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## IMPACT OF DEMONETIZATION ON INDIAN ECONOMY

**NEERAJ**  
**EXTENSION LECTURER**  
**GOVERNMENT COLLEGE**  
**FARIDABAD**

### ABSTRACT

*Indian governments declare that the five hundred and one thousand rupees' notes will no longer be legal tender from midnight, 8<sup>th</sup> Nov. 2016. The RBI will issue 2000 rupee note and 500 rupees note which will be placed in circulation from 10<sup>th</sup> Nov. 2016. Notes of 100, 50, 20, 10, 5, 2, 1 rupee are unaffected by this decision. This decision has been taken by the prime minister of India Mr. Narendra Modi to address the resolve against black money, corruption and counterfeit notes. This study will help us to know about advantages and disadvantages of demonetization decision taken by central government of India. The main purpose of demonetization in India is stopping of corruption, black money tracking and promotes the cashless transaction. The study based on secondary data.*

### KEYWORDS

Indian economy, black money, tax evasion, corruption, cash less economy.

### INTRODUCTION

In 2016, the Indian government decided to demonetize the 500- and 1000- rupee notes, the two biggest denominations in its currency system these notes accounted for 86% of the country's circulating cash. With little warning India's Prime Minister Mr. Narendra Modi announced to the citizenry on Nov. 8 that those notes were worthless effective immediately and they had until the end of the year to deposit or exchange them for newly introduced 2000 rupee and 500 rupee notes.

Chaos ensued in the cash-dependent economy (some 78% of all Indian customer transactions are in cash), as long snaking lines formed outside ATMs and banks, which had to shut down for a day. The new rupee notes have different specifications, including size and thickness, requiring re-calibration of ATMs only 60% of the country's 200,000 ATMs were operational. Even those dispensing bills of lower denominations faced shortages. The government's restriction on daily withdrawal amounts added to the misery, though a waiver on transactions fee did help a bit.

The government's goal (and rationale for the abrupt announcement) was to combat India's thriving underground economy on several fronts eradicate counterfeit currency, fight tax evasion (only 1% of the population pays taxes), eliminate black money gotten from money laundering and terrorist-financing activities and to promote a cashless economy. Individuals and entities with huge sums of black money gotten from parallel cash systems were forced to take their large-denomination notes to a bank, which was by law required to acquire tax information on them. If the owner could not provide proof of making any tax payments on the cash, a penalty of 200% of the owed amount was imposed.

### OBJECTIVES OF DEMONETIZATION

#### 1) Removing black money from country

Prime Minister Mr. Narendra Modi has done a really good work, as People who are having black money will now be left with nothing particularly. All the Cash which resides below the pillow, will now be useless (Although small amount of black money can be converted in to white, but amount in hundreds of Crore of rupees Is almost next to Impossible to make It white)

#### 2) Stopping of corruption

By removing the currency notes from circulation, it will have a direct Impact On corruption. People who have these notes will now be left with nothing.

#### 3) Stopping terror funds

Because of demonetization, the people or organizations who used to fund terror groups will be now sitting without any works, they will naturally die and that too with starvation.

#### 4) Curbing fake notes

Demonetization will also stop the circulation of fake notes in the economy (although the amount of fake notes revolving in the economy was around 400 Corers).

#### 5) Stopping Illegal dabba trading

Due to demonetization, the Illegal share trading and dabba trading will cease to exist. This will ensure stability in share markets, especially at these 'Times of Turbulence'

#### 6) The Uttar-Pradesh elections

It is generally seen that, there is ample liquidity in the states, where elections are to happen, and this thing is considered as vote bank and politicians buy votes of people by offering them money, if they vote for them. Now because of demonetization, vote bank system will not be in existence (The proof here is currency notes, which were found from river Ganga). As an ultimate result, we would see transparent elections.

#### 7) The Betting On U.S. Presidential election results

It seems that prime minister Mr. Narendra Modi is well aware of the fact that Indians are a master in betting at anything like as because of his address to nation at 8:00 pm, there will be no betting done on the US Presidential election results, or at least Its quantum would be less than, what It should be have earlier.

#### 8) To send a clear message that this Government is well inclined towards working for the development of nation

Because of his bold step, it will send a clear message that this Government is well inclined towards Development of Nation. It will also send a message to the International community, that the Government is doing constant efforts to make India a better Place to Invest and a Better Place to do business.

### RESEARCH METHODOLOGY

The data has been collected from secondary sources from websites, blogs, journals, magazines, newspapers etc.

### IMPACT ON ECONOMY

The Indian Economy which was billed as the "fastest growing major economy" in the world and the "only bright spot" among Emerging Markets seems to have slowed down even before the latest "shock therapy" of "demonetization". Indeed, the recently released growth figures from the CSO or the Central Statistical Office considered to be the official department that releases projected, and actual growth figures (apart from the RBI or the Reserve Bank of India and the Finance Ministry) hints at a slowdown in the Indian economy even during the quarter before demonetization happened.

While this is indeed cause for concern with projected growth figures revised downwards from 7.6 % to 7.2% for the financial year ending March 2017, what is cause for greater worry and even alarm is the view among some economists including the former Prime Minister Dr. Man Mohan Singh (who is a reputed economist in his own right) that the current and ongoing attempt to flush out black money would shave a good 2% of the GDP or the Gross Domestic Product.

TABLE 1

Year-on-year change in %	FY17			
	Q1	Q2	Q3	Q4
GVA at basic prices	7.6	6.8	6.7	<b>5.6</b>
Private consumption	8.4	7.9	11.0	<b>7.3</b>
Investment demand	7.4	3.0	1.7	<b>-2.1</b>
Agriculture	2.5	4.1	6.9	<b>5.2</b>
Industry	7.4	5.9	6.2	<b>3.1</b>
Services	9.0	7.8	6.9	<b>7.2</b>

GVA: Gross value added

Source: Central Statistics Office

Some economists, said nearly 90% of the total cash in circulation has come back into the banking system and hence, the stated purpose of the Demonetization exercise which was to “extinguish” black money and enable the RBI to lower its liabilities thereby providing the government with a huge dividend seems to have been belied. Of course, there are some who now argue that the Indian Banking System is now “flush with cash” and this has enabled the government to “nudge” the RBI to cut rates as well as to allow banks to pass on the benefit of ample liquidity to consumers by lowering lending rates.

However, the flip side of this has been that banks have cut their deposit rates as well which is natural considering that any cuts to lending rates have to be accompanied by cuts to deposit rates. This has resulted in a situation where banks with enough deposits seem to be encouraging spending more than saving and this can indeed create demand in the system since more money with consumers means more spending thereby leading to an uptick in sales of goods and services and which has the “multiplier effect” of resulting in more growth.

On the other hand, with more taxes being collected due to higher deposits in banks that can be taxable as well as increased compliance due to greater scrutiny and oversight by the IT (Income Tax) Department, the government too might be tempted to announce lower rates for taxes and other aspects of what are known as fiscal measures. In this context, it is worth remembering that fiscal stimulus which is by lowering taxes and providing more incentives to consumers as well as producers by boosting supply can be complemented and supplemented by the monetary stimulus which is by boosting demand for goods and services by lowering lending rates thereby putting more money in the hands of consumers.

As economic theory states, both fiscal and monetary stimulus can be implemented in isolation or taken together and hence, the Demonetization or the Demo as it is being called might indeed act as a catalyst for growth. Having said that, one must remember that India is primarily a cash transaction based economy and hence, removing 86% of the money in circulation is indeed a “brave” move since there are reports that large sections of the informal economy have come to a grinding halt.

Moreover, there are also reports of farming sector taking a hit due to lack of cash as well as sales of automobiles and other capital goods falling even though inventories are building up. Thus, it remains to be seen as to how the growth figures for the next quarter and the overall financial year turn out to be. Given that mainstream economists tend to debate and argue both sides with equal passion and vigor, it is the case that as the cliché goes, the “proof of the pudding is in the eating” and hence, the actual growth figures have to be watched.

Of course, there are other indicators to keep track of as well in the form of various Indices such as the PMI or the Purchasing Managers Index which tracks industrial activity as well as the rates of investment and the credit pickup as well as the Inflation figures. Having said that, one must also note that given the lack of communication about some of the economic indicators from the government is indeed worrying given that Demonetization has been billed as the “Biggest Monetary Experiment” in recent times in the entire world.

TABLE 2

## Demonetization: Impact on the Economy

Extent of Impact	Reason	Sectors
Positive Impact	Higher taxes to spend	Infrastructure, public health, education
Minimal Impact	Low cash usage or Low value bills	IT Companies, Utilities, Telecom
Temporary Impact	High cash usage / low value transactions	Pharma, Consumer Products, Oil Marketing Companies, Banks
Sustained Impact	High cash usage High value transactions	Jewellery, Real Estate, Construction Material, Luxury products, Wedding arrangements

### ADVANTAGES

The main advantages of demonetization are given below:

#### BLACK MONEY TRACKING

This move will help the government to track unaccounted black money or cash on which income tax has not been paid. Individual who are sitting on a pile of cash usually do not deposit the amount in the bank or invest anywhere as they would be required to show income or submit PAN for any valid financial transactions. They would hide it somewhere and use it as when necessary. Banning high – value currency will impact people who will have no option, but to declare income and pay tax on the same or destroy the cash somehow. Now it is not possible to hide the money as the notes have been declared invalid.

#### REDUCTION IN ILLEGAL ACTIVITY

Banning high- value currency will halt illegal activity as the cash provide for such activity has no value now. Black money is usually used to fund the illegal activity, terrorism, and money laundering. Fake currency circulation will come to halt in a single shot. Corrupt officers, money launders are under threat as income tax department is taking all the measures to track such people.

#### TAX PAYMENT

Most of the businessmen who have been hiding some income are ready to pay advance tax as current year’s income. Tax payers who have been hiding some income can come forward to declare income and pay tax on the same. Individuals are required to submit PAN for any deposit above Rs. 50000 in cash, which will help tax department to track individuals with high denominations. Also deposit up to Rs, 2.5 lakh will not come under tax scrutiny.

**JAN DHAN YOJANA**

Now individuals are depositing enough cash in their Jan Dhan Yojana accounts which they were reluctant to do so a few days back. The amount deposited can be used for the betterment of the country.

**DISADVANTAGES**

The main disadvantages of demonetization are as follows:

- There has been a drastic Decrease in the Purchasing Power of People.
- The biggest disadvantage of demonetization is that once people in the country gets to know about it than initially for few days there is chaos and frenzy among public as Everybody wants to get rid of demonetized notes which in turn sometimes can lead to law and order problem and chaotic situation especially in banks and ATMs which are the only medium to change the old currency units to new currency units.
- Another disadvantage is that destruction of old currency units and printing of new currency new units involve costs which has to be borne by the government and if the costs are higher than benefits then there is no use of demonetization.
- Another problem is that majority of times this move is targeted towards black money but if people have not kept cash as their black money and rotated or used that money in other asset classes like real estate, gold and so on then there is no guarantee that demonetization will help in catching corrupt people.

**CONCLUSION**

Demonetization in India is a great decision taken by central government of India to combat the corruption and black money tracking. The government of India has become success to some extent. Most of the black money amount has been crushed. The demonetization drive will affect some extent to the general public, but for larger interest of the country such decision is inevitable. Also it may not curb black money fully but definitely it has major impact in curbing black money to large extent.

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