Comparing the Economies of China and India and its Impact on India's Strategic and Security Interests*

Shri Sanjaya Baru[@]

Introduction

One of the most influential research projects undertaken in the past quarter century was the study commissioned by the Paris-based Organisation for Economic Cooperation and Development (OECD) on structural changes in the world economy. British economic historian Angus Maddison led the study and gathered statistical data that shows, among other things, changes in the structure of world income and trade over the past millennium. The most striking result of the study was that in 1700 China and India accounted for nearly half of world income, with the two Asian neighbours having roughly equal shares (around 23.0 per cent each) and that their shares declined sharply to close to around 5.0 each by the middle of the 20th Century. Over two centuries of colonial rule and the fact that Asia missed out on the industrial and maritime revolutions were largely responsible for this. From 1950, both China and India have improved their shares of world income and even as recently as 1980 the two economies were more or less around the same level of development. It is now well known that in the post-Mao Dengist era, during the 1980s and 1990s, the Chinese economy took off and rapidly marched ahead of India. There was a further acceleration of China's growth and its share of world trade after the year 2000.

Consequently, by 2016 the Chinese economy was over four times the size of the Indian economy (please refer **Table 1** below). India's nominal gross domestic product, in terms of US Dollars,

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[@]**Shri Sanjaya Baru** is an eminent academic in economic affairs and was Media Adviser to the Prime Minister from 2004-08 as also a member of the National Security Advisory Board. He is also Visiting Fellow of School of Economic Studies, University of East Anglia, UK and East-West Centre, Hawaii. He has authored a number of books, the latest being *1991: How PV Narasimha Rao Made History.* Dr Baru is a Distinguished Fellow at the USI.

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was USD 2.5 trillion in 2016, while China's was USD 11.2 trillion. This gap is expected to persist over the short to medium term. China's recent economic slowdown (see graph of China real GDP growth below) and India's improved economic performance may help reduce the gap provided these extant trends persist.

However, in the foreseeable future, next five years, India has to live with the reality of this wide national income differential. Clearly, one consequence of the income gap would be a potential power gap, with China having the economic capacity to sustain larger defence budgets.

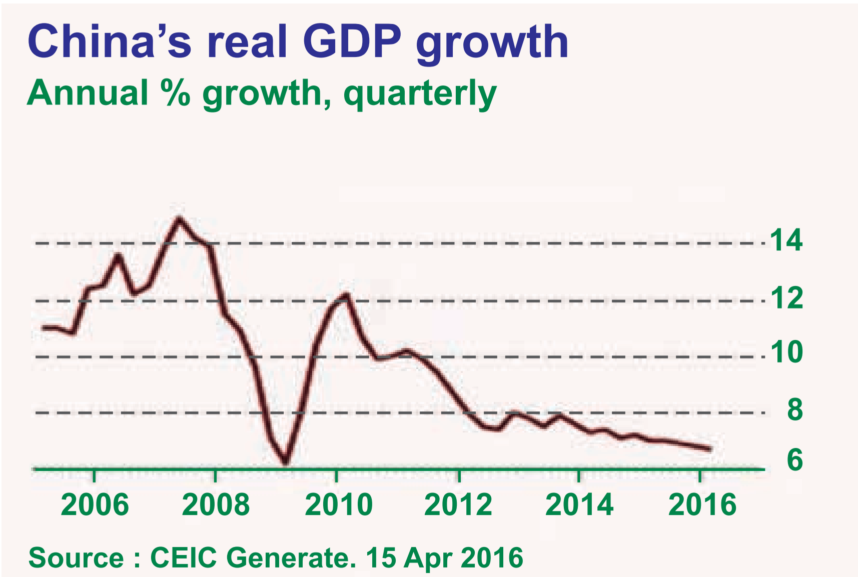

Table 1 : China – India – Size of the Economy & Per Capita Income, 2016-2020

	India		China	
	2016	2020	2016	2020
Nominal GDP (Trillion USD)	2.5	3.6	11.2	16.2
PPP GDP USD	8.7	12.7	20.4	28.2
Nominal GDP Per Capita USD	1,942.0	2,672.0	8,659.0	11,449.0
PPP GDP Per Capita USD	6,746.0	9,328.0	14,813.0	20,004.0

China's Economic Slowdown

China's economic growth rate has slowed since 2012. A report on the economy presented to the National People's Congress states that the 'target rate of growth' set by the country's economic policy makers for the period 2016-2020 is 6.5 per cent. This is way below the double digit levels that China recorded over the past quarter century. Several China-watchers, however believe that the 6.5 per cent target is perhaps an ambitious one because the real rate of growth recorded last year and this could be closer to 4.0 to 5.0 per cent. Whatever the numbers, the fact is that the Chinese economy is slowing down. One reason for this is the slowdown of the world economy. China has been increasingly dependent on the world economy for sustaining its income growth and so the global economic slowdown after 2008 has hurt China more than a country like India that has been less dependent on the global economy for its own economic growth.

In response to this slowdown macro-economic authorities in China have sought to rebalance the economy by shifting the earlier emphasis on investment-led growth to consumption-led growth. However, this has not been an easy switch to engineer. Chinese consumers continue to be frugal consumers, opting to save over 40 per cent of their income. The slow growth of domestic consumption along with the rapid decline in export demand and investment demand remains a major challenge for China.

One consequence of the slowdown in exports has been that China's current account surplus has reduced sharply from 10 per cent of GDP in 2007 to 2 per cent of GDP in 2014. Along with the sharp fall in the current account surplus there has been a rise in the fiscal deficit. The attempt to sustain growth through some investment even when demand has been constrained has contributed to a decline in the rate of return on investment and a sharp escalation of internal debt, which has risen from 150 per cent of GDP in 2010 to 250 per cent by 2016.

China's growth has been sustained by its emergence as a global trading power. Its total foreign trade in 2015 was estimated to be USD 4 trillion, compared to India's USD 0.5 trillion. China is the largest trading partner for 130 countries. More than its exporting power, what has contributed to rising Chinese geo-economic power is the fact that it has emerged as a major importing power, especially with respect to its Asian neighbours and Africa.

China-India Bilateral Economic Relations

While China has emerged as one of India's major trading partners, the persistently high trade deficit that favours China (please refer **Table 2** below). This has become a major political issue. In 2015, total bilateral trade between India and China stood at USD 70 billion, but the trade deficit (favouring China) was as high as USD 53 billion. India's trade deficit with China was almost half of India's total trade deficit.

Table 2 : China – India : 'Importing' Power

	Total Trade / GDP 1960	Total Trade / GDP 2015	Imports / GDP 1960	Imports / GDP 2015
China	9.0	41.0	4.4	18.7
India	11.0	42.0	6.7	22.6

Given these trends and concerns, where are India-China trade relations headed, and how can the problem of the trade deficit be tackled? First, it is important to recognise that the mounting trade deficit has become political mainly on account of persisting concerns about lack of transparency in China's domestic policies and the larger problem of a trust deficit between the two countries. Absence of credible data enables critics to speculate about intentions, including charges that China is out to 'subvert' India's manufacturing sector. In fact, both China and India have levelled anti-dumping charges against each other. According to the Indian Ministry of Commerce, out of a total of 290 anti-dumping investigations initiated by the Directorate General of Anti-Dumping and Allied Duties between 1992, when the WTO system came into being, and 2013, as many as 159 cases involved imports from China. Hence, China must address the issue at a political and administrative level to gain India's trust. Establishing trust is the first major challenge.

Second, Indian exporters must do more to win brand recognition and the trust of Chinese consumers. India's overall image has to improve before ordinary consumer resistance can be overcome. China has been trying to overcome such consumer resistance around the world, including in India. If a select number of Indian brands emulate Lenovo's strategy in India, they may be able to overcome consumer resistance and widen the market for Indian goods in China.

Finally, China will have to graduate from exporting products to India to making India a part of its global supply chain and manufacturing some of these products in India. This is the only way in which the problem of the trade deficit can be tackled.

China's Financial Power

One consequence of the build-up of current account surpluses by China has been that it has begun to deploy these dollar reserves in pursuit of its geopolitical objectives. China's overseas development assistance (ODA) budget now exceeds that of the World Bank. The China Development Bank is now bigger than the World Bank in terms of its asset base and lending profile. China has created the Asian Investment and Infrastructure Bank (AIIB) in order to invest in overseas infrastructure and industrial development projects through tied aid that helps push Chinese investment and trade. China has acquired a stake in the European, African and Asian regional development banks, thereby, deploying its reserves to acquire voting power in almost all major development financing institutions globally.

Going beyond such unilateral initiatives, China has emerged as a major shareholder in the BRICS New Development Bank, headquartered in Shanghai, and has increased its vote share in the International Monetary Fund (IMF). The Chinese RMB is now one of the reserve currencies of the IMF, along with the US Dollar, the Euro and the Japanese Yen. Taken together all of this has given China enormous clout in the global financial system, enhancing China's geo-economic power.

Geo-economics of China's Rise

The fact is that even before China's emergence as a geopolitical power it has already become a major geo-economic power. It has been able to deploy its 'trading power' – especially its 'importing power' to reward and punish countries. Thus, after Mongolia hosted a visit by the Dalai Lama, China threatened punitive economic action, including blocking IMF aid to Mongolia, and secured an apology and an assurance from Mongolia that it would not host another visit by the Dalai Lama. China has threatened or taken such economic action against several countries establishing its geo-economic clout.

India has to take cognisance of the fact that China is today the largest trade partner, a source of increasing investment and even defence supplies to several of its South Asian neighbours. Notwithstanding the deceleration in economic growth, China has funded a sustained increase in its defence budget, reminding us of Kautilya's aphorism in the *Artha Shastra,* "from the strength of the treasury, the army is born." China has emerged as a "strategic economic partner" with respect to many of India's neighbours, investing in port, power and other infrastructure projects that enable China to extend its power projection into the Indian Ocean region.

It is worth noting the fact that while the US's so-called 'pivot to Asia', in terms of deployment of troops in the Indo-Pacific, has not been matched by an economic commitment to the region (with President Donald Trump abandoning the Trans Pacific Partnership (TPP) project), China remains in play on the economic front bilaterally as well as multilaterally, with the Regional Comprehensive Economic Partnership (RCEP) negotiations. China has evolved from being a Trading Power to becoming an Investing Power and the launch of the One-Belt-One-Road (OBOR) project is a manifestation of this new phase in China's geo-economic power projection.

Conclusion

China is presently dealing with a loss of competitiveness, rising debt burden, and excess capacity, all of which have combined to slow down its rate of growth. China has been hurt both by a decline in domestic investment, inadequate consumption demand and the global economic crisis. But, China has the capacity – both economic and political – to deal with the challenges posed by these factors. We must assume that China will come out of this and retain its geo-economic and geopolitical clout. If China's ruling class cannot manage the domestic political consequences of an economic slowdown, there could be changes in the way China manages itself. For example, the Communist Party of China (CPC) may yield political space to the Peoples' Liberation Army (PLA). But, one must assume that between the two they would be able to manage the domestic political situation, the economic situation and their external implications.

From India's view point the major challenge in China-India relations will remain the current imbalance in the relative geo-economic power of the two countries. It will take more than a decade for India to be able to bridge the economic gap with China. This economic gap is fast converting into an overall national power potential gap. Dealing with this challenge will remain India's principal strategic challenge in the near term.