

E-Notes

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Black Money & It's Impact On Indian Economy

There is no uniform definition of black money in the literature or economic theory. In fact, several terms with similar implications have been used including 'unaccounted income', 'black income', 'dirty money', 'black wealth', 'underground wealth', 'black economy', 'parallel economy', 'shadow economy', and 'underground' or 'unofficial' economy. All these terms usually refer to any income on which the taxes imposed by government or public authorities have not been paid. Such wealth may consist of income generated from legitimate activities or activities which are illegitimate. Thus 'black money' can be defined as assets or resources that have neither been reported to the public authorities at the time of their generation nor disclosed at any point of time during their possession.

Parallel Economy :

The term parallel economy is used in the sense that the black and white economy is separate from each other. But in reality it is the opposite. Particularly in India the black and white economy are mixed with each other. From the same economic activity one generates black income as well as white income. For example, in case of real estate business the purchaser has to pay some part of the payment as black component and remaining part as white component. Sometimes one can convert the black income into white income and vice versa.

In a broader definition parallel economy includes

(a) Illegal economy

(b) Unreported economy

Illegal Economy :

The economic activities allowed by law are called legal. The economic activities which are not allowed by law are called illegal activities. Income generated from illegal activities is not counted in national income. Incomes from illegal activity are not declared for tax purpose and thus generate black money. These activities include smuggling, human trafficking, arms trafficking as well as normal economic activities without paying tax.

Unreported economy: But sometimes people engaged in legal activity sometimes do not declare part of their income for tax evasion. This type of activity cannot be considered as legal. The tax evasion also generates black money. So in India the black money includes the entire illegal economy generating black money as well as undeclared income generating by normal activities.

Informal Economy:

94 percent of the workforce in India is engaged in Informal or Unorganised sector. The earnings in these sectors are very low. So most of the people working in the informal sector are out of the tax net and therefore income generated in this sector cannot be considered as black income.

But some people working in the informal sector may earn taxable income. But their incomes remain unreported and by this way the informal sector generates black income. But the vast majority in this sector cannot earn taxable income and thus do not generate black money. On the contrary many people in the formal sector like trades, corporate, brokers, builders generate huge amount of black income by keeping a major part of their income unreported.

Impact of Black money on Indian Economy

Effect on National Income:

Black money is generated through unreported income or low income to avoid tax. This results in low national income which in turn results in low investment and low productivity. If true income is revealed there will be a sharp increase in national income which may improve the quality of life for the entire population. Low level of national income creates shortages of resources for development plans, capital expenditures and essentials like education and health.

Loss of Government revenue:

The main source of Government revenue is tax paid by the people of the country. Black money is generated through tax evasion. It results in a loss of Government revenue. The amount of black money in India is so huge that it can run a parallel economy. If some part of it was transferred to Government exchequer as tax payment, then the development

programmes taken by the Government would be benefitted to a large extent and this in turn improved the conditions of livelihood of common people.

Vicious Circle: Black Money and Corruption

Indian economy is known for its corrupt practice. The problem of black money add to this and a vicious circle of black money and corruption takes place. Therefore black money is considered as a result as well as cause of corrupt economic activities. The bribes given by the people to the bureaucrats, government officials, etc. for getting their work done go to the unaccounted books and is never shown as income which adds more black money to the society. Black money has corrupted our political system in a most vicious manner and at various levels.

Higher Taxation and Inflation:

If the amount of black money is revealed and included in the budget then there may be surplus budget and the existing high rate of taxation will come down. Inflation or rising price are the result of too much money in circulation in the economy. The actual amount of money in circulation which includes black money is much higher than the calculated amount. The excess amount of money causes rising prices or inflation.

Difficulties in Monetary and Fiscal policy:

Monetary policy:

The main aim of central bank's monetary policy is to curb inflation. But because of the existence of huge black money it is not possible to estimate the actual amount of money in circulation. Actually the velocity of circulation of money is much higher than that calculated with white economy. This results in difficulties in controlling inflation. Under this situation the credit control policy of RBI does not work.

Fiscal policy:

The existence of black economy has serious consequences for fiscal policy due to **shortages of Government revenue and high cost of expenditure**. The black economy results in loss of revenue of about 25% of the GDP at current rate of taxes. In comparison the fiscal deficit is about 4% of GDP. If the black economy has not existed the revenue deficit as well as the fiscal deficit and the rising Government debt would be wiped out. A surplus budget may generate more investment in infrastructure and poverty removal.

Effect on Balance of Payment:

Balance of payment is adversely affected due to various reasons like Under-invoicing of exports shows less amount of export. It in turn shows large trade deficit. White economy data does not track activities like Under and over-invoicing of trade of goods and services. Illegal flows due to illicit activities. Flows through the parallel banking system like hawala.

Effect on poverty:

Substantial growth in black money, most of which is concentrated in the hands of a few richest people has very adverse effect on the people living at the lower income level. Both absolute and relative poverty grow with the growth of black economy. The disparities between rich and poor has grown significantly due to the growth of black economy.

Absolute poverty is also impacted due to the growth of black economy since the Government cannot spend enough for poverty removal programmes due to shortage of government revenue.

Illegal Financial Flow:

It has been estimated in a report of Global Financial Integrity (2010) that since independence 462 billion dollar has been lost due to illicit financial flow. These flows take place through shell companies set up in tax havens. This money laundering is indulged by businessmen, corrupt politicians, corrupt bureaucrats, professionals and others. As a result, a capital short country like India has lost capital on a large scale. If the amount lost was invested in the country, there would be a remarkable improvement in social and economic infrastructure and agricultural and industrial sector as well.

Increased criminal activities – The illegally earned income or the black income usually gives rise to various illegal activities. Local criminal activities are linked to global criminal activities through terrorism. These are done with the help of printing of counterfeit currencies, operation of ‘Hawala’, production and distribution of narcotics, arms trafficking, smuggling of electronic items, gold and gems.

Almost all the activities involve the secret agencies of our neighboring countries like Pakistan, Afghanistan, Bangladesh and Myanmar. Smugglers develop link with organized crime abroad. To do this they rely on Hawala operations. The profit generated from those activities finance terrorism to destabilize the country. Hawala operation in India grew in a large scale. They get political protection also because of the self- interest of the politicians.

Various murders are the result of black money which are done for political revenge and are done by the contractors engaged by the various political leaders. It is usually said money corrupts the life of even a normal person, and money in excess corrupts excessively. The situation is worse when that money is black money.

Impact of parallel economy or black money on real estate market in India

The parallel economy has an enormous effect on Indian economy. Particularly in the real estate sector the use of black money has become almost as a norm. It affects the real estate market in the following ways. Black money plays a huge role in the real estate market of India. It is one of the sectors where people with illegitimate income convert the black money into white money. The effects of black money in real estate market affect different people like buyers, promoters, politicians and bureaucrats, Govt. in different ways. There are two types of purchasers. One types are those who are honest and don’t have black money. And the other types who have huge amount of black money which they want to convert into white money through the payment as black of real estate property.

The promoters or builders always ask some part of the payment as black money from the purchaser to avoid tax. So the honest purchasers become deprived of getting a property in fair price and the people with illegitimate income can buy huge amount of property. The builders or promoters are most of the time encourage this corrupt system and generate huge amount of black money by which they can bribe politicians and bureaucrats. The honest businessman cannot survive in this system because they don’t have huge amount of unaccounted money to bribe politicians and Govt. Officials.

CONCLUSION:

The problem of black economy in India is huge and very much complicated in nature. There is no magic to solve the problem easily. It must be kept in mind that the heart of the problem is political.

The Black Economy causes various macroeconomic problems like fiscal crisis, inflation and BOP crisis.

Micro problems and sectoral problems caused by black money are poor living condition of the people, inadequate health and educational facilities and poor economic infrastructure.

The black economy adversely affected economic, social, political and cultural life of India. So it is our national interest to free the nation from the curse of black economy.

The Government, political parties and common people should move together to fight the problem and to make our nation a more civilized, democratic and socially developed society.

- **Reference**
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