



A CRITICAL REVIEW OF INDIAN ECONOMIC SCENARIO POST DEMONETISATION

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Abstract

Demonetisation can be defined as the act of stripping a currency of its status as legal tender, the demonetised currency notes and coins are no longer accepted as legal tender and are sooner replaced by newly issued currency notes or coins. Demonetisation has been used as a tool to stabilize a currency when there is inflation in the economy, to facilitate trade and access to markets, and to move the economic activity towards more transparency and away from black and grey markets.

The Government of India withdrew 500- and 1000-Rupee notes from the monetary circulation on November 8, 2016 and the announcement came as a surprise and brought with it a lot of hassle for the citizens of the country. The economic agents were given limited time to return the demonetised currency notes to Reserve Bank of India through the Banking Channels. The Prime Minister in his address to the nation for announcing the demonetisation had emphasized the main objective was to remove black money and reduce corruption and money laundering. The RBI Annual Report 2017-18, released, shows that almost all the banned banknotes, or 99.3% of the notes withdrawn, were returned to the central bank. Thus, we can say demonetisation was a success as 99% of the withdrawn currency reached RBI and India is moving toward a cashless society, but it also brought about some problems for Indian Economy like slow GDP growth, less cash in the economy thus slower development basically in the agricultural sector which flowed to other sectors of the economy. Through this paper we would like to discuss and throw light on the implications of demonetisation on the Indian Economy.

Keywords: *Demonetisation, Unaccounted Money-Black Money, Cashless Society, Corruption, Money Laundering.*

Introduction

Demonetisation is the act of stripping a currency of its status of being legal tender and then replacing the old currency by a new legal tender. Demonetisation generally happens when there is inflation or excess circulation of currency, when there is corruption which leads to hordes of black money and to facilitate trade and access to markets. In India the 500-1000 rupees notes which formed the major part of the monetary circulation i.e 86.4% of the total money circulation, were ripped of their status of being legal tender and the main reasons for demonetisation as brought forward were to eliminate black money, fake money, money laundering, terror funding.

When we look at Indian history, the first demonetisation was on 12th January 1946 (Saturday) when notes of 1000, 10,000 were demonetised, second on 16th January 1978 (Monday)- when notes of 1000, 5000, 10,000 were demonetised and the third was on 8th November 2016 (Tuesday)- when 500, 1000 were demonetised.

Demonetisation in the short run would be a blow to the overall production activity in the economy as there will be shortage of liquid money in the economy this will lead to increase in unemployment index. The GDP growth of the country will also be adversely affected. But, demonetisation in the long run would make Indian economy one of the fastest growing economies and will also make the Indian tax structure a buoyant one with more people paying taxes. It will help formalize India's informal economy, by reducing the amount of cash transactions and helping India move towards a cashless economy.

Purpose

The main purpose of this paper is to understand what demonetisation is? and why does it happen? And to throw light on the path the Indian Economy has taken post demonetisation.

The paper tries to bring forth some positives and negatives of demonetisation.



The inferences of this paper are based on secondary data available across various literatures works and government sources.

Literature Review

CHARAN SINGH (2018)-India Since Demonetisation

<https://www.iimb.ac.in/sites/default/files/2018-06/Demonetisation.pdf>

In this paper the author has discussed, about the effect of demonetisation on the Indian economy. The paper brings forth, that the experiment of demonetisation by the Government has largely been successful in educating the masses about the benefits of electronic payments and digitalization. It has tried to limit cross border militancy funding and to curb corruption. He has highlighted on the point that India being a developing economy is cash driven and withdrawal of currency notes from circulation has slowed down the economic growth and had its effect on the GDP of the country.

The paper by Mr. Charan Singh, attempts to capture the course of the Indian economy since demonetisation of November 2016. By this paper, an attempt is made to understand demonetisation in a continuum of other major policy reforms taken in the economy like GST, and Digital India. The paper attempts to evaluate major fiscal and monetary variables and their trends pre and post-demonetisation along with an analysis of sectoral performance of economy during the period.

Analysis and Rationale

The rationale of this paper is to understand Demonetisation and to put light on the reasons behind demonetising or stripping a currency of its status of being a legal tender.

The paper tries to analyse the aftermath of demonetisation in terms of the positives and negatives which have come forth as result of withdrawal of currency from monetary circulation.

Core

The Indian economy was struck with its third demonetisation in its history on November 8, 2016. The aftermath of demonetisation brought about many positives as well as negatives. The demonetisation led to the withdrawal of 500-1000-rupee notes from the money circulation, these notes were forming 86.4% of the total money supply in the economy. The withdrawal of the 500-1000- rupee notes from the monetary circulation was a jolt to the Indian economy as it led to shortage of liquid cash in the economy which affected production and other sectors of the economy and the resultant was slow GDP growth and unemployment in the economy. But the major plus point was the movement of the Indian economy towards a cashless economy.

Demonetisation led to withdrawal of 500-1000-rupee-notes from monetary circulation and they were replaced by new 500- and 2000-rupee notes by the Reserve Bank of India. The public was given limited time to deposit the stripped currency to the RBI through banking channels, there was a cap on the amount of demonetised currency which could be deposited by an individual, which was ₹2,50,000 and the account holders were asked to submit a copy of their PAN cards for deposits above ₹50,000 to enable the Income Tax department to track the movement of cash. The people could exchange the banned banknotes for legal tender over the counter at all banks. The limit for such exchange was ₹4,000 per person from 8 to 13 November which was increased to ₹4,500 from 14 to 17 November and reduced to ₹2,000 from 18 to 25 November. The exchange of banknotes was stopped completely on 25 November. Cash withdrawals from bank accounts were restricted to ₹10,000 per day and ₹20,000 per week per account from 10 to 13 November. This limit was increased to ₹24,000 per week from 14 November 2016. Limits on cash withdrawals from Current accounts/ Cash credit accounts/ Overdraft accounts were withdrawn later. RBI increased the withdrawal limit from Savings Bank account to ₹50,000 from the earlier ₹24,000 on 20 February 2017 and then on 13 March 2017, it removed all withdrawal limits from savings bank accounts. A daily limit on withdrawals from ATMs was also imposed varying from ₹2,000 per day until 14 November, and ₹2,500



per day until 31 December. This limit was increased to 4,500 per day from 1 January, and again to 10,000 from 16 January 2017. From 17 November, families could withdraw 250,000 for wedding expenses. Farmers were permitted to withdraw 25,000 per week against crop loans.

The government in its announcement mentioned the banned notes could be used at government hospitals, fuel pumps, railway and airline ticket counters, state government recognised dairies and ration stores, crematoriums, the travellers could exchange demonetised for foreign currency at airports until December 2, 2016.

The Indian government had taken a few steps in the direction of demonetisation in the background before demonetisation was actually announced on November 8, 2016, the government had urged the people to open bank accounts under 'Pradhan Mantri Jan Dhan Yojana' and carry out all monetary transactions through banking channels only. The government had also urged all the taxpayers for Tax Declaration and had given a deadline till October 30, 2016.

The government in its announcement for demonetisation had highlighted the following objectives

1. To tackle black money in the economy.
2. To reduce the amount of cash circulation in the economy and thus control corruption.
3. To eliminate fake currency and money laundering.
4. To curb tax evasion in the economy and thus increasing the amount of tax collections which will further development.

Demonetisation led to lot of benefits for the Indian Economy, the following are some

The Indian economy took a step towards digitalization as more people starting using internet banking, digital wallets, BHIM UPI and there is less dependence on liquid cash. This has brought the cash transactions in the purview of accountable money thus curbed corruption to some extent. Economic Survey 2016-17 showed that currency in circulation contracted by 19.7 per cent whereas reserve money contracted by 12.9 per cent.

According to the 2018, RBI Annual report 99.3% of the demonetised currency had reached the Central bank, thus helping remove the counterfeit or fake currency from the monetary circulation.

As per the Income tax department there was a marked improvement in the number of IT returns filed post demonetisation, It further stated that the total number of all returns (electronic + paper) filed during the entire Financial Year 2016-17 was 5.43 crore which is 17.3 per cent more than the returns filed during FY 2015-16. The Tax department also put out number of new taxpayers and said: "For Financial Year 2016-17, 1.26 crore new taxpayers (return filers + non-filers making tax payments) were added to the tax base."

The government post demonetisation was able to identify many shell firms which were involved in suspected activities and government cancelled their registration. The CBDT claimed to have identified over 300 Benami Properties in their Income Tax's clean money operation after demonetisation.

The Government also introduced Goods and Services Tax post demonetisation, thus bringing all indirect taxes under one window, thus a step towards more and efficient tax collections.

Demonetisation brought about many benefits but alongside there were some negatives which the economy had to face; we would like to bring forth some of them

There was huge pressure and strain on the Central Bank and the banking institutions in the aftermath of demonetisation as the banned notes were returned through the banking channels. There were huge queues at banks and people had to go through lot of hassle.

When demonetisation was announced, the RBI and the currency printing presses were unprepared to replace the volume of the recalled currency notes. The RBI spent close to Rs 13,000 crore over the next two years to remonetise Indian money market and issue the new 500- and 2000-rupee notes.



There was a reduction in Industrial output, The Purchasing Managers' Index (PMI) fell to 46.7 in November 2016 from 54.5 in October 2016, recording its sharpest reduction in three years. The agricultural activity was adversely affected as agricultural transactions are based on cash.

The GDP growth rate took a fall due to demonetisation, the Q4'16-17 rate was 6.1% as against a forecast of 7.1% by economists. The rate for the financial year 2016-17 was 7.1%, a reduction from the 8% in 2015-16.

There was a fall in the in the number jobs and in the rate of wages post demonetisation especially in the informal, unorganised and small enterprise sector. As per CMIE, the number of employed forces fell from 439.7 million in 2016-17 to 426.1 million in 2017-18, due to demonetisation.

**(The references for the figures quoted above are mentioned at the end of the paper)

Conclusions

This paper has tried to through light on demonetisation and bring forward the effects of demonetisation on a developing economy like India. There are many positives as well as negatives which have come forth as result of demonetisation. The Indian economy has taken a step towards digital transactions and cashless society but still far away from a fully cashless society as India is still a primarily agricultural economy wherein major transactions involve cash.

The GDP growth rate is coming up as per the, the Economic Survey India's GDP is set to grow at 7 to 7.5 percent in 2018-19.

As per the economic survey the import and export sector are also bouncing back with the export growth to 13.6 percent in the third quarter of Financial Year 2018 and deceleration of import growth to 13.1 percent.

As per Economic survey the Income Tax collection is at a new high post demonetisation and introduction of Goods and Services tax.

Though we are improving on the drawbacks, we are still not able to fully curb Black money, corruption and money laundering in the economy and till we do that successfully we cannot say that we have fully realised the benefits of Demonetisation of November 8, 2016.

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