

Demonetisation in India: A Blessing or a Cause of Misery for the Indian Economy

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ABSTRACT

Indian government has taken a surprising move to demonetise the two large denomination notes of Rs 500 and Rs 1000 notes on 08 November 2016. The demonetisation was done in an attempt to curb corruption, counterfeiting, reducing income inequalities among the people of India and especially the accumulation of black money. Demonetisation's impact was felt by every Indian citizen. It came like a flood that washed out about 86% of Indian currency that was held as black money and fake currency and it was removed out from the economy and converted it into the legal, authorised and taxable part of the economy. The present study is an effort to apprehend about the demonetisation decision and its impact on the Indian economy. The purpose of the present work is also to explain the impact of such a step on black money and corruption.

Keywords: - Demonetisation, cease, economy, black money.

INTRODUCTION

Demonetisation is the move to cease a currency unit or put an official stop on its status as a legal tender. It is a considerable step the government of India has taken on 08 November 2016 to cease the currency units of Rs 500 and Rs 1000 notes as a legal tender and the newly designed notes Rs 500 and Rs 2000 notes were placed in circulation from 10 November 2016. In other words demonetisation is the death of old currency units and birth of new currency units in order to combat the black money and root out the corruption from the economy.

The bold action was taken by the Prime Minister Narendra Modi in an effort to curb the menace of corruption, fake currency, black money and unaccounted money. This step is expected to restore the established economic system and discard black money from the same.

Demonetisation is a rich and symbolic landmark in the history of Indian economy. To some extent demonetisation created agitation in the minds of people who entertain in illicit activities like tax evasion or money laundering of any kind. When on 08 November 2016 Prime Minister Narendra Modi announced that the Rs 500 and Rs 1000 notes will no longer be a legal tender, and Reserve Bank of India issued newly designed and of different sized notes of Rs 500 and Rs 2000 notes which were highlighting the cultural heritage and scientific achievements of the country were introduced and placed in the circulation. During a short span of time from 09 November 2016 to 31 December 2016 the Reserve Bank of India geared up 23.8 billion pieces of bank notes into circulation. Demonetisation policy is likely: an accumulated demand shock because it decreases the supply of money and affects private wealth (especially of those holding unaccounted money and owning real estates, and an uncertainty shock because economic agents face imponderables related to the impact and duration of the liquidity shock as well as further policy responses (causing consumers to hold off or reduce discretionary consumption and firms to reconsider investment plans).

Objectives of the study

1. To ascertain the causes and impact of demonetisation on Indian economy.
2. To identify the future of note ban decision in India.

Research Methodology

The study is all descriptive in nature and is all dependent to secondary data which is collected from the various journals, newspapers, various bulletins of Reserve Bank of India and various publications and websites which has been published and focused on various aspects of demonetisation.

REVIEW OF LITERATURE

Lokeshuke (2017) Demonetization in India is a great effort taken by India government to fight with black money and root out corruption. Government of India become successful to some extent. Most of the black money has been crumpled. Some economics expert said that positive impact of demonetization will showed in future. Government has also increased the removal limits. The lines in front of banks and ATMs have reduced. Somehow black money also comes out. Now we should wait and watch the overall impact of demonetization drive.

Prasannkumar das and Nirmal Kumarrouitia (2017): Black money holders will definitely lose out eventually boosting the formal economy in the long run. Short term fall in real estate prices might benefit for middle class citizens in India.

Suprabha (2017): Demonetization of Rs 500 and 1000 Rs notes will benefit the economy in long run. This process would also effectively bring in huge amount of money from the informal sector, which was unaccounted for. This will help in the growth and therefore GDP would not face a negative impact.

Amartya Sen (Leading economist; Noble Laureate; recipient of the Bharat Ratna) According to Indian express, Professor Amartya Sen said that millions of innocent people have deprived from their money and being suffered to get their own money back.

Dr. Manmohan Singh (Former Prime Minister; eminent economist; former RBI governor)

According to Indian express, the former prime minister, RBI governor, and economist Dr. Manmohan Singh said in Rajya Sabha that this demonetization is an organized loot. In his speech he said that, the way the scheme has been implemented will harm the agricultural sector in India, it will also harm the small scale industry and informal sectors of the economy.

He also said that India's GDP can falls about 2 percentage point as a result of this note banned policy. Cooperative banks which serves the rural areas are non-functional and has been prevented from cash. Former prime minister also said that this note banned policy is a monumental mismanagement.

Arun Jaitley (Current Finance Minister of India; Senior Advocate, Delhi High Court)

According to Indian Express Mr. Arun Jaitley gives his opinion that the demonetization is good for economy, Indian banks were facing NPA problem since last many years, now banks will have more money to lend for many sectors of the economy.

BACKGROUND / HISTORY

This is not for the first time the Government of India have demonetised the currency. Earlier to this India has witnessed demonetisation into two episodes:

1. The first episode

For the first time demonetisation took place in pre - independence period. In January 1946 the currency units of Rs 1000 and Rs 10,000 were taken out from the economy. The withdrawal of these notes did not have much blow as the currency of such higher denominations was not approachable to the ordinary people. After all the two currency units were put back in 1954 along the new entry of Rs 5000 currency unit. Rs 500 and Rs 1000 currency units were brought in 1934 and later four years in 1938 Rs 10,000 were bring forwarded.

2. The second episode

In the second episode the Janata Party Coalition Government, the then Prime Minister Morarji Desai in 1978 announced the demonetisation of Rs 1000 , Rs 5000 and 10,000. The exclusive objective was to curb the black money production /generation in the country. In January 1978 episode currency worth INR 1.46 ban (1.7 %) of total notes in circulation was demonetised of this INR 1.0 ban or (68 %) was enlisted back. In 1978 the value of demonetisation was very small (only 0.1 % of G.D.P) However the 2016 demonetisation efforts covers 86 % of the total currency in circulation (11 % of G.D.P)

IMPACT OF DEMONETISATION

The Indian economy which was labelled as the "fastest growing economy "in the world , the only "bright spot" among emerging market's seems to have slowed down even before the latest "shock therapy "of demonetisation. In fact it is a matter of concern because as per the central statistics office released the projected growth figures that are downwards from 7.6 % to 7.1 % for the financial year ending March 2017.

Nobel Laureate Amartya Sen has called the Narendra Modi government's demonetisation move "despotic action that has struck at the root of economy based on trust. Demonetisation undermines notes, it undermines bank accounts, and it undermines the entire economy of trust. That is the sense in which it is despotic. "It's a disaster on economy of trust. In the last 20 years, the country has been growing very fast. But it is all based on acceptance of each other's word. By taking despotic action and saying we had promised but won't fulfil our promise.

Academic and writer Kanchallaiah has termed the note ban exercise as the "biggest instance of social smuggling" ever, and alleged that the big capital of the country has earned 27 per cent more profits post-demonetisation despite the gloomy trend of GDP growth rate.

1. Impact of Demonetisation on GDP

Demonetisation is technically a demand shock that reduces the supply of money and affects private wealth (especially of those holding UN accounted money and owning real estate) in a short run. Growth rate was lowered by this move, but in near future it could be beneficial in long run if formalization increases and corruption decreases. Cash intensive sectors (agriculture, real estate, jewellery) were affected more. Informal output could decline but recorded GDP will increase as the economy becomes more formalized

2. Impact of demonetisation on black money

Only a little part of the black money as a matter of fact is collected in the form of cash. Generally majority of the black money is kept in the form of physical assets like real estates, gold, building etc. The long term effect will be much impactful and depends considerably over how government disposes more measures to detect black money.

3. Impact of demonetisation on bank deposits

It is well-known fact that near about 86 percent currency circulation in India was composed of 500 and 1000 currency notes. And demonetization of these notes made people deposit their money which was in the form of 500 and 1000 Rs notes into the banks. RBI had declared Bank had received Rs 5.12 trillion worth of deposits until 18th November. This deposit of money can boost Indian GDP by 0.5 to 1.5 percent. India's largest public sector State Bank of India (SBI) said it had received Rs.1.27 trillion worth of cash deposits.

4. Impact of demonetisation on Fake Currency

According to the ISI (Indian Statistical Institute, The ISI study was based on volumes of FICN detected and cash transactions in the banking sector), the circulation of the total amount of fake currency in India is Rs.400 crore at any given point of time. It is also estimated that around Rs 70 crore fake currencies are being injected into India every year. The value of fake currency in circulation at any given time is Rs 400 crore, and 250 in every million notes are fake, according to this 2015 joint study by the Indian Statistical Institute and National Investigation Agency, to analyse fake-currency trends, especially those originating across India's borders.

The study estimated that fake currency worth Rs 70 crore enters circulation every year, with agencies only being able to intercept one-third of it, the Times of India reported in May 2016. The detection of fake currency is carried out primarily by commercial banks, but such reporting is irregular: Only three banks i.e. HDFC, ICICI and Axis bank report about 80% of fake currency is detected.

Positive impact

A well planned demonetisation order can be affirm beneficial for any economy, despite in case of fumble support this may also account complication, so a public backing is needed for the overall success of the demonetisation. By a flawless implementation demonetisation decision can provide a great boost to the Indian economy. The few reasons which were the positive and negative part of the demonetisation decision are:

- ★ The prime objective of demonetisation was to eradicate black money and use of fake currency. Some portion of the black money is eliminated from the economy. This money can be spent by Indian government for the development of country.
- ★ To some extent corruption was rooted out from the economy and black money generation was reduced.
- ★ Removal of old currency will carry UN accounted money back into the banking system through extensive increase in bank deposits. By this, out of action money will become active and beneficial.
- ★ Demonetisation leads to cut down tax avoidance by boosting higher tax payments and the most important thing is the number of new income tax payers increased. Income taxes could go up because black money was deposited in bank accounts.
- ★ Demonetisation made Indian economy less dependent on cash which is a boost to Indian economy. It boosted the digital payment process to attain the target of a cashless nation

Negative impact

- ★ Cash/liquidity crunch is dominant disadvantage of demonetisation due to the unavailability of Rs 500 currency units and Rs1000 currency units which make it difficult to make small purchases.
- ★ GDP growth was earlier estimated as 7.6%. Post-demonetization, estimates are lowered to 7.1%.
- ★ Disintegration and break down of economic activities makes the economic growth at pause for short period of time
- ★ The withdrawal limit from banks and ATMs was reduced when demonetisation was on its peak.
- ★ Demonetisation couldn't help in flushing out the black money fully because the other forms of black money i.e.; many people who had not kept cash as their black money and rotated or used that money in other assets like real estates, gold, and electronic equipment's etc. This needs to be duly tracked controlled and judiciously detected. If we need to accomplish the particular goal of total decrease of black money from Indian economy

- ★ Consumer demand was hit by demonetization, hence retail inflation fell to 3.17% a multi-year low. With this, growth of economy will slowdown.
- ★ Agriculture sector, small and medium scale businesses and informal sectors are the worst hit by demonetization. It takes a lot of time for them to recover from the losses. This has a negative effect on Economy.

CONCLUSION

Demonetisation of Rs 500 and Rs 1000 notes will lead the economy towards the prosperity in a long run by reducing the black money generation and fake currency. For overall success of the demonetisation it must be properly handled and implemented and it is important to reduce the ill effects of demonetisation else it may become a cause of misery for the Indian economy. Now it depends on the government policies and strategies how well they are planned and executed. Demonetisation will bring back the unaccounted money into the banking system. This will help in the growth of economy and G.D.P will be geared up. Demonetisation has negative impact on some sectors but for short period only. It is expected that the demonetisation will bring economic revolution in India and country will get rid from black money and corruption.

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