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# 1

## India and China: An Essay in Comparative Political Economy

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### 1.1 Introduction

India and China are two of the oldest and still extant civilizations. For Europeans, they were legendary seats of immense wealth and wisdom right up to the eighteenth century. Somewhere between the mid-eighteenth century and early nineteenth centuries, both of these countries became, in the European eyes, bywords for stagnant, archaic, and weak nations. For China, this happened between the adulation of Voltaire and the cooler judgment of Montesquieu; in India's case, it was the contrast between Sir William Jones's desire to learn things Indian and James Mill's dismissal of Indian history as nothing but darkness.

The twentieth century brought nothing but a deepening of the perception of the two countries as bywords for misery and the perceptions were not too far behind actual conditions of the two countries. For one thing they were, and remain, the two most populous countries. In 1820, they had a combined population in excess of half a billion and by 1900, it reached 700 million. Within the twentieth century, their population had trebled. But they were also two of the poorest countries, typically thought of as locations of famine, disease, backwardness and superstition, of women with bound feet and men with long pony-tails in China, untouchables beyond the pale and myriads of gods with many heads and limbs in India.

In the mid-twentieth century, particularly in the 1960s, the fortunes of these two countries seemed to have reached their nadir. They were independent republics supposedly launched on their path of development, but both suffered devastating famines. China's famine was hidden, perhaps more from China's own ruling classes than from its people or the world, but it had followed swiftly upon the debacle of the Great Leap Forward, a memorable piece of policymaking by fantasy. A double harvest failure in 1965 and 1966 brought India to its proverbial knees in terms of foreign policy and dependence on US food aid. These two countries were "basket cases" in the then fashionable terms of international diplomacy.

In the span of less than forty years, we are discussing China and India not as failures nor for their ancient wisdoms, but as dynamic modern economies. The *Economist* has to write editorials to tell the world not to be afraid of China's economic power. American legislators pass laws to prevent their businesses from outsourcing work to India's software and telecommunication services. China ranks as the second largest economy in terms of gross domestic product (GDP) in purchasing power parity (PPP) dollars. Together the two countries account for 19.2 percent of gross world product—China 11.5 percent and India 7.7 percent. This is still below their share of world population 37.5 percent—with China 21 percent and India 16.5 percent.

National income estimates covering a long period are, by their nature, broadly indicative rather than precise.<sup>2</sup> Angus Maddison, to whom the profession is indebted for making these calculations his lifetime work, gives the shares of gross world product and population of China and India for two earlier dates in the twentieth century as follows:

Table 1.1 succinctly describes the course of the two economies over the twentieth century. They start with the share of income below that of population. Over the previous century they had slightly different trajectories. India's per capita income is estimated to have grown from M\$533 in 1820 (Maddison dollars [M\$] or 1990 international dollars) to M\$673 in 1913 while China's per capita income declined from M\$600 in 1820 to M\$552 in 1913. But during the first half of the twentieth century, both countries saw a decline in their per capita incomes—India from M\$673 in 1913 to M\$619 in 1950 and China from M\$552 in 1913 to M\$439 in 1950.<sup>3</sup>

Table 1.1 says two things: India and China both suffered a declining per capita income and a rising population during the first half of the twentieth century, but India was slightly better off than China between 20 percent<sup>4</sup> and 40 percent.<sup>5</sup> By 1998 this was reversed. Both countries were better off, but China was much better off than India. China's per capita income was M\$3117 while India's was M\$1760. Thus, while India roughly trebled its income, China increased it sevenfold. In earlier periods, China, while more populous than India, was not noticeably richer. In terms of GDP, the two

*Table 1.1* Share of world output and population (in percent)

Year	Share of gross world product		Share of world population	
	China	India	China	India
1913	8.9	7.5	26.4	17.0
1950	4.5	4.2	21.1	14.2
1998	11.5	7.7	21.0	16.5

Source: Maddison (2001).

economies were of roughly similar size. The ratio of China's GDP to India's was 1.18 in 1918; 1.08 in 1950; but in 1998, it was 2.28.

Therefore, one theme of this chapter is the contrast between the economic performance of China and India and its proximate causes. But there are also a lot of similarities between the two, both in the path to modernization and, as we shall see later, the future prospects for their economies. There are also political similarities and contrasts between the two, both as to their twentieth-century history and twenty-first century challenges.

## **1.2 Historical legacies**

### **1.2.1 Political legacy**

While both India and China have a long history, their histories are very different. China has been by and large a stable, centrally run state throughout its history with limited periods of instability and lack of a single authority. India's history has been exactly the reverse. The periods when a single king or political authority ruled over even the major part of India's territory can be counted on the fingers of one hand. In China's case there was a deep desire for unification of the country as a driving force of nationalism in the twentieth century. But it was called reunification. Thus at the onset of the Second World War, China was divided, and Jonathan Spence (1999) expresses the drive for nationalists as follows:

The solidification of such a group of new states, that is, war lords, KMT [Kuomintang], communists and Japanese enclaves, would return China to the situation that had prevailed before the Qin conquests of 221 B.C., during the so-called Warring States period when ten major regimes controlled the country among them; or it might bring a recurrence of the shifting patterns of authority and alliances that typified China's history from the third to sixth century A.D., and again from tenth to the thirteenth.<sup>6</sup>

In India's case, there never was any authority which has ruled over all of India; indeed, not even the British or even the present Indian government. India has been an idea in world culture for millennia, but its borders had been fixed only in the late nineteenth century sometime after the British gave up on Afghanistan and drew the Durand line. Kings have ruled over much of North India—the Maurya and Gupta dynasties just before and after the BC/AD division. The Mughals could be said to have ruled over much of India between the years of Akbar's maturity in 1570 and Aurangzeb's death in 1707. Their empire extended to Kabul but did not take in all of South India. The British could be said to have ruled over two-thirds of India between 1857 and 1947, with the remaining third being ruled by native princes under their paramountcy but not direct rule. In 1947, India was

partitioned and thus even what is now called India is not what Nehru in 1946 wrote about in *The Discovery of India*.<sup>7</sup> Indian system of kingly power was not so much like a pyramid, but like a multitiered cake. It was flatter and while there was a top and a bottom plus layers in between, the power of the top king over his vassals below was not absolute. Loyalty, though owed by the lower tiers to the top, was always negotiable and there had to be some give and take.<sup>8</sup> The British were perhaps the first rulers to try a more absolute and hierarchical structure of power under the limitation of oversight by a democratic Parliament back in London.

Yet in one sense it was British rule which gave India its definitive territorial extent, fixed its boundaries and gave it a structure of provinces and central government with an administrative “steel frame.” The British gave India their language, which facilitates even today India’s access to global markets, as do the legal system of property rights and Western orientation of its elite. India’s independence movement was critical of the economic ruin the British had caused—deindustrialization, drain of treasure, deskilling and diversion of agriculture into commercial crops away from food crops, and so on. But India began to acquire railroads and modern industry in the 1850s—a quarter of a century earlier than China. More foreign capital per capita was poured into India than in China; in 1913 India had US\$6.9 per capita foreign capital while China had US\$3.7.<sup>9</sup>

There is however another much less-mentioned benefit that India derived from British rule. Of course, it might have been better for India to have never suffered foreign rule, but to have been united under a native king or republic. But between 1500 and 1800, India had several foreign trading companies vying for control—the Portuguese, the Dutch, the French, the Danes, and of course, the English. As a counterfactual of history, it is possible to imagine what we call India today and take it for granted as a single country being made up of several different “countries” in the west, south, east, and north with different foreign languages being spoken along with local languages. Thus the Tamils could have been French speaking and the Maharashtrians Portuguese speaking and so on. Thanks to the religious wars of Europe in the seventeenth century and British victories in European wars in the eighteenth century, India ended up with a single foreign power, and thus the idea of India as a single country developed with its modern nationalism. This is not entirely fanciful since Southeast Asia with a population and extent not dissimilar to India’s was ruled by the Dutch (Indonesia), the French (Indochina) and the British (Burma, Malaysia, and Singapore) with Thailand being independent. What is more, the hegemonic political ideology of the nationalist movement—liberal democracy—was also borrowed from the foreign rulers. The India we talk of today is a nineteenth century product in more than one sense.

China, by contrast, never suffered foreign rule over majority of its territory. There were foreign concessions in ports and later in interior towns extracted by several foreign powers in circumstances that the Chinese found humiliating.

But it had not suffered classic imperial rule until 1931 when the Japanese invaded Manchuria and later in 1937 when they occupied large chunks of eastern and central China.<sup>10</sup> Yet China's attitude to foreigners was and is much more hostile than India's. The removal of foreigners, especially the reversal of concessions, became a driving force for China. For India, the hostility to things foreign, except perhaps for foreign private capital, melted like snow in spring soon after independence. If anything, India in its early days after independence sought foreign capital from public rather than private sources and from a variety of countries rather than merely its old colonial masters. China after 1949 relied on one country, the USSR, and soon came to regret its connection. China's problem, unlike that of India, was the multiplicity of foreign powers gnawing at its sides with no single hegemonic ruling ideology as India had had with liberal democracy from Britain. It had the Germans, Japanese, Americans, French, and the British jostling not so much for rule over Chinese minds as over their cash boxes. There was some missionary input, more than in India, but eventually China had to forge its own ideology of modernity. It had to struggle to confront Confucianism against Western ideologies—liberalism, Fascism, and Communism.

These historical legacies shaped both the politics and economics of the two countries. For India, the problem was in achieving unity in diversity and in accommodating various languages and religions in a political structure, so as to give its center enough power to maintain its territorial integrity but its regions enough room to develop their diversities. India had a problem of articulating a single vision of Indian nationhood since it had been a nation only since the mid-nineteenth century and even this was asserted against by the foreign rulers who saw India not as a single nation but a motley collection of races and religions.<sup>11</sup> India thus chose a federal polity with a strong center able to alter state boundaries, split up states or create new ones. India even so is a soft state in Myrdal's famous description where the government has to work consensually and exert control sparingly and, that too, only against serious threats to national integrity.<sup>12</sup> India's fear is a break up of its territorial unity as had happened in the Partition.<sup>13</sup>

China has always had a vision of itself as a nation. Through much of its history, there has been a strong central power, and China has been run as a unitary polity. Indeed, Sun Yat Sen and his Communist supporters viewed the prospect of federalism as akin to feudalism.<sup>14</sup> The theme of reunification in early twentieth century China meant recentralization of authority. China has its minorities, but it is viewed and indeed views itself as a country of the Han people—a solid homogenous mass. While there are differences between Mandarin and Cantonese, the language is the same for an overwhelming majority of the Chinese. China is thus a unitary hard state which can pursue a single goal with determination and mobilize maximal resources in its achievement. It has ever been thus, be it in building the Great Wall or the system of grand canals, or in recent times in the Great Leap Forward.

There was a further advantage of being a unitary state which has often not been recognized. As Kent Deng has said in a recent survey of Chinese economic history:

a basic structural factor—namely, that for most of the time most of China had a nationwide market, a single government (which was active in maintaining food supply, famine relief, and price control), a standardized written language, a uniform calendar and a system of weights and measures, a dominant Confucian code of conduct, a nationwide transport network, and the mechanisms for social mobility and inter-regional migration ... China could claim to have been a proto industrialized country by the 13th century and indeed has been considered by many scholars to have been a prime candidate for a capitalist revolution which it missed.<sup>15</sup>

But anticipating somewhat later themes, strong states can also be brittle states, while soft states are difficult to smash and break since they are pliable. India has through its history been ruled by many authorities and sometimes none, but it has had a social stability which is remarkable. In India's case the enveloping unity was provided by the Hindu social structure, especially the caste system, which determined the basis on which inter-regional mobility could be conducted. Indeed the caste system proved to be so powerful that even among the Muslims and Christians a caste hierarchy took root and developed. While the concept of the Asiatic Mode of Production (AMP) is much derided nowadays, its essence was about a society in which the state was epiphenomenal and the peasant society went on impervious to changing rulers. India was throughout its history like that.<sup>16</sup> China, on the other hand strong as it was, became subject to spasmodic breakdowns which lasted several years. Within the modern period, we have had the Taiping Rebellion (1851–64), the Boxer Uprising (1900) which eventually led to end of empire (1911) and four decades of warlordism, and more recently the Cultural Revolution (1966–76). Even the Tiananmen incidents of 1989 are more a sign of brittleness than of strength.

### 1.2.2 Economic legacy

Both India and China were a highly urban civilization by the eighteenth century, though of course the bulk of the population lived in rural areas. China was much advanced in science and technology, with gunpowder, printing, paper, and paper currency as its inventions. China's scientific and technological achievements are known to us thanks to the monumental efforts of Joseph Needham.<sup>17</sup> India was known for its mathematics and its philosophy. The Chinese gave the world the wheelbarrow and bureaucracy; India gave the world the zero, decimals and Buddhism. Both were major exporters of fine textiles, silks and muslins; their ships sailed around the

world and indeed dominated the seas till 1500. After that the Chinese withdrew from the seas and while the Indians continued, the powers that be in Delhi or Agra had no need for a navy. It was the kingdoms in South India which were maritime adventurers. As they declined in power under the Mughals, Indian shipping began to be conducted increasingly on a private basis rather than a state sponsored one. The control of the seas passed to a series of Western European countries. Yet China and India remained economically vibrant till the late eighteenth century.

China had a higher productivity in its agriculture, the iron tipped plough having been in use at least half a millennium before it made its appearance in India. Thus Needham attributes the animal drawn plough to the period of the Warring states, while Habib says that the iron plough came to India in the first century AD.<sup>18</sup> Chinese irrigation systems were bigger and better than any in India.<sup>19</sup> Thus Maddison's estimate of M\$600 per capita income for China and M\$533 for India in 1820 is roughly the right sort of relative difference.

The difference was made up in the next 130 years. By 1950, India had caught up with China, as we saw earlier, in the per capita as well as total income estimates. In output per person employed, Maddison shows India at M\$1377 in 1950 and China at M\$1297. The story is that in the nineteenth century India did enjoy a rising per capita income. This is not uncontroversial, as everything else about British impact on India. But it is consistent with much data.<sup>20</sup> India was a land surplus rather than a labor surplus country in the nineteenth century with a population of about 200–230 million, that is, one-fifth of the current level, and much the same amount of land. It became for a while an agricultural exporter rather than industrial exporter, but still managed a trade surplus. By the late nineteenth century, India began to acquire modern infrastructure and industry, not large relative to its population, but large relative to other countries. India is in this sense an early industrializing country. In 1945, it was the seventh largest industrial country by volume of output.

But their history drove both China and India to define industrialization rather than economic development as their prime goal. Even within industrialization, the strategy was one of concentrating on basic goods such as steel and machinery—"Department I goods" in Marxian terminology—rather than consumer and low-tech goods. Both countries were inspired by the example of the USSR and its planning achievements. They both sought independence of foreign capital and self-sufficiency.

The contrast between the two was most stark in agriculture. Being vast territories there is a similar diversity in the eco-agricultural make up of regions in both countries. But China's central rule meant that a uniform revenue collection system and land ownership pattern prevailed especially while the central power was effective. India by contrast had different legal patterns of revenue collection and different land tenures as a result of a lack

of central authority reinforced by British experimentation with Ryotwari, Zamindari, Mahalwari, and the like. Land reform was a straightforward issue of changing ownership of large landholdings across China as far as the Communists were concerned. They were also committed to it as soon as they could become the sole powers. In India land reform was a maze of regional complexity and the Congress Party was not a revolutionary organization. Land reform thus became a state/provincial subject rather than a union/central policy issue. Thus India added legal and economic variation to the eco-agricultural one.

### 1.3 Development paths

Differences between China and India appear much greater from the current vantage point than they would have in 1973 or even 1983. Each has gone through two broad phases, which I characterize in this section.

#### 1.3.1 Taking nationalism seriously—mistakes and learning

Both countries feared foreign domination and considered development as synonymous with industrialization. Both considered the State as the engine and the driver of growth and suspected the private sector's initiatives. The ideology forged during the long march to independence—Marxism, Leninism, Maoism in China and Gandhism in India, plus an amalgam of social and liberal democracy in India shaped the response more than economic realities warranted. One man ruled the roost though his closest associates did not share his beliefs as much as they said they did while he was still around. Mao for China and Nehru for India laid down the path from which each country had to deviate, if only because the path led to a blind alley.

For China the first period lasted from 1949 to 1978; for India from 1947 to 1980. China learned quickly thanks to Deng Xiao Ping. India did not have a Deng. Blood proved much thicker than pragmatism in matters of economic ideology. India began a halfhearted change in 1980 when Mrs Gandhi abandoned self-sufficiency as an ideal and took a big loan from the international monetary fund (IMF). But that loan and subsequent hard currency borrowing were frittered away. India could be said to have wasted ten years in a halfhearted liberalization, which hit the buffers in 1991 when the country nearly went bankrupt.

#### 1.3.2 Living in the modern world and adapting to it

In the second phase, each country forgot the lessons it had thought it had learned from its history, xenophobia, fear of foreign trade and foreign capital, distrust of private initiative and decentralization. Each adapted to the rhythm of the world economy rather than sail against the wind. Being large vessels, they have a bit more freedom of maneuver than small countries. They misused the freedom in the first phase and corrected themselves in the second phase. Their comparators would be two smaller countries both with

a colonial past—South Korea and Taiwan who did not go through a two-phase path. After 1960, South Korea single-mindedly pursued growth with spectacular results. Taiwan had a similar colonial background to Korea's but it also had the influx of the Guomindang elite, which transformed property rights in Taiwan and achieved what it could not on the mainland—a successful growth strategy.

The comparison between the two pairs of countries is revealing. In 1950 China and India had per capita incomes of M\$439 and M\$619, while South Korea and Taiwan had M\$770 and M\$936. By 1999, the numbers were: China M\$3259, India M\$1818, South Korea M\$13,317 and Taiwan M\$15,720. Let me examine the two phases in some detail.

### *The first phase*

Both China and India saw a development of Department I goods—steel, cement, machine-making equipment—as pivotal to their growth strategies. India had at this time a viable world-class textile industry which it chose to stifle in its search for an employment-intensive growth strategy meant to favor small-scale and low-tech firms over large-scale industrialized firms. India diverted resources from the production of domestic consumption goods, especially of the machine-produced variety, to the production of investment goods by the industrial sector and consumer goods by small-scale industries. However, its savings rate was not significantly raised and the growth rate remained modest. China seems to have concentrated its industrial efforts also on the basic goods sector initially, but after the first three or four years switched to an all-round emphasis on heavy as well as light industries. Apart from the aberration of backyard steel furnaces in the Great Leap Forward phase, it was not saddled with a small-scale industry strategy. But China had a more successful resource mobilization strategy than India did. India's Second Five-Year Plan (1956–61) ran into a resource constraint by 1958. China on the other hand ran into the evils of overweening ambition in launching the Great Leap Forward. There seems to have been a slowdown in China in the 1960–65 period, whereas in India it came in the second half of the 1960s after the Third Five-Year Plan (1961–66).

China managed its agrarian reform better than India. Starting from a higher level of productivity, China went on to transform not only the tenurial relations in agriculture but also the production conditions. Thus abolishing of landlords and forming cooperatives and then communes changed not only the distribution of surplus, but also its size. India concentrated on changing the tenurial relations by abolishing zamindari and intermediaries and redistributing the surplus. Reform was of course different across regions as the polity dictated. But India did little to change production conditions—land pooling, technology used, or labor deployed. These changed in India in the 1960s with the advent of the Green Revolution, where a combination of foreign knowledge, domestic subsidies, and rural private initiative brought a

*Table 1.2* Human development indices, 1950–2000

	1950	1960	1973	1980a	1980b	1992	2000
China	0.163	0.248	0.407	0.475	0.554	0.594	0.726
India	0.160	0.206	0.289	0.296	0.434	0.439	0.577

*Sources:* Crafts (1997) for 1950, 1973, and 1992; United Nations Development Programme, *Human Development Report* (HDR) (1997) for 1960 and 1980a; and *HDR* (2002) for 1980b and 2000.

capitalist revolution to the Indian countryside. Despite this, China's lead in agricultural productivity remained to the end of the first phase and indeed increased, when in the second phase, China moved to a more private initiative system.

But above all, China did very well by human development. Long-run calculations of Human Development Index (HDI) have been made by Nicholas Crafts. For China and India he has estimates for 1950, 1973, and 1992 (Table 1.2). The World Bank's Human Development Report (HDR) has over the various years published trends in countries' HDIs from 1960 onward. Its methodology has evolved over the years and so the estimates have also been revised even for earlier years. Using the 1997 HDR and the 2002 HDR we can see the trend up to 2002. The HDR estimates start in 1960 and are not strictly comparable to Crafts's estimates, but they are close enough.

Thus we see that despite having similar HDIs in 1950, China had left India behind by 1973, even with similar per capita incomes. Over the 50-year period, while the HDIs are not strictly comparable, China enhanced its HDI four-and-a-half times while India did so only three-and-a-half times. Taking the estimates for 1950, 1980b, and 2000, we see that in the first 30 years, China advanced much faster—by three-and-a-half times—than in the last 20 years—only by a third more. India on the other hand took its HDI up two and three-quarter times between 1950 and 1980 and again by a third in the next 20 years. Some writers have argued that the slowing down of China's advance in human development was due to the disbanding of the communes and with it the downgrading of the health care facilities available to all.<sup>21</sup> On the other hand, the closer a country's HDI comes to the limit of 1.0, the harder each step becomes. Whichever way we look at it, China has done much better in human development than India.

While there may be an argument about the state of health care facilities in China after the Deng reforms were launched, it is in other dimensions that China kept on doing well. Its emphasis on education for all from early on paid handsome dividends, while education remains a blot on India's record. Here again the centralist versus federal polity makes a lot of difference. Social conditions differ immensely across India in terms of caste structures,

religious influence, and superstitions. Hinduism is not an egalitarian religion even in theory and Islam at least in India is not so in practice.<sup>22</sup> It is only when you go south where the influence of Christian missions was felt and social movements against the caste system were successful in early twentieth century that you witness an improvement in human development statistics. India continues to pay a heavy price for its neglect of education, especially as it concerns women.<sup>23</sup>

The first phase, despite the differences in approach to agrarian transformation and human development, altered the relative positions of China and India from what they were in 1950, but not by much. By 1978, per capita income of China was M\$979 and of India M\$966. China had caught up with India over the thirty years, but not dramatically surpassed it. Agricultural productivity per worker was almost identical in 1975 in the two countries—China 2.3 and India 1.9 (relative to the United States = 100).<sup>24</sup> One may ask why this was so. Why is it that China did not do much better than India despite its revolutionary effort in industry and agriculture and its immense achievements in education and poverty reduction. There are two responses to that question.

One, of course, is that it did. China's income doubled while India's only went up by 50 percent. Of course, China had suffered from the ravages of foreign and civil war through the 15 years since Japan's invasion of Manchuria in 1933. So its per capita income in 1950 was below its potential. But even then we must acknowledge that China's growth was not smooth. While it was rapid, China's growth suffered from the tendency of Mao to take immense risks and plunge the economy into catastrophes. I am personalizing the problem because Mao was a dominant influence in China to an extent that Nehru never was. This is where a totalitarian system can differ from a democratic one. It can accelerate growth and mobilize immense resources, but if the direction is wrong it can also crash and waste an awful lot of resources in a short period of time. But added to that, the political culture of China has been long used to such imperial power, while India has been a much less commandable polity. Thus Mao plunged China into the Great Leap Forward as well as the Great Proletarian Cultural Revolution (GPCR), with the structure of centralized and personalized power which led to the catastrophic famine of 1962. China paid a price for this in terms of death, starvation, and wasted resources in abandoned projects. Much human capital, of both university teachers and students, was revalorized during the GPCR.

India, by comparison, had its muddle and mess but no great discontinuities in its development experience. It had a multiparty system and even within the Congress Party had antagonistic factions, which could mobilize opposition to Nehru. Even before his death, Nehru was forced to abandon his preferred policy of cooperatives in agriculture by the farmers' leader Charan Singh, but then besides Nehru no one else in the Congress took cooperative

agriculture seriously and had done nothing about it since the Agrarian Reforms Committee of the Congress proposed it in 1949. The Second Five-Year Plan had to be modified due to resource shortages, but the Third Five-Year Plan kept to the same basic strategy. During the 1960s, India went through what was known (in a Maoist parody) as the Three Twos—death of two prime ministers, two harvest failures and two wars. There was a policy reversal in agriculture when the High Yield Variety program was adopted. In addition, rural and regional political bosses asserted their hold over the Congress Party and displaced the urban Westernized elite after Nehru's death, but they in turn were displaced after 1969 when Mrs Gandhi regained control of the Congress. India also had to devalue its currency and felt the heat of the US and World Bank disapproval. Yet the economic strategy did not (sadly) change. The crisis of slow growth came in 1975 when in face of popular unrest, Mrs Gandhi was driven to suspend democracy and declare the Emergency. But that did not last long, proving yet again that India cannot be commanded by centralized and personalized power.<sup>25</sup>

### *The second phase*

It was China, after 1978 under the influence of Deng, that accelerated, leaving India far behind. In the next 35 years China's per capita income more than trebled while that of India merely doubled. The logic of compound growth rates is pitiless, and China's per capita income is now almost double that of India. How did China do this?

China did this paradoxically by adopting a much more "capitalist road" or Bukharinist strategy<sup>26</sup> than any other communist regime (the former Yugoslavia included). What is more, China adopted a road that India could always have adopted; indeed, this was possible right after independence except that no one, not even the Indian capitalists, were advocating greater import of foreign capital, opening up the economy to an export orientation, with Special Export Zones (SEZs).<sup>27</sup> While India went on restricting its large native capitalist class after independence, China had to practically reinvent its own bourgeoisie after 1978. Indeed according to a newspaper story cited by Dharma Kumar,<sup>28</sup> China, which had invented an examination system for the selection of bureaucrats in the mists of time, approached India in the 1980s to seek its guidance about conducting examinations for its civil servants on the lines of the Union Public Service Commission (UPSC) exams in India.

Of course, China's policy revolution was not seamless and Deng had to struggle to establish his hegemony. There is a debate among China scholars about the fang/shou (stop-go) cycle in Deng's reforms between 1978 and 1989.<sup>29</sup> But once established, his control over policy was absolute; the political culture's habit of obedience to emperors helped.<sup>30</sup> Deng transformed agriculture by introducing the Family Responsibility System—privatization Chinese Communist style. He then took on the industrial sector and opened it up to foreign capital while making room for the growth of village and local

enterprises. He left the public sector enterprises untouched but slowly brought modern methods of fiscal and financial control to China. China had to introduce property rights and contract laws which India has had since Macaulay in British times.

India meanwhile also started to jettison some of its own orthodoxies, but the personality in power was still the same. Mrs Gandhi abandoned the fetish of national self-sufficiency and began to borrow abroad, from the IMF to begin with. She, however, changed little else in the dirigiste logic of Indian economic policy. The collapse of India's textile industry was symptomatic of the malaise. Within 35 years of independence, India had managed to bankrupt its once globally competitive industry. Freed from the constraint of food grain availability thanks to the Green Revolution, India did not manage to apply to its industrial sector the lessons learnt in its agricultural revolution—that is, to use foreign knowledge, rely on the dynamic private sector and deploy subsidies selectively. Instead, foreign borrowing was used to ease the consumption constraint in the public sector and to cushion loss-making public enterprises. Ian Little and Vijay Joshi (1994) argue in their book on Indian economic reforms that Indian policymaking alternates between five-year spurts of radicalism then quiescence, flaring up under political or economic pressures.<sup>31</sup>

India really changed course only after the shock of 1991 when it was nearly bankrupt and had foreign reserves which would cover only two weeks' imports. But in changing the same personalities were involved as in the old dirigiste regime. Manmohan Singh as Finance Minister was crucial to the reform, but he was no Deng and neither was Narasimha Rao, who was Prime Minister 1991–96. Indeed, by 1994, India began to reveal its reluctance about economic liberalization. Ever since, India has been reforming its economy, but in a much more embattled way than China. Given the nature of the political culture, reform can only be introduced by broad consent, and all the potential losers (many of whom are in power) have to be bribed (sometime literally so) to advance matters.

Thus, while China has received a lot of foreign capital, India has not. By 1998, Maddison's calculations show that foreign direct investment (FDI) per capita in China was US\$183 and in India US\$14. Even if a lot of China's FDI was due to the Chinese diaspora, it only shows the failure of India to attract its own diaspora to invest, in spite of a lot of trying. Indeed, India has sought portfolio capital more than FDI since suspicion of foreigners remains strong, not only among India's politicians but even more among its capitalists. There has been some change for the better in the five years under the government of the Bharatiya Janata Party (BJP) and its National Democratic Alliance, but there is a long way to go.<sup>32</sup> There are other more usual reasons for the difference in economic performance. For one, China's savings rate is almost 50 percent of GDP, nearly twice that of India. Indeed given the higher savings rate in China plus the FDI influx, the growth rates are less far apart than should be

the case. India averaged 5.5 percent in the 1980s and around 6.5 percent in the 1990s. Even at 7–9 percent, China's growth rate implies inefficient use of capital barring gross measurement errors. Or it could indicate sharply diminishing returns to capital, but I doubt that given that a lot of FDI embodies the latest knowledge.

The reason may be that in both countries there is a large public sector where enterprises are seriously loss making. Both countries are wedded to Soviet-style emphasis on inputs rather than outputs and accumulation for its own sake. India had begun to shed some of these traits and has always had a smaller public sector than China. So the waste of resources by mal-investment<sup>33</sup> is larger in China. In both countries, there is also a budget deficit which is out of control; perhaps more so in India due to the exigencies of democratic and coalitional politics, as well as weak central control over provincial budgets.

The two countries have mobilized savings through their financial structures, but the mobilization has left the financial sectors in fragile states. Nonperforming assets in the banking systems as well as the nonbank financial sector (international trade and investment corporations in China) indicate a problem ahead. India has failed to impose arm's-length regulatory regimes free of politics and the result has been fraud and corruption in equity market-related activities—Unit Trust of India (UTI), stock market scams of Harshad Mehta, and so on.

It is difficult to predict whether a combination of budget deficits, domestic debt, and financial sector weakness will cause a major crisis in either country. Both have managed to run their external accounts fairly well. Their reserve positions are healthy, exchange rate policy—pegged to the dollar in China and a dirty float in India—are prudent. India has moved faster to full capital convertibility in recent years while financial sector reforms have yet to be fully undertaken. China has not moved as far with convertibility but its peg to the dollar may cause problems if the dollar weakens to any significant extent. India's foreign liabilities are more weighted toward the short run and portfolio end, while China has a larger FDI flow. The Asian crisis reminded us that even sound macroeconomic performance is no guarantee against a run on the currency if the markets suspect a mismatch between internal and external balance. Here it is India which is more fragile than China.

#### 1.4 Speculations and counterfactuals

I now turn to some very broad and highly speculative considerations. Having looked at China and India over the years since 1820 against a longer background, it is worth exploring a longer future. What follows is even more my own view than what has been said so far. In a *long duree* perspective, the present strong relative position of China can be attributed to the radical changes there since 1978, thanks to Deng. Of course the foundations laid in

the first phase wherein China doubled its per capita income obviously helped. But the similarities in their respective per capita incomes in 1980 merely reflects the longer history of the two countries. *A priori*, there is no reason why China should have opened such a large distance in such a short period of time. This is especially so because as I have already remarked earlier, China adopted a policy which it was always possible for India to adopt. Indeed anyone looking at the two countries at any time between 1950 and 1975 could have thought that India had a better capitalist infrastructure as well as commercial culture than China had. The diasporas of both China and India have always been adept at commercial activity so there is nothing in Chinese or Indian culture as such which could make a difference. The difference arises out of the political and institutional differences inside the country and these are very much short run and changeable.

### **1.5 Can China combine capitalism with one party rule?**

China appears to have been able to separate the political institutions of a Leninist state with single party dominance from its economic imperative of state ownership of all means of production. This is unique in the political economy of modern times. The transition is not yet fully complete as there is still a lot of central control over economic life and a large state-owned sector. It would be a bold person who could predict how far China could go in this separation. Thus could one have a fully capitalist or even a largely capitalist economy with a Leninist state? This is not the same as market socialism but more like state capitalism, although the word has now been much maligned in the polemics on the left. When Lenin spoke of state capitalism, he had the German war economy during the First World War in mind—a private ownership economy run in a centralized fashion.<sup>34</sup> The Chinese version of state capitalism could in the limit amount to private diffuse ownership with single party monopoly of political power. Is this feasible or likely?

Normally we associate rise of democracy with a prosperous middle class with plenty of “bourgeois” elements. A private ownership economy is bound to require a lot of economic freedom and as we are all crude materialists in this matter, we associate economic freedom with political liberties. While there is some opening out in the direction of separation of powers in some local jurisdictions,<sup>35</sup> it is difficult to envisage separation of powers in the absence of multiparty democracy with free elections and a possibility of change of the party in power. China's experiment is thus one of the most interesting episodes in modern political economy. Will China be able to sustain one-party rule with a private enterprise economy? Is state capitalism feasible in peaceful post-revolutionary times?

The implicit Chinese answer seems to be that if the Chinese Communist Party (CCP) delivers on fast and sustained economic growth while restructuring

the economy continuously in a capitalist direction, then the CCP monopoly on political power will become feasible with limited concessions such as separation of powers but no party competition. Marxian and every other political economy says that this is not easy, even not possible.<sup>36</sup> Economic freedom will spill over into demands for political freedom. Even authoritarian governments—that is, noncommunist dictatorships—have been unable to sustain a monopoly on political power with developed capitalism. Leninist state formations in Europe collapsed along with their economic forms. Apart from China, only North Korea and Cuba remain as major non-capitalist economies and non-liberal democratic polities. Can China defy the so-called laws of historical materialism (or even cross section growth regressions of new political economy) and avoid the transition to democracy?

One particular problem in this respect relates to the legal framework. While civil and political liberties can be curtailed, once you grant property rights certain liberalizing consequences inevitably follow, as any eighteenth-century political economist will tell you. Thus, the Communist Party *qua* contractor or buyer and seller of property cannot be above the law. There has to be accountability and auditing, legal sanctions and punishments for non-delivery or nonperformance. From this requirement follows the need to have law courts and a legal profession which enjoy a certain degree of immunity from the perennial habits of communist parties to bully if not liquidate all those who disagree with them. An independent legal profession needs further freedoms of speech and association and so on. It is this compulsion to establish a rule of law which will be crucial for China. In a fascinating and detailed study of the growth of the rule of law in China, Peerenboom makes the following observation:

In the end, however, a transition to democracy is likely to be necessary to overcome the [Communist] Party's legitimacy deficiencies, to address accountability issues, and to reduce growing social cleavages. It is possible that over time the Party could stave off extinction by transforming itself into a Social Democratic party. The Party could well gain support of its citizenry if in the next decade it is able to reduce corruption to a tolerable level and to sustain economic growth while dealing with such pressing problems as SOE [state-owned enterprise] reforms, reform of the banking and financial sectors, and the need to establish a social security system and to clean up the environment. It could further broaden its appeal by gradually relaxing its grip on society and allowing citizens greater, albeit still limited, freedom of speech, assembly, and association. In short, it could adopt a more communitarian approach. If it does not, and elections are held, it could very well lose out to the party that does adopt such an approach, all else being equal.<sup>37</sup>

This is a tall order for any country much less China. Indeed India itself has not eliminated corruption nor reformed its banking and financial sectors.

But people will tolerate corruption if they can throw the corrupt out of office, even if this exit is only through a revolving door. Democracies coexist with all sorts of imperfections and can indeed even withstand a lot of misery unlike authoritarian regimes, as the fate of the USSR in face of the stagflation crisis of the 1970s showed in contrast to Western economies. What Mrs Thatcher could do to the British economy, Brezhnev, Chernenko or Gorbachev could not. So China does not have to make things perfect if it can only grant bourgeois freedoms to its people. If not it has to be better than the most perfect democracy. Can China find its way out of this paradox?

My interim answer to this is that the odds are stacked against China being able to do this. Not that it is impossible or even unlikely but the odds are not favorable. There is one major reason for this, for which I appeal to Chinese history. This is China's inability to handle dissent and defiance of central rule without a lot of damage. The episodes of the Taiping and Boxer Rebellions in the Imperial era and GPCR, as well as the 1989 troubles which were not confined just to Tiananmen, show that China is fragile if not brittle when it comes to dissent. In the next ten years, China will be adjusting to economic restructuring in response to the demands of the World Trade Organization (WTO), as well as facing up to global media exposure due to the 2008 Olympic Games. It will be an open invitation to human rights movements and Falung Gong to expose the regime to international scrutiny. Moscow's experience of the 1980 Olympic Games proved crucial in the way the Soviet Union collapsed. What about China?

I expect China to survive as a powerful economy, but after a short period of political turbulence on the lines of the Taiping Rebellion or GPCR. China will be forced to make a political transition as profound as the Eastern European states did with their economies. The final shape will be a more democratic China, but it may not necessarily be a liberal democratic Western-type regime. There are after all living examples of "less-than-liberal" democracies—Singapore, Taiwan, Malaysia—which China can follow. You can have a multiparty democracy with a single party dominance as in Mexico and Japan, and India till 1989. One can also have dual power as in Iran, with the Ayatollahs vying for control with a democratically elected power. There are many choices on the way to a full transition to liberal democracy.

## **1.6 Can India catch up with China?**

India has problems about delivering strong, focused government pursuing a single objective with total commitment. Its great achievement is to have constructed the world's most populous democracy against all the odds—illiteracy, multiple languages and religions, racial and social heterogeneity. There have been spurts of committed action—in the mid-1950s when the Second Five-Year Plan was formulated, in the early 1970s when Mrs Gandhi pursued her anti-poverty program, in the mid-1980s when Rajiv Gandhi

pushed the import liberalization policy harder, the early 1990s with Narasimha Rao and Manmohan Singh liberalizing the economy, and finally in the last five years when the reform process has been kept up rather than reversed as many had feared. The average growth rate has gone up from 3.5 percent in the 1970s to 5.5 percent in the 1980s and now to 6.5 percent in the past decade.

India has also achieved another miracle relative to many post-colonial societies. It has maintained its territorial integrity, unlike for example Pakistan. It has not had a civil war, unlike Nigeria or Sri Lanka, and while multiethnic federations such as the former Yugoslavia and the USSR have broken up, India has not. This has absorbed resources as India has had to fight subnationalisms in the northeast Nagaland, in Panjab with Khalistan, and in Kashmir with international subversion added to internal dissension. It has had communal strife between Hindus and Muslims, Hindus and Sikhs, between caste Hindus and Untouchables/Dalits and so on. It has also faced class-based revolts in Telangana in the 1940s, in West Bengal, Andhra Pradesh, and Bihar with the Naxalites. Through all this it has survived as a democratic open society based on consensus and debate. Life is about more than per capita income and its growth.

For India any hope of growing faster depends on less government rather than more, on harnessing the private sector entrepreneurial talent which has always been there but was stifled for a long time. This requires a less interventionist government but also a better regulatory regime. India's bane is the politicization of all aspects of economic life and the difficulty of constructing an arm's-length regulatory regime free of political interference. This is because of and despite its democratic politics.<sup>38</sup> Thus even after a major stock market fraud or the mishandling of Unit Trust of India (UTI) customers' investments, there has been little by way of punishment. Indeed, a large number of financial scandals have thousands of victims but no culprits convicted.<sup>39</sup> One cannot expect a flourishing private enterprise culture in the absence of trust and effective regulation. Thus a black economy, smuggling, and criminalization of financial markets flourish. Depoliticization of the economy, therefore, remains a challenge. This is the same challenge as the more frequent complaint about control of the budget deficit, because the deficit is due to the compulsions of consensual politics with a coalition government and weak powers over regions.

What then are the chances for India that we may see a strong effective government emerge at the Center with effective fiscal control over its own budget as well as the budgets of states and an ability to depoliticize regulatory structures? Herein lies the deep dilemma of the Indian polity. India was set up after Independence as a federal polity because of the awareness of the first generation of leaders of the difficulty of holding the various linguistic and religious groups together. Indian nationhood was defined as unity in diversity. But lately a new, more unitarian construction of Indian nationhood

has been advanced by the forces of Hindutva nationalism. Thus far, it has been muted in its approach, but is also quite successful. If in the forthcoming months and years the Unitarian approach were to be pursued harder and if it was to be electorally successful, then India may emerge simultaneously as a nonsecular, majority Hindu polity with single party dominance by the BJP and its parivar. The advocates of Hindutva often cite Israel as their ideal example.

Historically, modernity in India was supposed to come with a secular and perhaps even socialist society. This was certainly Nehru's ideal, as well as practice, and at least the rhetoric if not practice for the two Gandhis. But the events of the last ten years or so raise the serious possibility that modernity in India will come with a Hindu or religious rather than secular as well as a capitalist dispensation. It is conceivable that such a Unitarian nationalism may accelerate growth by following a more liberal policy. But it is also likely to lead to greater social disharmony. Of course a majoritarian rule of the largest religious group is possible with nondiscrimination of the minorities, but in the Indian context and given the history, it is not very likely.

## 1.7 Conclusion

My own view is that India will remain a soft state, a consensual polity, and it will not be capable of sustained growth at the sort of rates which China has attained. To stay a stable, peaceful society, India has to be a muddle and a mess. It is a miracle that proceeding in the way it has done, it has come as far as it has done, trebling its per capita income. But there will not be growth convergence between China and India.<sup>40</sup> India and China will both remove poverty in their midst and cease to be bywords for misery that they had become for 150 years after 1820. China will again become a viable Great Power; India may become just a Great Democracy.

## Notes

1. Emeritus Professor of Economics, London School of Economics; Founder-Director, Centre for the Study of Global Governance; and Member of the House of Lords, The United Kingdom Parliament.
2. Beyond this vague assertion I do not intend to go into statistical measurement problems.
3. Dharma Kumar (1998), who independently made comparative estimates of India and China over the early twentieth century, arrives at not dissimilar estimates. She puts India's per capita income as US\$60 in 1952 and China's as US\$50 (at current prices).
4. Kumar (1998).
5. Maddison (2001).
6. Spence *et al.* (1999, p. 426).
7. Nehru (1946) and Keay (2001).
8. Inden (1999).

9. Maddison (2001, p. 99).
10. I am treating the Manchus as not being foreign, though many Chinese at the beginning of the twentieth century emphasized that they wanted to remove the Manchu empire and establish a Chinese republic.
11. Desai (2000).
12. I have learned a lot about federal structures and federalism in India while co-supervising Katherine Adeney (see Adeney (2003)).
13. Myrdal (1968).
14. Spence *et al.* (1999).
15. Deng (2000, p. 6) surveys this literature. There has been a similar though less extensive discussion among Indian historians as to whether India could have had its own capitalist revolution (see Habib (1971)).
16. See O'Leary (1989) for a critique of the Asiatic Mode of Production (AMP). Also see Habib (1983) for a sympathetic account of Marx's views on India, and Deng (2000), who sees the AMP as a useful concept.
17. Needham *et al.* (1954).
18. Needham *et al.* (1954) and Habib (1995).
19. Oriental Despotism, a notion begotten by Wittfogel from Marx and Engels's AMP, was supposed to be good at hydraulic projects. Be that as it may, the abandoned city of Fatehpur Sikri is a monument to how a Mughal king built a city where he failed to provide water supplies.
20. See Heston in Kumar and Desai (1983).
21. Dreze and Sen (1989).
22. The distinguished French anthropologist Louis Dumont has celebrated India's inegalitarianism in his *Homo Hierarchicus* as well as other books (see Dumont (1980)).
23. The usual exception in India is of course Kerala, which shows what can be achieved even in a democratic society by committed public action. Kerala has had the benefit of a democratically elected Communist government ever since the mid-1950s. But historically Travancore Cochin, which was the native state in what became Kerala, had a higher literacy rates even by the 1940s than its surrounding British India districts. Matriarchy and Christianity plus an enlightened ruler played their role here.
24. Maddison *et al.* (2002).
25. Desai (1975).
26. For those old enough to recall these arcane labels.
27. In China's case, the SEZs are not all that different from the foreign concessions in ports which were so much resented before 1949.
28. Kumar (1998)
29. See Baum (1994) and Shirk (1993).
30. After all, the establishment of Imperial authority had to go through such transition periods throughout Chinese history, but to support that claim will take me too far away from my theme as well as my competence.
31. Joshi and Little (1994).
32. For recent restructuring efforts in the organized private sector in India, see Forbes, N. (2002) in *Doing Business in India: What Has Liberalisation Changed?* (ed. by Krueger, 2002).
33. An old fashioned Hayekian word.
34. Desai (2002a).
35. For example, SEZs in China such as Shenzhen.

36. See Moore (1971) and Desai (2002a).
37. Peerenboom (2002, p. 5723).
38. Desai (2002b).
39. See *India Today* (2003) for a recent list.
40. Except unless China has a long breakdown in its transition to democracy.

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