

Some Unseen Forces Which Creates Fertile Ground for the Growth of Parallel Economy

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Abstract --- Every economy consists of two types of activity. One that is recorded and other that is hidden. The hidden economy can be referred as Parallel Economy. Parallel Economy refers here to that of underground economy. As per the estimates of IMF the aggregate size of the underground and illegitimate market is between 2% to 5% of words GDP. Terrorist financing, drug trafficking, and black economy is nothing but pitfall of this growing means. This is the biggest industry in the whole world. According to a study made on Afghanistan, as of January 2002, income generated by the parallel economy is no less than three times larger than foreign funded economy prevailing in Afghanistan, same for Pakistan, according to a report by Geo TV published on September 3 2013, that only Karachi's black economy generates staggering Rs. 830 million every day. According to news reported to Financial Express, the rate of growth in parallel economy in India was higher than that of GDP in the period from 1980-81 to 1987-89.

It was seen that most of the countries having lager contribution of parallel economy towards GDP are mainly less developed straightforwardly poor countries. African countries like Nigeria and Egypt almost have 68-79% share in GDP. On the other hand central European countries like Hungary Slovakia and Czech Republic has 7-16% share in total GDP. Here a question lies. Why less developed or developing nations are mostly affected. My main concern of this paper is to study this non mainstream economy and the effect of Poverty, Unemployment, corruption and a circle among this variables and parallel economy. Actually I tried to break the circle by only affecting a single variable and I will try this method with every variable and explain them in this article. Due to less availability of data article took only four major economy of Indian Sub continent likewise India, Pakistan, Afghanistan and Bangladesh. The concept going to develop in this article is a "May be" concept not any conclusion due to lack of available data and if exist they are out of my reach and needs further research to develop.

Keywords---Corruption, Parallel Economy, Poverty Unemployment

Parallel Economy Keeps Indians Poor

– **By Ranjit Devraj (IPS)**

(INTER PRESS SERVICE News Agency Published on October 4, 2013 and retrieved on 2nd March 2015)

I. INTRODUCTION

IN today's world most discussed topic is terrorism. Terrorist activities needs fund. When I start finding the source of fund I met the parallel world of transaction known as parallel economy or underworld economy or black market economy.

Latter I found that major economic and social variables like poverty unemployment and corruption are somehow related to this economy. Fact is today's economy is a global economy and it is not restricted to one place or country and every economy is interlinked one country's economical conditions effect others. An economy is less affected when it is strong from inside but it was not the case for India and many other less developed of developing countries; existence of parallel economy, black money, fake currency problem, political crisis, high population and high unemployment rate acted as catalysts. Feige describes the parallel economy as including those economic activities which go unreported or unmeasured by society's current technique of monitoring economic activity. Parallel economy often could be demonstrated as hidden economy of a country. People or business entities when do not show their exact income as per government rules the income comes under parallel economy. In this article I tried to draw a casual and cyclical relation among those variable from my view point. I am not saying that what I am going to discuss next all are perfectly correct rather I try to express my way of viewing this parallel world and related variables. Sometime I used the word "YOU", this is because I want the reader to think about the consequences I am going to describe.

II. HOW CORRUPTION, UNEMPLOYMENT AND POVERTY DO EXTROLS PARALLEL ECONOMY

Corruption and Black Money-The inevitable consequences of corruption is Black Money generation through tax evasion in the form of income tax, custom duty etc. Transparency international has published corruption perception index (CPI) annually ranking countries "by their perceived level of corruption, as determined by expert assessments an opinion survey". According to CPI, corruption is defined as "the misuse of public power for private gain"

Corruption-Corruption is an improbity or decay in the decision-making process in which a decision-maker consents to deviate or demand deviation from the citation which should rule his or her decision-making, in exchange for a reward or for the promise or expectation of a reward, while these motives influencing his or her decision-making cannot be part of the justification of the decision. – by Dr. Petrus van Duyne, (retrieve from www.corruptie.org/en/corruption/what-is-corruption)

On latest index published in 2014 out of 177 countries on a 100 scale {100(very clean) to 0(highly corrupt)} ranked India 84 (38 point out of 100), Pakistan 126 (29), Bangladesh 145 (25 point) and Afghanistan 172. Starting from India according to a report Global Financial Integrity (GFI) in December 2012,

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India is among the top 10 developing nation in the world with a Black Money out flow of \$1.6 billion in 2010. Estimated amount of Indian black money stored in Swiss bank is almost \$1456 billion. In Pakistan a news report published by Geo TV on September 3 2013 says, that only Karachi's black economy generates staggering Rs. 830 million every day. DAWN on May 10, 2014 published a report which says at least \$200 billion of "Pakistani money" was stashed away in swish bank. (<http://www.dawn.com/news/1105356>). According to a report published by Economic times of India on June 29, 2011 on Bangladesh states Tax Evasion here is widespread with a new study by the finance ministry of Bangladesh finding that under claimed income could account for up to 80% of GDP some \$110 billion. (<http://southasianmonitor.org/detail.php?type=n&nid=3035>).

III. IMPACTS OF BLACK MONEY ON ECONOMY

- *Less tax for government* which leads to reduction of Expenditure of government in developmental projects like poverty elevation, employment generation due to less revenue collection.
- *Increase in inflation*, which leads to a cumbersome situation for the poor and middle earners. They face difficulty to meet their daily need due to price hike. Result is poor becomes poorer and middle class become poor.
- *Increase in poverty*, because of concentration of wealth in few hands.
- *Corruption and increase in parallel economy activity*.

Poverty-With the highest CPI ranking Afghanistan's poverty condition is poorest among these four countries with an estimate of 45% people of country's total population lives below poverty line according to government estimates. Another 20% people live just above that line. 45% of rural population compared to 20% of urban population is poor. According to HDI, 60.3% of Pakistan's population lives below \$2 a day. Some 28.6% live under \$1 a day. Bangladesh till now is in better condition. World Bank announces that Bangladesh had reduced the number of people lives below poverty line from 63 million in 2000 to 46 million in 2010. According to a survey found by Bangladesh bureau of statistics in 2010 17.6% of populations are found below poverty line. An estimated 36% people of total rural population and 28% people of total urban population are poor. In 2012 India government stated 21.9% of its population lives below poverty line. The World Bank in 2011 estimated 24.6% of India's population lived below \$1.25 per day on purchasing power parity.

Unemployment-From 1983 till 2011, average unemployment rate in India was 9% with 9.4% in 2010, which is an all time high. Bangladesh in respect to other countries shows a good position rather with 4.50% in 2012 followed by 4.50% in 2011 reported by Bangladesh Bureau of Statistics. According to Trading Economics unemployment rate in Pakistan averaged 5.43% from 1985 until 2013 and in Afghanistan unemployment rate averaged 8.70% from 1991 until 2013.

There may be much reason for poverty and unemployment in a country. I took corruption as one of the main reason. Corruption through black money generation also creates disparity in the economy and resulting in poverty expansion and unemployment generation.

Among many ill effect of prevailing corruption in economy and black money generation, revenue loss of government is one of the worst result. We all know that every government has to meet some fixed cost to run the administration which he can't avoid. Poverty elevation scheme, Employment generation programs and Skill development programs belongs to those development activities which government seeks to meet after spending on the fixed cost. This is the general view point, it was seen in some cases that government took those initiative as a part of fixed cost. Those are exceptions and I am not going with that. Generally those developmental activities belong to excess fund activities.

Hypothesis-Before going into the main discussion I am going to test a hypothesis here. The hypothesis states:

H₀: parallel economy activity can not start without the injection of black money. (Null hypothesis)

H₁: parallel economy activity can start without the injection of black money. (Alternative hypothesis)

A. UNEMPLOYMENT LEADS TO POVERTY AND AGAIN POVERTY LEADS TO UNEMPLOYMENT

Arguments- If a person is unemployed then poverty is his obvious choice. Merriam Webster defines poverty as "the state of one who lacks a usual or socially acceptable amount of money or material possession." A person with lack of money to survive or to full fill his and his belongings basic need can be considered as poor. And to full fill that he needs a certain amount of money. This definitely implies that he must have some source of income which again implies he must possess any kind of jobs. There may be two types of job a person can afford in a regular economic activity. One is in formal sector and one in informal sector. If you are employed in a formal sector then you are definitely employed, now if you working in informal sector you are not unemployed but not even so employed that you can avoid of being poor. How? Informal job does not guarantee a fixed income but the cost of living is fixed and utter rising due to prevailing inflation in the economy. Neither informal sector provides any job security also though currently most of the formal sector is not providing security also. Most of the cases informal sector employment is in the form of street vendor. I never see a street vendor who is rich or rather not poor. And it can be proved with easily available data. Again there can be a case if you are a part of cyclical unemployment or right now you don't have any job but in very near future you are capable of getting job, you don't belong to my set. This phenomenon is not a part of developing countries rather can be seen in developed countries. My set of unemployment consists of those who belongs to a part of structural unemployment or rather possess no skill to be employed in current economic activities. So if you are in my set of unemployment you are poor also.

Now if you are poor unemployment also is your obvious choice. To justify let's start with the definition I stated earlier. Merriam Webster defines poverty as "the state of one who lacks a usual or socially acceptable amount of money or material possession." I define poverty as "the state of one who is unable to meet his/her present need and even if he/she is meeting his/her present need, he/she is not ready to meet any kind of speculation in his livelihood in near future like any kind of increase in his/her planned expenditure regarding health problem (ignoring health insurance as this is not so much effective in above countries), increase in cost of education, etc". In most of the less developed countries face problem of malnutrition (statistics can be easily found in internet). One reason is that they have very less access to those food grains which will provide adequate nutrition, and another reason is they can't afford due to poor financial condition. Now if you are sick you can't afford hard work then your status will be same because you are unemployed due to your physical condition. Now a poor people can't afford proper education that can provide them good employable position. One reason is that opportunity cost of affording education is always higher for poor. So again they can't get any good job in a formal sector and can't improve his/her status. Now they are left with informal sector jobs or no job. So if you are you can't escape unemployment.

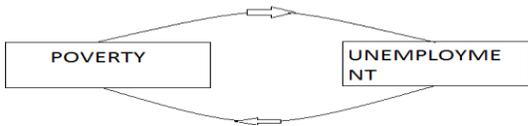


Fig. 1 Cyclical relation between Poverty and Unemployment

According to India Skills Report launched in 3rd CII National Conference on Skill Development 34% were found to be employable out of about 100000.

B. CORRUPTION LEADS TO BOTH UNEMPLOYMENT AND POVERTY

Arguments-Corruption leads less revenue generation and which reduces the amount which can be expected to be used in Employment generation, poverty elevation, and skill development. An increase in corruption lowers productivity and decreases net capital inflow in the economy. Now as I previously argued that to be employed you need to adopt skill (formal employment) and for that you need at least basic education. Most of the developing countries literacy rate is not so high.

It was seen that due to corruption in bureaucrats many private party shows unwillingness in establishing new industry as their cost increases rapidly. In most of the cases foreign funds came for developmental prospects have inefficient use though corruption is not only the case but surely one of the major causes.

TABLE I
LITERACY RATE

Country	Adult Literacy Rate	Youth Literacy Rate (15-24 age)
India	74.04%(2011)	81.1%(2006)
Pakistan	50.2%(2007)	70.8%(2011)
Bangladesh	53.5%(2007)	63.6%(2001)
Afghanistan*	31%	
World	84%(2010)	89.6%(2010)

Source: Wikipedia

(*)UNESCO (Enhancement of Literacy in Afghanistan (ELA) Program.)

If we go through these countries literacy condition though India is in better position other countries positions are really not good at all. Illiterate people can easily be made fool as they have very less knowledge of actual. This actually implies that they become part of the corruption due to ignorance.

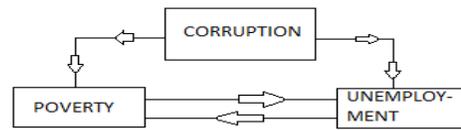


Fig. 2 interrelation among Corruption, Poverty and Unemployment

Government of India launched though many scheme for generating employment likewise MNREGA (Mahatma Gandhi National Rural Employment Generation Act, 2004) but it was not so much fruitful at this was expected and one of the main reason is corrupt Bureaucrats. Similarly MID-Day meal scheme also did not get so much success as it was expected. This was a part of literacy program.

C. PARALLEL ECONOMY AND CORRUPTION POVERTY AND UNEMPLOYMENT

A beautiful characteristic of parallel economy is to be employed one does not need any kind of skill and a very high educational background. Though those warlords are enough educated but to work in grass root level a rookie can be used for ill purpose.

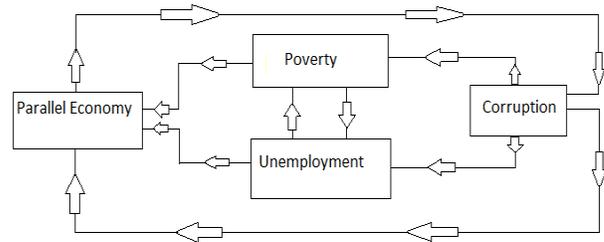


Fig. 3 Interrelation between Parallel Economy and above Variables.

Above flow chart easily describes the mechanism which connects above four major variables each other. I already discussed earlier about relationship between corruption poverty and unemployment. Now we have to concentrate who poverty and unemployment connects with parallel economy.

"No government, no global nonprofit organization, no multinational enterprise can seriously claim to be able to replace the 1.8 billion job created by economic underground. In truth, the best hope for growth in emerging economics lies

in the shadow.” – **Neuwirth, Robert (August 18, 2011). Global Bazar: Street Market and Shantytowns Forges the World’s Urban Future Shantytowns, favelas and jhopadpattis turn out to be place of surprising innovation. Scientific American 56-63.**

Arguments- In parallel economy the most important part is played by Black Market, as it is one of the main sources of fund generation. Black market economy is sometime treated as informal economy. Person those who are employed in this market are also a part of parallel economy. Most of activity of Black market economy is nurtured by corrupt bureaucrats. And again money generated from these activities is also used for bribing bureaucrats. It was seen that those who are employed in this economy are formally unemployed and poor. If you have nothing to eat you will not care about moral values. We should always remember that “opportunity cost of indulging in parallel economic activity is always higher than formal economic activity”.

Black market-Black market is an essential part of parallel economy. It sometime referred as Underground Economy. This is a market where goods and services are traded illegally. Sometime black market is considered as a subset of informal economy.

Traded goods and services in black market:

- Sexual exploitation and forced labor**
- Illegal drugs dealing**
- Prostitution**
- Weapon trading**
- Illegal logged timber trading**
- Illegal trading of animal and animal product**
- Illegal alcohol trading**
- Illegal tobacco trading**
- Illegal biological organ trading**
- Racketeering**
- Counterfeit medicine, essential aircraft and automobile parts etc**
- Illegal selling of currency, fuel etc.**

Size of global Black Market

Largest Black Markets	Estimated Amount market value(Billion USD)
Total	1829
Counterfeit pharmaceutical drugs	200
Prostitution	187
Counterfeit electronics	169
Marijuana	142
Cocaine	85
Prescription Drugs	73
Opium and Heroin	68
Software piracy	59
Movie Piracy	58
Gas and Oil smuggling	53
Cigarette Smuggling	50

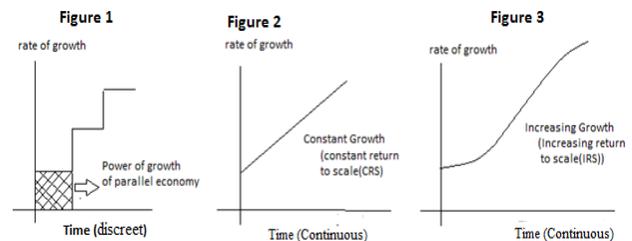
Source: Wikipedia

As emphasized by Becker (1968), individuals should allocate their time between working in the legal job market or working in criminal activities in such a way that maximizes their utility. After accounting for the risk of being caught and

penalized, the size of the penalty and any stigma and moral distress associated with involving in crime, those who receives higher income by criminal activities would choose involvement in crime. (Becker, Garry S. 1968 “Crime and Punishment: An Economic Approach.” Journal of Political Economy, March/April, 76:2, pp. 169-217)

Aristotle wrote “Poverty is the parent of crime”. I am not going to the Economics related to the criminal activities, but one can’t deny that parallel economy activity is also a part of criminal activity. I already discussed how parallel economy is related with corruption. Now if you are poor and unemployed at least to survive you must need to earn. Now option of working in parallel economy is always widely open and the remuneration is also very much attractive. More or less if you are poor and unemployed you can easily get attracted to this world which requires almost no skill and education for fresher. I can’t say that all poor and unemployed are part of parallel economy, but I must definitely say that those who are currently working in this sector, once was unemployed and poor.

D. ASSUMED PATTERN OF GROWTH OF PARALLEL ECONOMY (MY POINT OF VIEW)



Above figures represents my view point about the pattern of growth of parallel economy. Starting from figure 1, the intercept represents the how much push we need to start the parallel economy activity in an economy. I assumed generation of black money as a part of parallel economy activity, and generation of black money can’t serve for growth in the economy until or unless that money gets some utilization. Assuming time here as a discreet. The shaded area represents the power of activity. I define Power of Activity as a component which decides how much expansion will going to take place in next time period.

Say’s Law and Parallel Economy-Supply Creates its own Demand this is the formulation of say’s law. Now let’s see how this law holds in this economy. I assumed again money as a commodity and money is invested for more revenue generation. A flow chart can easily describe the money is invested for more money.

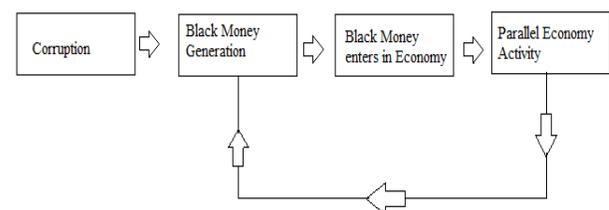


Fig. 4 Circulation of Black Money

Above flow chart easily describes how money rotates in the economy. Money is used for activity now to continue those activities more money is needed and the money created by the activity again injected in the economy for more activity and money. This is how the economy operates and starts through the injection of money.

Now recall the hypothesis we assumed earlier. Above notions verifies the acceptance of the hypothesis. Now suppose we rejects the null hypothesis and assumes that there is no corruption in the economy. The black market economy starts without the black money. Now to buy arms, produce drugs, and to perform other economic activity described above needs money. Suppose I am not big gun of this economy. I can easily avail those things on debit. But those who will supply me those things how they will get. Most importantly this economy services on prepaid basis. Now you can't assume that taxed money is involved in the start of the economy as because if you are spending your white money the respective authority who imposes rules and regulation on your, always keeps eye on you. In little moment you will be exposed. So you cannot just use your white money for ill use. So this notion rejects the possibility of accepting the alternative hypothesis. Our null hypothesis holds that without black money generated through corruption this economy cannot start its activity.

Now we can say that the intercept term in figure one is a function of corruption. If we denote the intercept term by "a" then,

$$a = f(\text{corruption}), \text{ Ceteris Paribas}$$

Figure 2 & 3 takes continuous time and interpretations are same as figure 1. The difference between figure 2 and figure 3 is in figure 3 growth pattern is IRS (increasing return to scale) and in figure 2 it is CRS (constant return to scale). The pattern of the curve in figure 3 shows initially bureaucrats are hard to crack and regulations are bit strict.

One important feature of this economy is there is no bushiness circle only there is a move towards boom.

IV. CONCLUSION

I want to conclude with the notion that due to some reason all rehabilitation, poverty elevation and employment generation programs are not working properly. As I told earlier that will try to alter my variables and I did it with corruption only as because poverty and unemployment is essential part of this model. I will try to alter then in my next publication and I will try to relax some assumption also. As we know this economy is expanding daily. For example, According to news reported by Financial Express, in India Black money was estimated to be 9.5 percent of GDP in 1967-68, rising to 49 percent of GDP in 1978-79 and 50.7 percent in 1987-88. The rate of growth in the parallel economy was higher than that of GDP in the period from 1980-81 to 1987-89; the former rose by 46.7 percent, and the later by 40 percent. I just tried to show that somehow corruption is responsible for this. According to The Indian EXPRESS India accounted for 15% of the volume of global arms imports in the

last five years (retrieve on March 16, 2015). Somehow political ball game is also involved behind this. I propose further research in this topic to find way outs from this dead trap.

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