs clarification, especially what does 'rival' mean and what should we consider to be 'the world's workshop'? According to the Oxford dictionary to rival means 'competing with another for the same objective or for superiority in the same field of activity', i.e. not necessarily to surpass, but at least to come very close. The 'world's workshop' usually refers to manufacturing: China's economic importance rose after Mao's death with mass production of manufacturing goods, while India became successful in services export, mostly based on information technology. Since then we talk of China as the world' workshop and of India as its office (in German: *die Werkbank und der Schreibtisch der Welt*). In economic terms, we thus could ask: When will India reach China's industrial output?

At a first sight, the answer seems to be simple: As long as India's manufacturing growth is lower than that of the much bigger Chinese economy, as it presently is, China's lead will become more rather than less. But history has shown things can change quickly: Compared to England, all other industrial nations have been latecomers. 25 years ago Japan rivalled the USA in industrial production. It is only now as China could be at the beginning of a serious crisis, that India is seen as another coming economic superpower. That would be nothing new. As Angus Maddison in his seminal work proved, China and India have been the two leading economic powers over most of the last twenty centuries. Since China was 'lost' in 1949, there has been wishful thinking that India, the world's Greatest Democracy, should challenge Communist China.

Ten questions

In my short presentation I shall address the following questions:
1. Where do we stand: Is China really all manufacturing and India all services?
2. What have been the dynamics over the last half century?
3. What are the prospects?
4. What about services in China and manufacturing in India?
5. What are the driving and limiting forces?
6. What are the powers and limitations of the Indian government?
7. What are the structural shortcomings?
8. What is the role of outside factors?
9. How powerful is the Prime Minister?
10. What can be expected from Prime Minister Modi?

1 *Where do we stand: Is China really all manufacturing and India all services?*

China's economy is five times as big as India's: GDP 2014: US$10,360 bn vs. US$ 2,067. The share of industry in GDP (2014) is much higher in China: 43 per cent versus 30 per cent (World Bank 2015). Accordingly, China's industry is seven times as big as India's. The difference is more, if we only look at manufacturing industry with shares of 33 per cent and 14 per cent. In 2014 total manufacturing value added at 2005 prices was US$1,699 bn in China and US$213 bn in India, meaning that China's manufacturing industry is 8 times as big as India's (UNIDO 2015).

2 *What have been the dynamics over the last half century?*

In the early years of Communism, services were regarded as unproductive and China only had a comparatively small services sector, while the Indian society already in pre-colonial times was characterized by a detailed division of labour. Indian labour laws protect employees, but only in the 'organized' sector. This keeps undertakings with ten and more employees from hiring workers. Instead, they outsource services. Statistically this attitude leads to lower employment figures in manufacturing and higher in services, because services are usually not part of the 'organised sector'. The effect is that less value added is counted under industry and more under services. Value added and employment in manufacturing, thus, tends to be undercounted (Example: A cleaner in a steel factory will be counted under manufacturing; if cleaning has been outsourced to a services firm, he will be counted under services). India's labour laws work as disincentive for larger firms in the 'organized' sector, to hire permanent workers for in-house services. In recent years the share of services in GDP increased substantially, while it remained almost stagnant in India for a century.

In 2012 Oxford Economics reported that manufacturing production had been growing faster in China than in India in 2011 (10.6%/4.5%) and 2012 (8.8%/1.8%) and assumed the same for 2013 (8.9%/7.5%), but predicted a slow down in China and higher rates in India for the coming years (2014: 7.1%/10.1%; 2015: 8.3%/9.9% and 7.8%/8.3).

China's statistical office reports, indeed, a slow down of the growth of the index of value added in industry from 10.8 per cent in 2011, to 7.9 per cent in 2012, 7.6 per cent in 2013 and 6.9 per cent in 2014 (NBS 2015).

India in its Economic Sturvey 2014-15 confirms the slow progress in manufacturing: The average growth rates of 3.7 per cent in the years 1994 to 2000 could be raised only to 4.2 per cent in the years 2000-2010 (GoI 2015, I-105). A revision of the system of national accounts has raised manufacturing growth rates: For the year 2012-13 from 1.1 per cent (2004-05 series) to 6.2 per cent (2011-12 series) and for 2013-14 from -0.7 per cent to 5.3 per cent. A growth rate of 6.8 per cent is expected for 2014-15 (GoI 2015, II-93). The changes for total industry (including also mining, electricity/gas and construction) the change is less dramatic. The new growth rates would be 2.4 per cent in 2012-13, 4.5 per cent in 2013-14 and 5.9 per cent in 2014-15.

Changes in measuring growth are the reason of the different growth rates published in the media.

3 *What are the prospects?*

UNIDO expects a higher growth of value added in manufacturing industry in India than in China for 2014 to 2016; 2014: 10.1%/9.0%; 2015 9.9%/8.4%; 2016:8.3%/7.8%. China's official figures have been subject to scepticism in the past, while India has changed the system of national accounts from January 2014. Therefore, growth rates have to be read with caution.

India can be expected to take decades to catch up with China, as a simple model shows: At a ten per cent growth of value added in manufacturing industries it would take India 20 years to reach China's present level of manufacturing industries. At a growth rate twice as high in India, i.e. 10 per cent vs. 5 per cent, it would take around 45 years.

High growth rates are, of course, possible, if only we remember that India and China had the same GNI per capita as recent as in 1991 (World Bank).

4 *What about services in China and manufacturing in India?*

In Communist countries services were regarded as non-productive. When China started a more market oriented economic policy, services gained importance. Today (2014) in China the share of services in GDP at 48 per cent is almost as high as in India (53%). In absolute terms China's services sector is almost five times as big as India's (2014: US$4,993 bn vs. US$1,012 bn; World Bank 2015). This also shows in trade: With exports of (2013) US$205 bn China at position 5 of commercial services exporting countries was ahead of India (US$151 bn) at position 6. However, China is the second biggest importer of commercial services (US$329 bn) and runs the highest deficit in trade in services(US$ 250 bn), while India with much less imports worth US125 bn stood at position 9, with a decent surplus of US$26 bn (WTO 2014).

5 *What are the driving and limiting forces?*

The build up of China's manufacturing industry was export driven while India only hesitantly was giving up its policy of sel-reliance and delinking from the world market. With the absorption capacity of export markets more or less reached, China has started to focus more on its domestic market, while India's new 'Make in India' would be again more inward looking.

6 *What are the powers and limitations of the Indian government?*

The powers of India's new government are limited in many ways. First, Prime Minister Modi and his BJP have a majority only in the Lower House and need the approval of the Upper House in many cases, for example for the new land law. Second: Indian states have far reaching competences. Third: Effectively, India is ruled by a small corps of mainly generalist elite bureaucrats that have seen governments come and go. Fourth: In order to obtain also a majority in the Upper House, the government has to be careful not to alienate their followers. Bihar with its 100 million people will see elections in October and November. Fifth: The RSS will see that the government stays on course ideologically.

7 *What are the structural shortcomings?*

Infrastructure and human capital are precondition for a modern economy. There are substantial deficits, e.g. in transport (rail and road), electric power supply, water, sewerage and waste disposal, public transport, housing, bureaucracy ('red tape'), corruption.

Besides the size of her market, India is much less competitive than China: Among 144 countries we find India at 71th and China at 28th position (Schwab 2014, 13).

8 *What is the role of outside factors?*

Foreign investment, home remittances and the international trade regime are among the most important outside factors. FDI (c. US$50) and home remittances (c. US$70 bn) allow a large trade deficit.

9 *How powerful is the Prime Minister?*

Mr Modi's exceptional popularity helped the BJP to win an absolute majority of seats in the national elections of 2014, although they got only 31 per cent of the votes. In his speeches he has addressed a number of urgent problems like public hygiene or the role of women in society. Nevertheless, he has been criticized for a lack of bold steps in economic policy and too much micro-management, leading the country like a chief minister rules his state.

10. *What can be expected from Prime Minister Modi?*

Professor T. B. Hansen of Stanford University said: 'A lot of people are realizing that there's no magic wand, no formula that this government has that can do anything radically different ... They went to Modi because they thought there was some one who could get it together, but that's not happening.' (Nemana 2015)

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