

Sales Across The Seas

The Telegraph, Calcutta, December 7, 1998

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India could match or exceed the economic success of China. To do so, it needs a three part growth strategy of export led growth, rural improvement and macroeconomic stability. This article takes a closer look at the first prong: export led growth.

If there has been one lesson of recent development experience, it is that fast overall growth depends on rapid export growth. The strategy of inward looking development, in which exports would be unimportant because imports would be held to a minimum, proved ineffective in all countries that tried it. It failed even with populous countries like Brazil, China, India and the former Soviet Union.

All economies, even giants like China and India, need to import huge amounts of capital goods, technology and intermediate products if they are to achieve technological efficiency and dynamism. These imports must be paid for. A country can try to rely on debt finance for a while. But as India found in 1991, the external debt route is precarious.

Even reliance on foreign direct investment is precarious unless the FDI is accompanied by rapid export growth, since the FDI inflow is motivated by an expected future stream of repatriated profits. That profit stream must have, as its counterpart, a rise in future exports. Otherwise the repatriated profits will come in the form of highly depreciated domestic currency as foreign investors attempt to repatriate domestic currency earnings.

The result: an imperative to export. Countries must export to import. And they must import to grow, since they require massive and continuing import of capital and intermediate goods that are only available at reasonable cost from abroad. It is not surprising, therefore, that all fast growing economies in the developing world are also export success stories.

China achieved rapid overall growth on the basis of rapid export growth. India managed only moderate success in exports and moderate overall growth. In China, exports of goods and services went from six percent of gross domestic product in 1980 to 21 percent of GDP in 1995. In India, by contrast, the figures were seven per cent of GDP to 12 percent.

There has been some opening up of the Indian economy, but the results have been modest in terms of export led growth. In dollar terms, China's merchandise exports (excluding services) rose from \$18.1 billion in 1980 to \$148.8 billion in 1995. India's merchandise exports rose from \$8.6 billion to a mere \$30.8 billion. China exported \$123 per person in 1995. India managed only \$33 per person. Nothing better accounts for the difference in growth performance of the two countries - 8.3 per cent average annual growth per capita in China during 1985-95 compared with just 3.2 percent in India than the difference in export growth.

India could have matched China in this field. But India failed in basic policy strategy. China's export growth was based on core policy and economic management decisions beginning from the early Eighties.

First, China understood the base of export growth would be diversification away from traditional sectors, especially raw materials, to nontraditional sectors, especially manufactured goods. But China lacked the technology to be competitive in manufactured goods. Therefore, it invited foreign direct investors to provide the capital and expertise to achieve export competitiveness in a wide range of sectors: These included electronics, apparel, toys, ceramics and other labour intensive sectors. In each sector, the key was to link foreign investor capital and expertise with a large and low cost Chinese labour force. The foreigners brought product designs, specialized machine tools and capital goods, key intermediate products and knowledge of world marketing channels. The Chinese assured these foreign investors certain key conditions for profitability: low taxes, infrastructure, security, power, logistics for the import and export of good.

At the centre of China's export strategy were the special economic zones. These coastal SEZs were designed to give foreign investors and domestic enterprises favourable conditions for rapid export promotion. All key aspects of the export environment were secured. Exporters, for example, were allowed to import intermediate products and capital goods duty free. They were given generous tax holidays. They were assured decent physical infrastructure.

India has experimented with export processing zones. But India's approach to export zones has been one of neglect rather than support. China's five main SEZs exported \$26 billion in 1994, roughly 22 percent of the national total. India's six main EPZs managed a fraction of that, both in absolute levels and as a proportion of total exports. In China, responsibility for the SEZs rests with local and provincial governments. In India this remain with New Delhi. Many state governments have actually been against having EPZs.

India's export environment suffers from several institutional weaknesses. India's labour laws make it costly to dismiss workers in enterprises with over 100 workers. The result: formal sector firms are loath to take on new employment. The majority of India's jobs are informal, in small, tax evading, inefficient enterprises. Equally remarkable, India's legislation continues to restrict the entry of large firms, or the growth of small firms into large firms, in several areas of potential comparative advantage. Thus garments, toys, shoes and leather products are still reserved for smallscale producers. Such restrictions assure China's dominance in these export sectors. India's tax and tariff structures remain biased against exports. India's high tariffs, especially on intermediate products used by exporters, impose a heavy indirect tax on export competitiveness.

The 1998-99 budget has imposed an additional levy of eight per cent on imports. There are duty drawback systems to reduce this anti-export bias, but such programmes are administratively burdensome and often too costly to use effectively. Finally, the regulatory attitude to foreign direct investors, the fuel for India's export drive, remains ambivalent. The government promotes FDI on the one hand. On the other it blocks full foreign ownership or insists on lengthy approval processes.

In addition to labour intensive manufacturing exports, India's growing capacity in service sector exports based on information technology deserves mention. The "1998 Global competitiveness

report" confirmed the high international opinion of India's engineering and scientific capacities. India's prowess has been most evident in software. Operating through satellite links, Indian programmers are providing infotech support to United States and European firms in areas ranging from software development to data transcription. Software exports have been growing around 50 percent per year in recent years, reaching an estimated \$1.75 billion in fiscal 1997-98, or roughly five per cent of merchandise exports. This proportion is likely to rise to an estimated 10 per cent in the year 2000. A tenth of Microsoft's worldwide programmer workforce is Indian.

Here Indian government policy could do much more to spur export growth. One plus has been the government's long term commitment to education centres like the institutes of technology. More recently, the government has supported software technology parks in Bangalore, Pune and other cities. These are infotech industry's equivalent to manufacturing's EPZs.

Serious negatives remain. The state monopoly in international telephony as well as internal service provision within India seriously raised the costs of telephone and infotech services in India. Its continuation will do considerable damage to India's international competitiveness in this sector unless rectified. India's telephone density is abysmal: 1.3 per hundred in 1995, compared with 62.6 per hundred in the US. The costs of international telephone calls from India are among the world's highest, largely due to lack of competition. Physical infrastructure for data transmission, like fibre optic cables, remains underdeveloped. Restrictive policies on FDI have kept international chip makers out of India. The lack of enforcement of intellectual property laws inhibits inward investments in infotech sectors.

All of these problems are remediable by further deregulating telecommunications and FDI, as well as tightening law enforcement in a more liberalized and competitive environment. India's strengths in infotech will be an important export bulwark for years to come - assuming administrative barriers are overcome.