The ‘Emerging Giants,’ China and India, and the world economy: a note

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Abstract

Globalization is an historical process. Its contemporary phase is marked by compression of the world, a blurring of national borders, and interlocking of states driven by new information and communication technology and rapid transportation. This is underscored by a shift in emphasis from state to non state market led policies and the creation of a ‘new space’ which coexists with the nation state. This calls for global governance centred on ‘collective action’ to tackle economic and political challenges.

In this context there is intense controversy over the capacity of China and India, two key nations among the ‘Emerging Giants’ or the ‘Rising Powers,’ to become major players in the world. They function under different socio-political systems-China a ‘planned,’ ‘state directed,’ and ‘centralized democracy’ run by one party and India a ‘mixed’ state and market economy based on ‘multiparty democracy.’ In this respect, the focus of this paper is on capturing more fully through political economy the key forces which enhance and inhibit the capacity of both to pursue their goals. This is underscored by (a) structural transformation to diversify and boost growth and employment while tackling domestic socio-economic and political strife and (b) strategic ties or alliances with nations/regions and institutions within and beyond Asia to bolster economic and political influence. Insights emerge into the realism of both pursuing their vision.

Globalisation and the ‘Emerging Giants’

Globalisation is an historical process. Its contemporary phase is marked by compression of the world, a blurring of national borders, and interlocking of states driven by new information and communication technology and rapid transportation. This is underscored by a shift in emphasis from state to non state market led policies and the creation of a ‘new space’ which coexists with the nation state. This calls for global governance to tackle challenges beyond the capacity of nation states centred on collective action through international institutions. This may be supported, or indeed opposed, by nation states and non state actors.

In this context this paper unfolds more fully through political economy the forces which enhance and inhibit China and India, two key nations among the ‘Emerging Giants’ or the ‘Rising Powers,’ to become major players in the world. They pursue different socio-political systems-China a ‘planned,’ ‘state directed’ and ‘centralized democracy’ under one party and India a ‘mixed’ state and market driven ‘multiparty democracy.’ They embrace ‘hard power,’ based on economic and military strength,

2 These include Brazil, Russia, India, China and South Africa-coined as the BRICS

3 See Archibugi, 2010, Roy, 2006
and increasingly ‘soft power,’ rooted in institutional, cultural, and technological norms. The scope of both to wield influence is underpinned by (a) structural transformation while coping with domestic (internal) strife and (b) strategic alliances or ties with other nations, regions, and international and south south institutions.

Both dominate the world’s population (about 40%). Historically, they exerted major hold on the world in the 18th and the 19th century. Thus, in 1700 their share of world income was 45.7%; China’s accounting for 23.1% and India’s for 22.6%. However, this started declining in the 20th century from 16.4% in 1913 to 8.7% in 1950 but then rose to 12.59% (average between 1985 and 1995) and 16.88% (between 1995 and 2003), and about 20% (2012). The two nations are expected to control over 40% of world GDP by 2025-30 and dominate the world economy by 2050.

On trade and FDI in relation to the global economy there are prospects of China and India, and in particular the former, playing a major role in the world economy. Their trade as a % of global GDP rose from 1.1% in 1990 to 3.6% in 2004. But over 2001 to 2008 China’s exports as a % of world exports increased from 4% to 9% while India’s share jumped fourfold but remained stable at 1%. In fact China’s export share reached 10% in 2010. Its exports have become more complex and sophisticated than India’s though the gap has been narrowing. Alongside, the share of FDI as a % of global GDP, though modest at present, is expected to increase in the future. In fact, gradually, FDI is assuming more importance. This is exemplified by FDI inflows: five countries accounted for 44% of the total FDI inflows in 2012 with China having the largest share-18%.

Overall, the two powers are expected to re-shape the world economy.

Both show impressive growth. However, they were hit, though to a lesser extent than developed nations, by global slowdown stemming from the financial crises of 2008 and 2011. Thus, China’s record shows an impressive annual growth rate: 9.25% over 1989-2012. This, however, fell to 7.4% in the third quarter of 2012 and 7% in early 2013. It also has to cope with inflation: over 1994-2012, the rate of inflation was 4.3% but the trend is a declining one from 4.57% in January 2012 to 2.10% in June 2012 and 1.59% in October 2012. India, before 2008, had a growth rate of 8.9% but this slipped to 6.5% in 2011-12. This marked a 9 year low. Indeed, the rate of growth was only 5-5.5% in early 2013. Optimists suggest that India will return to a growth rate of 8%-9% over the next 2-3 years. It, too, faces inflation which is higher than that of China fuelled by domestic supply constraints and adverse external conditions: 7.45% in 2012 and 7% in early 2013.

Long term forecasts on both are optimistic. In the near future the OECD suggests that the rate of growth in the world in 2013 will be 1.4%. This is down from earlier estimates of 2.2%. In the longer term it expects that global growth will be 3% a year over the next half century. This will be mainly driven, as in the past, by productivity improvements and accumulating human capital. It goes on to show that China and India will account for 28% and 11% respectively of the output among 42 major economies by 2030 compared with 18% for the US, 12% for the Eurozone, and 4% for Japan. In this respect, China is ahead of India in terms of strong productivity and intensive investment over the past decades. Both are forecast to grow 7 fold in the

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7 These are based on OECD forecasts made in 2012 on growth of China and India. Also see Goldman Sachs, 2003 and Asian Pacific Economic Literature, 2011. See Subbachi, 2008 on the ‘Rising Powers’ including China and India
8 Based on OECD forecasts made in 2012
next 50 years. It is expected that by 2060 China’s per capita income will be 25% higher than the current US income while India’s will languish at half the present US level. Though at present China’s GPP per capita is just one sixth of the US it is forecast that by 2060 it will reach 60% of the US’s income level. This would put China just behind Spain and France but in front of Italy. The OECD also emphasises the importance of demographics as in the long term it impinges on savings, investment and growth. In this respect, China’s savings rate, which now exceeds 50% of GDP, is expected to plunge by no less than 40% by 2060 with half of the drop due to aging.

In terms of reshaping the world economy it should be emphasised that China, with reserves of about $ 3 trillion, has been under intense pressure, especially from the USA, to curb imbalances between debtors (developed countries) and creditors in the world. This has led to pressures on China to revalue the Yuan on the premise that it is overvalued enabling the nation to boost its exports while curbing imports from developed countries. Alongside, there has been emphasis on re-focussing on stimulating her domestic consumption rather than exports to stimulate growth. This could lead to an increase in her imports ie. the exports of developed countries. In fact, it could be a possible ‘saviour’ of the ongoing financial problems facing Europe and US. But it has challenged such notions. Its politicians allege that as the developed regions caused the present crisis they should resolve it.

Essentially, China and India are ‘re-emerging’ powers with the potential of recapturing their status in the world.

Structural transformation

Structural transformation centres on economic diversification and boosting growth and employment-shifting from agriculture to industry and services in the context of intensifying exposure to the world economy. This is an ongoing process in China and India underscored by a move from state to market led policies based on ‘liberalisation.’ Alongside, domestic (internal) socio-political obstacles have to be tackled.

The thrust in both to liberalise is discussed against a backdrop of their economic performance-growth, shifts in trade and economic structure, and poverty and inequality:

- both, as mentioned earlier, have experienced high rates of growth in recent years though they confront inflation and are subject to the vagaries of a changing world economy: the average rate of growth (before the financial crisis of 2008 and 2011) was 10% in China and 8% in India

- both have been opening up their economies to external forces. Thus, for instance, merchandise trade (ie. exports and imports divided by value of GDP) as a % of GDP in 2011 was 49.8% for China and 40.5% for India; this can be compared with 19.9% for Brazil, 45.5% for Russia and 53.5% for South Africa in 2011. FDI, too, as indicated earlier, has been growing, and in particular in China

- shifts in economic structure over time can be measured by the contribution of sectors to GDP and employment. In this respect, in both, the % contribution of agriculture to GDP has been declining and that of industry and services has been rising. Alongside, the % employed by agriculture has been
gradually declining and that of industry and services has been rising albeit slowly. This is unfolding in both but is more marked in China compared to India—the former can be defined as a manufacturing and the latter as a services led economy. Thus, in China manufacturing contributes 50% to GDP, agriculture 22%, and services 28% while in India, services contribute 53%, manufacturing 25%, and agriculture 22%; in terms of % employed by sector, in China, agriculture accounts for 40%, industry for 27% and services for 33% while in India agriculture accounts for 54%, industry for 20%, and services for 26%.

- both, despite their growth, confront poverty and inequality. However, China has performed better than India in terms of satisfying basic needs such as nutrition, health, and education.

In this frame growth in per capita income enabled both to reduce poverty. Historically, India was ahead of China in terms of per capita income in the early 1950’s when the latter’s manufacturing and services sector was retarded. Over 1952-65 the rate of growth of national income was about the same—China 3% and India 3.6%. Even in 1966, after launching of economic reforms in China in 1979, and before India launched its reforms in 1990, per capita income in China was $ 315. But by 2004, a quarter of a century after the reforms in China, and just over a decade of ones in India, per capita income in China rose sharply to $ 4660 which was twice that of India’s $ 2460. In fact China succeeded in curbing poverty in the early years of its reforms. By mid 1980’s exceptionally high growth in agriculture, and equality in landholdings, were underlying explanations. In recent years (2012-13) the % below the poverty line (less than $ 1 a day) in China was about 8% in contrast to India’s 28%.

Inequality has been worsening in China in the developed coastal regions due to in migration from poorer regions while in India poverty is concentrated in slow growing less developed central and eastern regions. Income inequality was lower in China compared to India in the pre-reform period (ie. in the late 1970’s). But this started rising sharply and became significantly higher in China than in India some years after the introduction of reforms. Thus, by 2004, income inequality in China was 0.47 while in India it was 0.40. In this respect it should be stated that the level of inequality is problematic if it is > than 0.40. For instance, developed countries such as Denmark, Sweden, and Japan have low Gini Coefficient of 0.25 while developing countries such as in Brazil, Columbia, and Peru in Latin America have high levels exceeding 0.40.

Structural change in both was driven by domestic and external reforms based on ‘liberalization.’ This marked a shift from the state to the market to usher in economic change through curbs on state intervention with the price mechanism guiding production, distribution and consumption.

The pre-liberalisation phase impacted on subsequent policies. In China this phase formed a firm basis for executing reforms—a high savings level with significant capital formation, investment in infrastructure, health care, literacy and primary health care, and the virtual elimination of landlessness. In contrast, the Indian pre-reform era was marked by landlessness, high levels of poverty and inequality. These thwarted subsequent reforms.

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9 See Vries, 2012 for discussion on aspects of structural change
10 On pre and post liberalisation in China and India see Roy, May 2010, p 20-23, and Roy, 1998
The liberalization phase as stated was rooted in reducing the role of the state in the economy and emphasizing the market to allocate resources set in the context of ‘opening up’ and removing barriers to trade and investment. This approach shaped their own version of liberalization under different socio-political systems.

In China liberalization emerged in 1978 (in the post Mao era) unleashing the use of markets in agriculture, industry and services, state owned sectors, and de-regulation of product prices. The emphasis was on export led growth and foreign direct investment and on ‘strategic liberalisation’ based on domestic priorities. However, the curbs on the state and reliance on the market aroused controversy. This was in part due to exclusion of the poor and the marginalized and worsening of inter-regional inequality in spite of professed benefits of the new approach. The policies uncover a marked withdrawal of the state and Maoist ‘centralised planning’ which were seen as ‘shackles on development.’ At the same time it is alleged that ‘political liberalization,’ exemplified by democracy and human rights, has yet to emerge in China. This calls for its leaders to balance economic and political rights.

In India liberalisation surfaced much later than in China, in the early 1990’s, to selective use of market forces. It has been more gradual and protective set within a ‘democratic’ system which allowed diverse interests to challenge or support the measures. Industrialists and the urban middle classes welcomed the new policies but there was stiff resistance from the rural and the urban poor.

The debate on the virtues of liberalization resurfaced in the aftermath of the ‘Great Recession’ of 2008 and on the re-emergence of the financial crisis in 2011. This has led to fresh debates on the relevance of the ‘Washington Consensus’ and the ‘neo-liberal’ approach and the scope for evolving a ‘Beijing’ or even a ‘Delhi Consensus.’ This impinges on a shift in the balance of power in the world from the developed to the Rising Powers. The virtues of the state versus the market and the relevance of fully ‘opening up’ an economy are being reposed. Indeed, there has been an onslaught on the limits of the market and the need to re-emphasise the state in structuring policies and stimulating domestic demand as opposed to relying on exports. In this respect, state expenditure, fiscal and monetary, coupled with stringent regulations over financial transactions were key measures to boost growth after the financial crisis of 2008. This is illustrated by the use of ‘stimulus packages’ in China and India to revive their economies-the former, for instance, explicitly focused on domestic rather than on external demand.

Measures to induce liberalisation in both coexist with having to confront varying forms of historical and contemporary domestic socio-political strife. This impacts on sustainable growth thwarting growth and absorbing valuable financial and human resources.

China, under a ‘centralized’ and a more ‘authoritarian’ and ‘state directed’ system faces challenges from forces which desire greater autonomy and independence from the norms laid down by the state. These include human rights, freedom of speech and movement, and religious beliefs, as well as anxieties over internal terrorism, and the demand of groups such as migrant workers for basic rights. Corruption, too, at all levels is a major threat. This could undermine socio-economic and political stability. These, of course, are intertwined with the nature of economic change due to liberalization of the economy, and the worsening of regional and socio-economic conditions of particular groups and regions.

India, too, despite having a ‘democratic multiparty’ system faces critical domestic obstacles. This includes major threats from internal terrorism, sparked by demands of
the Maoist or the Naxalite movement, in the relatively poorer regions such as Bihar, Orissa, and districts of West Bengal, for basic economic, social and political rights. There is also a call for greater autonomy from the federal (central) government in regions such as the North East. Alongside, there are pressure groups championing the plight of the deprived exemplified by tribals, landless agricultural workers, and urban poor and marginal. Moreover, more recently, 'blue collar' workers, such as those in banking and insurance, and in the retail trade, have challenged facets of liberalization which may affect them adversely, eg. job losses due to privatization of sectors run by the state. Corruption at many levels has also plagued administration and execution of policy.

The socio-economic challenges faced by both impinge on the nature of the state and its capacity to encompass and fulfill diverse and complex economic and socio-political demands. Their different political structures may exert a major influence on coping with such challenges and the potential for achieving inclusive and sustainable development. In this respect, India's democratic framework may be an asset which can enable diverse voices to be expressed in shaping policies. However, maladministration and corruption inhibit and frustrate their execution. In China's case its somewhat 'top down' political system may result in delayed response to discontent due to resistance of the party hierarchy to initiate changes. At the same time, the party may become more open and react positively to changing needs and take decisive and timely action to redress socio-economic imbalances. The capacity of both to cope with complex economic and political change poses a major challenge.

Strategic ties

Strategic ties are alliances of China and India with nations and institutions within and beyond Asia to bolster their goals.

First, the urge to curb 'old' (pre-1990) and 'new' (post 1990) tensions between China and India is critical for peace and development—the division based on the era before and after economic liberalization in India which intensified such measures from 1990 onwards. The 'old' tensions stem from inter China-India rivalries and suspicions, rooted in military and territorial disputes, while the 'new' ones arise from rivalries and competition in world markets. Both have a sizeable level of expenditure on defence though China's is higher ($ 95 billion) than India's ($ 32 billion). But this is still far below the level of the US ($ 700 billion). However, competition between China and India over military and defence expenditure could worsen tension and insecurity in Asia. This could have adverse effects on the rest of the world. At the same time dialogue between the two nations has underscored long term targets to reinforce ties through trade and investment. This in turn could diminish historical anxieties over security. Such hopes have been aroused by their meetings. For instance, in April 2011, both agreed on a trade target of $ 100 billion by 2015, and China pledged to reduce the trade imbalance between the two nations which has been tilted against India. Such goals were re-iterated in May 2013 at a meeting of the Chinese and the Indian Prime Minister in India.

Secondly, both have been actively forging their relationships with nations and regions and institutions within and beyond Asia.

Within Asia the ties between China and India have been evolving. This is rooted in building on their past links and intensifying those with other nations and regions.

11 On conflict and cooperation between China and India see Roy, May 2010, and March 2012.
through bi-lateral and institutional exchange in Asia (SAARC, ASEAN and APEC) and in Africa (AU), China exercises more power in South East Asia while India has more influence in South Asia. At the same time, the triangular relationship between China, India and US has a major influence on security in Asia. In this respect, China and India have been vying for the support of the US in their regional policies in Asia though they do not wish the latter to be dominant in the region. However, India may see the US as a balancing force in Asia in the context of China’s mounting power.  

Outside Asia the two nations have been forging ties with developed and developing regions, the former illustrated by those with Europe, embodied in the European Union, and the latter by those with Africa. This has given rise to controversies over the China-EU and the India-EU relationship—the first is more significant in terms of trade and investment despite anxieties on the political front, and the second is perceived as being ‘lacklustre’ though there is hope of reinforcing economic and strategic ties.  

There is also much interest, since the early 1990’s, in the growing exchange between China and India, and Africa, motivated by the desire of the two Asian powers to gain access to raw materials (eg. energy) and new markets. This has been galvanized by a shift in emphasis in their policies from politics and ideology, in the ‘cold war,’ to economic development in the ‘post cold war’ phase. However, the extent to which this will usher in economic diversification and development in Africa is debatable. Much depends on the response of African states and their leaders and their people to bargain forcefully with the two nations. Again, rivalries and competition between China and India in Africa over access to resources (especially energy) and markets have surfaced.  

Thirdly, both have been trying to intensify their influence in world affairs through international and South-South institutions. The mounting economic clout of the two nations has to be matched by political influence to mirror the gradual shift in the balance of world power. Indeed, they could join forces to confront the challenges plaguing developing nations in world affairs. This encompasses inadequate voice in international institutions on financial, economic, climate change and peace keeping. This could have far reaching effects on initiating genuine ‘global governance’ through drastic reform of the key institutions, the IMF, the World Bank, the WTO and the UN, while actively supporting new ones such as the G 20 (comprising developed and rising developing nations). This should encapsulate the aspirations of nation states and non state actors embodying local and community based institutions and social movements. India, supported by China and developing nations, could enhance its role in this process by satisfying its long cherished desire to get a seat on the UN Security Council. The financial crisis, no doubt, has intensified the urgency of ensuring that policies of international institutions reflect the wishes of new powers such as China and India. However, re-balancing of the global economy may create new political, military and security tensions between and within the existing (eg. US) and the new powers.  

Alongside, growing South South groupings, exemplified by Brazil, Russia, India, China and South Africa (BRICS), have potential of bolstering their global prowess. 

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12 See Roy, May 2010  
14 On ties between China and India and Africa see Roy, May 2013, Roy, July 2012 and Roy, May 2012, Section 2  
15 On the history of the Bretton Woods institutions and their reform see Singer and Roy, 1993  
16 On BRICS see Petropoulos, 2011
BRICS account for over 45% of the world’s population, about 30% of global GDP, and about 25% of global trade and investment. It poses opportunities and obstacles due to the different economic and political structures of its members. Their separate and often conflicting pursuits may inhibit collective action or cooperation. However, it could emerge, despite internal differences, as a pressure group to champion the plight of developing nations.

Insights

The realism of China and India pursuing their vision of becoming major players in the world is influenced by conflicting forces. This goes beyond simple economic forecasts and impinges on their capacity to tackle interlinked domestic and external challenges. Undoubtedly, their rise will induce opportunities and create tensions between and within themselves, and with other nations and regions, and institutions. In this respect, their mounting ‘hard’ and ‘soft’ power may be challenged, in particular by the dominant nations (eg. the US), and frustrate their ambitions to reshape the nature of global governance. The rise of both is likely to be subjected to diverse domestic and external economic and political pulls. These have to be critically examined and constantly monitored to assess the likely outcomes.
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