

ANALYZING THE FINANCIAL AND ECONOMIC RIVALRIES BETWEEN CHINA AND INDIA AND THEIR CONSEQUENCES ON THE WORLD ECONOMY FOR INTERNATIONAL FINANCE

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ABSTRACT

Since the last decade of the 20th century China and India have become emerging economies with GDP rate growths systematically and widely exceeding those of the world economy. Both countries have become powerful players in the world economy. Therefore, it is relevant to study some of the most conspicuous positive and negative sides of their paces of development.

This paper analyzes the economic, political, and social similarities and differences between these countries. This analysis is done in the context of the sustainability of their policies with special consideration of their aging populations in close relation with their support ratios, and the application of expansionary fiscal policies under different political systems in the largest democracy of the world and in the largest market - leninism system of the world.

The paper intends to establish a comparison between India and China and to anticipate their perspectives of development in a holistic way.

INTRODUCTION

China and India are the two largest countries in the world measured by proportion of the world's population in each of the countries. The Population Reference Bureau estimates the total world population, as of mid-2012, is 7,058,000,000. China's mid-2012 population, estimated by the same source, is 1,350,378,000, or 19.1% of the world's population. Using the same source, India's population at mid-2012 is 1,259,721,000, or 17.8% of the total. Together the two countries are home to almost 37% of the people in the world.¹

In addition to the population measurements, China and India are two of the largest economies in the world. World Bank data place China as the second largest economy in the world and India as the fourth largest economy in the world. Those data rank the United States as the largest economy in the world.² Several sources estimate that currently China is experiencing 8% and India is experiencing 5% annual GDP growth. Those sources expect China and India to each maintain approximately those growth rates for a number of years.³ There are no estimates that the United States can expect such GDP growth in the coming years.

China and India are big and growing. Population growth trends are different in the two countries, however. The Population Reference Bureau estimates India will be larger than China, based on population, before 2050.⁴ The population growth trends in the two countries indicate different social situations in the two countries will continue as they advance through the twenty-first century. Those social situations currently differ due to India’s democratic system and China’s market-leninism form of government. The economic differences between the two countries will be magnified over time as long as those fundamental social systems remain unchanged.

The political and social paths upon which China and India continue during the remainder of the twenty-first century will necessarily be tied to their economic fortunes. China is trying to advance economic change without advancing political freedom. India is attempting to continue economic growth without addressing serious social problems. What happens to 37% of the world’s people is important to the global economy.

POLICAL FACTORS

India and China are strikingly different from a political standpoint. While India is the largest democracy, China is the largest dictatorship. *Freedom in the World* yearly surveys indicate India’s status is a free electoral democracy with good rankings in Asia while China’s status is non-free as shown in Table #1.

Table #1- Political rights, civil liberties and status for India during 2010 – 2012⁵

Country	PR 2010	CL 2010	Status 2010	PR 2011	CL 2011	Status 2011	PR 2012	CL 2012	Status 2012
India	2	3	Free	2	3	Free	2	3	Free
China	7	6	NF	7	6	NF	7	6	NF

The number 2 rating in political rights (PR) refers to countries having slightly weaker political rights than those with rating 1 due to some political corruption or limits on the functioning of political parties and opposition groups. A number 3 rating in civil liberties (CL) includes those governments with unequal degrees of protection to different civil liberties. The worst score in political rights is number 7, while the worst score in civil liberties is number 6.

Another important factor in this context is the index of democracy. Results for that index, during select years, for India and China are shown in Table #2.

Table #2 Index of democracy⁶

Year	Rank	Overall score	Electoral process	Functioning of government	Political participation	Political culture	Civil liberties
INDIA – Flawed democracy							
2006	35	7.68	9.58	8.21	5.56	5.63	9.41
2008	35	7.80	9.58	8.21	5.56	6.25	9.41
2010	40	7.28	9.58	8.57	4.44	4.38	9.41
2011	39	7.30	9.58	7.50	5.00	5.00	9.41
CHINA - Authoritarian regime							
2006	138	2.97	0.00	4.64	2.78	6.25	1.1
2008	136	3.04	0.00	5.00	2.78	6.25	1.18
2010	136	3.14	0.00	5.00	3.89	5.63	1.18
2011	141	3.14	0.00	5.00	3.89	5.63	1.18

India’s ranks, overall scores and individual indicators related to functioning of government and political participation show a fluctuating trend. As a whole the democracy index is not improving. If India could maintain indicators in the levels of “electoral process and pluralism” and “civil liberties”, it would surely occupy a higher rank and overall score as a full democracy. China’s indicator levels are much worse than India’s. While India is classified as a flawed democracy, China is considered to be an authoritarian regime.

The Indian state is relatively weak and unstable. The Chinese state is stronger. Indian political parties are relatively weak because they are not supported by social institutions and are afraid to adopt economically necessary measures that might unleash upheavals in the population. In China there is only one political party which imposes its power through strong repression. However, China’s communist dictatorship is cautious about inflation and unemployment because those have been the main factors leading to events such as the Tiananmen Square revolt in 1989. In addition, the increasing environmental damage originated by the sustained high rates of GDP growth of the Chinese economy has been responsible for a considerable increase in protests both in the Western and the Eastern provinces.

Corruption is present in both countries as shown in the following table. The index of corruption is established between 10 (zero corruption) and 0 (absolute corruption).

Table #3 Index of corruption according to Transparency International in India and China⁷

Year	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Index of Corruption										
India	2.7	2.8	2.8	2.9	3.3	3.5	3.4	3.4	3.3	3.1
China	3.6	3.5	3.6	3.6	3.5	3.3	3.2	3.4	3.4	3.5

As can be seen from data Table #3, there are no significant differences in the levels of corruption of both countries. Indian corruption shows slight improvement, but the level of corruption in China has remained relatively constant. As far as their ranks are concerned, India ranks 95th and China ranks 75th out of 182 countries.

With indexes of corruption ranging from a maximum of 2.7 in 2002 to 3.5 in 2007, India’s corruption is decreasing. According to Agarwal⁸, the most relevant facts gathered from a survey to 1,069 respondents in India are the following: a) sector-wise, on a scale of 1 to 5 (1 meaning not at all; 5 meaning extremely corrupt) – political parties scored high (4.6), followed by police (4.5), parliament/legislature (3.9), legal system (3.8), and registry/permit services (3.7), while the least corrupt service is perceived to be the military (1.8); b) poor families were perceived as hit hardest by demands for bribes; and c) as compared to 2006, there was a perception of deterioration in all the sectors, except the military.

Corruption in the Indian political parties is extremely high. In 2010, according to the Economist⁹ India was considered to be an emerging economy, despite having a weak state and weak political parties (both stifled with corruption), because of strong private companies. The Economist¹⁰ included among India’s economic advantages a younger labor force, explosion of commercial energy, growth driven by 45 million entrepreneurs to satisfy the needs of domestic consumers as a primary focus, and a potential great level of consumption. However, at the same time the source noted disadvantages for the Indian economy which included lousy infrastructure, shortage

of skills as a bottleneck, deficient public schools, and increasing corruption, especially in the political parties and the government. As stated in the Economist, “In the old days ministers asked for bribes. Now they demand shares in firms to which they are about to award contracts.” Business firms are mostly clean, but, “The messy stuff mainly occurs in transactions that involve land, public contracts or natural resources. Yet the rot in these areas is so bad that it threatens to undermine the moral legitimacy of capitalism itself.”

As recently as in 2012, The Economist¹¹ contained an analysis about how weaker national parties, stronger regions, new voter habits and corruption are changing India’s politics. Concrete examples are cited like, “one politician was recently filmed telling officials that it was acceptable to steal, and several ministers were sacked earlier this year for pocketing \$1.2 billion from a scheme supposed to help sick villagers. A political party is said to clear business projects in exchange for 30% equity in them. One satrap is believed to have become the biggest property developer in India.”

The specialized literature on China’s politics frequently mentions the presence of corruption such as the Economist¹², stating that “In China cronyism is even more ingrained. The state still has huge control over resources, whether directly through state-owned enterprises, monopoly control of industries from railways to mining or the distorted financial system, where interest rates are artificially depressed and access to credit is influenced by politics. The importance of the state means that the beneficiaries tend to be close to state power. “

The Financial Times¹³ refers to General Mao, who is the youngest major general in the history of the People’s Liberation Army: “ Gen Mao’s implicit criticism of his peers highlights a phenomenon party insiders say has become much worse in the past decade, and has been forced into the spotlight with the downfall this year of Bo Xilai, previously ranked 25th in the ruling party hierarchy. In a system that still calls itself communist but thrives on cut-throat capitalism, a group of powerful political families and their hangers-on have become fabulously wealthy while ignoring the rules and laws they set for the rest of society.”

In reference to the princelings and important political leaders, the Financial Times article states that premier Wen Jiabao, in an official journal in April, “railed against rampant corruption in the Communist Party.” Nonetheless, continues the article about Wen Jiabao: “But of all the families of senior party officials, his is the most notorious for its extensive business activities, and the advantage it has allegedly taken of his position at the pinnacle of power. His wife, Zhang Beili, is a famous businesswoman in the diamond and gem industry with a penchant for expensive jewelry. His son Winston blatantly uses his political background to get deals.”

Both in India and in China corruption is rampant, and corruption in both countries been growing at a high pace since the beginning of the current century. It appears that there is some relationship between rapid growth and rampant corruption in democracies and dictatorships. Nonetheless, the gap between the GDP growth of China and India is widening in favor of China (as shown in Graph #1) while at the same time corruption is somewhat higher in India than in China.

Graph # 1 – GDP growth gap between China and India¹⁴

SOCIAL FACTORS

The reduction of poverty requires economic growth as a necessary condition. There also is need for political will if a government is to reduce income inequality. Strong leaders are needed to increase taxes to the wealthiest class while reducing taxes to the middle and the lower classes, to increase financially grounded government investments in infrastructure and education and to control corruption. The Scandinavian countries are some of the best examples of successful combination of stable GDP growth rates, the lowest Gini coefficients, the highest levels of taxation, and the lowest poverty rates in the world.

Chavakraty's paper¹⁵ cites the following phrases from Deng Xiaoping, "It doesn't matter if the cat is black or white so long as it catches mice' and 'Poverty is not socialism. To be rich is glorious'. But there's another, less well-known and even more controversial quote also attributed to him: 'Let some people get rich first.' Deng doesn't seem to have been too bothered about inequality." The aforementioned author cites that the Chinese Gini coefficient worsened from 0.32 to 0.43 between 1990 and 2008 whereas for India, the indicator deteriorated from 0.32 in 1993 to 0.37 in 2010. It is interesting to note that Taiwan's coefficient was 0.34 in 2010¹⁶, and the openly capitalist country was evaluated with a corruption index of 6.1 (twice as high as China's) and ranked # 32 in the world scale.

According to INDEX MUNDI, The population below the poverty line in India has been reported as equal to 35% in 1994, 28% in 2000 and 25% in 2007. In China this indicator has shown to be equal to 10% during 1990 – 2004, 8% during 2005 – 2009, and 2.8% in 2011.

The Chavakraty paper includes an interesting comment about the relationship between percentage of employment growth (in the numerator) and percentage of output growth (in the denominator): in India this indicator has declined from 0.53 in the 90s to 0.41 nowadays. The real wage growth (2%) has been lagging behind the productivity growth (7.4%) during 1990-2007. Capital has benefited while labor has been harmed. In China the results of this indicator show an inverse relationship. On top of that, India's numbers have fluctuated considerably¹⁷ as in the period 1998 – 2003 with decreases in two digits in relation to years of small reductions and increases with a maximum of 2.7 and a minimum of 0.1 in the period 2005 – 2011. However, in China average real wages have been consistently higher than the labor productivity growth with an average range of approximately 2%.

Hotze, T.¹⁸ in an extensive study of poverty in India states, "... nearly a third of the urban population lives below \$1.25 a day, and 60% lives on less than \$2 a day, PPP. In fact, as a cut off

line, 90th percentile of the urban population still makes less than 70 Indian rupees a day. As was the case with inequality in India, official government of India statistics hide the extent of poverty and make Indian economic performance to seem relatively stronger than might otherwise be the case using more widely-seen definitions.”

The comparison between India and China in the social context can also done in connection to education and healthcare based on data taken from The World Bank¹⁹:

In relation to education: a) Expenditures in education as % GDP: India with 3.09% in 2006 with a world rank of 144; and China 1.91% in 1999 with a rank of 172. b) Public spending in education as a percentage of total government expenditures: India with 10.74% in 2003 with a world rank of 145; and China with 12.97 in 1999 with a rank of 109. c) Literacy at age 15 and over (read and write): India in 2007: 61% in general – male 73.4% and female 47.8%. China in 2007: 92.2% in total – male 96%, and female 88.5%. d) School life expectancy (primary to tertiary education): India in 2007: 10 years in total – male 11 years, and female 10years. China in 2007: 12 years in total – male 11years, and female 12 years.

In relation to healthcare: a) Health expenditures as a percentage of GDP in 2009: India – 2.4%, and China – 4.6%. b) Physicians density per 1000 people in 2005: India – 0.599, and China 1.415. c) Hospital bed density per 1000 people in 2005: India – 0.9, and China 4.06.

Because infrastructure is a necessary condition for social and economic development, it should be included in this comparison. The analysis of the data contained in table #4 can be summarized as follows: a) China’s infrastructure is better than India’s, not only in absolute numbers, but also in relative numbers per capita, and b) the most noteworthy indicators are waterways, pipelines, merchant marine, airports, electricity consumption per capita, and internet users.

The Economist²⁰ states examples of the disastrous situation of infrastructure in India, such as: a) a quotation from Jairam Ramesh, minister of rural development last September, “India’s sanitation challenge, especially in rural India, remains humungous;” b) “ ‘We ourselves have no toilets at all’ according to Parmershwari, one of more than 600m Indians who lack even primitive toilet facilities and therefore practise what is known as open defecation;” and c) “Some 400,000 – 500,000 children under five die each year from diarrhea in India, ‘largely caused by unhygienic practices including improper disposal of human excreta’ .”

Another paper from The Economist²¹ explains the main reasons why farmers in India are transferring to the cities at a slow pace. Collectively the rural voters have clout as shown by the fact they are subsidized, i.e. the government pays inflated prices for wheat and rice. However, the worst schools and health care facilities are located in villages. Approximately 30% of the Indian population dwells in urban areas while in China just over half the population is now urban.

Table #4 Transportation indicators in India and China²²

Type of transportation	INDIA's population: 1,189 million in 2011	CHINA's population: 1,335 million (2011)
RAILWAYS	total: 63,974 km (0.0538 km/million people)	total: 86,000 km (0.0644 km/million)
ROADWAYS	total: 3,320,410 km (2.79 km/million) expressways: 0.00006 % (2009)	total: 3,860,800 km (2.89 km/million) paved : 79% expressways : 1.6% (2007)
WATERWAYS	14,500 km (0.012 km/million) - (2012)	110,000 km (0.082 km/million) (2011)
PIPELINES	condensate/gas 2 km; gas 9,596 km (0.008 km/million); liquid petroleum gas 2,152 km; oil 7,448 km (0.006 km/million); refined products 10,486 km (2010)	gas 38,566 km (0.028 km/million); oil 23,470 km (0.017 km/million); refined products 13,706 km (2010)
MERCHANT MARINE	total: 340 (0.00028 ship/million)	total: 2,030 (0.0015 ship/million) tanker 2, vehicle carrier 23
AIRPORTS	352 (0.000296 airport/million) (2012)	497 (0.0003385 airport/million) (2012)
AIRPORTS – WITH PAVED RUNWAYS	251 (71.3%)	452 (90.9%)
AIRPORTS – WITH UNPAVED RUNWAYS	101	45
Electricity consumption per capita (kWh/person)	India 411 in 2000, 472 in 2005, 450 in 2008, 478 in 2011	China 804 in 2000, 1,248 in 2005, 2150 in 2008, 2572 in 2011
Mobile cellular subscriptions	India - 752,000,000 units 0.63 per person	China – 986,253,000 0.74 per person
Internet users	India – 61,338,000 units 0.05 per person	China – 389,000,000 0.29 per person

Sustainability is closely related to maintaining socio-economic stability in the short, medium and long terms. Therefore, the analysis of demographic parameters should be included in this comparison.

Table #5 – Demographic parameters related to aging populations in India and China²³

Life expectancy at birth						
Country	2000	2005	2009	2010	2011	
India	62.5	64.35	69.89	66.46	66.8	
China	71.38	72.27	73.47	74.5	74.7	
Age structure						
Country	0-14 years 29.7%		15-64 years 64.9%		≥ 65 years 5.4%	
India	Male 187.5 m	Female 165.4	Male 398.7 m	Female 372.7 m	Male 30.8m	Female 33.9m
China	0-14 years 17.6%		15-64 years 73.6%		≥ 65 years 8.9%	
	Male 126.6 m	Female 108.4	Male 505.3 m	Female 477.9 m	Male 56.8 m	Female 61.5 m
Median age						
India : 26.5 years						
China : 35.9 years						
Other population indexes						
Country	Population growth rate	Birth rate		Birth rate in the world (221 countries)		
India	1.312 %	20.6 births per thousand people		85		
China	0.481 %	12.31 births per thousand people		159		
Country	Total fertility rate		Infant mortality rate			
India	2.58 children born/woman		46.07/1000 live births – male 44.71 and female – 47.59			
China	1.55 children brown/woman		15.62/ 1000 live births- male 15.38 and female – 15.9			

The analysis of the data shown in Table #5 can be summarized as follows: 1) China’s life expectancy at birth is higher than India’s by approximately eight years which corroborates that health care is better in China as previously stated in this paper, but the percentage of people needing pensions is higher in China. 2) India’s age structure is better than China’s because the former has a higher percentage (12% more) in the range 0-14 years and a lower percentage (3.5% less) in the range of retirement age. Economically speaking India needs to invest more in schools and to spend less in health and social security. 3) The median age is almost ten years higher in China than in India; in other words, 50% of Chinese people are at least 36 years old, while 50% of Indians are at least 26 years old. 4) Population is growing three times faster in India than in China. The birth rate in India is 1.7 times higher than in China, and the fertility rate in India is 1.6 times higher than in China. (“Rates above two children indicate populations growing in size and whose median age is declining. Rates below two children indicate populations decreasing in size and growing older.²⁴”) 5) China’s infant mortality rate is lower than in India, which corroborates that health care is better in the former. However, India has the potentiality of reducing its mortality rate if its economic situation continues improving.

The analysis of the demographic parameters suggests that China’s financial situation should face greater challenges than India’s since the support ratio – the relation between working age population versus retirement age population – in China tends to descend and demand a larger

safety net and consequently a sounder budgetary balance. Table #6 data related to the financial situation of both countries.

Table # 6 – Financial indicators in China and India during 2000 – 2011²⁵

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
CHINA'S FINANCIAL INDICATORS												
Budget balance/GDP	-2.5	-2.3	-2.6	-2.1	-1.3	-1.2	-0.7	0.6	-0.4	-2.2	-1.6	-1.1
Public debt/GDP	27.6	27.3	27.1	26.8	25.0	23.2	20.7	17.1	15.1	16.4	16.1	15.3
INDIA'S FINANCIAL INDICATORS												
Budget balance/GDP	-5.5	-5.8	-5.7	-4.4	-3.8	-4.0	-3.3	-2.5	-6.0	-6.4	-4.8	-5.7
Public debt/GDP	53.9	58.2	61.6	61.2	61.5	61.2	59.1	56.9	56.1	54.4	51.4	48.9

China's budgetary and public debt situations are better than India's. As long as China's GDP keeps growing faster than India's, the Chinese economy should be able to cope with its unfavorable demographic situation which is an additional pressure on the Communist Party of China to sustain high growth rates.

In the world arena²⁶, India's situation is more favorable than China's as far as increase in the working age population is concerned. India is projected to increase 38% during 2010 – 2035 being ranked as number five in the world; while China is expected to decrease between 7 to 8% and is ranked as number thirty in the world. Generally speaking economic growth comes from having more workers and/or increasing productivity. If a country has fewer workers as China is predicted to have not only considering graph # 2 but the analysis done on the content of Table #5, productivity becomes even more important, demanding higher and economically grounded investment.

CONCLUSIONS

India is the largest democracy of the world with a growing working age population; whereas China shows the opposite situation by being the largest dictatorship with a diminishing working age population. India is classified as a free country with favorable scores in political rights and civil liberties; and China, as a non-free country with unfavorable scores in the same categories. India's index of democracy - 7.30 - is far better than China's - 3.14. India is classified as a flawed democracy; while China, as an authoritarian regime. India's state and political parties are considered to be weak; while China's are stronger. Both of them are cautious about the social institutions which have considerable influence in the India's electoral process and are strongly repressed in China. Corruption is rampant in both countries with indexes of corruption in the range 3.1 – 3.5 over a maximum of 10. As far as their ranks are concerned, India occupies the 95th place, while China ranks 75th out of 182 countries. Corruption is, therefore, a big problem in both countries.

The Chinese Gini coefficient worsened from 0.32 to 0.43 between 1990 and 2008 whereas for India, the indicator deteriorated from 0.32 in 1993 to 0.37 in 2010. It is interesting to note that Taiwan's coefficient was 0.34 in 2010. The increase in corruption partially explains the deterioration in the Gini coefficient and its improvement in Taiwan. The population below the poverty line in India has been reported as equal to 35% in 1994, 28% in 2000 and 25% in 2007.

In China this indicator has shown to be equal to 10% during 1990 – 2004, 8% during 2005 – 2009, and 2.8% in 2011.

The indicators about education, healthcare and infrastructure show better results in China than in India, including life expectancy and infant mortality rates. Nonetheless, China shows an alarming situation in the demographic factors such as age structure, median age, population growth, birth and fertility rates, and especially in the percentage of working age population. India shows a much favorable situation in the latter indicators.

China's projection for the period 2010 – 2035 shows a decrease in the order of 7 to 8% in the working age population that, along with the increasing percentage of retirement age population, shows a decreasing support ratio, with the resulting increase in government spending to sustain the requirement of a growing safety net. As long as China keeps growing at high rates and maintaining low levels of budgetary deficit and governmental debt, the Chinese government might weather its demographic problems. It should be born in mind, though, that the structural changes needed for reducing investment and exports in favor of increasing consumption might pose additional challenges aggravated by possible social outbursts.

NOTES

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20. The Economist (2012), "Toilets and jobs in India", October 9.
21. The Economist (2012), "Concrete jungles", Special report on India, Sept. 29.
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23. Index Mundi (taken from CIA World Factbook) Accurate as of July 26, 2012
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25. EIU. Com
 26. The Economist (2012), “The Vanishing Workforce”, February 24.

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