

“A study on impact of demonetization on Indian Economy”

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ABSTRACT

It is vital for an economy to initiate real change so that they can start to regain the public’s trust and rebuild their brands reputations.

Purpose – The aim of this paper is to study the impact of demonetization on the growth of Indian economy in present scenario.

Design/methodology/approach: The study will be carried out based on e-literature available, books, magazines etc .

Findings – The study will try to underline the essential reasons as to why the policy of demonetization was introduced without prior information as a secretive mission and its impact on the economy.

Practical implications – The action of demonetization leads to equal and opposite reaction by the various sectors of the economy.

Keywords: Black money, currency, Demonetization, Indian Economy and Gross domestic Product (GDP).

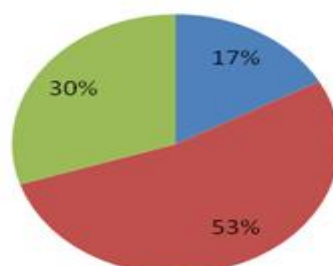
INTRODUCTION

Demonetization is an essential economic step in which some old currency is declared to be invalid. This is usually done whenever there is a change of national currency, replacing the old currency with a new one. Indian Economy has witnessed Demonetization three times till date. ^[2]It was a historic day Nov. 8, 2016 when Prime Minister of India Sh. Narinder Modi Ji addressed to the Indian Economy and declared that currency notes of 1000 and 500 will not be a legal tender of money. ^[1]In India Demonetization has been done three times. 1946, 1978 and in 2016. In first Demonetization the circulation of Rs. 1000, 5000 and 10,000 were taken out from January 1946 and in 1954 all these notes were Reintroduced. In 1978 high value notes were ceased to be legal tender at close of banking hour. The Third Demonetization has been done on Nov. 8, 2016. All 500, and 1000Rs. Notes has been ceased. All banks and treasuries shut for transactions on January 17.

^[5]As stated by CMA Jai Bansal(2017), demonetization affected majorly three sectors got impacted those were agriculture sector, service sector and manufacturing sector. The most affected sector was the service sector which deals with the more of cash based transactions. Also service sector includes the major sector that was banking and due to currency crunch they were burdened with new guidelines for successful implementation of demonetization. Further the tourism industry got affected, due to sudden announcements for which the tourists and the common public was not prepared.

Contribution in GDP

■ agriculture ■ Service Sector ■ Manufacturing Sector



Data Source: CMA Jai Bansal, “Impact Of Demonetization On Indian Economy”, ICIRSTM-17, January 22-23, 2017.

According to the RBI's (Reserve Bank of India), the Annual Report for the Financial year 2015-16, the currency value was 16.42 trillion Indian rupees. The currency value of 500 rupee and 1,000Rs. notes formed 86.4%. In one hit, the government removed 86.4% value of the currency in circulation. In terms of volume, the currency notes of Rs.500 and 1000 formed 24.4% of a total 90.27 billion pieces.

^[4]There are multiple reasons why nations demonetize their local units of currency:

- to combat against the rising prices of goods.
- to fight against corruption and crime .
- to encourage cashless transactions(to convert black money into white)
- to facilitate Sale / Purchase

LITERATURE REVIEW

- Jain, P.M (2006) in his article "E-payments and e-banking" reviewed that black money can be monitored by e-payments an analysis of growth pattern of cashless transaction system. Technology will be like boom through which quick payments and remittances will provide optimal use of funds for banks, business houses, financial institutions and Indian citizen. He also explained that the needs for modes of e-payments and communication networks will also be increased.
- HDFC Bank Investment Advisory Group (2016), elaborated that in the long run, demonetization would be a positive move in case of infrastructure and Banking through an equity market perspective. In short term, it can have negative impact on sectors like Luxury goods, Consumer items, Luxury, Jewellery and Gems, Real Estate and few related sectors. In long run, it can lead to improved tax compliance, better fiscal balance, lower corruption, lower inflation and complete elimination of fake currency .It will also help in improving the economic growth in long run.

Objectives of the Study

The purpose of the study is to know the impact of sudden announcement of demonetization in the growth of the Indian economy in banking sector.

- To identify the impact of demonetization among the public in India
- To identify the banking process in India.
- To know the impact of government. steps on control of black money in India.

Research Design:

This study comprised the descriptive research design. It reports the past and present situation of the public intention towards government action.

Impact of Demonetization in its third phase in India

^[3]There is a common saying that "Some of the most beautiful things worth having in your life come wrapped in a crown of thorns." In the same way although with the positive impact of demonetization on economy it has also some negative impact.

Positive Impact:

- Positive Impact of Demonetization is that it eliminates the black money and this money will be spent by the government for the benefit of country.
- Government blocked many routes to collect black Money.
- With the fear of government moves, everyone has to pay taxes, which will help to improve the income of the country.
- Demonetization encouraged the cashless transactions which help the country to move towards the progress and make it better.
- Due to Demonetization more money will be collected in Banks and more loans will be available to people.
- With the cashless transactions, people will keep more money in banks and hence savings will be increased.

Negative Impact:

- It is a practice or we can say that it is an experiment but not sure that Demonetization will turn India into a cashless economy.

- As stated in the “Group Discussion, updated on 19th Feb. 2017 by Aneka Aleti that In earlier it was estimated that GDP growth was 7.8%. Post-demonetization, it was estimated lowered to 7.1%.
- Demonetization affects very badly on Agriculture sector, informal sector and small/ medium scale businesses. It takes a long time period to recover them from the losses. It hits very badly on economy.
- Consumer demand also affects badly by demonetization, through which retail inflation goes down to 3.17%. This will slow down the growth of economy.

Aftermaths of the Demonetization on Indian Economy

Modi ji said in his speech that after demonetization, only 24 lakh (2.4 million) Indians acknowledge an annual income of Rs. 10 lakh each (Rs. 1 million). “Can we digest this? Look at the big bungalows and big cars around you,” he said. “If we look at any big city, it would have lakhs of people with annual income of more than [Rs.] 10 lakh. Do you not feel, that for the good of the country, this movement for honesty needs to be further strengthened?” The upshot of that is his government would now try to bring hundreds of thousands of tax evaders into the net.

Demonetization and Banking

Digitalization is the major step which Government of India under the leadership of Prime Minister Sh. Narendra modiji is promoting along with various other schemes. It is focused so as to bring transparency in system in terms of banking services. People here prefer to use more of cash transactions instead of card and terrorists use this currency for illegal and antinational activities. More flow of money using cash transactions also increase flow of black money in the economy, In order to curb the rising incidence of black money and hoarding the GOI in consultation with RBI and finance ministry withdrew the legal character of bank notes and introduced new currency notes with due support of RBI governor Sh. Urjit Patel.

Demonetization was not just a policy but a totally different phase public, organizations and every economic activity faced for which most of them were unaware of effects, history and legalities. As per the CEO and Managing director of Yes Bank Mr. Rana Kapoor “This was shock treatment, and sometimes India reacts positively to shock treatment” [8]. This policy made people faced enormous problems but they welcomed it also. The governments of any economy cannot make decision like demonetization at their own there are proper regulations mentioned .The legal basis for the order demonetizing currency can be found in Section 26 of the Reserve Bank of India Act, 1934. Under sub-section (2) of this Section, the Union Government is given the power to declare that any notes issue by the Reserve Bank will no longer be legal tender. The only procedural requirement is that the Board of the RBI recommends the same to the Union Government [7].

Banking system whose primary function is to accept deposits and lend loans were working more with functions of financial institutions and performing secondary and tertiary functions. The act of demonetization once again called for the main functions of the banks to be performed on priority. [6]The banks were the major role player during this phase. Some major steps taking by central bank of India i.e. RBI was as follows:

- To relieve the loan payers and small borrowers, the RBI announced a 60-day loan extension for repayments for managing the term loans/crop loans etc. This facility was applicable to loans payable between November 1 and December 31, 2016.
- It was the season of weddings going and to facilitate the Indian public to meet wedding expenses the RBI announced a higher limit of cash withdrawal upto Rs. 2,50,000.
- The weekly cash withdrawal limit was specified upto Rs. 50,000 by RBI in the denominations bank notes.
- Cash withdrawal limit for farmers was fixed upto Rs. 25,000 per week and for traders upto Rs. 50,000/- registered with Agricultural produce market committee.
- In order to manage the queues at the ATMs. The GOI directed RBI to introduce micro ATMs in rural areas, urban and semi urban areas. These ATMs will be Aadhar enabled which can manage around 70,000 transactions per week
- As per RBI report released on May 29, 2017 ; with effect from February 1, 2017 limits on cash withdrawals from ATMs have been removed. Banks may, at their discretion, have their own operating limits as was the case before November 8, 2016, subject to the overall cash withdrawal limit for an account.
- The overall positive impact of demonetization on banks was increase in CASA value of bank deposits which simply means increase in current and saving deposit rate.

To know the impact of government steps on control of black money in India:

According to National Institute of Public Finance and Policy (NIPFP) defines-
“Black Money is the aggregate of incomes which are taxable but not reported to authorities”. It is the money that is not fully legitimate property of the owner. It can be generated through legal ways i.e. not reported to public authorities or

we say to the govt. for the purpose to evade taxes and Trading and illegal ways like drug trafficking, weapons trading, terrorism, selling counterfeit, stolen goods or Corruption which includes bribe given to and by public officers etc.

Consequence of Black Money: The gap between rich and poor people is the main consequence of the black money. Wasteful consumption of our economy i.e. misuse of money on consumption rather than investment. Earning of black money is much easier than the hard work efforts which leads to decrease in the working efficiency of people.

Black money and demonetization:

[14] About demonetization, Singh and Singh (2016: 625) have stated as follows:

This move is expected to cleanse the formal economic system and discard black money from the same. But demonetization has been important to combat corruption, to control the crime of black money and counterfeit. People have been unnecessarily criminal today for the sake of earning money which has no limit.

According to news of Forbes magazine, eight people have got the equal sum of property of the half of the total population of the world today. That proves, the total property of 8 people is equal to the total property of 3,65,00,00,000 people. But this property is earned through their business with tax clearance where no fraud black money is noticed.

Immediate impact:

Immediate impact of demonetization comes to the effect through depositing of black money in the banks. It is believed that nearby Rs. 1.5 to 2 lakh crore is identified as the black money and nearby Rs. 1.2 lakh crore may be collected as the tax. [20] According to National Institute of Public Finance and Policy (NIPEP), black money will be amounting nearly 40% of country's GDP.

One major reason of Demonetization is to control the flow of black money in India. This issue has been solved but only to some limited extent. Beside cash, Physical assets like gold and Properties are also a part of black money. Therefore the amount of money that is countered by demonetization depend on the cash only and other factors remain unaffected. Secondly, people have to give complete declaration about the source of their income to the authorities but income in excess of threshold limit is only the subject to scrutiny. Thirdly, it will aware people and change its mindset to some extent about legal and punitive effects of demonetization over black money.

Future impact:

- Once the money will be in legitimate channels than effective utilization of it will be done and revenue will be generated from its use.
- the use of plastic money like debit cards, credit cards and online transactions etc. can put restriction on the flow of black money in future.
- [18] As per RBI rules, withdrawal from any account need PAN card and manager of each Bank need to file detailed weekly or monthly cash transaction statement which will help tax authorities to monitor the whole case.
- Land prices and gold prices are likely to be fall in future and if it so. The poor people can purchase land and in the case of gold, forex pressure on INR will be ease a bit.

CONCLUSION

Demonetization was no doubt a temporary phase but it affected the economy such as senserx reached its lowest point in whole year after this action. Sudden announcement of demonetization has produced a fear in the minds of public for government future secretive plans. This short term plan whether turned beneficial in terms of authenticity and transparency for Indian economy can be seen in long term only. Banks played a vital role in successful implementation of demonetization and found a net growth in their deposits

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