Economics Class 03

12th July, 2023 at 9:00 AM

INTERNATIONAL FINANCIAL ORGANIZATIONS (9:00 AM):

- Work Bank and International Monetary Fund(IMF) are known as **Bretton Woods Twins.**
- World Bank -Reconstruction and development.
- International Monetary Fund- Pulling out member countries of IMF out of financial crisis.
- The **Bretton Woods Conference (1944)** also proposed an International Trade Organization(ITO), but it could not come into existence.
- Instead, an agreement called **General Agreement on Trade & Tariffs (GATT)** came into existence, which later became **World Trade Organization (WTO).**
- GATT mainly handles multilateral trade.

Times of trouble in India:

- 1960-1966 was a very difficult phase for India.
- India faced wars with China, and Pakistan, droughts, a declining food supply, and a rising population.
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Expected GDP growth	5%	**Expected population growth**	1.5%
Actual GDP growth	2.5%	**Actual population growth**	2.5%

- Hence Indian GDP growth was less than expected and Indian population growth was more than expected.
- The **PL 480** plan of the USA was pulled back and India faced food insecurity.
- The need for increasing food production and maintaining a food buffer stock was felt.
- Under the supervision of **Norman Borlaug & M.S. Swaminathan,** India started the first **Green Revolution** in the mid-1960s.
- The first Green Revolution focussed upon:
- I. High Yielding Variety seeds.
- II. Chemical fertilizers.
- III. Irrigation facilities.
- IV. Fram credit.
- The **Food Corporation of India (FCI)** was set up in 1965 to maintain buffer stocks and operational stock of food grains (initially rice & wheat).
- FCI also implemented the **Public Distribution System (PDS)** (ration shops).

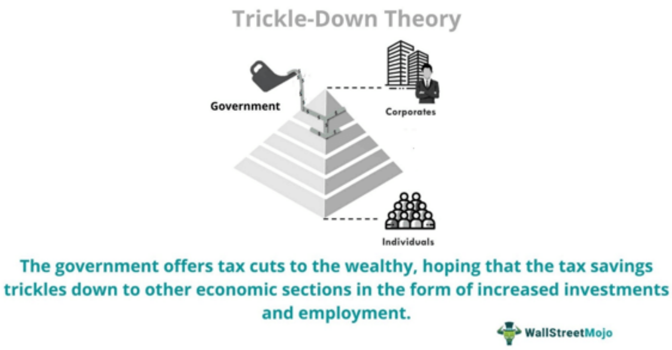
LAND REFORMS (9:30 AM):

- British rule destroyed the balance between agriculture and industries that existed earlier.
- British left us with a destroyed agricultural setup and insufficient industrialization.
- We had to start from scratch after 1947.
- British land revenue systems- **Zamindari, Ryotwari, & Mahalwari,** impoverished the farmers and caused the concentration of much land among a few people.
- Zamindars controlled almost 50% of the land.
- Farmers and tenants had to pay high taxes which pushed them towards money lenders to pay the rents and take credit for the next crop cycle.
- Redistribution of lands to farmers & zamindari abolition were highly prioritized to ensure social justice.
- Land reforms also focussed on **tenancy reforms**, under which tenant farmers were to be given security of tenure(not getting evicted from lands at short notice).
- **Financial Inclusion** was felt inevitable to ensure the financial security of the poor farmers.

- The institutionalization of credit was expected to push the farmers away from the clutches of the moneylenders.
- Achieving financial inclusion and socialistic re-distribution were the driving factors behind **Banks' Nationalization.**
- Nationalization of banks was felt necessary because private banks were not interested in setting up branches in rural or far-flung areas due to profitability concerns.
- In 1969, 14 banks were nationalized and 6 more banks were nationalized in 1980.
- The **Jan Dhan Yojana** aims to achieve financial inclusion.
- Financial inclusion helps in channeling money into the formal banking system.
- This helps in improving the national savings and investment scenario.

INCLUSIVE GROWTH (10:00 AM):

- **Trickle-Down Effect/Theory:**
- The theory believes that if the economy grows at a faster pace, poor people will not benefit immediately, but eventually.
- So government must provide a favorable environment to large corporations(public & private) so that they can contribute to economic growth.



- The theory is believed to have failed in India and we got a concentration of wealth in the society.
- A large part of the population was not skilled/educated enough to contribute or derive benefit from the growth that was promoted.
- Growth is a prerequisite for inclusiveness, but growth alone is not sufficient for ensuring inclusive growth.
- Inclusive growth focuses on including everybody in the economic growth process.
- Due to the failure of the **trickle-down theory** and the introduction of market principles, we have seen increased inequalities.
- Therefore, inclusive growth as a concept has become popular across the globe.
- To ensure inclusive growth, the government has to focus on efficient welfare programs, especially health and education.
- **Progressive taxing** mechanism, skill development programs, focus on agriculture, etc.
- **Economic development** can happen only if there is inclusive growth.
- **Economic growth** is a unidimensional concept that only measures progress in terms of numbers- GDP growth, income growth, etc.
- Economic development is a multidimensional concept that includes economic growth, human development, inclusive growth, etc.

DEPRECIATION & DEVALUATION OF CURRENCY (10:35 AM):

- **Currency depreciation** refers to a fall in the value of a currency in terms of its exchange value with respect to other currencies.
- This change in value happens due to market forces(supply & demand of the currency).
- As a result of currency depreciation, exports become cheaper and imports become costly.

- **Devaluation** of the currency means a reduction in the value of the currency based n the central bank or the government's decision.
- This decision will not be dependent on market- forces of demand and supply.
- The net effect on exports and imports is the same as that of depreciation.

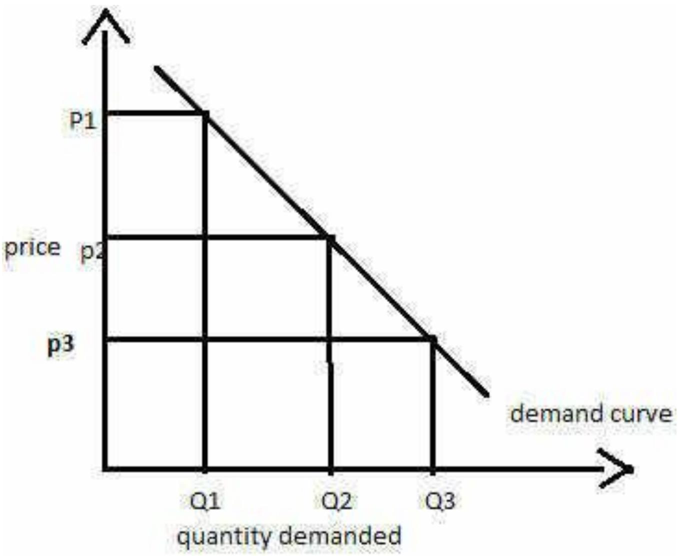
The link between currency depreciation, inflation, & trade deficit in India:

- When the import is more than the exports it is called a **trade deficit** and when the export is more than the import then it is called a **trade surplus.**
- Rupee depreciation would increase the cost of importing essential items like Crude oil.
- This increase in cost would widen our trade deficit.
- The rise in import costs would also make petroleum costlier for the common man.
- This will increase the transport costs for most items, making them costlier for the common man.
- Hence, we will most likely see increased inflation due to currency depreciation.
- When Rupee depreciates, our products will get cheaper and more competitive for foreign companies.
- **Case 1-** 1 $= 100 rupees and Indian pen also costs 100rs.
- In this case, the foreign importer will pay 1$ to import this Indian pen.
- **Case 2-** 1$= 50 rupees and Indian pen costs 100rupees so foreign importer will have to pay 2$ to import this Indian pen.
- In this case, foreign investors might not import the pen from India
- So weaker currency might increase exports and improve the nation's trade deficit.
- But that case is more likely for an export-oriented economy like China, and not for India which has much more imports than exports.

DEMAND (11:10 AM):

- Economically speaking, demand refers to a consumer's desire and capacity to pay for the desired goods and services.

Law of Demand:

- There is an inverse relation between the demand for a good and the price of the good.
- As the price increases, consumers will start demanding the good in lesser amounts.
- 

- A rightward shift of the demand curve will show a favorable demand.

Demand for goods depends upon various factors:

- **I.** Price of the good.
- **II.** Income of the individual.
- **III.** Individual preferences.
- **IV.** Prices of complementary goods:

- Cars might get cheaper due to less demand if the price of petrol increases.
- **V.** Prices of substitute goods:
- The demand for tea will most likely increase if coffee gets costlier.

Exception of the law of demand:

- The law of demand does not get followed under all circumstances for all kinds of goods.
- Certain goods do not follow the law of demand.

Veblen Goods:

- These are those goods whose demand increases as their prices rise.
- These goods are not purchased strictly for utility and durability but for the social significance associated with them.
- **For example-** Rolls Royce cars, iPhones, etc.

Inferior goods:

- Inferior goods will see a decrease in their demand as income increases.
- **For example,** if someone's income rises, he/she will shift from consuming coarse grain like Bajra to higher quality grain like wheat.
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TAX (11:30 AM):

- India had high tax rates in the 1960s and 1970s.
- There were high customs duties, high corporate taxes, excise duties, etc.
- High tax rates may temporarily increase revenue but over a period of time, tax revenue drips due to reasons like tax evasion, tax avoidance, etc.

Tax Evasion:

- It is illegal and an escape from paying taxes.
- Higher tax evasion will yield lower tax revenues for the government.
- **For example-** cash payment in high-value transactions like land deals.

Tax Avoidance:

- It is a legal mechanism to avoid tax.
- Corporations use tax loopholes to shift profits from the base/source country to a **Tax haven** through **Base Erosion & Profit Shifting.**

Tax havens:

- These are the countries with liberal tax rules where the source of money is not questioned.
- Some examples are Mauritius, the Cayman Islands, Cyprus, Switzerland, etc.

Shell Company:

- These are the companies used for converting black money into white.
- These companies are generally not interested in the front-end business.
- Most shell companies operate from tax havens to avoid paying taxes.

The topic for the next class is the continuation of taxation.