BEHIND CHINA'S SUCCESS STORY: COMPARING THE ECONOMIC DEVELOPMENT OF CHINA AND INDIA[1]

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A. Introduction

Comparing the economic development in China and India has been interesting. While one has experienced an impressive economic growth performance, the other seemed to take a slower path. One popular argument says that the answer lies on China's success on attracting foreign capital. This argument is supported by some stylized facts related to the explanation for a country's attractiveness for foreign capital.

The main idea of this essay is that China's relative success over India is a result of its unique characteristics. The purpose of this essay is to deliver supporting arguments for such hypothesis by analyzing the stylized facts. The readers should note that the scope of this essay is the internal determinants of the relatively different speeds of reforms, rather than the policy analysis.

The essay is presented in three parts. The first part reviews the identical conditions which both countries shared in the beginning. The second part shows the different success stories. The third part is the comparison of some unique conditions which influenced the different outcomes of development.

B. The Identical Starting Points

India and China entered the post-imperialist era as two almost identical economies. The two economies continued to share at least four conditions during the early decades of their economic development. *First*, both had been relatively labor abundant. *Second*, they started at a same low level of GNP per-capita. *Third*, the industrial policies were inward-oriented. *Fourth*, the economies had experienced high distortions against market prices.

As two most populated countries in the world along history, India and China had been endowed with labor – especially unskilled –

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relative to other inputs. The relations between the labor abundance and their industrialization strategies were as followed:

> ... *This suggested the value of economic strategies focused on production of labor-intensive goods, exporting a proportion to support imports of the technologies, capital goods, and some natural resource-based products which were necessary for development* (Garnaut 1995:30).

But the two economies did not stick on the 'original' patterns of labor-intensive industrialization. Some heavy or high-technology industries such as software, military airplanes and equipment were introduced later.

Having the largest share of world's population did not bring the wealth of nations in. Referring to The World Bank data, China's per capita GNP was US$ 290 in 1980, while India's was US$ 240 (Table 1). These numbers put the two under World Bank's category as low-income countries. However, an extra attention has to be given when dealing with these numbers, since the reliability of the statistical methods – especially in China – is questionable. Since we do not have many alternatives, this essay will emphasize more on the trends.

The next similarity is the economic systems. After the World War II, China adopted Communism, and India adopted the so-called Fabian Socialism (Lal 1995:1477). Despite some differences in practice, both ideology are originally inward oriented. The difference was the reasons behind those choices. China took communism by default, because of its closeness with the Soviet Union. India by design, taking the historical spirit of nationalism into account (Sinha and Sinha 1997:5). The world's political trends change in 1970s then had some impacts but the inward-looking orientation remained still.

The shared ideology had driven their economic policy away from the market orientation. Both countries were somehow influenced by the Soviet-model of central planning (with democracy introduced in India). They systematically discriminated prices against agriculture by taxing it directly or indirectly. The market distortion was even greater in the pre-reform China since the prices – for commodity an factors – were more regulated and controlled. In the pre-reform India, the policy was directed more as incentives for producers (see Lal 1995 and Bajpai et al 1997).

C. Different Paths of Reform

The story about two look-alike economies finished at late 1970s. That was when China set up the reform plan in 1978, also known as the Open Door Policy (ODP). There had been major changes in the China economy since then, not only the policy reversal but also the growth performances. Meanwhile it took more than a decade for India to gather its reform momentum in 1991. But the outcome has never been as spectacular as in China (see Table 1 and 2).

During the 1980s, China experienced a 10.2 per cent annual GDP growth rate. The number increased to 11.9 per cent during 1990-97. This growth has increased the GNP per capita by more than double. The exports of goods and services also boosted after the ODP took place. Exports' share in the economy had increased from less than 9 per when the reform started to about 20 per cent recently.

India, on the other hand, grew modestly. During the first decade of China's ODP, India's GDP grew less than 6 per cent per year, even after the NEP had been set up. With the GNP per capita of only US$ 390 in 1997, the country is still stuck in the low-income classification. The exports performed better, which after reform grew at 13.7 per cent annually. But as the imports grew faster, 1997 India is recently still a net importer.

Explaining the different paths of the two countries has always been puzzling and interesting at the same time. The most popular explanation is China's success in achieving high levels of savings and investments. China's level of Gross Domestic Savings (GDS) and Investment (GDI) was around 28 per cent of total GDP before reform started. The number had increased to 35 and 37 per cent in the next 10 years, then around 35 and 40 per cent in 1997. India had nearly the same level as China before the ODP, but the numbers had not been increased significantly, even after the NEP (Table 2).

D. Behind the Difference Performances

The biggest account for China's relative performance over India is its achievement of attracting foreign investments, especially direct investments (see Table 3). The establishment of Special Economic Zones, tax and fiscal reforms are major policies which attracts the massive inflows of capital (see Lal 1995, Sinha and Sinha 1997). Since the policy evaluations are beyond not in the scope of this essay, our concerns are the unique characteristics which can or can not be the determinants of the capital inflows. Here four aspects are presented; human resources, physical infrastructure, role of nonresidents and the social-political management.

Human Resources

Two issues related to human resources are the market for unskilled and skilled labor. Both types of labor can be the determinant of investment inflow. Some studies tried to explain China's success story from the comparative population condition (see Bajpai et al 1997). But if it is to be the case, India should have been the more successful one. In other words, the stylized facts about the labor prices, labor force growth and the skilled labor supply of the two countries can not be the basis of a comparative analysis.

The first stylized fact is the price of labor. One main reason for investing abroad is the increasing cost of domestic labor. The higher labor cost drives a country to substitute from having relatively labor-intensive industries to the capital-intensive ones. As mentioned earlier, both India and China are relatively abundant in low-waged labor. According to Brahmbhatt et al (1996:22), hourly wages in the Indian and Chinese clothing industry are US$ 0.27 and 0.25. These figures can be a good approximation for both have relatively the same competitiveness in the labor prices.

In the supply side, China's labor force proportion to the total population had risen from 54 to almost 60 per cent in two decades (Table 4). But the rate of growth falls by a half between the 1980s and 1990s. The labor force proportion in India are always greater than that in China, 57 per cent (1980) and 61 per cent (1997). India also experiences an increasing growth rate of labor force, from 1.9 per cent in the 1980s to 2 per cent the next decade.

In terms of quality and skilled labor, India has a clear advantage over China. Indian government has more spending on education, 3.5 per cent of their 1995 GNP, compared with 2.3 per cent spent by the Chinese government (The World Bank 1999). The rate of university graduates is 9 per cent of total tertiary education enrollment, while the number is only 2 per cent in China (The World Bank 1993). India has also more English-speaking and middle-class population than China, which is a great advantage in the business sector (Sinha and Sinha 1995:19).

These figures had shown that there is no significant differences in the labor market. India, however, is having the advantage of human capital. Comparing the two countries, we can say that the condition in the human resources can not be referred to as the source of different trends of foreign capital inflow.

Physical Infrastructure

The second determinant for a success in attracting foreign investors is the condition of infrastructure. In terms of infrastructure stock per capita, both countries are more or less similar. India has approximately US$ 800 stock of infrastructure per capita, meanwhile China has approximately US$ 600 (Brahmbhatt et al 1996:18). Both figures are relatively very low, compared with some East Asian Countries such as Thailand (slightly over US$ 2,000), Malaysia and Korea (around US$ 5,000), Hong Kong (US$ 20,000) and Singapore (almost US$ 50,000). Comparisons on some areas of infrastructure are presented as follows.

Electrical Power

Using the electrical consumption per capita as an approximation, China has the advantage over India in the supply of electrical power. In 1995, the consumption per capita in China is 637 kilowatt-hours, about twice as much as in India (The World Bank 1999). The data also shows that not only the lack of supply, the efficiency is also worse in India. There is a 18 per cent transmission and distribution losses, compared with only 7 per cent in China.

Railroads, Roads and Airports

India has more availability of infrastructure in these areas. With the land area only a third as large as China, India has 62,460 kilometer long of railroads and almost 2 millions kilometer of paved roads. China has total railroads of only 2,000 kilometers longer, and only a half lengths of India's paved roads (Sinha and Sinha 1997:7-9). India also has more airports, 0.38 per a million of population, with only 0.17 in China, or 0.11 per one thousand square-kilometer, only 0.02 in China (Brahmbhatt et al 1996: 20).

Telecommunications

The World Bank (1999) indicates that in 1996, there are 45 telephone lines in China, and only 15 in India for every one thousand people. In a different way, one telephone is shared by 100 people in China, and 200 people in India (Sinha and Sinha 1997:7-9).

Sea Transports

India has a lack in quality of ports and cargo handling efficiency (Sinha and Sinha 1997:9). Most of the ports are overcrowded, with the average utilization rate ranging from 118 to 135 per cent. It also takes about 5-6 days of vessels waiting time, contrasts with only 6-12 hours in most other ports in the region (Brahmbhatt et al 1996: 19).

In general, it is not easy to define which country has the advantage on physical infrastructure. There are no specific patterns on the quantity of infrastructure stock. However, China appears to be slightly better in terms of quality and efficiency.

The Role of Nonresident Diaspora

One important factor behind the foreign capital inflow to China is the role of the Nonresident Chinese (NRC). Many of the NRC retain their links with the countryside, and it is not really difficult to attract them back with all their capital to the homeland (Guha 1993:339).

There are around 55 million Nonresident Chinese all around the world, whereas the Nonresident Indian (NRI) are only less than half as much (Sinha and Sinha 1997:21). The investment by Overseas Chinese in their ancestors' land was estimated to be US$ 130 billion in 1996, and contributed approximately 75 per cent of total foreign investment. In contrast, the direct investment by NRI was only US$ 49 billion or about 5 per cent of total FDI inflows to India (Saez 1998:24).

What makes the roles not similar is the different status of the majority of the nonresidents. As Lal (1995:1482) stated:

But the nature of the capital inflow has been different because of the differing nature of the two streams of migrants. Whereas the Indian Diaspora (at least of its more affluent members) has largely consisted of the professional classes, the Chinese Diaspora, particularly to Hong Kong and Taiwan, was of entrepreneurs... Thus whereas India could at best hope to mobilize short-run capital inflows in the form of bank deposits and bonds, China was able to get foreign equity from its Diaspora.

In short words, the nonresidents' role is something which not only India, but also other foreign capital host countries does not have as much as China does.

Social and Political Management

India and China have a very different cultural background. Indian society is one of the most heterogeneous in the world. On the other hand, China has an almost uniform society who is tied up under a dominant central government. This cultural background differences have the impacts on the domestic stability as well as policy making and implementations.

Based on a very homogeneous society, Indian politics and policy have been dominated by the pressures of interest-groups. This creates many compromises, coalitions, also conflicts (Guha 1993:334). As a result, policy reforms – including those related to foreign investment and economic liberalization – are going in a sluggish acceleration. The central government also faces difficulties on implementing decentralized development because of the lack of cooperative behaviors from local governments.

Chinese government does not have to deal with such problems. The absence of natural-bases of interest-groups and ethnic tensions has facilitated and speeded up policy reforms (p.335). The Chinese central government has the ability to coordinate its foreign investment policy with the actions of selected provincial government, due to the lack of friction between the central and provincial governments (Saez 1988:208-9). This had also created a more stable business environment, which is a conducive precondition for foreign investment.

E. Conclusion

The comparison of both countries has shown that China's better performance is owing to its unique heritage. The homogeneity of its culture and the Nonresidents Chinese investors has played a vital role behind the rapid growth. The effects of the endogenous factors, human resources and physical infrastructures, are not as strong as the exogenous ones. The comparative analysis of human resources does not give a satisfying explanation, while the infrastructure only partially explained.

A further question can then be addressed: is China's model applicable for India? Since the biggest account for China's success stories are exogenous factors, a full replication in alien environments can not be the recipe of success. But a lesson from China is the way it creates the unique heritage as valuable assets in the economy which is growing towards further openness and market-orientation. India can do the same thing with its own potential advantages – the English-speaking society, the presence legal and political infrastructure which is one of the most democratic in Asia, also the middle class and worldwide professionals.

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Appendix: Tables

TABLE 1.
Average Growth of GDP (per cent per year)

	China	India
1965-80	6.4	3.7
1980-90	10.2	5.8
1990-97	11.9	5.9

Source: The World Bank

TABLE 2.
Structure of Demand (as percentage of GDP)

		GDI/ GDP	GDS/ GDP	Exports /GDP	Imports/ GDP
China	1976	27.9	28.5	5.0	4.5
	1986	37.7	35.2	12.2	14.7
	1996	39.6	41.7	21.0	18.9
	1997	38.2	42.7	23.0	18.5
India	1976	20.9	21.7	7.2	6.4
	1986	23.2	20.4	6.0	8.7
	1996	25.2	21.9	11.8	15.1
	1997	24.0	20.2	11.5	15.2

Source: International Monetary Fund

TABLE 3.
Foreign Investment Inflows (billions of US$)

	China		India	
	FDI	**Portfolio Equity**	**FDI**	**Portfolio Equity**
1976	n.a	n.a	n.a	n.a
1986	1,875	0	208	0
1996	40,180	3,466	2,696	3,312
1997	44,236	8,457	3,197	1,828

Source: International Monetary Fund

TABLE 4.
Population and Labor Force

		China	**India**
Population (millions)	1980	981	687
	1997	1,227	961
Average growth rate (% p.a)	1980-90	1.5	2.1
	1990-97	1.1	1.8
Total labor force (millions)	**1980**	**539**	**300**
	1997	726	416
Average *growth rate (% p.a.)*	1980-90	2.2	1.9
	1990-97	1.1	2.0

Source: The World Bank

TABLE 5.
Infrastructure Comparison

		China	India
Electricity consumption (kwh p.c.)[1]	1995	637	339
Railroad (km)[2]	1994	64,000	62,460
Paved roads (km)[2]	1994	1,029,000	1,970,000
Airports[2]	1994	330	336
Telephone lines per 1,000 people[1]	1996	45	15
Education spending to GNP (%)[1]	1995	2.3	3.5

Source: [1]The World Bank
[2]Sinha and Sinha 1995