



“DEMONETIZATION” ROLL OUT FOR ECONOMIC DEVELOPMENT IN INDIA: A REVIEW

K. Sindhura

MBA Final year student, VIT Business school, VIT University Chennai.

sindhurakannappan@gmail.com

Abstract

Demonetization was rolled out in India to bring change in the national currency. The author has reviewed various articles to capture the experience of the roll out. Prime Minister of India Mr. Narendra Modi stated that it was done for economic development of India. On 8th November 2016, the government announced the demonetization of Rs 500 and Rs 1000 bank notes. The execution and experience of common man had mixed feeling about the announcement. Various authors' views are reviewed and summarized in this paper. Common man faced both positive and negative consequences. It is a reform for addressing corruption and various sectors faced challenges. Real estate, Hawala transactions, Black money, Terror Financing, Counterfeit currency, Non-East insurgency, Kashmir unrest, Terror financing, Maoism etc. were challenged by the reform. Banks played vital role in execution and had to face pressure from the public. It affected the common man with its sudden implementation, scarcity of lower denomination notes to replace the old notes, restriction on amount of withdrawal, prolonged shortage of smaller denomination etc.

Keywords: Bank notes, Challenges, Demonetization



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Introduction

Demonetization is the process of withdrawal of old bank notes and introduction of new currency. India is not new to the process of demonetization of the Bank notes which were withdrawn earlier in the month of January 1946, and the notes were Rs 1000, Rs 5000 and Rs 10000. The Wanchoo committee was a direct tax enquiry committee which was set up in the year 1970 and it recommended that demonetization could be a measure to address corruption. Mr. Narendra Modi announced demonetization on November 8th 2016 announcing people in his live address over television at 8.00 PM. The bank notes Rs 500 and Rs 1000 were made invalid from midnight on that day. He stated that the notes can be exchanged for a bigger denomination Rs 2000 and the new bank note for Rs 500 (Rs 500 and Rs 1,000 notes pulled out, 2016). The demonetization was implemented suddenly which had terrific impact on the daily life of common man (India demonetization: Chaos, 2016). The long queues in ATM and in banks left people with night mare to manage daily life.

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Following the announcement Governor of Reserve Bank of India Mr. Urjit Patel and the Secretary of Economic affairs Mr. Shaktikanta Das stated in press conference that demonetization is rolled out to combat terrorism funded by counterfeit notes (Why Were the Notes Scrapped?, 2016). The demonetization faced lot of protests, criticism in both the houses of parliament (Demonetisation: Opposition parties, 2016). It hampered the industrial production and GDP growth. In the first quarter of 2017, the GDP was 6.1% but economists forecasted it to be 7.1 % (Demonetisation impact: GDP dips, 2017). In the end of August 2017, Rs 14,000 crores of the demonetized currency were discarded.

In this paper the author has reviewed various articles and the thoughts of the authors on the reform demonetization and has tried to summarize the procedure, benefits and challenges while demonetization was rolled out in India.

Objectives of the Study

- 1) To understand the rationale for the financial reform demonetization in India
- 2) To understand the aftermath of the financial reform- demonetization
- 3) To understand the challenges faced while executing the financial reform- demonetization

Research Methodology

The author collected articles which had the content on demonetization and conducted systematic review of the content. The data which were used for the study are completely secondary data. Review analysis was done and inferences were taken. The observations of the author are presented in this article.

Literature Review

1. Veerakumar (2017) conducted a study on people impact on demonetization and highlighted that how the purchasing power would be improved with the demonetization efforts and how it would have direct correlation with inflation of prices which means that the controlled prices will have direct impact on common man's purchasing power. The loan interest rates from banks will be reduced and people can avail loans at a lower interest. This exercise will help government to introduce new welfare schemes.
2. Dinesh Unnikrishnan (2018) explained the demonetization impact. Three sets of numbers tell us how Modi's gamble has slowed the economy. He has highlighted that growth in eight core sectors, which constitute 38 percent of the Index of Industrial Production (IIP), slowed to 4.9 percent in November as compared with 6.6 percent increase in October and 5.01 percent in September. The manufacturing sector also recorded a very slow growth

49.6 in December as against 52.3 in November. The key set of numbers which has to be looked upon is the consumer spending on durables and non-durables. Consumer spending has declined to 1.2 % in durables and it has declined to 3 percent in non-durables.

3. Lokesh Uke (2017) studied demonetization and its effects in India. The author stated that demonetization has reduced the consumption activity in economy of India. It has increased the deposits of money in banks. The reserve bank of India stated that the deposits have crossed 5 trillion rupees due to demonetization. Circulation of Rs 500 and Rs 1000 notes was 86% and the maximum fake currency was in the form of the same denomination.
4. Sundar (2017) explained the demonetization scenario in India and demonetization changes need whenever there is change of national currency. His article deals with impact of demonetization on Indian economy. It also highlights the merits of the demonetization exercise which is a catalyst for economic growth. There are report saying that large sector of informal economy has come to halt. It is a deep psychological strike on black money. Besides, the government employees are the honest tax payers as it is deducted from their salaries itself. A large number of industrialist and businessmen evade paying tax. Therefore the income from the industries and business activities should be regulated. Cashless transaction is the best option for solving this issue.
5. Preethi (2017) studied the impact of demonetization on Indian economy. She has analyzed the impact of demonetization on various sectors of economy as a whole. The demonetization exercise has been seen as a financial reform in the country. However it has its own positive and negative effects. The main agenda of demonetization has been to eliminate counterfeit currency, to shrink the parallel economy and black money, to reduce corruption and terror financing. Since India is cash based economy, the decrease in liquidity results in low productivity and slowdown in consumer market.
6. Shah, (2017) studied the impact of demonetization on rural India focusing on agricultural sector and also on common human beings. He has examined the demonetization impact on Indian economy. It is stated in the article that out 121 crore Indians of India's population, 83.3 crore population live in rural areas. The agriculture sector is accounted for 17 % of the GDP of India. The author stated that preparation for demonetization was lop-sided and the impact was terrible on Indian Public. Since it was executed suddenly

without proper preparedness, it created chaos and discomfort among people. This move would have major impact on the parallel economy.

7. Abhani Dhara (2017) studied the impact of demonetization over the banking sector with reference to Veravel city. The main objective of the study was to find out the impact of demonetization on banking sector. The author stated that people have become conscious about cashless transaction. Enormous pressure was there on bank employees and they supported with their work the execution of demonetization. It is a good effort by the government to reduce corruption.
8. Prabhu (2017) analyzed the demonetization and its effect on Banking Sector. He points out that demonetization had a significant effect on bank since it is a center for channeling the legal tender money to needs of the society. It increased the liquidity position of the banks.
9. Sunil (2017) looked at demonetization at glance in Indian scenario and demonetization move in India set history. Though the common man, unorganized sector faced lot of problems which are temporary. The article concluded that India would move towards strongest economy and the day is not far away.
10. Swaty and Sonal (2017) asked a question about curbing black money. Is demonetization the right move? The article discussed the concept of demonetization, the current status and reasons behind generation of black money and highlighted the impact of demonetization in curbing the black money. The author concluded that the demonetization effort could put a temporary brake on black money. When the cash based economy has returned, it is doubtful whether the effort will be fruitful.

Rationale for Financial reform “Demonetization”

Demonetization is done to introduce new national currency. To do so, the government has to withdraw the old currency used at that period of time. This is the procedure of demonetization and this can be called as financial reform. There are several reasons stated for the execution of the reform which came with a sense of sudden feeling to the public. Lots of debates happened for and against the reform. Critics looked at it from various angles; some gave political colour; some refused the rationale of the reform; some forecasted negative impact on economic growth of India and some stating that the reform is going to have a very positive impact on the economic growth of the country.

It is important to understand the rationale behind the introduction of the financial reform. The ***Black money tracking*** was the main agenda of demonetization. The old notes had to be deposited in the banks for exchange of new currency which makes the depositor accountable. The bank (ICICI) securities stated that the financial reform will un-wrap 4.6 lakh crore of black money. Withdrawal of old currency which is of high value will ***halt the illegal activities***. The high value currencies are used to execute illegal activities like terrorism, money laundering etc. With the execution of demonetization, ***fake currencies' use*** is halted with a sudden jolt. Pulling out of Rs 500 and Rs 1000 is expected to have ***impact forever on the syndicates*** which are producing Fake Indian Currency Notes (FICN). ***Real estate prices to decline*** as black money is used in resale transactions in the real estate sector. ***Promotion of more efficient cashless economy*** is expected to happen as people move towards digital payments. On line e-commerce has a great demand among people and it may increase more in future. This financial reform will enhance the ***transparency in financial transactions*** in the formal banking sector and thereby India will get a better ***ranking in Governance*** which is indexed by several bodies like World Bank, World economic Forum, United Nations etc. The demonetization will help the income tax department ***monitoring the collection of tax*** and penalties. This will increase the tax revenue of the government.

Aftermath of Demonetization

General public faced the gross route level problem of the demonetization though it had larger agenda which was focused for the welfare of the Indian Economy. The inconvenience which the people faced due to various reasons like very limited money withdrawal from the banks, long queues to exchange the notes, panic for daily management, less awareness on cashless transaction among people except the elite group etc. The list is exhaustive to describe the sufferings of people. The reduced money circulation made people carry Rs 2000 note but not able to transact it due to the shortage of lesser denomination bank notes. ATMs were not functioning and when they started to function, long queues and panic among people are to reach the machine. Media reported of deaths of people standing in queue. The larger perspective of the whole financial reform was lost in the traumas faced by the general public. It looks a considerable time for the public unrest to settle down.

The agricultural sector was affected severely during the demonetization execution period. Since the input and output channels of agriculture depend on cash transaction, farmers faced a great set back in their lives to manage their crops and for their living. Public deposited their

old currency in the banks and did not have cash for transaction. Therefore the consumption reduced but money in the banks increased. The RBI announced that the deposits have crossed 5 trillion rupees from 10th November to 18th November. The real estate was very negatively affected and the real estate investors tried their best to bring hopes to the public buyers but it was all not fruitful. They experienced a sharp fall in the prices of the property market.

Bank operations have been greatly influenced by demonetization and they had both positive and negative impact. Some of the positive impacts are free flow of deposits, improved digital interface, people surplus at banks, increased bumper of customers etc. However the bank operations was stressed up; some of them are cash reserve requirement (100% CRR on incremental deposits meant that banks did not earn any interest on Rs 3 lakh crore of deposits nearly a fortnight), waived of ATM charges (banks incurred loss of Rs 20 in every transaction of ATM). Since the ATM charges were waived off, banks faced loss of 1% for card transactions. Further banks focused on exchanging notes and they did not have the priority to sell any loan products. Bank employees faced tremendous stress with their work pressure.

Economist have forecasted that the cash crunch which has happened due to demonetization affects the GDP growth and it may reach 0.5 % in the second half of the financial year 2016-17. Main target of demonetization was to track black money holders. However, the black currency was exchanged from others with a commission of 20-40 %. Several other kinds of corruption and fraudulent activities were also reported to exchange the black money. It is perceived by economist that in the early stage of implementation of this financial reform, such things are prone to happen but in long run it will achieve the objective for which it was executed.

Black currency was operating in India in form of Hawala. It is a method of transferring money without having any actual money transfer. Demonetization has arrested the hawala rackets. It was reported that hawala operators have destroyed currency notes worth of more than Rs 500 crore.

The service sector dipped as the new orders dried up as the customers spending was reduced due to cash shortages. There was sharp decline in hotel business, restaurants and commercial rent services. This was all due to the dependence of cash transactions in all the service sector operations.

Negative sides of the people sufferings in the initial days of the execution of demonetization are captured by various authors. However many of them have concluded that the financial

reform is a bold step to set right the black currency operation and improve the economic status of India.

Challenges faced for the execution of Financial reform ‘Demonetization’

The major challenge which the financial reform had to take is to execute it suddenly before the hawala and black currency operators can work out strategies to save themselves. Therefore the pain was felt by the general public, since higher denomination of Rs 500 and Rs 1000 was pulled out. Cash transaction faced hardship and it affected the life of daily life. Though prime minister addressed the people on television, before the execution of the demonetization, adequate information was not available to the public to understand the larger perspective of the reform. Further the reform was looked with political colour which made things hard for smooth execution.

It was also felt that before the execution adequate volume of new currency and lower denomination bank notes was available with Reserve Bank of India. The bank had to cope up with the pressure from the public both for the deposits of the old notes and for withdrawing the minimum new currency notes. All banks faced big challenge for the execution and normalization of the financial reform.

The ATM had to be made dysfunctional for two reasons. One reason was cash shortage and the second reason was ATMs which were not calibrated to accommodate the new currency. It had taken some time for ATMs to operate and help the public to withdraw money.

Handing fraudulent activities of hawala operators and black currency were yet another big challenge for the government. The bank accounts which were not active were activated with commissions to the people who owned the account. This was yet another challenge for the bank.

It was observed that demonetization was bringing back the money inside the bank which can be used for commercial activities. Therefore banks will have better positive effect because of demonetization. It reduced the interest rates for loans but for the deposits inside the bank, the interest rates came down. This challenge will affect the future depositors in the bank. Therefore the shock absorbers are the general public. To implement the financial reform, the cost to the government to replace the new currency was more than Rs 12,000crore.

Conclusion

The demonetization financial reform had a larger spectrum to arrest black currency and to increase the economic status of India. It increased the accountability of money transactions. It was an eye opener for general public towards cashless transactions for their management of their daily needs. Any reform will face challenges, criticism and obstacles for implementation. Similarly demonetization also faced all the above. Since the public

inconvenience was high, the reform was politicized. It also affected various sectors but economists view that it will be temporary. The banks played a vital role for the execution and their systems were made strong. More data in the future will help us to predict and review the positive impact of the reform. With the current information available, it can be inferred that the demonetization was successful in arresting black money and bringing in systems for financial transaction though it had temporary challenges.

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