THIRTY SIXTH CONVOCATION ADDRESS

India and Globalisation

Address by

Bimal Jalan

Governor, Reserve Bank of India

STATISTICAL INDIAN INSTITUTE

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UNITY IN DIVERSITY

Indian Statistical Institute

Kolkata

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This is a truly momentous occasion in the life of this Institute, its students, its teachers, and its friends. Let me begin by conveying my heartiest congratulations to the students who are receiving their degrees today. For all of them, it is a culmination of years of hard work, and a recognition of their high academic merit.

All the teachers of this great Institute, who have put in so much time and effort to make this day possible, also deserve our gratitude.

I would like to specially welcome the parents of the students, who are present at this Convocation. Without some sacrifice and a good deal of support, successful completion of higher studies by young men and women, who are here today, would not have been possible.

I am personally grateful to the President of the Indian Statistical Institute, Prof. M.G.K.Menon and Director, Prof. K.B.Sinha, for inviting me to be a part of this occasion. A scientist, a scholar and a public figure, Prof. Menon has led this Institute with great distinction. He has been a source of inspiration for all those connected with ISI and its teachers and students. It is a particular privilege and honour to deliver this address in his esteemed presence.

On this important occasion, I would also like to pay homage to the memory of Professor P.C.Mahalanobis, founder of the ISI and the builder of the modern statistical system in India. His technical contribution to the development of statistics as a science are fundamental and well known all over the world. What was even more remarkable, in a developing country context, was his desire to use statistical methods including sample surveys to understand and solve the problems of an underdeveloped economy, including low productivity agriculture.

The high quality, the depth, and the breadth of research and teaching in statistics and other inter-related subjects at this Institute are tributes to the vision of Prof. Mahalanobis and his confidence in our country's future.

While I am thankful for being here on this occasion, I am also a little daunted by the task of having to say something useful which may be of interest to this varied audience from so many different walks of life. After some reflection, I have chosen to speak to you on "India and Globalisation", or how we in India should look at the process of so-called "globalisation" that the world has been passing through in recent years. I had an occasion to speak on this subject at Mumbai University Convocation a couple of weeks ago. This is a matter of considerable contemporary debate, and I thought some reflection on this may also be of interest here in Kolkata.

There is a debate not only in India but all over the globe about the pros and cons of "globalisation". There is hardly any important global meeting which does not witness vigorous protest marches or picketing by the opponents of the globalisation process.

Equally, on the opposite side, there are those who regard it as panacea for all the world's problems and key to unmixed prosperity and well being for all the countries and all the people. If you take a poll in any assembly, including I am sure this one, you will find some are strongly for and some are strongly against globalisation.

To my mind, neither view – for or against – is correct. The only rational view is to accept it as an emerging and powerful global reality which has a momentum of its own. Our job as an independent nation / state is to ensure that we maximise the advantage for our country and minimise the risks. It has both pluses and minuses like any other major global economic change – say, the industrial revolution of the 18th century. Some countries gained, some lost – partly because of the then prevailing political circumstances. India, for example, lost because of colonialism and fragmented nature of our polity. U.K., Europe, U.S. – and later Japan prospered. Same is the case with globalisation. One big difference, however, is that unlike the olden days, today our destiny is in our own hands.

Before we look at our opportunities and challenges from globalisation, it is good to be certain of facts – where exactly India is in terms of globalisation. If we look at some of our own debate, it would seem as if we were already well on the way to globalisation, which was shaking up our economy. A most common measure of globalisation is openness to trade and a country's participation in trade. By this measure, the extent of India's globalisation is insignificant – it is one of the lowest in the world. India's share in world trade is a meagre 0.7 per cent or so. If a map of the world were drawn on the scale of a country's participation in trade, India with a population of more than 1,000 million will occupy a smaller area than Singapore with a population of only 3 million. You would need a magnifying glass to locate India on that map!

A second commonly used measure of globalisation is a country's participation in international capital flows, particularly Foreign Direct Investment (FDI). As you know, annual flow of FDI across the globe is more than $ 1 trillion, *i.e.*, $ 1,000 billion. Annual FDI inflows into India is $ 3 – 4 billion only or 0.3 – 0.4 per cent of the total – that is all. Same is true of Foreign Institutional Investment (FII).

Therefore, the first point that I would like to emphasise is that despite all the talk, we are nowhere even close to being globalised in terms of any commonly used indicator of globalisation. In fact, we are still one of the least globalised among major countries – however we look at it.

An equally important point is that whether the so-called globalisation is considered to be good or bad for a country depends crucially on the sense in which the word is used. The word may be used in a purely descriptive sense to describe a "shrinkage" of distance among nation states due to technological changes in transport and communication and closer integration of product and financial markets across the world.

Another sense in which the word may be used is the effect of such changes on different countries or groups of countries, such as, developed and developing. In yet another sense, the word may also represent a "globalisation of ideas or ideology" and may be used as a synonym for triumph of capitalism or dominance of unfettered markets.

In discussing the issue of globalisation in the Indian context, I propose to confine myself largely to the factual and descriptive sense in which the word is used, *i.e.* the technological changes, and associated policy changes, that have brought the world economies closer and made them more integrated with each other.

In this particular sense, I believe that the changes that have occurred in the patterns of trade and capital flows in recent years are to India's advantage – although, unfortunately, so far we have not made much use of it. Today, in terms of the potential benefits of globalisation, India is in a very different position than would have been the case 50 or even 20 years ago.

This is because the sources of what economists call "comparative advantage" have changed dramatically in India's favour in the 1990s because of the technological revolution. In the old days, comparative advantage was largely determined by "factor endowments", *i.e.* land, labour and capital. Geographical location and early starts in industry also conferred greater advantages.

Thus, at one time, a country's trade pattern, was determined by its natural resources and the productivity of its land. Leaving aside political and institutional factors, a country's level of income was also largely determined by the global demand for its natural resources and its relative efficiency in exploiting them. The importance of land as a source of comparative advantage, however, changed dramatically after the industrial revolution. Today, it is almost insignificant. Thus, except for the United States, countries accounting for a predominant share of the world GDP have a relatively small share of global land area.

After the industrial revolution, the availability of "capital" or investible resources became the most dominant source of comparative advantage. At this Institute, established by the great Prof. P.C.Mahalonobis, I hardly need to elaborate on the importance that was attached to domestic capital accumulation in early development economics. In fact, scarcity of capital and low domestic savings were considered to be, and rightly so, as principal causes of a country's underdevelopment.

Today, availability of capital and productivity are still crucial in determining a country's growth rate. However, there has been a dramatic change in the global mobility of capital, and national boundaries are no longer important determinants of sources and uses of capital. A dramatic illustration of this is the fact that the most developed country in the world, which enjoyed unprecedented growth during the 1990s, is actually a capital-importing country, *i.e.* the United States. Similarly, the fastest growing developing country, *i.e.* China, is one of the largest recipients of capital from outside.

Similary, labour is no longer an important element in cost of production and in determining a country's comparative advantage. In most manufacturing industries in the world, it is no higher than 1/8th of total costs. In India, it may be somewhat higher because of our domestic laws, but the important fact to note is that India no longer needs to specialise only in the production of labour-intensive plantation crops or primary commodities.

A related development which is linked to the above changes, is the "Services Revolution". The focus of attention in conventional economics, was on production of goods – manufactured products and agricultural commodities. It was, of course, recognised that the services sector (which includes transport, communication, trade, banking, construction and public administration, *etc.*) was an important source of income and employment in most economies. However, overall, the growth of services was perceived at best as a by-product of developments in the primary and secondary sectors, and at worst as a drag on the prospects for long-term economic growth.

In the last few years, there has been a phenomenal change in the conventional view of services and their role in the economy. This change has been facilitated by unprecedented and unforeseen advances in computer and communication technology. As a result, the development of certain services is now regarded as one of the preconditions of economic growth, and not as one of its consequences.

The boundary between goods and services is also disappearing. Many industrial products are not only manufactured, but they are also researched, designed, marketed, advertised, distributed, leased and serviced.

An important aspect of the "services revolution" is that geography and levels of industrialisation are no longer the primary determinants of the location of facilities for production of services. As a result, the traditional role of developing countries is also changing – from mere recipients to important providers of long-distance and high value services.

From India's point of view, these developments provide opportunities for substantial growth. For example:

- The fastest growing segment of services is the rapid expansion of knowledge-based services, such as, professional and technical services. India has a tremendous advantage in the supply of such services because of a developed structure of technological and educational institutions, such as this one, and lower labour costs.
- Unlike most other prices, world prices of transport and communication services have fallen dramatically. By 1960, sea transport costs were less than a third of their 1920 level, and they have continued to fall. The cost of a telephone

call fell more than ten-fold between 1970 and 2000. Moreover, the cost of communication is also becoming independent of distance. The most dramatic example in this area is, of course, provided by the "Internet". India's geographical distance from several important industrial markets (for instance, North America) is no longer an important element in the cost structure of skill-based services.

- It is now feasible to "unbundle" production of different types of goods and services. India does not necessarily have to be a low-cost producer of certain types of goods (*e.g.*, computers or discs) before it can become an efficient supplier of services embodied in them (*e.g.*, software or music).

At the same time, it must be recognised that the "death of distance" and the growing integration of global product, services and financial markets in recent years have also presented new challenges for management of the national economy – not only in India but all over the world. The trend towards integration of markets, particularly financial markets, is by no means an unmixed blessing. Unlike the old days, a heavy price may have to be paid by national economies for somnolence, sloth and non-conformity to generally accepted international norms and standards of macro-economic management, disclosure, transparency and financial accountability.

Another consequence of recent global trends is the greater vulnerability of national economies to developments outside their own borders. A crisis in any one or a group of countries, can be transmitted to other countries – including countries which may not have any strong economic linkages with crisis-affected countries. Thus, the 'nineties have been marked by a large number of currency crises (for example, in Mexico, Russia, East Asia and Brazil – and currently Argentina and Turkey); substantial swings in exchange rates (including the exchange rate of three leading currencies – the dollar, the Euro and the Yen); and run ups in asset prices followed by sharp collapse (for example in Japan and East Asia earlier and the United States last year). While the crises initially occur in one or two specific countries, their adverse effects are felt across the world.

While we must be careful, on the whole, in my view, – the death of distance, the services revolution, and the mobility of capital – which characterise globalisation – present unprecedented opportunities for India. The primary source of comparative advantages today are : skills and ability to adapt and change. And, India has the advantage – of skills, of entrepreneurship and of managerial competence in taking advantage of these changes.

If what I have said is correct, then, why are we not jumping with joy and optimism? Why are we so "unglobalised" in terms of our share in trade, investment or communication?

Transition from a closed to a vibrant, open and a more globally dominant economy will certainly take time and will not be painless.

As of now, we also have much greater tolerance for waste, non-work and survival of the inefficient, and the self-seeking than other fast growing countries. Somehow to make this transition – from a less productive and less challenging economy to a more work-oriented and competitive economy – is the real challenge of globalisation.

If we continue in our old ways, I see real social problems and inequalities emerging in our society. We will have islands of prosperity and excellence – IT, beauty parades and media entertainment amidst growing disparity, rising unemployment and immiserisation. And as has happened in several countries in the 1990s, including Turkey and Argentina - just now, those who are with us today will be the first to leave.

The principal lesson of recent economic and technological developments, and growing tensions and inequalities within and across countries, is that our fate is in our hands. Our public policies have to respond to our own requirements rather than to any fixed global ideology or a pre-determined and internationally prescribed model of economic progress. In my view, this is the real lesson of the 1990s.

My fervent hope is that as you – the best and the brightest of our country – go out and face a "globalising" world, you will keep India's interest, its integrity, its indivisibility and its future potential close to your hearts and your minds. I have no doubt that, with your help, India of 2025 will be a very different place, and a much more dominant force in the world economy, than was the case twenty five years ago or at the beginning of the new millennium.

Thank you.