22 May 2025

How globally integrated is India?

Economics
India

Challenging myths, seeking opportunities

- It is in periods of rising integration with the world that India has grown its fastest
- Financial integration has outpaced trade integration, creating a divergence between (high-end) consumption and (household) investment growth
- An opportunity to ramp up trade integration and grow faster is knocking at the door

There is a general sense that India is mostly a domestic demand-driven economy. We disagree. We find that India has grown at its fastest pace in periods of rising global integration with the world. We use the rolling correlation between India and world GDP growth as a measure of global integration, and find that the 2000-2010 decade was a period of falling import tariffs, as well as rising global integration, export share, and GDP growth. In the next decade, 2010-2020, all of this changed. Tariffs were raised, and global integration, export share and GDP growth fell. Encouragingly, the few years following the pandemic reflect a rise in global integration once again, though so far it remains slightly one-sided – more financial integration, less trade integration.

We drill down into GDP sectors and find that consumption is most integrated with world growth (95%), followed by investment (70%), and then exports (35%). Surprising, as one might imagine exports to be most globally aligned. One reason could be that India's global connections are stronger in finance (Indian equity markets have become far more aligned with global equities over the last two decades), and this impacts consumption. But integration remains weaker in trade, which influences export and investment.

Within investment, we find corporate investment is more globally integrated, something we notice across countries. Meanwhile, integration is lower for household investment, which includes both real estate and investment by small firms. **Within consumption**, discretionary consumption is more globally interlinked than essentials. If indeed financial integration has been strong, it is likely to support high-end consumers who tend to be better invested in financial markets. **Within exports**, weak integration has been led by more labour-intensive mid-tech exports (like textiles and toys), which have been sluggish for a decade. Bringing all sectors together, we have two distinct stories unfolding.

Stronger financial integration: Those who have been able to enjoy the gains of financial integration, have seen incomes and discretionary consumption rise. Many of these individuals are associated with large firms (where global capex is globally correlated) or new sectors (e.g. rapidly rising professional services exports). **Weaker trade integration:** On the other hand, lower global integration in mid-tech exports explains weaker growth and incomes, and why individuals in these sectors are largely focused on consumption of essentials, without much surplus for investment. A corollary here would be that steps which raise mid-tech labour-intensive exports can boost India's trade interlinkages, mass consumption, investment, and India's GDP growth. An opportunity to grow exports as supply chains are getting redrawn is knocking at the door.

HSBC

More open, more benefits

There is a general sense that India is a relatively inward-looking economy. After all, agriculture makes up c18% of GDP and depends more on weather patterns than international demand. And India is more domestic demand-driven, compared to some export-led Asian economies.

India grows faster when more globally integrated, e.g. the 2000-2010 period

Having said that, we find that India has grown at its fastest pace in periods of rising global integration with the world. After all, a whole new market opens up when a country is open to it.

We use the rolling correlation between India and world growth as a measure of global integration in this report, and find that the **2000-2010** decade was particularly striking as a period of rising global integration and strong India GDP growth (c8% per year, see exhibit 1). This is the time India was slashing import tariffs and integrating further into global trade, resulting in higher export growth, global export share and GDP growth.

In the next decade, **2010-2020**, India began to raise import tariffs. This period saw a fall in export growth, global export share and GDP growth.

We also note that during the **last few years**, i.e. those following the pandemic, have seen a rise back up in global integration and GDP growth. As we will discuss later in the report, India is making efforts to integrate more with the global economy. But how large and lasting a growth impact, will depend on continued efforts to integrate.

Positive impact of global integration trumps negative impact from higher volatility

One may argue that higher integration exposes a country to global volatility, which may be negative for growth. We look into this carefully through a VAR regression analysis, and find that the positive impact of being more integrated with the world is higher and longer lasting than the negative impact of being exposed to global volatility (see exhibits 4 and 5).

All said, deeper interlinkages with the world have led to higher growth over time, more than offsetting the negative impact of rise in volatility.

How integrated are the various sectors?

Next, we turn our attention to sectoral flavours, because they shed light on the nature of integration with the world and its impact back home.

Consumption seems more globally integrated than investment and exports…

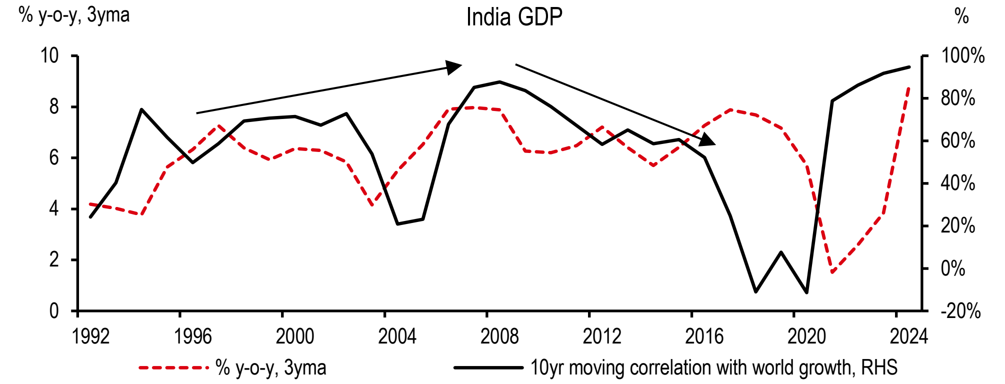
We break down GDP on the expenditure side into consumption, investment and exports, and find some interesting, and even surprising, takeaways.

Comparing investment, consumption and export trends. In the pecking order, consumption is most integrated with world growth, followed by investment and then exports (see exhibit 6). This is rather surprising as one might imagine exports to be most correlated with global growth.

…likely influenced by global financial integration outpacing trade integration

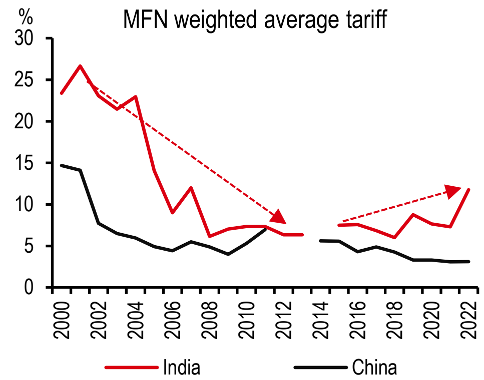
As we explore more closely later, one reason could be that India's linkages with the world are strong on the financial integration side, which impacts consumption, but more limited on the trade side, which influences exports and thereby, investment.

Ex 1: India's global integration over the years



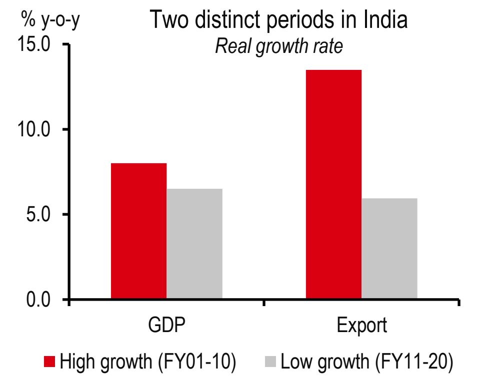
Source: CEIC, HSBC

Ex 2: When India was raising import tariffs…



Source: World Integrated Trade Solution, HSBC

Ex 3: …exports and GDP growth fell



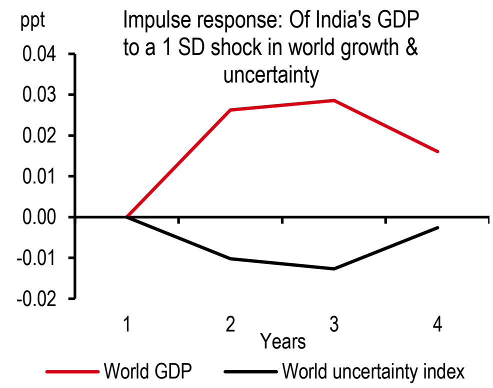
Source: CEIC, Bloomberg, RBI, HSBC

Ex 4: Our global integration model

Dependent variable: India GDP, % y-o-y, 3yma		
Method: Ordinary least squares		
Sample: 2004 to 2024; Frequency: Annual		
Regressors	**Unit**	**Coefficient**
World growth	% y-o-y, 3yma	0.80**
World uncertainty index	Change in index	-0.02**
Dummy	Binary	-1.96**
India GDP lag	% y-o-y, 3yma	0.41**
Constant		1.52*
R-squared		**86%**
Adjusted R-squared		**83%**
Durbin-Watson		**1.9**

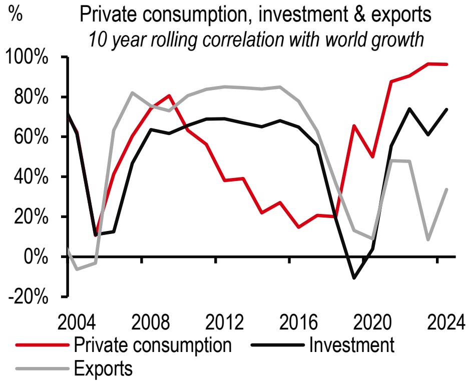
Note: Model includes appropriate lags for the variables. Dummy assigns 1 to the global crisis period i.e. FY8-FY9 and FY20-21 and assigns 0 otherwise. Level of significance **5%, *10%.
Source: CEIC, HSBC calculations

Ex 5: The positive impact of global integration outweighs the negative impact of global volatility



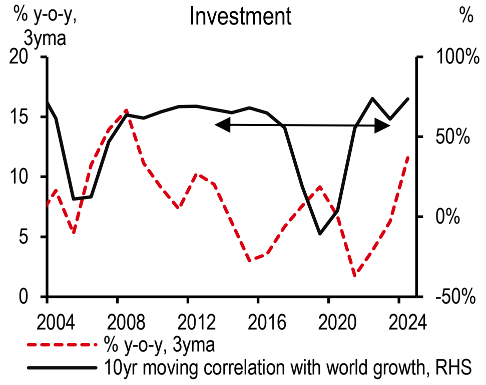
Note: World uncertainty index is the Global Economic Policy Uncertainty (GEPU) index which is weighted average (PPP adjusted) of national EPU index of 21 countries.
Source: CEIC, HSBC calculations

Ex 6: Consumption is most integrated with world growth, followed by investment, and then exports



Source: CEIC, HSBC

Ex 7: India's investment growth has a strong correlation with world growth



Source: CEIC, HSBC

Investment details. India's investment growth has a strong c70% correlation with world growth (see exhibit 7). We break down investment growth into several parts – public, private corporate and household investment. What stands out is the rather divergent trend in corporate versus household investment.

Corporate investment is more globally interlinked than household investment

Corporate investment has a higher correlation (of 75%) with world growth compared to household investment (of 40%). The global interlinkages of corporate investment did not really fall in the 2010-2020 period (barring the pandemic years, see exhibit 8).

This is not surprising. We find that corporate capex globally moves in unison, driven by common factors (for instance, risk sentiment impacting FDI flows).

On the other hand, household investment has a smaller correlation (of 40%) with world growth (see exhibit 9). It is important to note here that household investment in India includes not just real estate and housing, but also investment by small firms.

Within consumption, discretionary is more globally integrated than essentials

Consumption. Consumption has an even higher correlation with world growth than investment. It fell in the 2010-2020 period, but has risen since. In fact, the correlation has risen to 100%, which is above previous highs.

We break down private consumption into two parts – discretionary and essentials (see exhibits 10 and 11)[1]. Between these, discretionary consumption has a much higher correlation with world growth (of almost 100%), while essentials have a lower correlation (of 70%).

After all high income earners (and high-end consumers) are more invested in financial markets

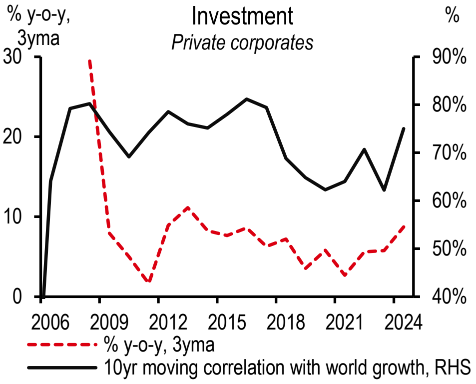
This is understandable. If indeed financial integration has been strong (as we mention above and explore further later in the report), it is likely to have impacted incomes at the top of the pyramid. High-end consumers, who are typically high income earners, tend to be better integrated with (or invested in) financial markets.

Meanwhile, those associated more with sectors like agriculture and small firms, where incomes may not be as high, are focused on consuming essentials. This consumption group may not have much investible surplus, and therefore not as strongly integrated with financial markets.

Exports. We probe the surprisingly low correlation of export growth and global growth a bit more. The fall in correlation was pronounced in the middle of the 2010-2020 decade when import tariff rates were being raised and export growth was falling (see exhibit 12).

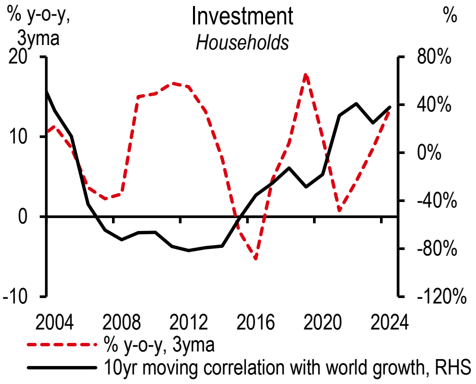
[1] In essential consumption, we include food, clothing, footwear, house rentals and water services. Discretionary consumption includes all else.

Ex 8: Corporate investment has a higher correlation with world growth of 75%…



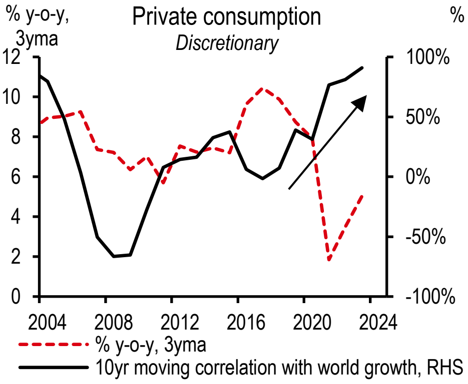
Source: CEIC, HSBC

Ex 9: …compared to household investment correlation of 40%



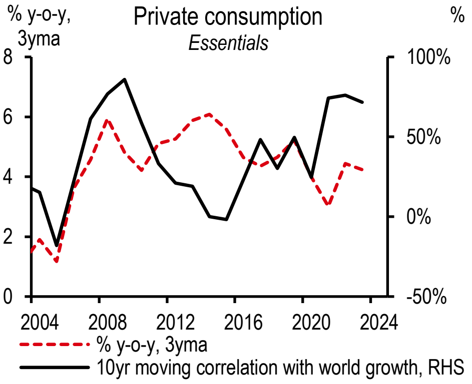
Source: CEIC, HSBC

Ex 10: Discretionary consumer spending has a high, 100% correlation with world growth



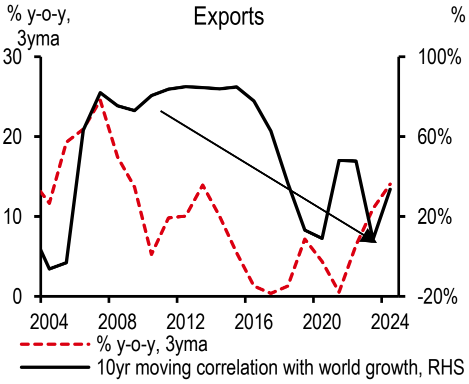
Source: CEIC, HSBC. Discretionary spending is calculated as consumer expenditure excluding spending on essentials.

Ex 11: Essentials have a relatively low correlation of 70% with world growth



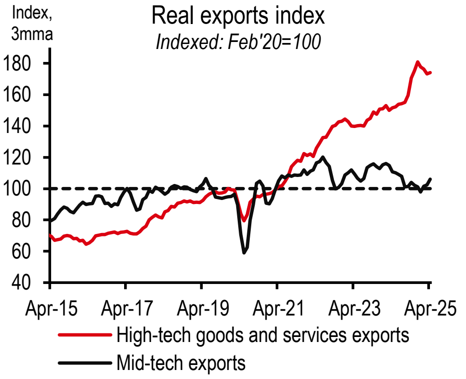
Note: Essentials spending is sum of consumer expenditure on food, clothing, footwear, house rentals and water services.
Source: CEIC, HSBC

Ex 12: The fall in export correlation with world growth was pronounced in the middle of the 2010-2020 decade



Source: CEIC, HSBC

Ex 13: Growth in high-tech exports has far surpassed growth in mid-tech exports



Source: World Bank, CEIC, HSBC

Sluggish mid-tech exports have weakened India's trade integration with the world

We divide exports into the more capital-intensive high-tech and the more labour-intensive mid-tech exports. We find that growth in high-tech exports has far surpassed growth in mid-tech exports (see exhibit 13). In fact, the latter has been rather sluggish for a decade.

One can thereby deduce that, led mainly by sluggish mid-tech exports, India's trade integration with the world has been weak.

Bringing it all together

So now we have two sets of results:

High-end earners and consumers aligned with large firms and financial markets are more globally integrated

Stronger financial integration. Rising equity market correlation (of the S&P500 and SENSEX indices, see exhibit 14) and the rise in international financial inflows into India show that India has become a lot more financially integrated with the world over time. Those who have been able to enjoy the gains of financial integration have seen incomes and discretionary consumption rise. This even explains the strong correlation between global growth and discretionary consumption.

Many of these individuals could well be associated with large firms in the formal sector, where global capex tends to be highly correlated globally. These individuals could also be associated with high-tech exports, such as India's rapidly rising professional services exports.

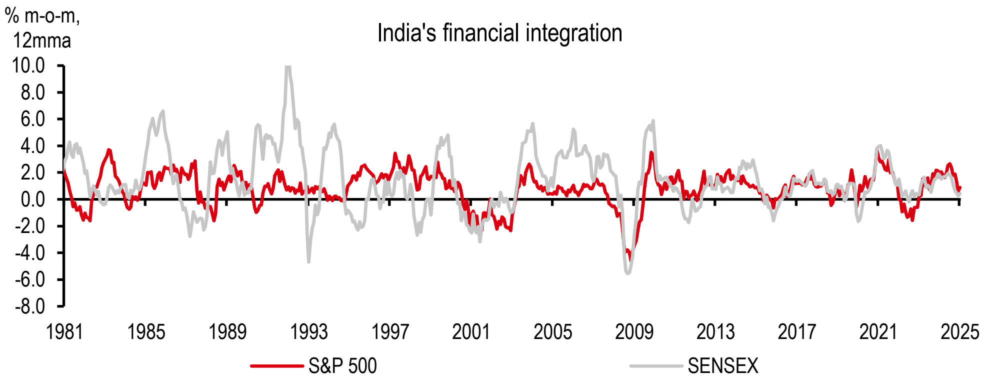
Lower global integration in mid-tech exports explains weak consumption and investment

Weaker trade integration. On the other hand, as discussed above, trade integration has been relatively weaker, led particularly by mid-tech exports. About 45% of India's goods exports come from small firms. Lower global integration here, then, explains lower mid-tech export growth, and lower incomes in this category. Lower incomes go on to explain why this group is focused a lot more on consumption of essentials, and do not have much surplus to trigger investment. This, then, explains why integration of essential consumption and household investment growth with world growth remains low.

A corollary here would be that steps which raise mid-tech exports and India's trade integration with the world can boost consumption, and particularly investment.

But what needs to go right?

Ex 14: India's financial interlinkages with the world have deepened over the years



Source: CEIC, HSBC

An opportunity comes knocking

An opportunity to raise exports has arisen

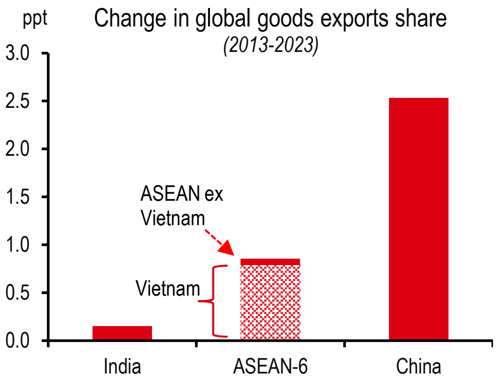
Elevated import tariffs have hurt India's export potential over the last decade, and mid-tech exports, which are also more labour intensive, have been hurt most. In fact, we believe India was not able to fully seize the opportunities in the first Trump presidency, when supply chains were rejigged following the imposition of new and elevated tariffs[2].

Other blocks like ASEAN made more progress in raising their global export share (see exhibit 15). Vietnam, in particular, made substantial gains in both mid-tech and high-tech sector exports. If supply chains are rejigged again during the second Trump administration, India may have a chance to grow.

As supply chains are redrawn India may play a bigger role

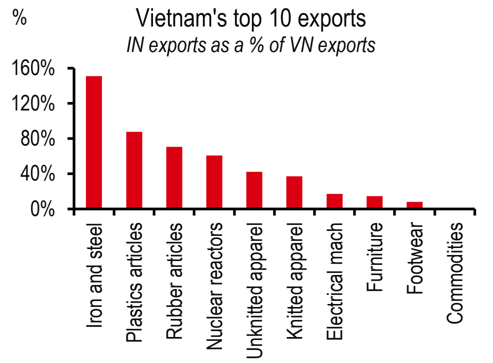
If the sectors where Vietnam made the most progress during the first Trump administration reflect where global opportunities from supply rejigging lie, note that India is already a player in these sectors. India's exports in sectors like electronics, apparel, furniture, and footwear are 15-40% of Vietnam's exports (see exhibit 16). This shows that India's footprint is large enough to show capability, but with room to grow. After all, wage competitiveness is still on India's side (see exhibit 17).

Ex 15: ASEAN and China gained global export share in the first Trump presidency



Source: UNCTAD, HSBC

Ex 16: India's exports of electronics, apparel, and furniture are 15-40% of Vietnam's exports, reflecting room to grow

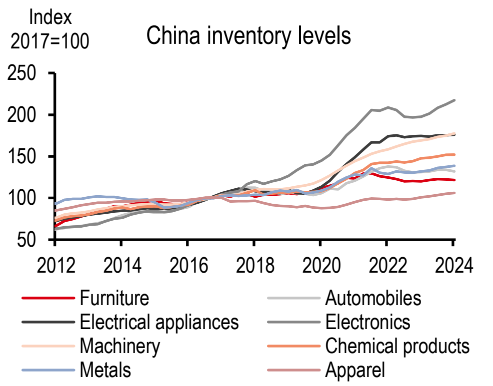


Source: ITC trade map, HSBC

Ex 17: Wage competitiveness is still on India's side

Source: JETRO, CEIC, HSBC

Ex 18: China has larger excess capacity in high-tech sectors, compared with mid-tech ones like apparel and furniture



Source: Macrobond, HSBC

[2] Did India benefit at all? Yes, but narrowly. It did gain market share in the export of electronics and iron & steel articles. But it was not able to gain significant market share in most other sectors, largely mid-tech (e.g. furniture, footwear, apparel, and toys).

Incidentally, China's excess capacity is not as large in these mid-tech sectors (see exhibit 18). Space for another manufacturing economy may well be there.

But first, India needs to make changes to do it right this time around.

External reforms have begun, but must run deep

India has embarked on external sector 'reforms' but these must run deep

Potential US tariffs on Indian exports may have become a catalyst for external sector reforms. In fact, India has recently taken a few steps which signal that it is becoming more 'open for business':

- **Lowering import tariffs:** In the February budget, import tariffs were cut for items like high-end motorcycles, smartphone components, solar cells and chemicals. Recent news articles show that the government plans to cut tariffs for several other categories of goods such as automobiles, agricultural products, chemicals, pharmaceuticals and medical devices[3].
- **Opening up to regional FDI:** The economic survey of July 2024, which is an important policy document, made a case for India to become more open to regional FDI, in particular from China[4]. However, this has not culminated in higher FDI inflows yet.
- **Fast tracking bilateral trade deals:** India plans to sign a bilateral trade agreement with the US in 2025, with the first phase expected to be finalised by July[5]. Reports suggest that it plans to buy more oil and defence equipment from the US and increase cooperation in nuclear energy[6]. All of these would likely reduce India's trade surplus with the US. It has also shown signs of wanting to fast-track its trade agreement discussions with other regions such as the EU[7]. The finalisation of the India-UK trade deal on 6 May, following more than three years of negotiation, signals to us a sense of urgency in concluding trade agreements quickly. This may provide some tailwind for other negotiations too.
- **Making the INR more flexible:** A flexible rupee does not just act as a shock absorber during times of external volatility, but also helps make exports competitive, and give manufacturers the confidence to export from India. After a period of REER appreciation, the rupee has mean reverted over the last few months.

These are a good start. But for long lasting impact from greater integration with the world, and stronger growth and more jobs, these reforms will have to run deep.

Key forecasts

Ex 19: India's key forecasts

	Unit	FY25f (Apr'24-Mar'25)	FY26f (Apr'25-Mar'26)
Real gross domestic product (GDP)	%y-o-y	6.3	5.9
Consumer price index (CPI)	%y-o-y	4.6	3.7
Central government fiscal balance	% GDP	-4.8	-4.6
State government fiscal balance	% GDP	-2.9	-2.9
Current account balance (C/A balance)	% GDP	-0.6	-0.8
Repo rate	%, end-period	6.25	5.25

Source: CEIC, HSBC forecasts

[3] Government considers tariff cuts on cars, chemicals as Trump duties loom| Business Standard, 27 February 2025
[4] Indian economic adviser backs more Chinese direct investment in annual report| Reuters, 22 July 2024
[5] India aims for three-stage trade deal with US ahead of July tariff deadline| Financial Express, 20 May 2025
[6] India to buy more US oil, F-35 jets as Modi, Trump strengthen ties| The Hindu Business Line, 14 February 2025
[7] India, EU aim for two-phase free trade deal amid global trade uncertainties| Ministry of External Affairs| 20 May 2025

Disclosure appendix

Important disclosures

Additional disclosures

1 This report is dated as at 22 May 2025.

2 All market data included in this report are dated as at close 21 May 2025, unless a different date and/or a specific time of day is indicated in the report.

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