Suddenly vulnerable

THE speed with which clouds of economic gloom and even despair have gathered over the global economy has been startling everywhere. But the change has been especially sudden in the world's two most populous countries: China and India. Until quite recently, the world's fastest-growing big economies both felt themselves largely immune from the contagion afflicting the rich world. Optimists even hoped that these huge emerging markets might provide the engines that could pull the world out of recession. Now some fear the reverse: that the global downturn is going to drag China and India down with it, bringing massive unemployment to two countries that are, for all their success, still poor—India is home to some two-fifths of the world's malnourished children.

The pessimism may be overdone. These are still the most dynamic parts of the world economy. But both countries face daunting economic and political difficulties. In India's case, its newly positive self-image has suffered a double blow: from the economic buffeting, and from the bullets of the terrorists who attacked Mumbai last month. As our special report makes clear, India's recent self-confidence had two roots. One was a sustained spurt in economic growth to a five-year annual average of 8.8%. The other was the concomitant rise in India's global stature and influence. No longer, its politicians gloated, was India "hyphenated" with Pakistan as one half of a potential nuclear maelstrom. Rather it had become part of "Chindia"—a fast-growing success story.

The Mumbai attacks, blamed on terrorist groups based in Pakistan and bringing calls for punitive military action, have revived fears of regional conflict. A hyphen has reappeared over India's western border, just as the scale of the economic setback hitting India is becoming apparent. Exports in October fell by 12% compared with the same month last year; hundreds of small textile firms have gone out of business; even some of the stars of Indian manufacturing of recent years, in the automotive industry, have suspended production. The central bank has revised its estimate of economic growth this year downwards, to 7.5-8%, which is still optimistic. Next year the rate may well fall to 5.5% or less, the lowest since 2002.

Still faster after all these years

If China's growth rate were to fall to that level, it would be regarded as a disaster at home and abroad. The country is this month celebrating the 30th anniversary of the event seen as marking the launch of its policies of "reform and opening", since when its economy has grown at an annual average of 9.8%. The event was a meeting of the Communist Party's Central Committee at which Deng Xiaoping gained control. Tentatively at first but with greater radicalism in the 1990s, the party dismantled most of the monolithic Maoist edifice—parcelling out collective farmland, sucking in vast amounts of foreign investment and allowing private enterprise to thrive. The anniversary may be a bogus milestone, but it is easy to understand why the party should want to trumpet the achievements of the past 30 years (see article). They have witnessed the most astonishing economic transformation in human history. In a

country that is home to one-fifth of humanity some 200m people have been lifted out of poverty.

Yet in China, too, the present downturn is jangling nerves. The country is a statistical haze, but the trade figures for last month—with exports 2% lower than in November 2007 and imports 18% down—were shocking. Power generation, generally a reliable number, fell by 7%. Even though the World Bank and other forecasters still expect China's GDP to grow by 7.5% in 2009, that is below the 8% level regarded, almost superstitiously, as essential if huge social dislocation is to be avoided. Just this month a senior party researcher gave warning of what he called, in party-speak, "a reactive situation of mass-scale social turmoil". Indeed, demonstrations and protests, always common in China, are proliferating, as laid-off factory-workers join dispossessed farmers, environmental campaigners and victims of police harassment in taking to the streets.

The gap between mouth and trouser

One worry is that China's rulers will try to push the yuan down to help exporters. That would be a terrible idea, not least because the government has the resources to ease the pain in less dangerous ways: it is running a budget surplus and has little debt. Last month it announced a huge 4 trillion yuan (nearly $600 billion) fiscal-stimulus package. Some who have crunched the numbers argue that this was all mouth and no trousers—much of it made up by old budget commitments, double-counting and empty promises. It was thus mainly propaganda, to convince China's own people and the outside world that the government was serious about stimulating demand at home. That may yet prove to be unfair: what matters is when infrastructure money is spent, not when it is announced. Yet there is little sign that the regime is ready to take radical steps in the two areas that would do most to persuade the rural majority to spend its money rather than hoard it: giving farmers better rights over their land; and providing a decent social safety-net, especially in health care.

Still, China does at least have trousers, with deep pockets. India, in contrast, is not seen as a big potential part of the answer to the world's economic problems. Not only is its economy far smaller; its government's finances are also a mess. Its budget deficit—some 8% of GDP—inhibits it from offering a bigger stimulus that might mitigate the downturn (see article). This is alarming. If China reckons it needs 8% annual growth to provide jobs for the 7m or so new members of its workforce each year, how is India to cope? A younger country, its workforce is increasing by about 14m a year—ie, about one-quarter of the world's new workers. And, perversely, its great successes of recent years have been in industries that rely not on vast supplies of cheap labour but on smaller numbers of highly educated engineers—such as its computer-services businesses and capital-intensive manufacturing.

In two respects, however, India has a big advantage over China in coping with an economic slowdown. It has all-too extensive experience in it; and it has a political system that can cope with disgruntlement without suffering existential doubts. India pays an economic price for its democracy. Decision-making is cumbersome. And as in China, unrest and even insurgency are widespread. But the political system has a resilience and flexibility that China's own leaders, it seems, believe they lack. They are worrying about how to cope with protests. India's have their eyes on a looming election.

It used to be a platitude of Western—and Marxist—analysis of China that wrenching economic change would demand political reform. Yet China's economy boomed with little sign of any serious political liberalisation to match the economic free-for-all. The cliché fell into disuse. Indeed, many, even in democratic bastions such as India, began to fall for the Chinese Communist Party's argument that dictatorship was good for growth, whereas Indian democracy was a luxury paid for by the poor, in the indefinite extension of their poverty.

But as China enters a trying year of anniversaries—the 50th of the suppression of an uprising in Tibet; the 20th of the quashing of the Tiananmen Square protests; the 60th of the founding of the People's Republic itself—it may be worth remembering that the winter of 1978-79 saw

not only a party Central Committee plenum but also the "Democracy Wall" movement in Beijing. It was a brief flowering of the freedom of expression, quite remarkable after the xenophobic isolation of the Cultural Revolution. Deng, like Mao Zedong before him, tolerated the dissident movement as long as it served his ends, and then stamped it out. In so doing he thwarted what Wei Jingsheng, the most famous of the wall-writers, had dubbed "the fifth modernisation": democracy. China still needs it.

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