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With Triple the Wages, China Still Attracts Indian Producers

by Unni Krishnan
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Glass blowers work molten glass in the blowing area of a Pooja Group of Glass Industries factory in Ferozabad, Uttar Pradesh, India, on Feb. 21, 2015. As part of "Make in India," Modi plans to raise the share of manufacturing in the economy to 25 percent by 2022 from 18 percent now. Photographer: Udit Kulshrestha/Bloomberg

(Bloomberg) -- Prime Minister Narendra Modi wants India's companies to embrace their homeland as a manufacturing base. It's a hard sell for businesspeople like Himanshu Baid.

Baid can still make more money in China even though he pays his workers three times more than at his two factories in India, which supply the domestic market. Congestion at ports, a lack of skilled workers and a shortage of raw materials offset any advantage India has with cheaper labor costs, he says.

"It was a risk for a small company like ours, but it worked as China is an easy place for business," Baid, the head of Poly Medicure Ltd., a New Delhi-based company with annual sales of $53 million, said in an interview at his wood paneled office in the nation's capital. "It's a struggle in India."

Modi has sought to reverse those perceptions since taking office last May with a policy initiative to entice companies called "Make in India". Industry groups are now looking for him to fill in the details when his government presents its budget on Saturday.

"What India must demonstrate is a convincing vision and the means to implement it," Jean-Pierre Lehmann, a professor of international political economy at the IMD, a business school in Lausanne, Switzerland, said in an e-mail. “There is a lot to be done that will require profound transformations in policies, structures and attitudes.”

As part of “Make in India,” Modi plans to raise the share of manufacturing in the economy to 25 percent by 2022 from 18 percent now. Doing so will create 100 million jobs, the government estimates, enough to absorb the world’s largest working-age population.

Trailing China

In about seven decades since India achieved independence from the British in 1947, the share of industry in the economy has remained largely unchanged. Services replaced farming as the dominant growth driver, and now accounts for 65 percent of the economy, according to the finance ministry.

While China emerged as the world’s factory with manufacturing accounting for about a third of its economy, India suffered from a stifling bureaucracy that required permits to produce goods until 1991. English-language skills and an edge in information technology has allowed India to win back office business from a range of multinationals since then.

“The goal should be to strengthen Indian manufacturing so it can stand on its own and compete effectively in domestic and world markets,” said Eswar Prasad, a former chief of the International Monetary Fund’s China division and now an economics professor at Cornell University. “Relative to China, India has a cheaper and younger workforce that could boost the country’s attractiveness to foreign investors.”

‘Archaic Rules’

Modi has already taken some steps to make it easier for companies to do business, including moving the application process for industrial licenses online. Investors planning to set up a factory can leave queries on the Make in India website and they will be answered in 72 hours.

Modi has also prioritized military equipment made or assembled in India to cut reliance on foreign purchases. India, the world’s large arms importer, has approved 251 proposals from 150 companies to make defense hardware locally, Junior Defense Minister Rao Inderjit Singh told lawmakers on Tuesday.

Still, much more needs to be done. India fell to 142 of 189 countries on the World Bank’s latest Ease of Doing Business Index, falling behind Ethiopia, Yemen and Sierra Leone. China improved several notches to 90th on the index.

Young Workforce

It takes 30 days and 12 clearances to get a company registered in the industrial hub of Noida, near Delhi, according to the World Bank. That is three times longer than it takes on average in the 34-member grouping of Organisation for Economic Co-operation and Development.

“Ancient and archaic rules have to be all removed,” said Sumit Majumdar, a professor at University of

Texas at Dallas. “India has to realize she is starting the race to prosperity last, but needs to come first.”

Modi’s administration must clean up a maze of tax rates in which components in some sectors are higher than the finished product. Business groups are also calling for the end of the minimum alternate tax, which offsets any financial incentives exporters get from investing in special economic zones.

Attracting investment is key for Modi to provide jobs for the 64 million new entrants in the five years ending 2016. By 2021, almost two-thirds of its 1.2 billion people will be of working age, according to the finance ministry.

As India becomes more productive, it will be in a better position to compete with China. By 2020, India will have an average age of 29 years old, eight years younger than China.

‘I’m Tempted’

Manufacturing share in output surges when a country’s average income in terms of purchasing price parity is about $5,000 and peaks at $10,000, according to a study by McKinsey and Co. India’s per capita income is $5,850, while in China it is 11,850, according to the World Bank.

For Poly Medicure’s Baid, China’s advantages include the scale of its economy, superior infrastructure, proximity to component suppliers and established logistics networks.

Over the past month, he’s had to pay extra to fulfill orders from European clients due to a backlog of more than 30 days at ports in western India.

“Things are improving and I’m tempted, but not sure if I’m willing to bet my money yet,” Baid said about investing more in India. “For now, China works.”

To contact the reporter on this story: Unni Krishnan in New Delhi at ukrishnan2@bloomberg.net

To contact the editors responsible for this story: Daniel Ten Kate at dtenkate@bloomberg.net Jeanette Rodrigues