

Is India the World's Next Great Economic Power?

by Bhaskar Chakravorti and Gaurav Dalmia

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Summary. Is India's economic rise inevitable? There's good reason to think that this latest round of Indo-optimism might be different than previous iterations, but the country still has major challenges to address to make good on this promise. In terms of drivers, demand... [more](#)

In 2002, India's government launched a ubiquitous international tourism campaign known as "Incredible India." Were it to launch a similar campaign today, it might as well be called "Inevitable India." Not just enthusiasts within the country, but a chorus of global analysts, have declared India as the next great economic power: Goldman Sachs has predicted it will become the world's second-largest economy by 2075, and the FT's Martin Wolf suggests that by 2050, its purchasing power will be 30% larger than that of the U.S.

We have been through similar surges of Indo-optimism before. But the on-the-ground reality has continued to frustrate even the most ardent of India's champions. From bold predictions that it would overtake China (an economy still five times larger than India's), to McKinsey's 2007 "bird of gold" promise of the Indian consumer that never quite panned out, to deregulation followed by policy reversals and crises of confidence in doing business with India, to devastating periods through the pandemic, the country's promised inevitable rise has remained elusive. What's different now?

There are several positive trends converging, from different sides of the Indian business ecosystem: demand, supply, and the system-wide facilitating factors; in combination, they can transcend economic cycles, macro shocks, and policy reversals. Some are new, and the older ones are reaching critical mass and they can finally reinforce each other to create a growth flywheel. But as with all flywheels, it is important to remain vigilant about rattling noises and burning smells, and in India's case, these exist in abundance. It's essential for both business and government leaders to pay attention and act before the flywheel breaks.

Demand

Three forces are converging on the demand side to fuel India's economic growth.

Consumer boom

The starting point for any discussion of India's promise is, invariably, the promise of the Indian consumer. With 1.4 billion people and myriad unmet needs, India's growth is driven mainly by domestic consumption and investments. Real wages are expected to grow at 4.6%, whereas disposable income will continue to grow in excess of 15%. Industries that are mature in the West are fast-growing in India: Private health insurance, for example, has almost tripled between 2015 and 2021, while consumer durables were expected to grow between 15% and 18% this year.

Context-appropriate innovation

International companies have struggled to grasp what constitutes India's "middle class" and craft the appropriate value propositions. While some analysts argue that one out of every three Indians is "middle class," only 66 million are genuinely "middle income" by global standards, while a whopping 1.16 billion are low income. However, many in this second group constitute a vast aspirational consuming class.

This has many implications. For one, competing in India means selling at much lower price points, which in turn requires reconfiguring activities, production, and supply chains in ways that

are hard for competitors to mimic. India's best-selling car is Wagon R, priced at \$7,000 and made by Japan's Suzuki, a company whose 41% market share in India is an outlier in the auto industry globally.

That said, as Netflix discovered through its stumbles in the country, it takes more than low prices to win in India. Localizing the content, working in multiple Indian languages, and leveraging synergies across products that Indian consumers want, as Amazon or Disney can do, is essential. In a very different sector, McDonald's, has incorporated vegetarian options, Indian snacks, and menus for multi-generational families, building a contextualized value proposition.

Those that can crack the code of the Indian consumer are handsomely rewarded: Many McDonald's franchisees in India are billionaires. The home appliances manufacturer Havells introduced a product line with "India-friendly" offerings such as water purifiers and compressor-less air coolers, relevant to both the Indian consumers' needs and affordability. Since its listing 30 years ago, Havells' profits have grown 826 times, and its market cap has jumped 5,800 times.

Green transition

A burgeoning new source of demand growth comes from India's urgent need for a green transition. The scale of its economic potential means that its energy demand will be enormous. As the third-largest energy-consuming nation, it is already 4th in the world in renewable energy installed capacity. The country has set ambitious targets: installing 500 gigawatts of renewable energy capacity, producing 5 million tons of green hydrogen annually, cutting emissions by 45%, along with a billion tons of CO₂ — all by 2030. A 2021 report by the World Economic Forum projects 50 million net new "green economy" jobs in India — which means more consumers — and \$15 trillion in economic opportunity by 2070, with \$1 trillion by 2030.

Supply

There are several positive forces converging on the supply side as well.

Demographic dividend

One part of the supply-side story is old news: By 2030, India's working-age population is expected to be 1.04 billion with a dependency ratio to be the lowest in its history at 31.2%, contributing just under a quarter of the incremental global workforce. The working-age population bulge is expected to last till 2055.

The "Asian Miracle" was built on harnessing this trend: Japan entered this sweet spot in 1964, South Korea in 1967 and China in 1994. Additionally, India also has the largest pool of English-speaking STEM graduates in the world.

Access to finance

India's financial markets are in a better state than ever before. With the China opportunities cooling, investors need alternatives, and India comes closest. The MSCI India Index is up 12% this year, compared to 2% for the MSCI Emerging Markets Index.

Bank balance sheets are stronger and credit markets are functioning well. It's telling that many Indian banks are valued higher than U.S. peers. HDFC Bank — which merged with its parent, mortgage lender HDFC — has a market capitalization of \$171 billion, making it the 4th largest financial company in the world. Even before the merger, the 29-year-old upstart was more valuable than the 154-year-old Goldman Sachs.

The change can be seen even in the traditionally underfinanced informal sector, comprising over 86% of India's workforce. Avendus, a leading Indian investment bank, calculated that Indian small-and-medium-enterprise sector's total demand for debt is \$1.5 trillion. Of this, \$725 billion is unaddressable because of lack of collateral, and formal credit is only available to the tune of \$289 billion. This is motivating lenders to deepen their offerings. New-to-credit customers are at 34% up from 9% of customers for small business lenders in 2017. Loans by small business lenders have jumped 43% annually in the past two years.

Infrastructure upgrades, both physical and digital

A critical barrier that sticks in the mind of anyone who has visited India is its lagging infrastructure. Historically, investing in handouts may have been more politically expedient, but the current administration's popularity gives it greater leeway to invest in infrastructure. Capital expenditure as a percentage of total government expenditure has increased from 11% in 2010 to a projected 22% this year. Infrastructure expenditure this year will see a 33% hike to \$122 billion.

The outcomes have been striking. India has been adding 10,000 km of highway annually. Since 2014, the number of Indian airports has doubled and an upgraded train system will have new high efficiency "freight corridors" connecting the economic centers of India.

In addition, one of most distinctive changes has been in the digital infrastructure. With 881.25 million internet subscribers, India has the second-highest internet-enabled population in the world behind China's 1.05 billion. Riding on this access, there is a digital public infrastructure — a model being studied by other countries — that combines a population-scale unique identity system, a payments interface that makes digital payments seamless, and a data management system, whereby citizens can access essential documents online, such as tax documents, vaccination certificates, etc. All of this helps make public services and credit more easily accessible to a wider swath of the population.

As an indicator of the resulting change, India has topped the list for digital payments beating China by a huge margin. Interestingly, India's payments are more than the digital payments made in the next four leading countries combined.

Facilitators

On top of these forces in motion, there are several system-wide facilitators in the mix.

Domestic policy reforms

Many regulatory and policy reforms have been put in place, from implementation of the 2016 Insolvency and Bankruptcy Code to the elimination of more than 39,000 regulations to foster ease of doing business.

Many other reforms, such as construction permits and power connections, are the domain of state governments and there is a drive towards change at these levels as well. State governments are competing by helping speed up the process of setting up businesses, providing incentives for investment and even attracting clusters of competing companies, which enables more business-friendly environments in more regions across the country.

Geopolitical sweet spot

Another transformation is a more distinctive geopolitical positioning for India, triggered, most significantly, by the growing rift between China and Western economies, particularly the U.S. This is translating into new business opportunities for India, most visibly — the manufacturing of Apple’s smartphones. With a goal of producing 20 million iPhones a year, 50,000 new jobs will be created by one such project alone. In addition, when it comes to military-grade technology used for space launches, there is greater confidence in India as a host than China and there is already a thriving ecosystem in place. India has hosted 111 international space launches since 2020, and successfully landed a rover on the moon in late August.

To consider another prominent example, chipmaker, Micron Technology, announced plans to build a new assembly and test facility, as part of moves to diversify beyond China. In fact, the new president of the World Bank has suggested that there is a narrow window for India to “cash in” on the growing trend behind companies seeking to diversify their supply chain and manufacturing beyond a massive dependence on China.

Diaspora dividend

It is interesting to note that both the CEO of Micron Technology and the World Bank chief are Indian-born, which brings us to the third key facilitator: the Indian diaspora, now the world's largest and influential in ways that it had never been before. In the business world alone it is telling that 25 of S&P 500 company CEOs are Indian-born. Beyond this, senior management ranks of numerous companies are populated by Indians. It's the leading country of origin for immigrant founders of U.S. unicorns. These connections help build global connectivity to Indian business and facilitate India's integration into global value chains.

Barriers

While these factors reinforce each other, many barriers remain – and they could cause the multiplier effect to stall. Consider three major bumps in the road and the actions needed.

Unbalanced growth

Despite impressive growth numbers at the national level, the economic benefits have been highly unequal. The top 10% of Indians hold 77% of the national wealth. Almost 2 people every second are pushed into poverty because of health care costs alone. India's population density – amongst the highest in the world – exacerbates the zero-sum nature of resource allocation and environmental stresses. Regional imbalances – southern and western India growing 12% faster than northern and eastern India – will magnify over time. Superimpose on this linguistic fault-lines, new inter-regional tensions could surface. Handling these will require deft management of the political economy.

Other imbalances are growing because of divisive politics. An increasingly assertive form of Hindutva ideology is overshadowing core issues such as job-creation, enhancing productivity and shared economic benefits. The root cause of this problem was a belief in large sections of society that what started as affirmative action projects in a newly independent India should have had sunset clauses leading to discontent over minority appeasement by political leaders. The

pendulum has now swung in the other direction creating new challenges of exclusion and identity politics. For many India-watchers it hasn't helped that India has declined in its position on the World Press Freedom Index. Consequently, potentially, bottled-up sentiments in large sections of the disaffected and minority segments of the population can explode, triggering a downward spiral. Such developments can undermine objectives of shared prosperity. For international investors and trade partners, this can add a risk premium of majoritarianism in a country with as much religious, linguistic and socio-cultural diversity as India. More significantly, these developments exhaust political capital, which can otherwise be leveraged for social and economic transformation.

There are at least two solutions to these challenges. One is of political parties moving away from identity politics to inclusive growth and job-creation as the most reliable means of winning over the widest swath of the country's vast population. Two, India sees a constant flow of state-level elections, which distorts public dialogue by skewing it away from longer-term economic growth-oriented perspectives. Streamlining and bunching elections will give breathing space to public discourse and push political leadership and voters toward longer-term horizons.

Unrealized demographic potential

Less than half of urban workers have full-time jobs, while far too much of India's employment is in under-productive informal sectors. Education, skill-building, and health care are grossly inadequate. The India Skills Report 2023 found only half of young Indians are employable. Even the "crown jewels" technology services sector is vulnerable; demand for outsourcing is falling and the labor-cost arbitrage model will be disrupted by secular shifts towards cloud computing and AI for coding and routine functions. Alarming, India's female labor participation rate has been in a steady decline, having dropped from 32% in 2005 to 19% in 2021.

Emulating, say, Vietnam, public and private investment in upskilling must be prioritized, which could add \$570 billion to the Indian economy. A major handicap has been manufacturing — a key jobs

creator in comparable economies — which has plateaued at 13.3% of GDP. The current infrastructure thrust, policy reforms, geopolitical drivers and capital influx could help unlock Indian manufacturing, but the barriers discussed here must be removed.

In emerging sectors, the surge of potential in AI could be an opportunity for India to take leadership in a cutting-edge area, given the emergent AI talent hubs in the country that can be massively expanded, paired with the vast pools of data that accumulate in India. Cultural and organizational changes are needed to create on-ramps for women in the workforce and retain them. Such projects have long gestation periods, so a focused and disciplined long-term plan is required.

Unrealized ease-of-business and innovation potential

Doing business in India has improved, but many challenges remain. Land acquisition can stall construction projects and the courts are slow-moving institutions. Land records may be non-existing or outdated and environmental clearances have created additional barriers. On top of this, contract enforcement remains challenging. According to an index created by The Economist, India ranks 10th in the prevalence of crony capitalism, in spite of the large-scale liberalization of the past three decades. A legacy of protectionism still persists.

India's state capacity needs change. Contrary to popular perception, the Indian state is not big and bungling, but weak and waning. Institutions — from regulators to civic bodies to the judiciary — often juggle conflicting demands and are playing catch-up to market and social realities. Many important decisions are made with a crisis as a frame of reference and India's story of victories is often of individual heroism amidst institutional failure. Making India's state machinery cutting-edge may well be India's pivotal project.

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In sum, while barriers remain, the positive forces can, indeed, create a domino effect: "Inevitable India" is within reach. India's greatest challenge will be to make its inevitability tangible and believable to

the many constituencies that wish to see India succeed. To get from “Incredible India” — aimed at tourists — to now bring the global economy to its door, India next campaign ought to be “Credible India.”

Bhaskar Chakravorti is the Dean of Global Business at The Fletcher School at Tufts University and founding Executive Director of Fletcher’s Institute for Business in the Global Context. He is the author of *The Slow Pace of Fast Change*.

Gaurav Dalmia is the Chairman of Dalmia Group Holdings, an Indian holding company for business and financial assets.

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