Comments on Professor Panagariya’s Paper on “India and China: Past Trade Liberalization and Future Challenges”

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# Major Economic Indicators of India versus China

<table>
<thead>
<tr>
<th></th>
<th>Unit, Period</th>
<th>China</th>
<th>India</th>
<th>India/China, %</th>
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</thead>
<tbody>
<tr>
<td><strong>Level of Economic Development</strong></td>
<td></td>
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<tr>
<td>Per Capita GDP</td>
<td>$, 2005</td>
<td>1703</td>
<td>723</td>
<td>42.5</td>
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<tr>
<td>Human Development Index</td>
<td>Global Ranking, 2004</td>
<td>81</td>
<td>126</td>
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<tr>
<td><strong>Economic Growth</strong></td>
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<tr>
<td>GDP Growth Rate</td>
<td>%, 1979-2005</td>
<td>9.7</td>
<td>5.5</td>
<td>56.7</td>
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<tr>
<td>GDP Growth Rate</td>
<td>%, 2001-2005</td>
<td>9.5</td>
<td>7.0</td>
<td>73.7</td>
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<tr>
<td><strong>Market Size</strong></td>
<td></td>
<td></td>
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<tr>
<td>Population</td>
<td>billion, 2005</td>
<td>1.3</td>
<td>1.1</td>
<td>84.6</td>
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<tr>
<td>GDP</td>
<td>billion dollars, 2005</td>
<td>2200</td>
<td>800</td>
<td>36.4</td>
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<tr>
<td><strong>Global Links</strong></td>
<td></td>
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<tr>
<td>Share of World Trade</td>
<td>%, 2005</td>
<td>6.7</td>
<td>1.1</td>
<td>16.4</td>
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<tr>
<td>Exports</td>
<td>billion dollars, 2005</td>
<td>762</td>
<td>95</td>
<td>12.5</td>
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<tr>
<td>Imports</td>
<td>billion dollars, 2005</td>
<td>660</td>
<td>135</td>
<td>20.5</td>
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<tr>
<td>FDI</td>
<td>billion dollars, 2005</td>
<td>72.4</td>
<td>6.6</td>
<td>9.1</td>
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<tr>
<td><strong>Investment Climate</strong></td>
<td></td>
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<tr>
<td>Inward FDI Potential Index</td>
<td>Global Ranking, 2004</td>
<td>33</td>
<td>82</td>
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</tbody>
</table>

Sources: Official statistics of China and India, UNDP (human development index), WTO (share of world trade, exports and imports), UNCTAD (FDI, inward FDI potential index)
Pro-comparative Advantage versus Anti-comparative Advantage Strategy

- Difference in strategy explains
  - Why China has outperformed India
  - Why economic growth in India has accelerated in recent years
  - Why economic growth in China has been much higher in the post-reform period
- Like India, China pursued an anti-comparative advantage strategy until the late 1970s
- China turned to a pro-comparative advantage strategy since the late 1970s
- Reform: Integration of China into the global economy according to comparative advantage *(The China Miracle: Development Strategy and Economic Reform*, Professor Justin Lin, Peking University)
  - Liberalization of trade and FDI
  - From plan to market
Changes in Production and Relative Prices Resulting from the Rise of China

Labor-intensive products

Global Production Possibility Frontier

Technology-intensive products
Immiserizing Growth?

- Whatever China buys becomes more and more expensive
- Whatever China sells becomes cheaper and cheaper
- Deterioration in China’s terms of trade (real exchange rate)
  - Slow growth in real wage and sharp depreciation of the RMB in real terms, despite rapid economic growth (absence of Balassa-Samuelson effect)
  - Japan’s terms of trade versus China have improved sharply over time
- Should China introduce an “optimal tariff” to maximize its gain from trade?
The Improvement in Japan's Terms of Trade vis-a-vis China

Source: Japan Tariff Association.
Criticism of FDI Policy by “New Left”-Latin Americanization of China?

- Exploitation of Chinese labor – China as the sweat shop of the world
- Exploitation of Chinese consumers -- Monopoly pricing by foreign firms
- Exploitation of China’s environment – China as a pollution haven
- Swapping market for technology or losing market without gaining technology?
- Automobile – South Korean model versus Brazilian model
- Foreign companies pay lower corporate tax rates than Chinese companies and enjoy tax holidays
- Chinese companies demanding national treatment in their home market
- China is ready to reduce preferences (tax preferences) granted to foreign companies
  - Differential tax rates applicable to domestic and foreign firm will soon be unified
China-India FTA?

- **Chinese perspective**
  - China is a major trading partner of India (second largest trading partner, 7.8% of total trade)
  - But India is not a major trading partner of China (accounting for only 1.3% of total trade)

- **Better for China to form FTA with Japan**
  - Japan is China’s third largest trading partner after US and EU, accounting for 13.0% of total trade
  - China is Japan’s second largest trading partner after the US, accounting for 17.0% of total trade
  - Strong complementarity between the two countries favors trade-creation
  - China and Japan together account for more than 80% of East Asia’ GDP
  - China-Japan FTA should pave the way for a pan-East Asian FTA

- **Domestic FTA**
  - Unified domestic market for goods and services, labor and capital
  - Reforming the household register system to enhance labor mobility
  - Promotes efficiency and reduces regional income disparity