Emerging Giants: Perspectives on China and India

Cletus Coughlin, Senior Vice President
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The views expressed here are those of the speakers, and do not necessarily represent the views of the Federal Reserve Bank of St. Louis or of the Federal Reserve System.
Emerging Giants
World GDP: 1980 Onwards

Percent of World GDP

Sources: VisualizingEconomics.com & The Madison Project
Last Observation: 2008
World GDP: 1500 Onwards

Sources: VisualizingEconomics.com & The Madison Project
Last Observation: 2008
Our Speakers:

YiLi Chien, Senior Economist

B. Ravikumar, Vice President
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Rapid Growth of the Chinese Economy

Total Real GDP: the U.S. and China

Average Growth Rate of U.S.: 2.40%
Average Growth Rate of China: 9.85%

Source: IMF
Key Questions

• What drives the growth of the Chinese economy?

• Is the high growth of China sustainable?

• Does trade with China hurt the U.S.?
Investment and Export Driven Growth

Investment and Export to GDP Ratio for 2011

Source: Haver Analytics
Investment-driven and export-driven growth are not sustainable

- The return and efficiency of investment have to go down eventually
- Limited export market
- Competition with other developing economies
Other Challenges

• Inequalities
• Inefficiencies
• Environmental problems
• Corruption and crony capitalism
What If China Becomes the Largest Economy?

• If China keeps its high growth, China will be the largest economy within a decade

• Even if China and the U.S. have the same GDP, the U.S. per capita GDP is still 4 times higher than that of China
Trade with China

Last year, the U.S. imported $394 billion and exported $103 billion

• Advantage: improve welfare of U.S. consumers

• Disadvantage: cost jobs in the U.S.?
Large in Quantity while Small in Share

- Imports from China: $394B or 2.6% of U.S. GDP

- Exports to China: $104B or 0.68% of U.S. GDP
Does Trade with China Reduce U.S. Jobs?

Yes, but not much

- U.S. consumers do not spend much on Chinese products
- A small fraction of the U.S. economy produces goods similar to Chinese imports
- However, a fraction of manufacturing workers might suffer the most
Summary

• Per capita GDP will still be much higher in the U.S. than in China for several decades

• Trade with China does reduce U.S. jobs, but probably not as much as thought

• Rising China provides great opportunities for U.S.: Sell services to China (financial, education, entertainment)
Emerging Giants: Perspectives on India

B. Ravikumar, Vice President

November 13, 2012

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Basics

• An ancient civilization
• A diverse country
• World’s largest democracy
• Population: almost four times the U.S.
• Area: one-third of the U.S.
Economic Reforms

- Comprehensive reforms began in the early 1990s
  - Transition from piecemeal reforms
- Inward competition
- Outward competition

Source: “India: The Emerging Giant” by A. Panagariya, 2008
Economic Reforms

• Inward competition
  ➢ Removal of licensing restrictions
  ➢ Privatization

• Outward competition
  ➢ International trade
  ➢ Foreign investment

Source: “India: The Emerging Giant” by A. Panagariya, 2008
Impact of Reforms

- Telecommunications: Private sector share of telephone subscribers
  - 0 in 1980s
  - 4.7% in 1998
  - 79% in 2009

Source: BSNL, India. [http://www.dnb.co.in/IndianTelecomIndustry/industrystructure.asp](http://www.dnb.co.in/IndianTelecomIndustry/industrystructure.asp)
Impact of Reforms

• International Trade: Imports + Exports as a percent of GDP
  ➢ Pre-reform: 12% (1987)
  ➢ Post-reform: 50% (2010)

Source: World Development Indicators, World Bank
Power of growth

- Sustained per capita income growth rate of 2% → next generation, on average, is twice as well-off as the current one

- 6% growth → almost 8 times as well-off
Rapid Growth

Real GDP per capita

Source: The Penn World Tables, version 7.1. Normalized PPP 2005 International dollars
Closing the gap

- 1988
  - U.S. GDP per capita: 23 times that of India

- 2010
  - U.S. GDP per capita: 12 times that of India

Source: The Penn World Tables, version 7.1. Normalized PPP 2005 International dollars
Growing Tourism

An Unusual Transition

Source: World Development Indicators, World Bank.
Size of the Indian Economy

- Total Real GDP in 2010
  - India – $4.69 trillion
  - Japan – $4.39 trillion
  - Germany – $3.13 trillion
  - U.K. + France – $4.68 trillion

Source: The Penn World Tables, version 7.1. Current PPP International dollars
Future Growth

- Hurdles
- Opportunities
Future Growth: Hurdles

- Labor regulations
  - Obstacles to large scale manufacturing
  - Moving unskilled labor from agriculture to manufacturing

Source: “India: The Emerging Giant” by A. Panagariya, 2008
Future Growth: Hurdles

- Infrastructure
  - Railroads and highways growing too slowly

Source: http://www.hsbc.com/1/2/emerging-markets/gbm/stories/transport-gap
Future Growth: Opportunities

- Well-equipped with skills in science and engineering
- Total factor productivity
- Large consumer market
Total Factor Productivity

• More inputs imply more output, but this is not a sustainable engine of growth in the long run

• Long-run engine of growth – more output with less input: Total Factor Productivity
Japan’s Growth

Japan’s Real GDP per capita (relative to the U.S.)

Source: The Penn World Tables, version 7.1. Normalized PPP 2005 International dollars
Total Factor Productivity

- Increases in Total Factor Productivity is the long-run engine of growth

- Contribution of TFP growth in India
  - 1950-1990: 20%
  - After 1991: 55%

Source: The Penn World Tables, version 7.1, PPP 2005 International dollars; Barro and Lee (2010), NBER working paper 15902
Large Consumer Market

Population in India

Large Consumer Market

- More than 500 million below age 25
- That is more than the total population of the U.S. + Canada + Mexico
- This working age population will be earning and spending over the next few decades

Source: World Development Indicators, World Bank
Source: http://www.gapminder.org/
Summary

• Economic reforms in India are gradually paying off.

• India is integrated into the global economy.

• While there are hurdles to future growth, there are ample opportunities for future growth.