

Black Economy – The Missing Policy Dimension.

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What is the color of your money?

“This is not a simple question, this is something we all will be answering 1 year
down the line.”

- Professor Amir Ullah Khan

Scenario 1



- Do you own a vehicle?
- How often do you pay in cash at a filling station?
- Does that make your money white?
- Do you know for sure that any further transaction done using your money will have a tax liability?

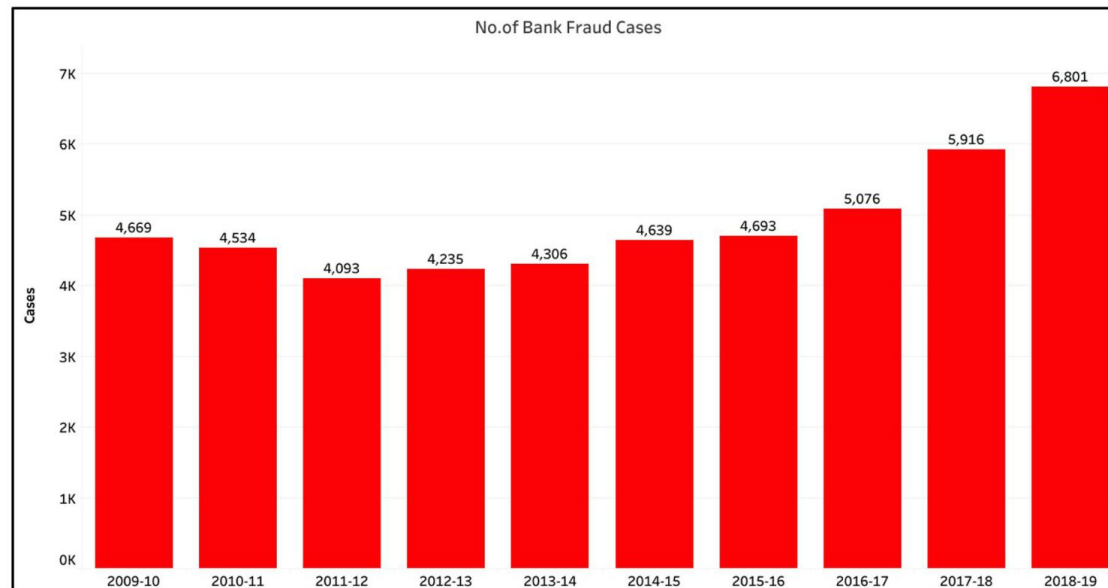
Scenario 2



- Khosla's have entered into a transaction with the real estate stalwart, and totally paid in cash out of his savings
- Do you think that this transaction will be accounted for fully in the economy?
- Do you think real estate sector is a generator or a circulator black economy?

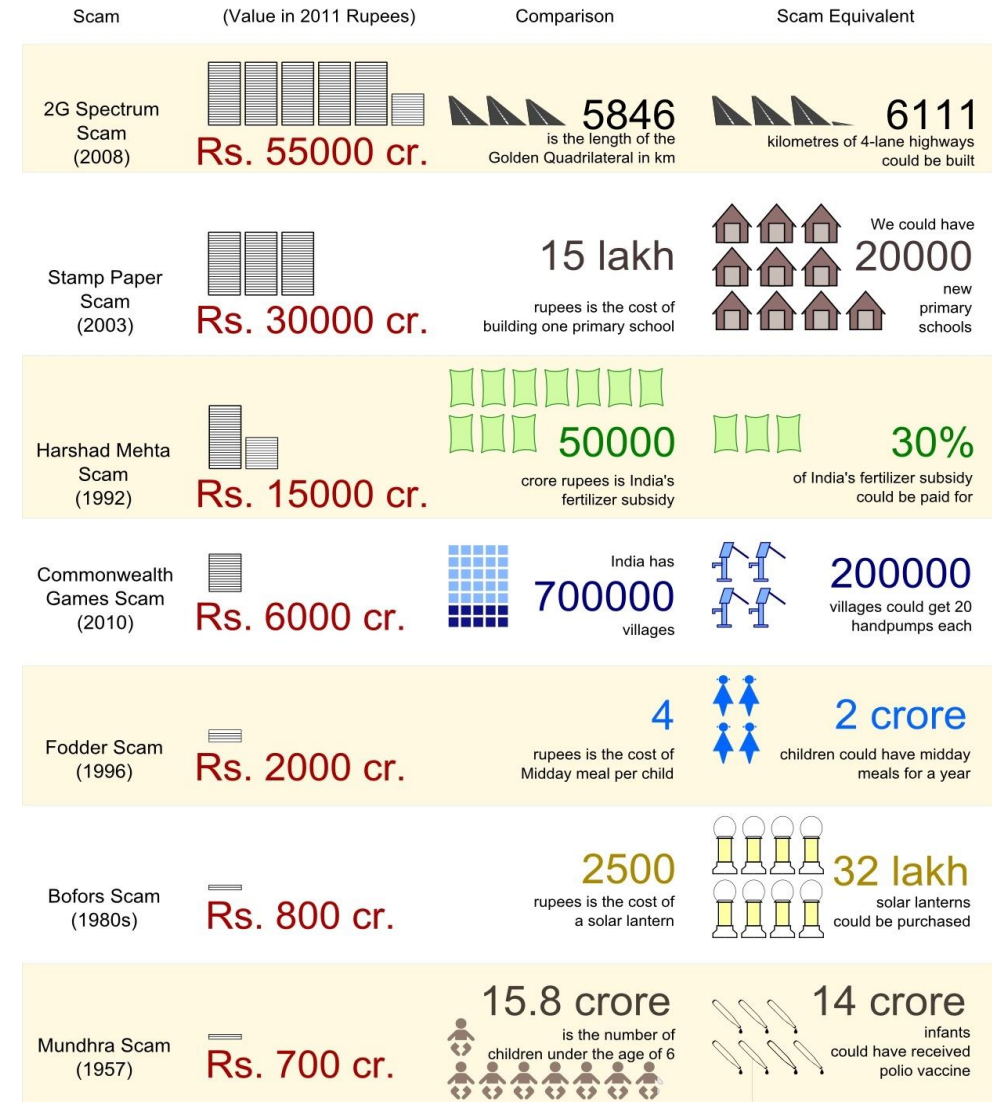
How large is India's Black Economy?

- \$272 billion (20% of GDP)
- \$454 billion (30% of GDP)
- \$636 billion (40% of GDP)
- Arun Kumar's estimate is around 62% of India's GDP in 2016 - 17



Illustrative

India's Biggest Scams (1947-2011)



Sources:

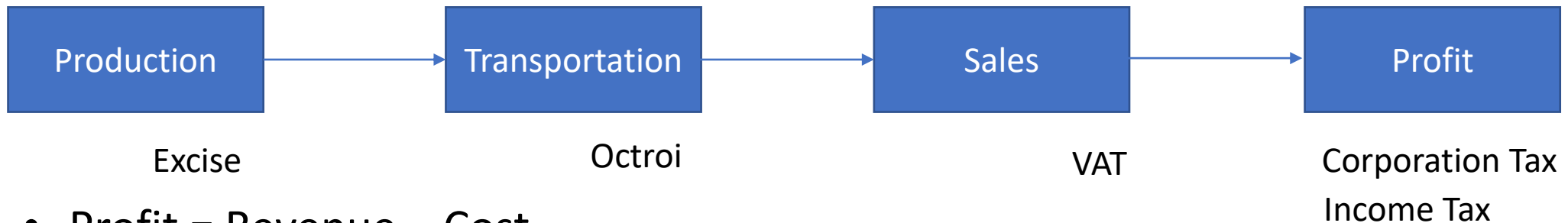
http://en.wikipedia.org/wiki/2G_spectrum_scam
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A Taxonomy of Black Economic Activities

Type of Activity	Monetary Transactions		Non Monetary Transactions	
Illegal Activities	Trade with stolen goods; drug dealing and manufacturing; prostitution; gambling; smuggling and fraud		Barter of drugs, stolen goods, smuggling etc. Produce or growing drugs for own use. Theft for own use.	
	Tax Evasion	Tax Avoidance	Tax Evasion	Tax Avoidance
Legal Activities	Unreported income from self-employment; Wages, salaries and assets from unreported work related to legal services and goods	Employee discounts, fringe benefits	Barter of legal services and goods	All do-it-yourself work and neighbor help

¹⁾ Structure of the table is taken from Lippert and Walker (1997, p. 5) with additional remarks.

Sugar Industry



- Profit = Revenue – Cost
- White Profit = Declared Revenue – Declared cost (Balance Sheet Profit)
- Black Profit = Undeclared Revenue + Overstated Costs (Off Balance Sheet Profit)

Macro Variables that get affected

- Employment
- GDP
- Taxes
- Inequality
- Wages
- Poverty
- Formality

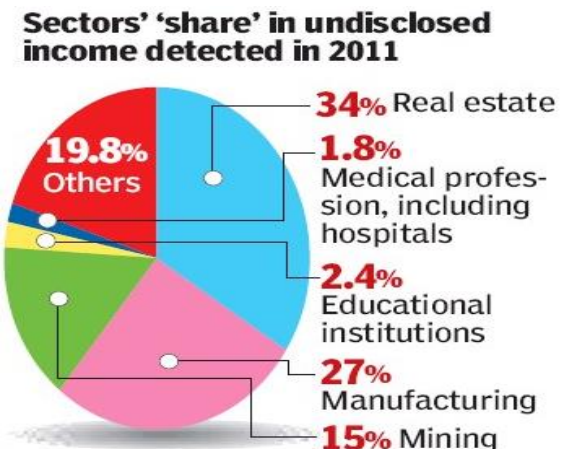
Incentive for a Black Economy Transaction

$$(\text{Success-Probability} * \text{Illegal-gains}) - (\text{Caught-Probability} * \text{Sanctions}) > \text{Legal Gains}$$

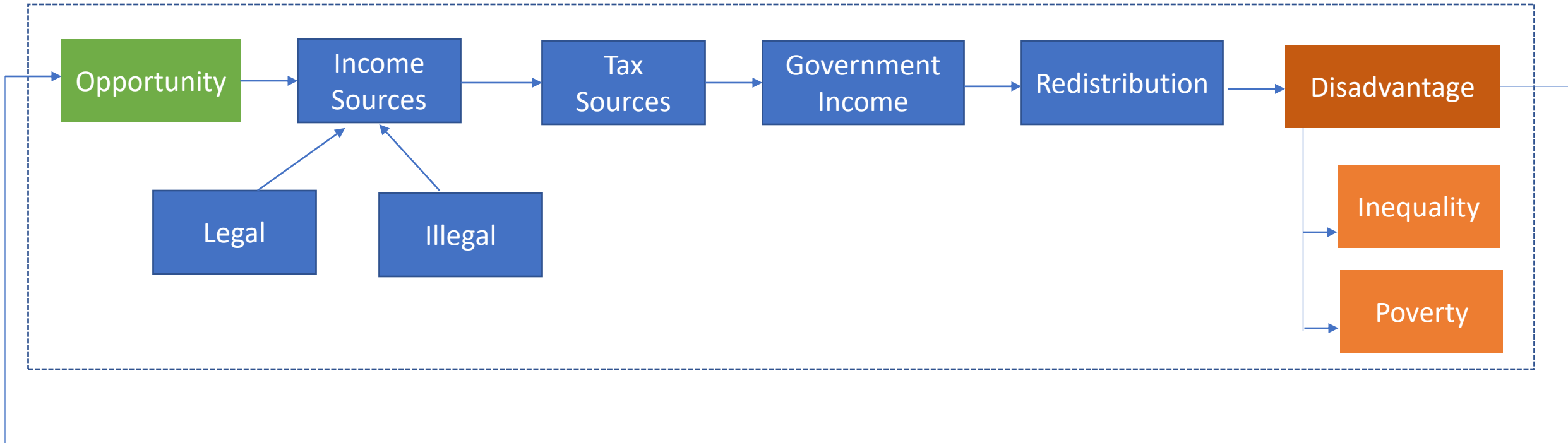
- (Success Probability + Caught Probability) = 1
- Probability will depend upon policing, other checks
- Sanctions go up LHS reduces
- Illegal gains go up LHS goes up
- It is clear that sanctions alone will not be able to deter evasion

Sectors that are affected:

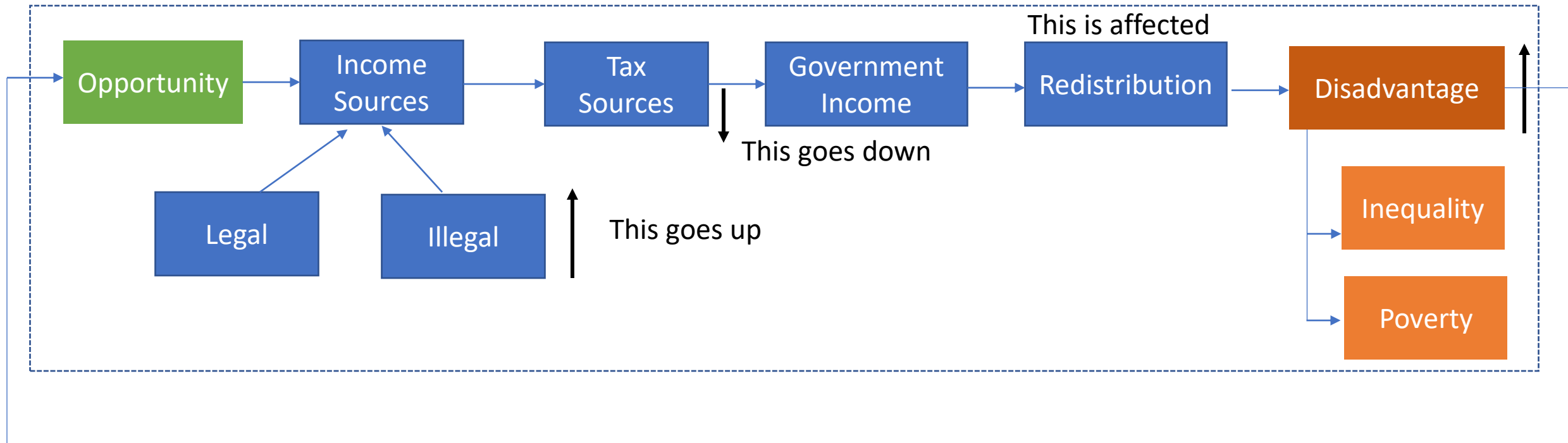
- Real Estate
- Land
- Jewelry
- Financial markets
- Public procurement
- Informal sector
- Cash economy



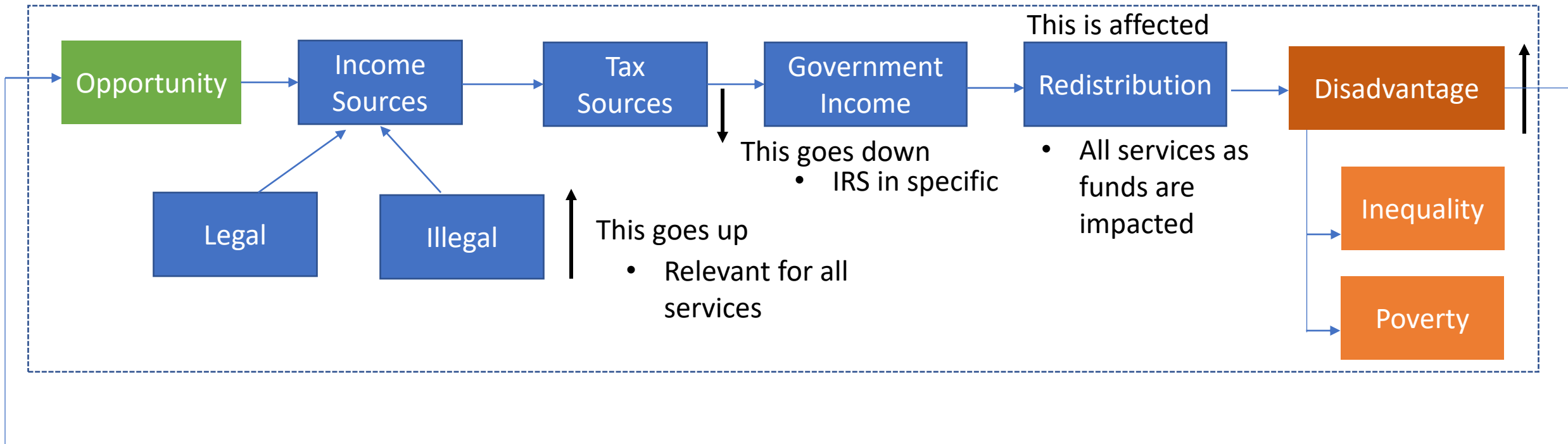
Underground Economy – Opportunity meets Disadvantage



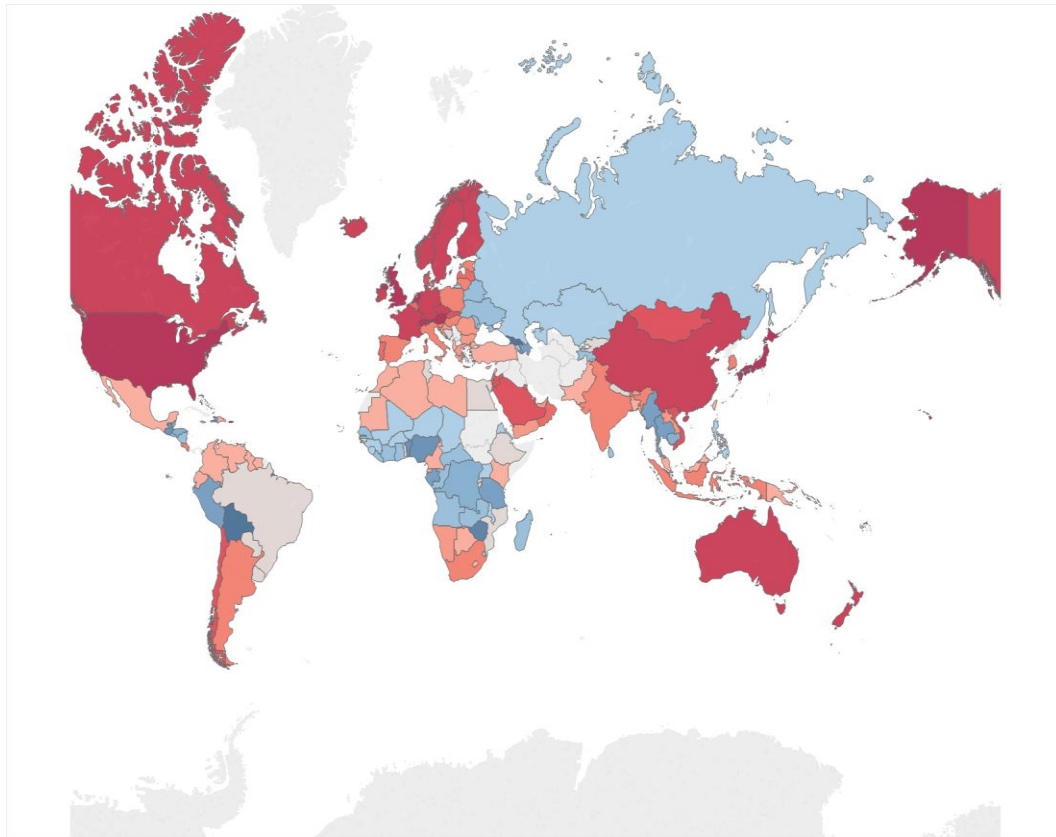
Underground Economy – Opportunity meets Disadvantage



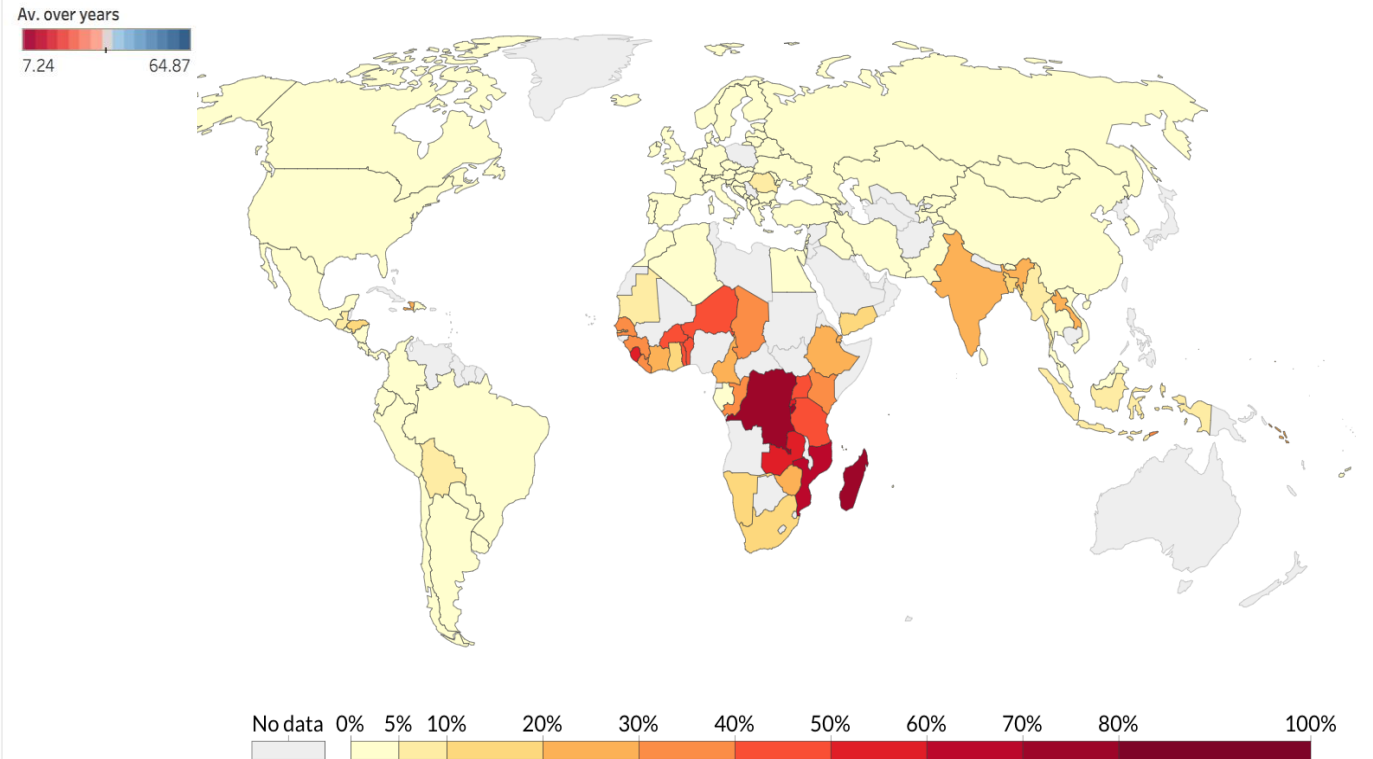
Underground Economy – Opportunity meets Disadvantage (Roles)



Black -Paradox



Size of the shadow economy as a % of GDP



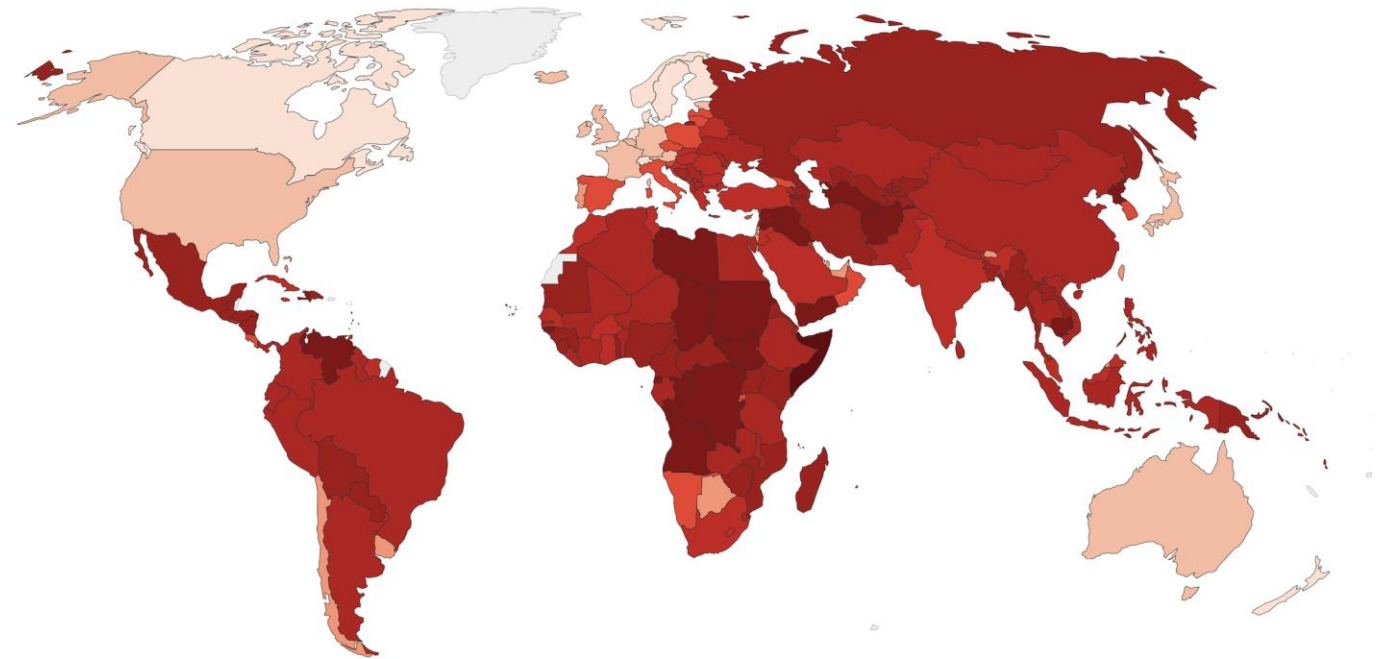
Extent of extreme poverty

Black -Paradox

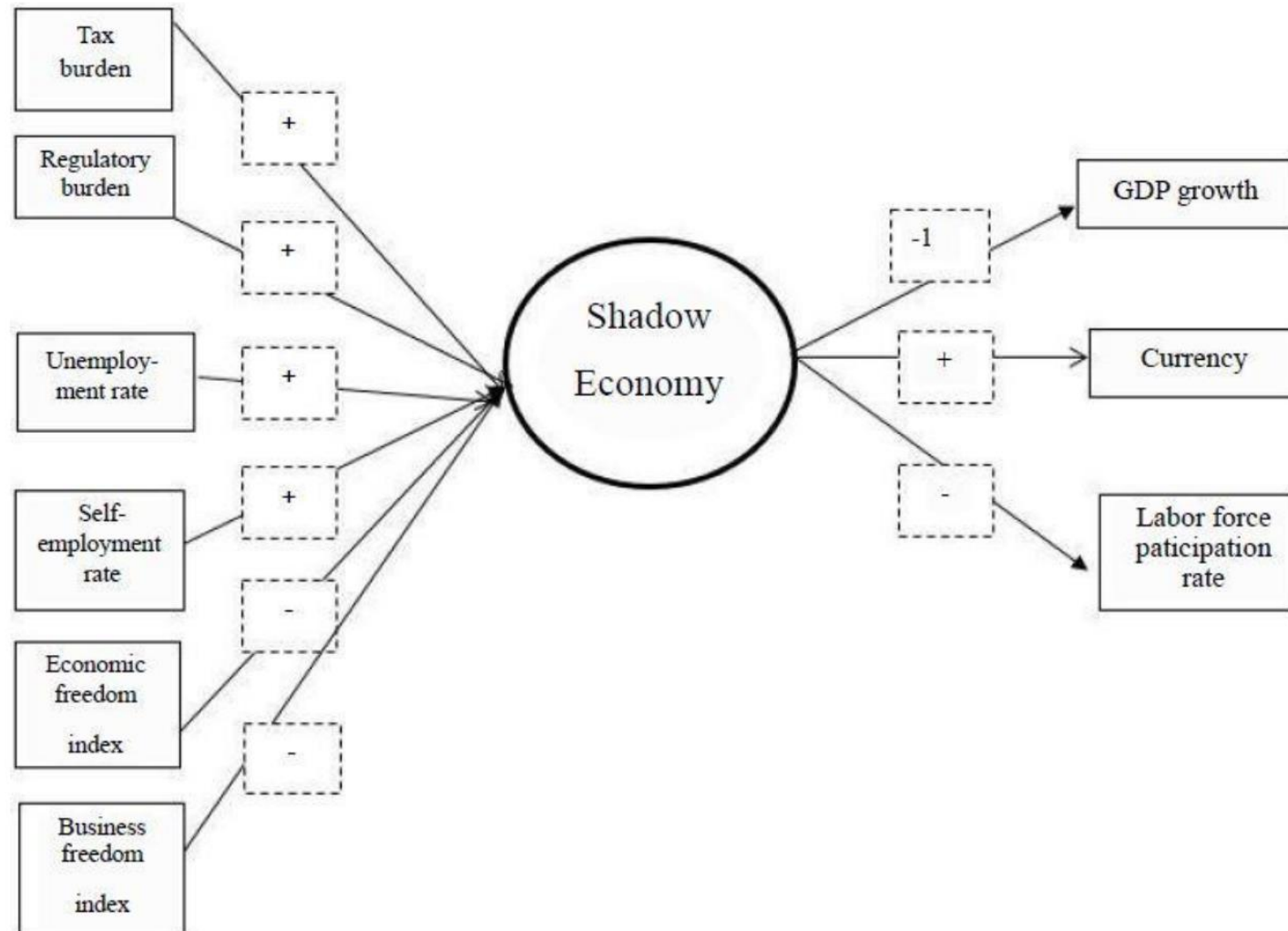
- Corruption is not synonymous to Black Economy
 - Corruption requires a quid pro quo
 - Example – Doctor not disclosing income involves no quid pro quo

Corruption Perception Index, 2018

Transparency International's Corruption Perception Index. Scores are on a scale of 0-100, where 0 means that a country is perceived as highly corrupt.



Implications



The Biggest Problem

Convergence?
Measurable