India Shining is now a victim of its own hype

A FEW YEARS ago, when the Indian growth story had captured the world's imagination, an Indian friend of mine asked me, "Kishore, is there a danger of too much hype about India?" I replied, somewhat foolishly, "No such danger. Better to have hype than no hype."

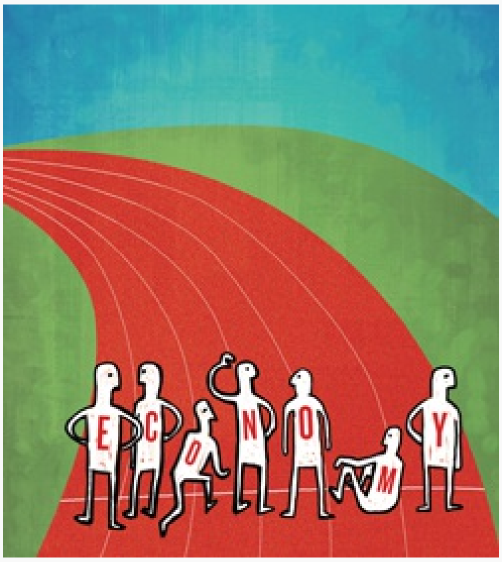

Illustration: Anand Naorem

How wrong I was! My Indian friend was wiser. India has become a victim of its own hype. In doing so, it has forgotten some basic points about economic growth. Firstly, economic growth is hard work. It does not come naturally, like the sun rising every day. Secondly, it is often the result of tough and shrewd political leadership. Deng Xiaoping showed his toughness by smashing the communist iron rice bowl that Mao had given to the Chinese people. Zhu Rongji showed his toughness by declaring, "I will prepare 100 coffins. 99 for corrupt officials and one for myself." As a result of their toughness, China has continued progressing as the fastest growing economy in the world. By contrast, India has had to struggle to introduce foreign investment in retail, a relatively small move to boost the Indian economy.

Hence, India's economic growth has slowed considerably from 9.55 percent in 2010 to 6.86 percent in 2012. By the rule of 72 (a method for estimating doubling time for an investment), India will now double its economy every 10 years instead of every seven years.

Many would like to believe that this recent slowdown is a temporary stall. This may just represent wishful thinking. Instead, this slowdown may actually be a result of overconfidence that rapid economic growth would come naturally to India, no matter what it does. This overconfidence may have in turn led to disastrous decision-making that has damaged investor confidence. The most damaging decision was the proposed 2012 amendment to tax legislation that foreign investors feared would impose retrospective taxes on mergers and acquisitions dating from 1962.

One wonders what the Indian policymakers were actually thinking when they shot themselves in the foot. Then they asked themselves why the Indian economy had stopped running forward! Similarly, although it has been reversed, the decision to pull back on foreign retail investment showed sheer incompetence in economic management.

How did this incompetence come about? The simple answer is that policymakers began to believe in the hype about India. They assumed that even if India made disastrous economic policy decisions, the Indian economy would be strong and resilient enough to keep growing, no matter what they did. This overconfidence has also infected other members of the Indian establishment. As a result, there is little hard-headed thinking about how the Indian economy can be turned around. Let me stress one point here. There should be absolutely no doubt about the potential of the Indian economy. It remains enormous. What India desperately needs now are three things. First, a clear understanding of the scale of India's potential. Second, a brutal and dispassionate analysis of the factors blocking India's realisation of its potential. Third, a list of quick measures it can take to jumpstart rapid economic growth.

First, to understand India's real potential, all we have to do is to measure the productivity of Indians in the most competitive economy in the world, the US, with the productivity of the Indians in India. This simple calculation will show the gap between India's potential and India's current situation. In 2010, per capita income for ethnic Indians in the US was at $37,931 when the national US average was $26,708.

If the Indian population of 1.3 billion could achieve only half of the per capita income of the Indian immigrants in the US, the Indian GDP today would be $24.65 trillion. Sadly, today, India's GDP is only $1.848 trillion.

Second, given the enormous gap between India's potential GDP and its actual GDP, the Indian establishment needs to understand what is holding back the potential. Hundreds of books have been written about this subject. There is no shortage of analysis. Instead, there is an abundance of paralysis by analysis. The argumentative Indian, to use Amartya Sen's phrase, has no shortage of reasons to explain India's faltering performance.

Given the abundance of analysis, India should stop trying to reinvent the wheel. It should just pick a single credible list of factors that are holding back India's economic growth. One list that is as good as any other list is the Goldman Sachs paper, "Ten Things for India to Achieve its 2050 Potential". Since Goldman Sachs was partially responsible for creating the hype by predicting that India would have the second largest economy in the world after China (and ahead of the US) in 2050, the list prepared by the global investment bank is as good as any. The paper suggested 10 things India could do to achieve its 2050 potential: 1. Improve governance, 2. Raise basic educational achievement, 3. Increase quality and quantity of universities, 4. Control inflation, 5. Introduce a credible fiscal policy, 6. Liberalise financial markets, 7. Increase trade with neighbours, 8. Increase agricultural productivity, 9) Improve infrastructure, and 10. Improve environmental quality.

It may take several decades, if not a century or more, for India to achieve progress in the 10 areas that Goldman Sachs has spelled out. What the firm does not point out is the list of all the vested interests that are holding back India's progress in these 10 areas. Demolishing some of these vested interests will be difficult, especially in a democratic system like India where these interests have entrenched themselves by forging deep partnerships with the electorates that keep them in office. This is why corruption that is legally entrenched in democracies like the US and India is harder to eradicate than illegal corruption.

Therefore, while still trying to work slowly on the long list that Goldman Sachs has provided, India should also focus on a shorter list that could provide a more immediate jumpstart to India's economy. The first is the easiest thing to do: create a special window for investment and economic participation by overseas Indians. Since the overseas Indians have demonstrated that they are far more economically productive than Indians in India, a window that lets them in quickly would provide an economic benefit through new investment. Equally, if not more importantly, through a process of symbiosis, the productivity, energy and drive of the overseas Indians could have a catalytic effect on the economic and educational performance of Indians in India.

IT IS true that India has already established several schemes to link up overseas Indians with India. For example, India has set up a Person of Indian Origin (PIO) as well as an Overseas Citizen of India (OCI) scheme. Even though I hold a PIO card, I don't know what opportunities it confers apart from visa-free entry to India. At the same time, there are rumours that the PIO and OCI schemes will be merged.

Quite naturally, there is political resistance in India towards providing special privileges to OCIs. This is understandable. However, the Indian government should explain to the people that the economy already benefits enormously from remittances. Indeed, India gets more remittances than any other country in the world, with $70 billion coming in from overseas in 2012. Yet, India can benefit far more from its overseas population if it uses them as a source of ideas as much as dollars. New ideas for improving the Indian economy can do far more good than dollars to supplement monthly incomes.

The second quick thing that India can do to jumpstart the economy is to become a leading votary of open globalisation. The success of the overseas Indian, especially in the US, has demonstrated competition is good for Indians. Indeed, they succeed and thrive when there is open global competition, performing as well if not better than any other nationality. The record of India's economic performance also shows clearly that India's economy grew slowly when it was relatively closed and grew faster after the then finance minister Manmohan Singh opened it up from 1991.

Given this clear evidence, the rest of the world should, in theory, fear economic competition from Indians. Ironically, the situation is the reverse. Indians worry more about global competition from the rest even though they have outperformed the rest when there is level global competition. How does one explain this manifestly absurd situation? The simple answer is that many Indian policymakers still lack cultural confidence. Their policymaking mindsets still come from the 1960s and '70s when there was a remarkable unanimity of opinion that the opening up of the economy would lead to defenceless India being ravaged by avaricious western MNCs. Instead, it is now clear that the opposite would have happened. Any opening up to global competition would have made the Indians in India as productive as the overseas Indians as Indians thrive under global competition. Just by ditching the old mindsets of the '60s, Indian policy policymakers could make a huge difference. By adopting a bias towards openness in their daily decision-making, they would give a huge and immediate boost to the Indian economy.

The third quick thing that India can do is to seize geopolitical opportunities. After almost two decades of deft diplomacy, China has surprisingly begun to make mistakes in its relations with its neighbours, especially Japan. Over time, China will definitely learn and recover from its mistakes. In the meantime, however, Japan will begin hedging its bets by investing less in China and more elsewhere. Indeed, Japan has been the largest single investor in China, after Hong Kong and Taiwan. The total amount of Japanese investment in China is $12.6 billion, while that in India is $2.3 billion. Just imagine how the Indian economy would look if these figures were reversed.

At the same time, there are other low-lying economic fruits that India could pluck. India already has Free Trade Agreements (FTAs) with Japan and ASEAN. And ASEAN and Japan also have an FTA. India could show its diplomatic deftness by converting those three existing bilateral FTAs into a trilateral FTA and jumpstart a new trend of trilateral FTAs. Indian policymakers have been reluctant to do this because they fear India cannot compete with both Japan and ASEAN. Ironically, it is ASEAN and Japan who should fear Indian competitiveness. This is why the mindsets of the Indian policymakers have to change immediately.

In short, even though the Indian economy appears to be slowing down and losing its edge, a few easy things can be done to rev it up again. All it takes is a little more cultural confidence and some shrewd and tough decision-making by the policymakers. What India needs now is a little less hype and a little more quiet shrewdness. And, it can be done.

Mahbubani is the Dean and Professor in the Practice of Public Policy of the Lee Kuan Yew School of Public Policy at the National University of Singapore (The views expressed in this column are the writer's own)

letters@tehelka.com