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DEMONETIZATION AND ITS IMPACT ON INDIAN ECONOMY

SUMIT BANERJEE

ALUMNUS

RANI DURGA VATI VISHWAVIDYALAYA

JABALPUR

ABSTRACT

Demonetization of currency means to discontinue with the said currency and issuing new currency by replacing the old one. In any economy, demonetization refers to an act of government of nation who pulls or discontinues the circulation of one or more than one currency. The money is pulled from circulation, often to replace by new notes or discontinued permanently. Prior to last year demonetization i.e. (year 2016) that high notes of rupee 500 and 1000 ceases to be a legal tender, there were two similar instances in India i.e. in the year 1946 and in the year 1978 when an ordinance was proclaimed formally that rupee 1000, 5000 and 10000 would stop being a legal tender. This article explores the advantages and impact of demonetization and its role in uplifting the economic growth of Indian economy.

KEYWORDS

advantages and limitations, cashless economy, demonetization of currency, impact on Indian economy, objective of demonetization.

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1. INTRODUCTION

Demonetization refers to devastating a currency unit of its status to be a legal tender. It occurs when government want to make a change in currency either by replacing old notes with new one or discontinuing particular currency permanently. According to Forbes "**Modi's Demonetization is a cure worse than disease in India**". Prior to the year 2016 demonetization, two similar instances took place. In India it has been done in

- 12 January 1946, Where Indian rupee 1000 and 10000 were withdrawn.
- 16 January 1978, where Indian Rupee 1000, 5000 and 10000 were withdrawn.

2. A REVIEW OF DEMONETIZATION IN INDIA

◆ Year 1946

The impact of demonetization in 1946 was minimal as higher denomination notes (which ceases to be a legal tender; demortized currency) constituted only 3% of the Indian economy.

◆ Year 1978

The second demonetization was done by Finance Minister H.M. Patel in budget speech on 16 January, 1978 discontinuing Indian Rupee 1000 and 10000. The reason for demonetization aims at controlling illegal transactions and to determine anti-social elements. Reserve bank of India was mostly against this exercise and lastly its impact was not much. (Source: Reserve Bank of India- history 1967-1981, RBI currency and finance report)

◆ Year 2016

The third demonetization was done on 8 November 2017. Discontinuing Indian Rupee 500 and 1000 and issuing new notes of 500 and 2000. This demonetization led to drastic change in economic growth and affected many sectors of Indian economy as 86% of Indian currency was in circulation all during 2016.

Thus, we can conclude that the first demonetization was a case of conversion, second was a case of cumulation and third was a case of more of conversion!

3. OBJECTIVES OF THE STUDY

1. To study the Historical precedent of demonetization in India.
2. To study the impact of demonetization on various sectors of Indian economy.
3. To study the advantages and disadvantages of Demonetization.

4. RESEARCH METHODOLOGY

Descriptive design has been used in this research, which is based on secondary data. Secondary data has been taken from various government and non-government publications on demonetization and from articles related to it published electronically or otherwise. Data is also collected from journals, articles from newspapers and from relevant websites available on internet.

5. PURPOSE OF DEMONETISATION

1. **To Curb Terrorist Funding:** Indian money is primarily used to fund operation within Indian borders, provide finance to separatist movement.
2. **War on Black Money:** Black money is the money that has been earned illegally and not declaring them at the time of tax purposes. Black money is used in the form of real estate, foreign exchange, gold etc. Black money leads to cancerous growth in the country's economy which will surely lead to ruination.
3. **To Promote Cashless Transaction:** The main purpose of demonetization was to promote cashless transactions. Cashless transactions can be done through various banking instruments like internet banking, debit card, credit card etc.

Statistics have shown Belgium, where 90% payment is done cashless followed by France 92%, Canada 90%, UK 89% and Sweden 89%, where in India only 22% is non-Cash payment. This proves that there is strong negative correlation between India and other countries with reference to online transaction. A cashless society would discourage money laundering and terrorism.

6. THE SECTORIAL IMPACT

POSITIVE IMPACT

- E-Commerce
- Digital Payments
- Mobile Wallets
- Net Banking Payments
- Electronic Market.

NEGATIVE IMPACT

- Traditional Retail Business
- Commodities

- Real Estate
- Luxury Goods
- Agriculture

7. IMPACT ON VARIOUS SECTORS OF INDIAN ECONOMY

- ❖ **Real Estate:** 40%-plus drop in key markets in India. Dealers in secondary market have to stand still. Home buyers waiting for big price reduction. After demonetization real estate industries will be more transparent in the years to come. 7% buyers shifted from "Buying" now to "Renting" now.
- ❖ **Jobs:** Hiring Experts say jobs at senior level are not and won't be impacted. Overall hiring is right down as managers seek to protect revenue/profit targets. The sectors most affected are retail, consumer goods, real estate, infrastructure logistics and building.
- ❖ **Tourism:** Peak tourism period badly hit during demonetization. Tourism business in metro cities gone down by 10%.
- ❖ **Telecom:** Mobile phone shipment fell by 26%. Big seller who does card and online transaction less badly hit. Sales for feature phone gone down by 25%.
- ❖ **Agriculture:** Unfavorable impact of input and output channels in agriculture. Distribution break in supply chains etc.
- ❖ **Information Technology:** The demonetization had a very less or negligible impact on IT sector.

8. ADVANTAGES OF DEMONETIZATION

1. **Tracking Black Money:** A major achievement of demonetization is that it has helped the government in tracking black money. The Indian government claim that large sum of black money were hidden by tax payers. It helps the government to track people who are having large sum of unaccounted cash or cash on which no income has been paid.
2. **Tax Revenue:** Another benefit is that due to people disclosing their income by depositing money in their bank accounts government gets a good amount of tax revenue which can be used by the government towards the betterment of society by providing good infrastructure, hospitals, educational institutions, roads and many facilities for poor and needy sections of society.
3. **Cashless Economy:** Larger size of digital transaction in developed economies leads less corruption as compared to developing countries. Therefore, in order to escape from adversaries of corruption and black money and to have more transparent and cleaner economic growth with social Justice, less use of cash is one of the suggested measures.
4. **Terrorist Funding:** Black money was used for terrorist funding, money laundering, gambling etc, also inflating the price of major assets like real estate and due to demonetization all such activities will be reduced for some time and it will take years to generate that amount of black money again.
5. **Tax payers:** Another benefit is that due to people disclosing their income by depositing money in their bank accounts government gets a good amount of tax revenue which can be used by the government towards the betterment of society by providing good infrastructure, hospitals, educational institutions, roads and many facilities for poor and needy sections of society.
6. **Benami Properties Identified:** After demonetization 300 benami properties were claimed. These properties were identified during income tax clean money policy.
7. **Widening Impact of Tax Base:** The step of demonetization showed improvement in the level of voluntary compliance as a result of action taken by income tax department on the basis of cash deposits in the wake of demonetization the number of e-return of individual tax payers increased from 2.22% to 2.79% returns registering an increase of 57 lakhs returns or 25.3%.

Thus, from the above points we can conclude that the advantages of demonetization can be seen in the long run only.

9. DISADVANTAGES OF DEMONETIZATION

1. **Down shift in economic growth:** Economic growth will experience a period of pause due to business disruption, in short term.
2. **Unease and Anxiety to Public:** Sometimes, demonetization can be very inconvenient. Queuing up in banks to deposit money or exchange currency can be inconvenient.
3. **Panic:** Not everyone understands the essence of demonetization and, therefore, such an exercise is likely to result in panic among a section of the population.
4. **Financial Crises to poor people:** A small change in the value of currency about whether a currency is valid or not can mean a lot of hardship. As such demonetization can increase inequalities within society for short period.
5. **Other Limitations:**
 - Inadequate supply of new notes.
 - Destruction of old currency
 - Additional printing and distribution cost of new currency.
 - Problem situation for small-scale business operations that deal in cash.

10. CONCLUSION

Demonetization is one of the main initiative step taken by Indian government to root out black money, money laundering, benami properties etc. Demonetization will also help banks to recover from high dormancy rates (idle bank accounts), which is currently around 43 per cent. But there are plenty of ways where black money can be turned into white but Indian government realized it too late. The unorganized sectors were badly affected. Indian government achieved limited objective aftermath, but in the long run, people may realize. However, before any demonetization program is carried out, it should be carefully examine and the impact on poor should be considered. Demonetization can be a fresh new start, or it can be something that causes unnecessary confusion and inconvenience for the country.

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