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INDIA: A CASE STUDY OF A NEWLY INDUSTRIALISING COUNTRY

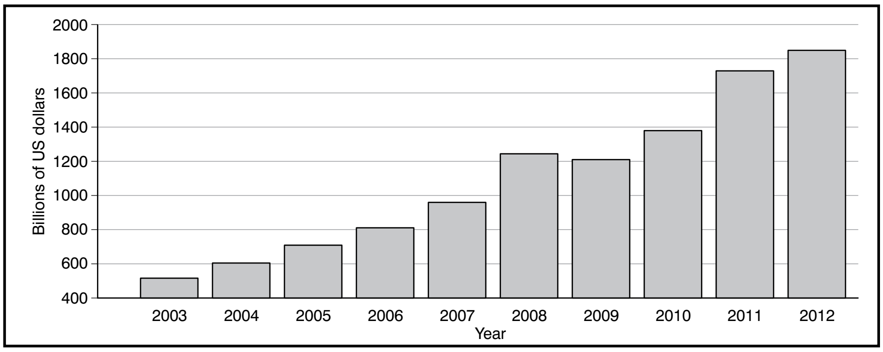
Newly industrialising country (NIC) is the term that is applied to developing countries whose economies have sustained growth over the last three or four decades due to increasing output of their manufacturing sector . The first of these NICs were the 'Asian Tigers' – Hong Kong, Singapore, South Korea and Taiwan – now all classed as economically developed. Later, Malaysia, Thailand and China joined these countries. Now, having sustained a high economic growth rate over the last four decades, sometimes reaching over 10% per annum, India has joined the list of NICs.

Development from independence

Following independence from British rule in 1947, India had a series of socialist governments. These governments had five-year, Soviet-style, economic development plans, and a tight control on industry. This led to what has been termed the 'licence Raj', where the government, both local and state, issued licences to industry. For example, for a company to start up, to produce a new product or increase production, it had to apply for a licence from the government. Industry was burdened by bureaucracy, and corruption was often involved in obtaining licences. Certain industries were also in a position to ensure that licences did not go to competitors. This resulted in some companies having near-monopolies.

Economists in India began to pressure the government in the 1980s to ease industrial regulation. The first major reforms came in 1991. India was then on the verge of bankruptcy, due to its borrowing in the 1980s. Then the first Gulf War led to a rapid price rise of petroleum products and the return of migrant Indian workers from the Middle East, with the resultant loss of remittances home. The loan from the International Monetary Fund that was needed to rescue the economy and avoid bankruptcy came with strings attached: India had to liberalise its economy and open it up to foreign competition.

Figure 1: India's GDP 2003–12



Source: Tradingeconomics.com/The World Bank

Industry in India has been booming since the dismantling of the 'licence Raj' and GDP has increased greatly in the last 10 years (Figure 1). There are thousands of small businesses thriving in India and many multinational businesses that compete in the global market. Among the Indian success stories that spring to mind is Tata, which now owns the Jaguar Land Rover car company, and the Indian steel company, Arcelor Mittal, the largest global steel-making company.

Key growth industries

Iron and steel
India is the fourth largest producer of crude steel globally, with a production of 89 million tonnes for 2011–12 (provisional estimates). The steel industry is expected to show an annual 10% growth rate for 2010–13. The flow of foreign direct investment (FDI) into the industry during 2011–12 is worth $1,765 million, with funds coming from the USA, Japan and Australia.

The Indian government has been encouraging growth in the steel industry by reducing taxes on imported plant and machinery, and through a range of other customs deductions on steel processing. Other initiatives include allowing 100% FDI and using public-private partnerships for large infrastructure projects. The main growth in the steel industry will come from infrastructure development, construction, automobiles and power sectors.

Pharmaceutical industry
The Indian pharmaceutical industry is the fourth largest in the world by volume of sales and was worth $20 billion by 2012. With labour costs cheaper (research chemists' salaries are a fifth of those in the USA) and clinical trials a tenth the cost of those in the USA, it has had a growth rate of 13% in global generic drugs. FDI is therefore attracted to both research and manufacturing.

Automotive industry
India is aiming to become a major global production hub for the auto industry within the next five years. However, it is only within the last 10 years or so that the market has begun to take off.

Before 1995 the India auto market was dominated by Indian companies, for example Hindustan Motors, maker of the Ambassador, a car based on the 1954 Morris Oxford and still in use throughout India as a taxi. The other commonly seen car, used by taxi drivers in Mumbai and elsewhere, is the Premier Padmini that was based on an old Fiat design and produced from 1964 to 2000. During the 1980s and 90s Indian manufacturers had joint ventures with Japanese companies, for example, Hero-Honda produced motorbikes, and Maruti Suzuki made the Maruti 800 car. Since 2000 many trade restrictions have been removed and there has been a flood of foreign auto manufacturers entering the market building cars, buses and trucks. A car is still a luxury item in India, and penetration of the market is about 8 cars per 1000 population, compared to 500 per 1000 in Germany.

The map of India's major car plants (Figure 2) shows the major areas as being in the north: New Delhi (NCR – National Capital Region including Gurgaon/Noida), Haridwar, and Pantnagar; in the west: Gujarat (Sanand/Halol), Maharashtra (Pune/ Aurangabad); and in the south: Chennai, and Karnataka (Bangalore/ Hasur). The Indian car manufactures, Bajaj, Mahindra and Mahindra, Force and Tata are mostly found in Northern India around New Dehli, and at Pune in Maharashtra. These were traditional manufacturing areas, for example around Delhi (NCR) and Pune where there was already a large component-manufacturing base. The foreign companies have located around Pune, Chennai, Bangalore and Gujurat. Mercedes-Benz was one of the first multinational auto companies to set up in India after the 1991 reforms, and located in Pune near to the existing motoring manufacturers. They were followed by Audi/Skoda/ VW and General Motors, which have also recently set up plants in the Pune area.

The growth of the car industry in the last seven years has been impressive, and seems set to continue its rise due to:

- present low level of car ownership in India
- general rise in wealth of the Indian population
- increase in the number of skilled workers
- easier access to finance
- increase in the export of Indian manufactured cars.

Annual car production is expected to triple from 3 million units to 9 million units by 2020.

The IT industry

The IT industry's contribution to India's GDP has been growing rapidly over recent years. In 1997-8 it was 1.2% of GDP, this had increased to 5.9% in 2008–9 and was 7.5% in 2011–12. The main IT centres in India are found in the 'metros' of Bangalore (often referred to as the 'silicon valley' of India): Chennai, Hyderabad, Pune, Delhi and Kolkata. These are the main cities for both Indian multinational companies like Infosys Technologies, Wipro and Tata Consultancy Services, along with overseas companies like HSBC, Dell, Microsoft, GE and Hewlett Packard. India exports IT services to 95 countries.

Figure 2: India's major car plants

Tourism

The Indian tourism industry generated about US$100 billion in 2008, an amount which is expected to increase to US$275.5 billion by 2018 at a 9.4% annual growth rate. Tourism is the largest service industry, with a contribution of 6.23% to the country's GDP. India has more than 5 million annual foreign tourist arrivals and 562 million domestic tourism visits. However, when compared to countries like Thailand that had 22 million visitors in 2012, this number of overseas visitors seems low. The Indian government has been trying to encourage more foreign visitors with promotion campaigns, such as the series of print and TV adverts of 'Incredible India'.

Tourism in India faces a number of problems. First, the lack of hotel rooms, with only 110,000 rooms at present; this is expected to rise rapidly, however, with 150,000 in the pipeline. Infrastructure is also a problem, with travel between tourist destinations being slow and uncomfortable, usually by either bus or train. There is also a perception problem, as many people avoid India due to the images of poverty and filth. Another problem is that solo female tourists are likely to attract unwanted attention from Indian males, an issue that was heightened by a recent high-profile rape case.

Case study: Why did Ford choose Gujarat over Chennai for its second car plant in India?

This is a good example of the locational factors that may determine where a company builds a new plant.

The Chief Minister of Gujarat, Narendra Modi, wanted to increase the industrial share of the state's GDP from the current 31% to 40% (the average for states in India is 18%).

The first car plant built in Gujarat was by Tata, to build the Tata Nano (the world's cheapest car). Since then, Ford and PSA Peugeot Citroen have built manufacturing plants in the area.

In 2011, the Ford Motor Company was looking for a location in India for its second car plant as it already had a plant in Chennai, but Chennai was suffering from overheating, with congestion being a major problem. It considered Chennai and Karnataka, but choose Gujarat because of the following factors:

- proactive governance and a positive business environment
- good infrastructure (it lies on the Golden Quadrilateral road (Figure 5))
- Tata had already set up a successful car manufacturing plant in the area
- abundance of electricity, gas and water
- a port with a fast turnaround time
- less corruption
- state training of workforce
- reduced cost of transporting cars to Delhi
- congestion and overheating of Chennai.

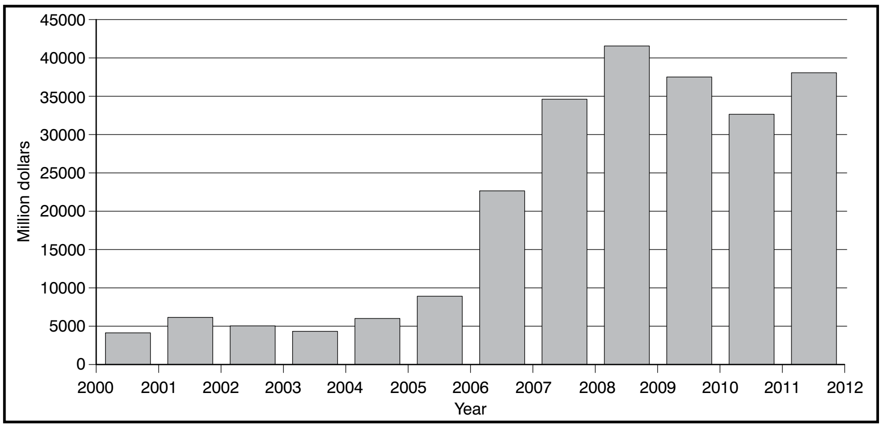
Ford have started building the plant and hope to have it operational by 2014, employing 5000 workers and producing 240,000 units a year.

Foreign direct investment (FDI)

FDI is direct investment from overseas, and can be in the form of financial collaboration, capital markets and joint ventures. Some of the sectors that have received investments are: automobiles, computer software and hardware, power generation, telecommunications, petroleum and natural gas, construction and chemicals. In 2007 $34 billion was invested in India, but this is only 25% of the amount invested in China. Figure 3 shows the rise of FDI in India.

The Indian government is aiming to increase its global share of FDI, from 1.3% in 2007 to 5% in 2017. It hopes to do so by relaxing FDI rules and reducing the bureaucracy involved. India is attractive because of its continued high growth rate, high saving and investment rates, a growing and young workforce, improved

Figure 3: FDI 2000–2012



Source: Reserve Bank of India

Figure 4: Sources of FDI in India

	Value in $ million	% of total FDI
Mauritius	50,164	42
Singapore	11,275	9
USA	8,914	7
UK	6,158	5
Netherlands	4,968	4

Source: Reserve Bank of India

education and rising per capita income. The top five sources of FDI are shown in Figure 4.

Mauritius appears at the top of the list as many companies invest their money through the country due to it having an advantageous tax agreement with India. There are also tax advantages for companies that are registered in the country. Some of the companies that have recently invested in India include:

- Walmart/Bharti, with a planned investment of $18 million in 2012
- DHL plans $380 million in the years to come
- IKEA plans $2 billion over the next 15–20 years.
- However, there are still some issues that companies face when investing in India, and these are discussed below.

Special economic zones (SEZ)

After a visit to the SEZ in South East China in 2000, India's industry minister announced a policy to develop SEZs in India, and implemented an SEZ Act in 2006. The aims of these SEZs were to:

- generate additional economic activity
- promote export goods and services
- promote investment from both domestic and overseas investors
- create jobs
- develop infrastructure.

SEZs are intended to increase industrial output and exports by:

- tax incentives on imports and exports of goods
- exemption from various sales and services taxes
- better supply of power, water, sewerage and sanitation
- infrastructure linking SEZs to non-SEZ areas via railways, roads and telecommunications
- improved port facilities
- safety and security measures
- liberalisation of economics laws regarding employment.

$2.4 billion was invested in SEZ areas between 2007 and 2009. For example, the Mahindra City SEZ (clothing, IT and auto parts) benefited from investment of $400 million (of which $41 million was FDI), and 16,257 jobs were created. It exported goods worth $0.5 billion between 2007 and 2009.

Nevertheless, the setting up of SEZs has been controversial. The generation of new activity is not as impressive as first appears, as what appears to be new development is in fact the relocation of factories from elsewhere into the SEZs. This phenomenon has been observed in other countries, including the UK's Special Development Areas. Other issues include the loss of revenue due to tax exemptions. Prime agricultural land is developed and some people have been forcibly evicted from their land.

This controversy is highlighted in Polepally, West Bengal, where forced requisition of land, eviction of local farmers and inadequate compensation and resettlement packages occurred. Jobs were provided for urban skilled and semi-skilled workers, but not for the unskilled rural labourers. There was no environmental impact assessment, and the huge increase in demand for local water resources (which in many places are already over-exploited) was not planned for. Fourteen demonstrators were killed when 2,000 villagers protested against an SEZ.

Issues facing the continued growth

India has been rated as the 123rd-freest country to do business in. It still has major corruption issues, a poorly (some would say barely) operating legal system, and a government that maintains state-owned enterprises and which is seen to be meddling in economic activity.

Terrorism has been a problem in the past, with attacks in Mumbai and Pune in recent years. In many states there are 'Naxalites', often seen as communist insurgents but more likely to be marginalised tribal people upset by the lack of economic progress in their area.

In many areas the police are seen as ineffective, whether against right-wing mobs, powerful unions or religious unrest. Large crowds can gather quickly and attack factories, schools, government buildings or police stations with impunity. Tata originally built its car factory in West Bengal, but union agitation prevented it from opening and resulted in the factory moving to Gujarat.

Electricity in most areas is insufficient, as illustrated by recent blackouts. On 29 July 2012 India's northern grid network collapsed and plunged 300 million people into darkness. India's industrial output is restricted, as companies often have to shut down for a few hours during the day due to lack of power. Many factories have their own diesel generators. Most of India's electricity is produced from coal and about 22% from hydro-electricity. However, there is a shortage of coal production in India and hydro-electricity can be severely affected by a poor monsoon.

Roads in India are slow, congested and often in a bad state of repair. This makes transportation by road slow and expensive.

India has built the 'Golden Quadilateral' (Figure 5), a four-lane highway connecting Delhi, Mumbai, Bangalore, Chennai and Calcutta, but more needs to be built. The 150 km of this road from Mumbai (pop 18 million) to Pune (5 million) climbs for 20 km up the Western Ghats. Rockfalls on this section of road mean that there are frequent lane closures, causing long delays.

Water supply is another problem that is looming large on the horizon. The lack of investment in the water supply means that many people face shortages towards the end of the dry season when reservoirs and rivers are low. Many places extract ground water but this is unsustainable and the water table is falling rapidly.

There are worries that water shortages will lead to a fall in food production and to social unrest.

Then there can be tax problems. As in many countries, the tax regulations have loopholes that companies try and exploit. Equally, a company may do something that it believes it quite legal, only to end up with a sizable tax bill, as recently happened to Vodafone following its

Figure 5: India's 'Golden Quadrilateral' road

(sourced from Wiki)

$11.2 billion purchase of 67% of Hutchinson-Essar, a company based in the Netherlands and the Cayman Islands. The tax authority in India demanded that $2.5 billion in tax should be paid. However, after 5 years of court cases, in 2012, India's Supreme Court found in favour of Vodafone.

Conclusion

Most of the economic growth and investment in India is concentrated in urban areas, which have become congested and polluted. China invests seven times as much in urban planning and infrastructure as India does. If the Indian economy is to grow efficiently, more investment in these essentials is needed.

Focus Questions

1. Describe and account for the growth in India's automotive industry.

2. To what extent were changes in government policy responsible for the growth of industry in India?

3. Evaluate the development of SEZs as a means of increasing industrial output.

4. Assess the issues facing companies thinking of investing in India.