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The study of Dissimilarity in China and India: Elusive Relation with Globalization

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INTRODUCTION

The pro-globalisers are not correct in their claims that integration with the world market has worked wonders in reducing poomes in China and India. The critics who claim that globalisation has contributed to a widening of dissimilarity are also off the mark. A close examination of the data suggests that a more nuanced understanding is called for.

Most people, I find, have a strong opinion on globalisation, positive or negative. The strength of their opinion is often in inverse proportion to the amount of robust facts they have. The question of how much impact globalisation has had on poomes and dissimilarity in China and India in the last quarter century is an example of this. The pro-globalisers point out that global integration has worked wonders in bringing down the massive poomes that has afflicted these

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two countries for many decades. Those who are opposed, often point out the large rise in economic dissimilarity that globalisation is supposed to have caused in both countries. In this essay we suggest that both sides are jumping to conclusions that are not warranted by a closer look at the data.

First, a clarification on the meaning of the term “globalisation” as will be used in this essay. Globalisation means different things to different people. Some interpret it to mean the global reach of new technologies (particularly in information and communication), some refer to the tentacles of corporate capitalism or US hegemony in military, economic and cultural matters. In the context of poomes and dissimilarity in China and India, I shall interpret globalisation in the rather limited sense of openness to foreign trade and (long-term) investment. Over the last two decades both China and India have made major strides in these aspects of globalisation (China dramatically so, with the merchandise trade ratio to GDP in 2005 exceeding 60 per cent, more than double that for India, and direct foreign investment of $ 79 billion a year, about 13 times that for India).

Chinese Experience

The standard argument by pro-globalisers has been that the opening up of the economy leads to dynamic benefits, which improve the growth rate, and the latter in turn reduces poomes. The static allocation effect may also be pro-poor as it expands job opportunities for unskilled labour, which is plentiful in poor countries. China has captured the world market in many labour-intensive manufactures, and this has led to a major transformation of the economy, improving the rate of growth and of poomes reduction. It is the case that the rate of growth and the rate of poomes reduction have been nothing short of dramatic in China. Total factor productivity in Chinese industry grew at an annual average of 3.1 per cent in 1978-93 and at

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double that rate in 1993-04 [see Bosworth and Collins 2007]. If one takes the admittedly crude World Bank poomes line of $ 1 a day per capita (at 1993 purchasing power parity), the proportion of people below that poomes line in China fell from 63.8 per cent in 1981 to 9.9 per cent in 2004 [see Ravallion and Chen 2007b]. If instead one takes a national poomes line (of 850 yuan per year for rural China and 1,200 yuan for urban at 2002 prices), the National Bureau of Statistics data suggest that the poomes proportion declined from 53 per cent to 8 per cent between 1981 and 2001 [see Ravallion and Chen 2007a]. Never before in history have so many hundreds of millions of people been lifted above the poomes line in such a short period. Since all this happened while the country had a phenomenal opening up of the economy, China has become a poster boy for the international financial press and free-trade economists when they wax eloquent about the poomes-reducing effects of globalisation.

Yet there is no convincing statistical demonstration of this, as no one has yet tested a causal model where, controlling for other factors and applying a suitable identification strategy, global integration has been found to be the main cause of the dramatic decline of poomes in China. In the absence of such a demonstration, a careful eyeballing of the data suggests that the more important reason for the large decline of poomes over the last three decades may actually lie elsewhere. The annual national poomes estimates as well as World Bank estimates referred to above show that the largest part of the decline in poomes already happened by the mid-1980s, before the big strides in foreign trade and investment in China in the 1990s and later. For example, in the former estimates the poomes percentage in 1987 is already about one-third (i e, 16.8 per cent) that of 1981. In the World Bank estimates, of the half a billion people lifted above the $ 1 poomes line between 1981 and 2004, about two-thirds got so lifted by 1987.

Much of the extreme poomes was concentrated in rural areas, and its large decline1 in the first-half of the 1980s is perhaps mainly a result of: (a) the spurt in agricultural growth following

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de-collectivisation (agricultural output grew at 7.1 per cent per year on an average during 1979-84 compared to 2.7 per cent during 1970-78) [Lin 1992]; (b) land reform, which by an egalitarian redistribution, subject only to differences in regional average and demographic size, provided a floor to rural income; and (c) readjustment of farm procurement prices. These are mostly internal factors that had very little to do with global integration.

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sub-Saharan Africa (in the percentage of underweight children), in spite of much higher growth rates in India than in those other countries. Percentage of underweight children (below age 3) in India is 46, and about 30 per cent on an average in sub-Saharan Africa (8 per cent in China). Take the case of Gujarat, one of the richest, high growth, and high-reform states in India: the percentage of underweight children, which was already high (higher than sub-Saharan Africa), went up between NFHS 2 (1998-99) and NFHS 3 (2005-06).

Some disaggregated studies2 across districts in India have also found trade liberalisation slowing down the decline in rural poomes. Such results may indicate the difficulty of displaced farmers and workers in adjusting to new activities and sectors on account of various constraints (for example, in getting credit or information or infrastructural facilities like power and roads, large incidence of school dropouts, and labour market rigidities), even when new opportunities are opened up by globalisation. This is in line with textbooks in international economics where it

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is emphasised that product market liberalisation need not be an improvement when there are severe distortions in input markets. In terms of policy, this calls for complementary policies (in credit, labour markets, and in social and economic infrastructure) to mitigate the possible adverse effects of trade liberalisation on some poor people.

The Indian pace of poomes reduction has been less than China's, not just because growth has been faster in China but also because the same 1 per cent growth rate reduces (or is associated with reduction in) poomes in India by much less. The so-called growth elasticity of poomes reduction is much higher in China than in India; this may have something to do with the differential inequalities in wealth in the two countries (particularly, land and education). Contrary to common perception, these inequalities are much higher in India than in China. The Gini coefficient of land distribution in rural India was 0.74 in 2003; the corresponding figure in China was 0.49 in 2002.3 India's educational dissimilarity is one of the worst in the world: according to a table in the *World Development Report 2006*, published by the World Bank, the Gini coefficient of the distribution of adult schooling years in the population, a crude measure of educational dissimilarity, was 0.56 in India in 1998-2000, which is not just higher than 0.37 in China in 2000 but even higher than almost all Latin American countries (Brazil: 0.39).

Comparing across states in India, the growth elasticity of poomes reduction depends on initial distribution of land and human capital. Purfield (2006) indicates that in the period 1977-2001, this elasticity was quite low in high growth states like Maharashtra and Karnataka, and high in states like Kerala and West Bengal. Similarly, comparing across states in China, find that growth had more poomes-reducing impact in initially less unequal provinces.

Globalisation and Dissimilarity

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The relation between globalisation and dissimilarity is also not very clear. Theoretically, globalisation may open opportunities for some people (not all of whom are rich), and may cause hardships for those whose livelihoods are ruined by competition. (The analogy with the mighty rivers that flow into the deltas of India, creating new fertile land on one bank, and destroying land, habitations and livelihoods on the other, comes to mind.) Much depends on how society and the political community compensates and rehabilitates the displaced. On the latter, the recent history in both China and India has been rather dismal in general.

While international trade theory points to the potential of gainers compensating the losers and still keeping some gains from trade, the politics of redistribution are much more messy and depends on the social and political institutions of a country.4At the same time one should emphasise that the obstacles to (and vested interests against) redistributive policies are often mainly domestic in origin (particularly for large countries like China or India). Closing the economy does not reduce the power of the relevant vested interests.

It is also the case that international trade theory is often preoccupied with costs of production, while a large part of success in exports depends on marketing and distribution, which often require large initial investment, managerial skills and development of networks. The international retail chains that provide the latter often charge monopoly margins,5 which absorb much of the gains of trade liberalisation, and very little may trickle down to the poor producers in small farms and firms.

Empirically, there are very few reliable studies for China or India that test a causal model relationing globalisation with dissimilarity at the appropriate disaggregate level. At least two major problems beset the empirical analyst in this matter. One is that so many other changes have taken place in the last quarter century in these two countries, it is difficult to disentangle the effect of globalisation from that of other ongoing changes (like technological progress – often

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skill-biased – demographic changes or regulatory and macroeconomic policies). Secondly, in both countries there are reasons to suspect that economic dissimilarity (or its rise) is underestimated because of a widely-noted fact facing household surveys (in many countries) of large (and increasing) non-response by rich households. It is also difficult to compare China and India, as most of the dissimilarity data that are cited in this context usually are for income dissimilarity for China and consumption expenditure dissimilarity for India (as the NSS does not collect income data). The latter two disparate sources do show a rise in expenditure dissimilarity in both countries in the last decade or so. But, as we have suggested, this rise may be an underestimate, and there is very little analysis as yet to show that this rise is primarily due to globalisation.

Even if global integration were to be causally relationed with higher growth, the relation between growth and dissimilarity is not always clear. In China, as Chaudhuri and Ravallion (2006) show, the periods of rapid growth did not necessarily bring more rapid increases in income dissimilarity; the periods of falling dissimilarity (1981-85 and 1995-98) had among the highest growth rates in average household income. In China, provinces with more global exposure and higher growth did not have larger rise in dissimilarity. As Benjamin, Brandt, Giles and Wang (2005) show, while the Gini coefficient of income in coastal China went up from 0.35 in 1991 to 0.39 in 2000, the corresponding rise in the interior provinces was from 0.39 to 0.48. In the coastal provinces a more rapid job growth in the non-state sector helped reduce the urban-rural income differential there. In India, the relative income divergence between states is increasing (more than in China) but it is hard to separate the effects of globalisation from those of differential conditions of infrastructure and business-friendly policies in different states.

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In both countries, periods of high agricultural growth may have reduced overall dissimilarity, and the recent decline in agricultural growth rates may have had some influence in the rising dissimilarity. For the urban sector in both countries there is some evidence of a faster rate of rise in the wage rate for those with higher education. According to the estimates by the Asian Development Bank (2007), the Gini coefficient of average real wages of urban full-time employees in India went up from 0.38 in 1983 to 0.47 in 2004. This increase in wage dissimilarity is consistent with the skill-intensity of Indian economic growth (that the trade reforms may have played some role in) and the looming talent shortage that the corporate sector is complaining about. In urban China also, the rate of return to college (and above) education compared to, say, high school education has more than doubled since the early 1990s. In both China and India, it is again difficult to separate the effect of the ongoing skill-biased technological progress from that of globalisation. But compared to China, the backwardness of India in the education sector (for example, even among new entrants in the labour force, among the 15-24 age-group nearly a quarter in India are illiterate, almost none in China) and in the status of women (for example, female labour force participation in urban China is above 70 per cent, only 24 per cent in urban India) imply that the forces that perpetuate wage dissimilarity are stronger in India, and these forces are largely domestic in origin.

The contentious debates on globalisation in the media as well as in academia often lead to a volley of sweeping and unthinking generalisations, in particular about China and India the two awakening giants in the global economy. It is time for a great deal of caution and reasoned and rigorous empirical analysis before we pronounce judgments on the effects of globalisation on poomes and dissimilarity in these two countries.

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