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Research Paper

DEMONETISATION IN INDIA**Dr. Anjana Bedi¹**¹Assistant Professor, BBK DAV College for Women, Amritsar, Punjab, India.**ABSTRACT**

Demonetisation of high denomination currency notes of Rs.500 and Rs. 1000 was a step taken by Prime Minister Narendra Modi to obliterate black Money and flush out fake currency in circulation in the economy. The objective of this paper is to have a comprehensive view of this measure, its impact on general public and economy as a whole. Various write ups of eminent personalities, recent news in newspapers and various websites have been consulted to write this paper. It concludes that this measure may act as a negative shock to the economy in the short run. The government should make efforts to improve the circulation of cash in the economy because access to cash is very-very important for marginalised sections of society. It will take time to convert cash-based economy to cash less economy.

KEYWORDS: Demonetisation, black Money, inflation, corruption**INTRODUCTION**

On 8th November 2016, Prime Minister Narendra Modi in an unscheduled live televised address to nation to withdraw all Rs.500 and Rs.1000 notes immediately from circulation. This sudden move rendered 86% of country's currency worthless outside a bank branch. Demonetisation of currency notes is not new to India. Rs.1000 and Rs.10,000 bank notes were first demonetised in Jan 1946. This exercise was again resorted to in Jan 1978 when high nomination bank notes of Rs. 1000, Rs.5000 and Rs.10,000 were demonetised.¹

Mr Modi propounded two primary reasons for this decision. The first was to "choke the funding channels of militancy and terrorism from across the border using counterfeit currency notes." and the other was to "break the grip of corruption and black money".

OBJECTIVE OF THE PAPER

The ultimate objective of this endeavour is to have a detailed view of demonetisation and its implications for general public and economy as a whole.

RESEARCH METHODOLOGY

Write ups of various eminent authors, recent news in newspapers and various websites have been consulted for writing this paper.

REVIEW OF LITERATURE

Charan Singh (2016), RBI chair professor, IIM Bangalore discussed about the mixed results of economic implications of demonetisation. According to him, it would inspire confidence of international community that India is serious about its commitment to fight corruption and enhance India's ranking in ease of doing business as well as in various global indices of corruption. However the ultimate pain in terms of non-availability of required currency notes if not corrected soon, may reflect in reduction of output in agriculture, which may spill over to industry and services.²

Tim Worstall (2016) favoured demonetisation as it would lead to lower budget deficit, interest rates and inflation.³ The effects of change on GDP will emerge from system itself because we cannot calculate an economy beforehand.⁴



Mamun Rashid (2016) viewed it as a painful exercise for not only the corrupt, but for the poorest and most marginalised people too. Demonetisation can be a futile exercise in the absence of steps to curb the generation of black money. Fake money once again may recirculate. Terror can not be stopped by banning notes. The economy will be catatonic in short term, followed by a period of easing out. Only time will tell if it was all worth it.⁵

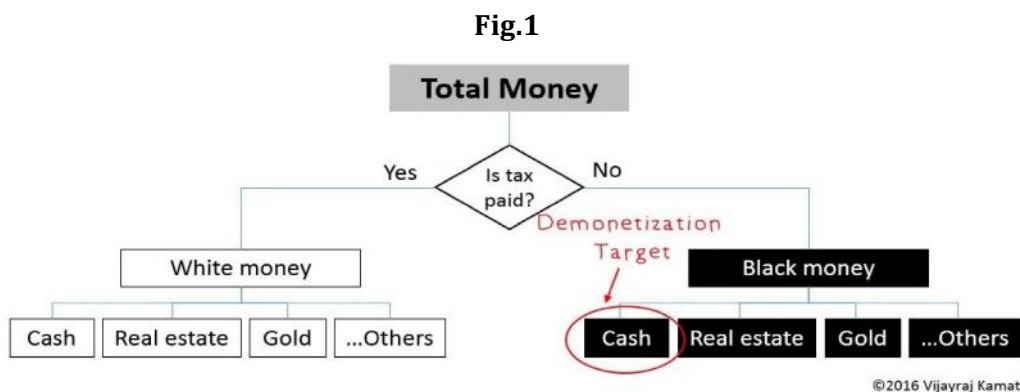
Dr. Manmohan Singh (2016), former Prime Minister of India contended that this measure has thrown the lives of millions of poor people in disarray as cash is the bedrock of lives of these people. This brazen policy measure has neither tackled the stock of black money nor has it stemmed the flow of it. The policy can act as a negative shock to the economy also.⁶

FACTS AND FIGURES

The demonetisation effort being led by PM Modi in India is the idea that Rs.500 and Rs.1000 notes should no longer be legal tender, to be replaced by other notes of different designs and denominations.

Money can take form of cash, real estate, gold foreign exchange etc. The only question making it black or white is “Have the requisite taxes been paid?” If taxes are not paid then it becomes black money. In order to hide this black money it is invested in benami transactions, off shore accounts, gold, real, estate etc.

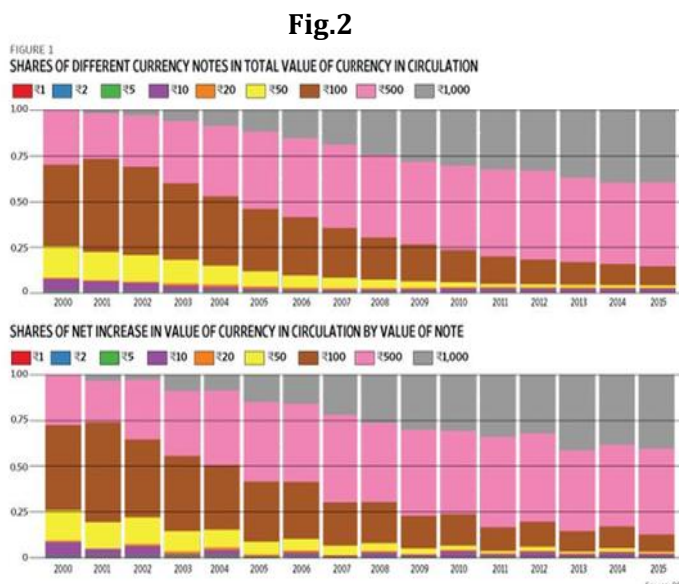
So cash is a very small part of black money. It is impractical to hoard it all in cash. Fig. 1 shows that total money is not the same as cash.⁷



Source: <http://www.quora.com/what-do-you-think-of-the-decision-by-theindian-Government-to-demonetize-500-and-100-rupee-notes>.

Why only 500 and 1000 rupee notes were banned? Most of the black money is saved in the form of Rs. 500 and Rs.1000 notes only. The total number of bank notes in circulation rose by 40% between 2011 and 2016, the Rs. 500 and Rs.1000 bank notes increased by 76% and

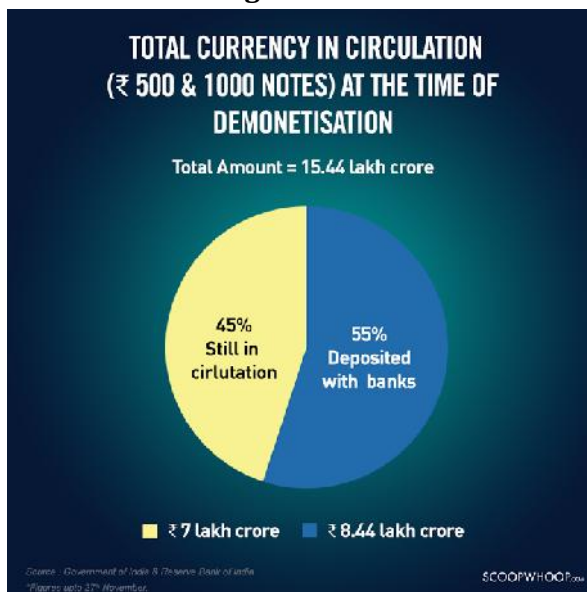
109% respectively in this period owing to forgery. This forged cash was then used to fund terrorist activities against India. As a result, the decision to eliminate the notes had been taken.⁸ Fig. 2 shows the facts regarding currency in circulation.



Source: <http://www.quora.com/what-do-you-think-of-the-decision-by-theindian-Government-to-demonetize-500-and-100-rupee-notes>.

Fig 3 depicts that at the time of demonetisation total currency (Rs.500 and Rs. 1000) of 15.44 lakh crore was in circulation, 55% of total currency was with banks as dePoSits while 45% in circulation.

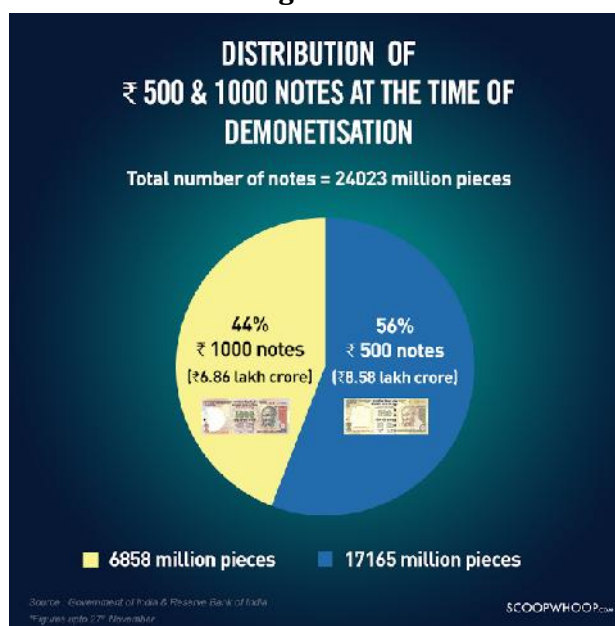
Fig. 3



Source: <https://www.scoopwhoop.com/These-Four-Illustrations-Explain-The-Cash-Situation-In-India-After-Demonetisation/#.oltco2xhw>

Fig 4 explains the distribution of Rs.500 and Rs.1000 notes in circulation at the time of demonetisation.

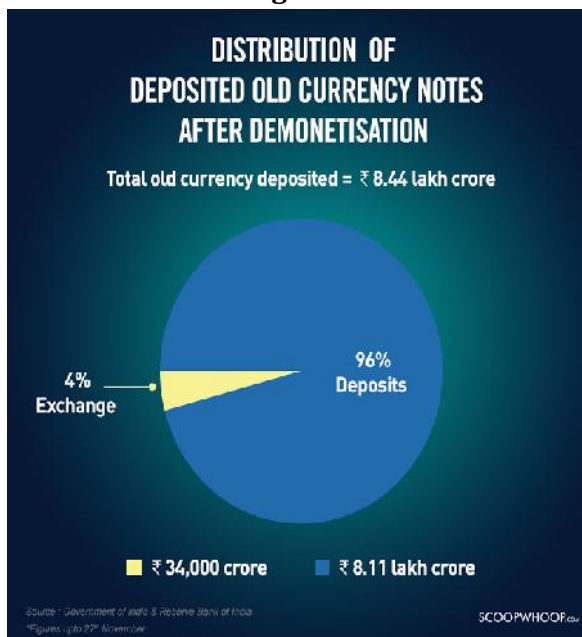
Fig. 4



Source: <https://www.scoopwhoop.com/These-Four-Illustrations-Explain-The-Cash-Situation-In-India-After-Demonetisation/#.oltco2xhw>

Fig 5 shows the effect of demonetisation on cash in India. After demonetisation the banks were flooded with dePoSits.⁹

Fig. 5

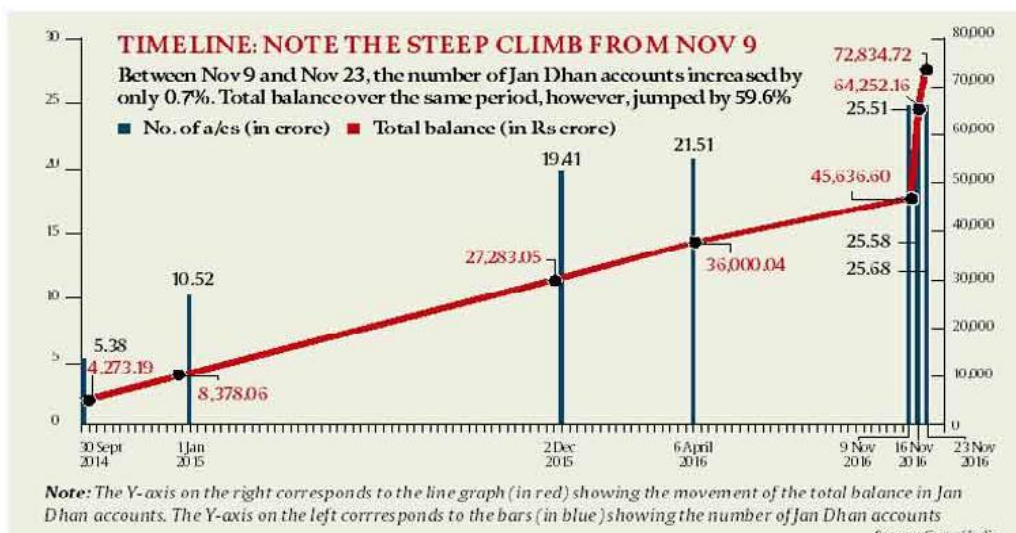


Source : <https://www.scoopwhoop.com/These-Four-Illustrations-Explain-The-Cash-Situation-In-India-After-Demonetisation/#.oltco2xhw>

Fig 6 decodes PoSt demonetisation boom in dePoSits in Jan Dhan Accounts. Within a fortnight balance in these no-frills accounts increased by 60% to Rs. 72,834.72

crore. Despite the dePoSit rush, banks were able to open 16.48 Lakh new accounts in this two week period taking the number of accounts under the scheme to 25.48 crore.¹⁰

Fig. 6



Source : <http://Indianexpress.com/article/explained/demonetisation-Jan-dhan-Yojana-dePoSits-4400468>

Various macro-economic indicators mentioned by Finance Minister Arun Jaitley are as follows:

- (i) ‘Till Dec 19, 2016, net increase in income tax collections (after refunds) has been 13.6%.
- (ii) Indirect tax collections soared 26.2% between April, and November 30, with revenue from excise jumping by 43.5%, that from service tax by 25.7% and customs by 5.6%

- (iii) Rabi crop sowing, tourism and petroleum consumption had shows growth while flow into mutual funds has increased by 11%.¹¹

IMPLICATIONS FOR PUBLIC

- 1) More than 600 million Indians who live in town or village without any bank. Over half of India’s population does not have any sort of bank

accounts and about 300 million don't have basic ID such as Aadhaar card and hence cannot access the banking system at all: so access to cash is very-very important for

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- 2) More than 90% of Indian population works in informal sector. This consists of agriculture workers, construction workers, people working in transport sector, and small businessmen. Their daily subsistence depends on cash earned by them. The scarcity of cash due to demonetisation has led to chaos all over the country. People have to line up at banks and ATMs for withdrawal of their own money. Several precious lives had been lost in these long queues.
 - 3) The government is promoting concept of digital money but due to various limitations, it becomes very difficult for people to adopt the habit for digital transactions.
 - (i) India has low level of literacy especially in rural areas. English literacy rate is just 10 percent of population. The use of electronic devices and digital banking needs knowledge of English. It is natural barrier in digitalising Indian economy.²
 - (ii) 30% of Indian population is below poverty line. These poor people will be slow in embracing digital economy.
 - (iii) Much of cash transactions in the country are small exchanges for goods or services Low volume of business in rural shops, shopping sheds etc. may not justify the cost of installing equipments like PoS machines. Mobile Internet penetration is must for these PoS machines which is lacking in many areas.
 - (iv) Financial Security over the digital payment channels is also a matter of concern due to common occurrence of financial frauds these days.¹³

IMPLICATIONS FOR ECONOMY AS A WHOLE

- (1) Presently it is very difficult to know the effect of demonetisation on India's GDP but it is expected that demonetisation-driven cash crunch and strong formalisation of informal economy will lower GDP growth rate in 2017-18 to 5.8% from earlier estimate of 7.3%. As per recent data released by Ministry of commerce and industry the eight crore industries growth slowed to 4.9% in November. The Nikkei's

Market India Manufacturing Purchasing Managers Index (PMI) which measures manufacturing sector activity fell to 49.6% from 52.3 in November.¹³

- 2) The flood of cash being deposited will reduce interest rate that has a stimulatory effect upon economic growth. Recently Top PSU lenders State Bank of India, Punjab National Bank and Union Bank of India slashed their benchmark lending rates by upto 90 basis points.¹⁴
- 3) It is estimated that Rs. 14 Lakh crore worth of Rs. 500 and Rs. 1000 notes that have been scrapped, roughly Rs. 3 Lakh crore are not likely to be exchanged for new notes ever and thus these Rs. 3 Lakh crore will be withdrawn from circulation. This will reduce base money supply by 16% or 17% thereby lowering inflation in the economy. But the most recent larger macro-economic picture shows the possibility of higher inflation rate due to hike in interest rate by U.S and increased oil prices internationally.^{13(a)}
- (4) In spite of various evasions through gold purchases, donations, multiple bank transaction, railway bookings etc, the Govt. revenues have increased through direct tax and indirect tax collections hence budget deficit will be smaller, again a positive effect on the economy. However India's trade deficit widened to 0.41 billion in November due to slow export growth and high imports of gold.^{13 (a)}
- (5) There is sluggishness in stock market and housing market. The exchange rate is depreciating in the short run because of huge demand of dollars. The real estate business has taken a severe hit since demonetisation. This will further impact 300 industries which provide inputs to housing sector.² Modi Govt has recently announced 4 percent waiver on housing loan up to Rs.9 Lakh and 3 percent in case of loan up to Rs.12 Lakh to boost this sector ¹⁵
- (6) Demonetisation has adversely affected agriculture. Farmers had to face numerous hardships in this sowing season and 60 days interest waiver for agriculture loans taken from co-operative banks has been announced by the government to redress their greivances.¹⁵
- 7) Small businessmen are up in arms against Govt's decision of demonetisation because

literally their businesses have been destroyed due to liquidity crunch. The Govt's decision to stand guarantee for loans up to Rs.2 crore given to small businesses is to revive their businesses. ¹⁵

CONCLUSION

Demonetisation has caused grievous injury to all those honest Indians who earn wages in cash, transact in cash and save in cash legitimately. It is well understood that black money is detrimental to a country's economy. All black money is not in cash, only a tiny fraction is. Holders of black money keep their wealth in form of real estate, gold, deposits in foreign bank accounts and beenami transactions. The government may have used other measures to obliterate black money to target holders of such unaccounted wealth and not on all citizens. The current measure does not address the continued generation of black money through tax evasion. Another reason behind demonetisation i.e. immobilizing counterfeit currency is also lacking in credibility, as such currency is estimated to be Rs. 400 crore, a very small proportion i.e. 0.03% of total currency demonetised in 500 and 1000 rupee notes. At a time of low export growth, less industrial production, and increased unemployment in informal sector, this measure can act as a negative shock to the economy. The boost in demand for domestic production can only come, when the circulation of money returns to normal. Last but not the least digital economy is indeed the future of India but the country is not ready for such an immediate shake-up.

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