

DEMONETIZATION AND IMPACTS ON INDIAN ECONOMY

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ABSTRACT

Withdrawal of cash from the legal tender is known as demonetization, which took place in the year 2016 November, the sudden implementation of this action aimed at eradication black money, funds to terrorists and to eradicate fake currency though it was a positive action it also affected the various sectors of the economy, the data was collected from secondary source, this paper helps us to know about the various sectors which were effected that is agriculture, automobile, and this study also examines the positive and negative aspects of demonetization and also the drastic change from cash to digitalization transaction.

KEYWORDS: *Demonetization, Black Money, Digitalization, Fake Currency.*

Introduction

Meaning

Demonetization refers to the removal of currency notes which were in circulation in the form of legal tender. Through demonetization, the existing currencies are being replaced with new currencies.

How does it Work?

Demonetization does not occur regularly, if the government regulates demonetization often, the economy may not indicate regular growth. There will no stability also it will impact the various sectors of the economy and undoubtedly affect the common public.

When is it used?

The countries implement demonetization when it experiences inflation or illegal activities such as corruption, black money, fake currencies. Countries take the initiative of demonetization to bring stability and growth to the economy.

History of Demonetization: World History

The act of demonetization has been experienced in the past by several countries across the globe. It was implemented to make the declining economy stronger, which would result in stability and reliability. The first country to implement demonetization was Ghana in the year 1982, to demonetize 50cedis currency in order to keep the check on money flow. Later many countries such as Britain, Congo, Myanmar, Nigeria, North Korea, and Russia implemented demonetization.

Demonetization: India

Demonetization was not a new act as it was previously implemented twice.

The first currency banned took place in January 1946. It demonetized huge denomination of Rs.1000 and Rs.10,000 which did not create a revolution as it was not accessible by the common people also its purpose was minor and a disciplinary gesture towards black marketing. "It was more of 'conversion' at varying rates of profits and losses than demonetization", said sources.

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The second currency was in January 1978. It demonetized the huge denomination of Rs.1000, Rs.5000 and Rs.10,000 currencies. The demonetization of high denomination banknotes was a step primarily aimed at controlling illegal transactions. Which in turn proves that demonetization neither created and a huge impact on the country's growth nor did it fulfill its aim of eradicating black money.

The recent demonetization that happened on 9th November 2016 which worked on demonetizing Rs.500 and Rs.1,000 currencies had a huge impact on the Indian economy and the common people as it was a denomination which was in high circulation across the country. It was initiated by our Prime Minister Narendra Modi with an intension of cracking down black money, choking downflow of funds to terrorists and Naxalites, expand the tax base, abolishing fake currencies and digitalization. The following was initiated for the growth of the economy but the sudden implementation of demonetization let to the fall of GDP growth rate

*The below table shows the GDP growth rate from the year 2011-2012 to 2016-2017

Table 1

Year	GDP Growth Rate
2011-2012	6.5
2012-2013	5.46
2013-2014	6.39
2014-2015	7.51
2015-2016	8.01
2016-2017*	7.11

*(Source: CSO)

Literature Review

Himanshu (2018): this paper entitled as “impact of demonetization on Indian economy” they used secondary data, and also briefly explained about various reasons for demonetization and also the negative and positive aspects of demonetization, also specified the ways how black money was recovered and encouraged the digital mode transaction.

Sourabh Dev Tiwari (2017): this paper entitled on “impact on demonetization in Indian hospitality and tourism industry”, their research was based on both primary and secondary data and collected data from the low and medium business people about the cause of demonetization, the swot analysis was made, and their short-term and long-term impacts of demonetization.

Bharath Kumar Meher (2017): this paper entitled on “impact of demonetization on banks” the research is based on the secondary data and briefly explains about the post and pre demonetization status, and the post demonetization deposits in commercial banks are increased to Rs.6,55,000 crores which was Rs.4,09,500 earlier and also briefs about the positive aspects of demonetization.

Sudesh Kumar (2017): this paper entitled “pre and post effect on Indian industry” this research is based on secondary data and compares the huge difference faced by different sectors agricultural, pharmaceutical, the automobile that is post and pre demonetization.

Objective of the Study

- To study the impacts on different sectors.
- To study the negative and positive outcomes of demonetization.

Research Methodology

This research is descriptive in nature and tells about the history and meaning, and the impacts on various sectors on demonetization and also describe the pros and cons of demonetization which is based upon the secondary data, the relevant data is collected from various journals, blogs, research paper, websites and many other.

Impacts

The sudden action of demonetization shock the entire nation, of banning the most frequently used currency notes such has Rs.500 and Rs.1000 which were even used by the rural and urban, lower and middle class people which led them to greater suffering by reducing their purchasing power and also it created a greater hit on all the sectors of economy, India still depends on the primary activities where the major transactions are made through cash. Although it was a good start to eradicating black money, corruption and stop the use of counterfeit of funds of illegal activities and terrorism it had a great impact on various sectors of the economy.

- Agriculture:** Agriculture is considered to be the backbone of the Indian economy. The sudden action of demonetization created a huge impact on this sector, demonetization took place during the post-harvest operation of Kharif crops (rice, maize, cotton) and sowing rabi crops (wheat, mustard, sesame, peas,) both these operation requires a huge sum of money. As Indians, 263 million farmers depend on the cash economy since cash is a primary transaction mode in these sectors and the agricultural dependent states like Madhya Pradesh, Uttar Pradesh, Punjab, and Kerala. The Sudden decision of demonetization turned to be a major burden on the farmers, as they faced difficulties in buying seeds, fertilizers, pesticides which were required on daily basis and huge landlords faced difficulties such as delay in paying their daily wages to the laborers which resulted in postponed work, and they were worried lot that their Kharif crops would be delayed to their want buyers without cash in hand which resulted in increase in the credit transaction. Though the government provided various flexibilities to farmers such as
 - Allowing the farmers to withdraw the sum of Rs. 25,000 per week against there loan
 - Allowed to purchase seeds with their older notes of Rs. 500.

Thus although the government provided flexibilities they faced serious difficulties of insufficient cash flow in their rural banks.

- Automobile:** Until demonetization, the automobile industry had steady growth. The various sectors under the automobile industry like private cars, two-wheelers, commercial vehicles, tractors, etc had a stable growth pattern until October 2016. The sudden announcement of demonetization had an immediate impact on the economy as, in India, nearly 50%-60% of sales are executed through cash, out of which most of it is executed in rural India. The industry could not sell its products, which brought an immediate fall in the industry. But it did not last long it began to boom again. It was recorded in various reports stating that buyers have just postponed their decision of purchasing as they are waiting for the circulation of money like as usual. It also says that the fall in the sale is also because it was a festive season and according to sentiments people do not buy new vehicles. Later once the money was in circulation the sales began to increase slowly and everything went as planned. Many automobile companies have reported similar statements mentioning that though they all faced a sudden dip during demonetization, they knew it would be temporary and found a quick pick up once money was in circulation.

Table 2

Domestic volume growth trends across segments in December, 2016

Segment-wise Sales	December, 15	December, 16	Change%
Passenger vehicles	230959	227824	1.40%
Commercial vehicles	56840	53966	5.10%
Two-wheelers	1167621	910235	22.00%
Three-wheelers	46894	29904	36.20%

The above table clearly indicates that overall decline in sales in all the segments of this industry due to demonetization as compared to the previous year of 2015

- Information Technology:** Information technology was a sector that was not given much importance before demonetization as it did not have much need in society. It did not have a very active role to play in the life of common people and also it was the initial stages of digitalization.

Later when demonetization hit and when the economy was trying to change into a cashless economy, digitalization was given more importance. Companies are starting to realize the need for IT systems to make online transactions easy for its customers. Which ended in giving IT companies more importance. Technology became important for tracking financial information, eKYC forms for IT departments. It also gave birth to UPI (Unified Payment Interface) which was something very new for the common public.

- Banking:** Since Indian was a cash-driven country most of the population did not own a bank account, and very few had a debit or credit card and the rest required a bank teller to carry out their bank transactions. Even for online shopping people preferred to pay through cash and not use the online modes.

According to government regulations, banks became the mode of exchange of old currencies into new currencies which proves that banks were a backbone for the entire process and also they benefited from it. There was an increase in the current account and savings account ratio, it reduced their high-cost deposit and also increased their liquidity position which helped in further lendings.

- **Real Estate:** It was one of the markets which had a huge hit after the force of demonetization. Black money was secured in the form of real estate as huge investors found it as a convenient way to hide their black money in the form of Benami property. House buyers had a free flow of currencies to purchase or sell their house as most of their transactions would happen in the form of cash. Demonetization was a difficult move for many to deal with. However, it has greatly contributed to the standardization of pricing in the sector. There is so much transparency now. From a developer standpoint it has immensely helped in sourcing funding from the banks and is assured that the source of funding is genuine. Many people out there believe that demonetization had an adverse effect on sales, but that's not true. It was the negative sentiment that due to demonetization the property costs will go down and that's exactly what the people kept waiting for instead of investing. Beyond this, it has also helped in creating a cleaner image for Real Estate.
- **Hospitality and Tourism:** Since India is a tropical region the best time to visit India from October to December where the country is dry and pleasant. Demonetization that took place during the months of October – November which also gave a hit on this sector.

Since it was a peak tourism season, where the high denomination notes that are 500 and 1000 were banned it was not possible for the travelers to spend money easily. Both the domestic and international tourist faced the struggle to pay their service providers such as their hotels, guest house, traveling expenses due to lack of availability of new currencies in banks and ATMs and most of the budget-friendly hostels, guesthouse, did not have an access other modes of transactions.

- **Aviation:** According to the recent news it states that there was no much harm to the aviation industry since the seats were pre-booked in contrast it just witnessed a growth by 23.91% in December. During December which is traditionally the peak season of travel, all the carriers than 80% filled seats individually the airlines gave their statements, wherein
 - Spice jet recorded a load factor of 93.7% with 90% full seats
 - Indigo came 2nd 91.45% full planes
 - Jet airways recorded 63.3% flight full
 - Air India was last in the list by flying 59% of its flights full.

*(source: Economic Times)

- **Gems and Jewelry:** Demonetization of high-value currency notes had a negative impact on consumer spending, especially for luxury items including gems and jewelry. The gems and jewelry sector was impacted at least in the medium-term. Though the export market and large diamondaires in the organized sector were not impacted much, small and medium players, carrying out local trade and sourcing, felt the pinch of the currency recall exercise. The substantial portion of the payment by customers involves cash for purchasing jewelry so the impact of demonetization in this sector was quite high. Demonetization made people with less cash available in their hands for fulfilling their daily needs where they couldn't imagine purchasing jewelry. Small retailers who survive in the unauthorized sector were likely to be affected more which reduced the demand for jewelry. Jewelers took advantage by selling the gold for more than their market price to take advantage of the banned notes which resulted in raids of income tax on this jewelry. This sector was seriously hit by demonetization as buyers prefer to pay in cash.

Negative Impacts of Demonetization

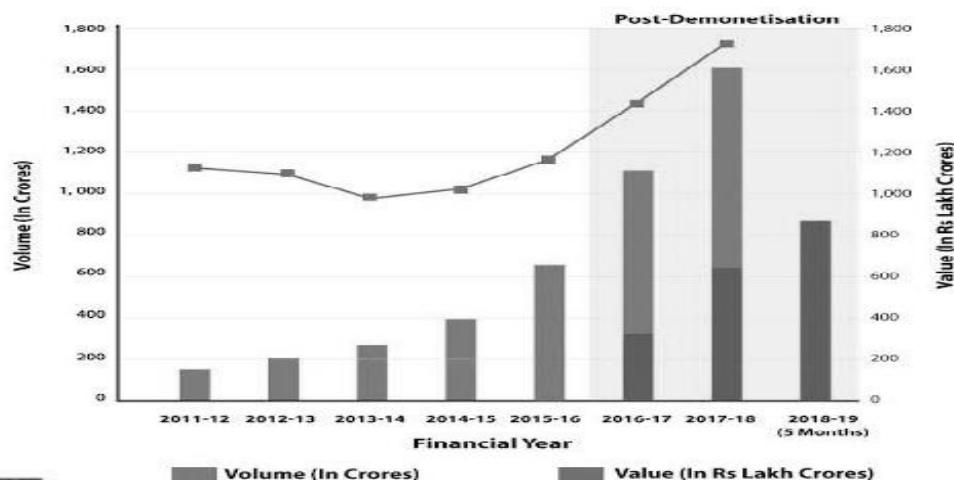
- Demonetization led to a severe cash crunch in the country, as people were finding difficult to get the cash in hand for day-to-day activities. Rural areas were affected most because, the banks set up their function with a very little amount, and even though ATM facilities were available there was no cash and very little promotion for digital transactions and lack of internet facilities. In Urban areas of India people starting making online transactions, many retail outlets also preferred paying online however people were not willing to pay through online mode because of internet theft and landed up standing in ques for hours which created huge distress among the people.

- Some of the small business faced a huge loss and some vanished, as cash is the only mode of payment practiced still in small business, since there were huge cash crunch the wages could not be paid to the laborers, which resulted in unemployment and limited their business activities which gave a severe hit to the small scale business.
- GDP rate of India has slow down after implementation of demonetization that is withdrawal of higher denomination notes reduced the growth of the country by decrease in consumption pattern, demand for the product in the domestic market, income, investment, etc and GDP in 2015-2016 had a prosperous growth of 8.01% and it finally fell in the year 2016-2017 to 7.11% which was a huge downfall, and the government had made a note to general public saying GDP will increase in later 4 to 5 months and the introduction to the new policy GST(goods and service taxes) is also one of the reasons for the decrease in GDP.

Positive Impacts of Demonetization

- Tracking of black money the biggest aim of demonetization was described as fighting black money, there were a lot of effects on black money out of which the direct or immediate effects were Rs.12 lakh crore of Rs.15.44 lakh crore demonetized currency came back to the bank immediately, It helped to tackle black money as it was important to completely stop the generation of black money, hence depressing of higher denomination was a good initiative but other effective means of investing black money is important.
- It proved to be Modi’s surgical strike on terror funding, drug money, and other anti legal activities, most commonly used mode of transferring value remains hawala especially Pakistan and Pakistan based terror groups, it does not involve physical moment of cash in borders but employing hawala agents to collect and disburse the cash across different countries.
- The larger purpose of demonetization was to move India from a non-compliant society to a compliant society so when cash is deposited in the bank the anonymity about the owner of the cash disappears. The cash deposited is now identified with its owner giving rise to an inquiry whether the amount deposited is in agreement with the depositor’s income, hence it was made mandatory for them to make tax payments.
- Facilitated saving tendencies among the people Demonetization helped in transferring cash to financial markets. It inculcated the habit of savings. Gross financial savings have increased from 10.9% of gross national disposable income (GNDI) in FY16 to 11.8% of GNDI in FY17, a notable climb of 90 bps. It changed the saving habits of people. Instead of keeping cash at home or in banks people are now investing in mutual funds and insurance companies. If we take mutual fund data, the investment has increased by 155% in the last one year and it reached Rs.3.43 lakh crore. Likewise, there was a 46% increase in the collection of premium insurance policies. Increment in these will help the government to raise money for a long duration that can be used to develop the infrastructure of the country.

Digitalization



When the decision of banning Rs.500 and Rs.1000 notes were announced on 8th November 2016 to curb black money and terror financing it bought mixed reactions in the minds of people. Demonetization had severe effects on people especially - domestic workers, small traders, and farmers. But its impact is not for along term. In a short period of time, demonetization has led to the rapid adoption of digitalization. Such digital payments have in a large way replaced cash transactions at least in urban areas. It eventually led to the growth of:

- **UPI:** The Unified Payments Interface (UPI) was launched in April 2016, and UPI transactions have increased 400 times as compared to November last year. This happened as banks and private entities worked towards the adoption of the government-backed payments system post demonetization.
- **BHIM:** The government's BHIM (Bharat Interface for Money) implementation announced by Prime Minister Narendra Modi on December 31, 2016, has seen notable development since then. Named after Dalit icon Bhimrao Ambedkar, the digital payment application was also launched for non-smartphone users on his birth anniversary in April. During the first nine months of operation, BHIM has reported transactions worth more than Rs 11,000 crore and lately accounts for almost half of all United Payment Interface (UPI) transactions in the country.
- **RuPay:** Mastercard recently complained to the Office of the United States Trade Representative that the Indian government associated the use of RuPay cards with nationalism, claiming it serves as a kind of national service. Slowly and steadily, RuPay card has been expanding in the Indian market, riding on the back of the government. Thanks to PM Modi's policy of financial inclusion, RuPay has made quick inroads into the hinterland.
- **Aadhaar Enabled Payment System (AEPS):** AEPS is a bank-led model, which allows online interoperable financial transaction at PoS (Point of Sale / Micro ATM) through the Business Correspondent (BC)/Bank Mitra of any bank using the Aadhaar authentication.
- **Electronic Clearing System (ECS):** ECS a substitute procedure for effecting payment transactions for the utility-bill-, love phone bills, electricity bills, insurance premium, card payments, and loan repayments, etc., which might remove the necessity for insurance and handling paper instruments and thereby facilitate improved client service by banks / corporations / firms / government departments, etc., collection / receiving the payments.

Conclusion

Demonetization which was bought in for the third time in our country by out P.M. Narendra Modi was a huge step towards creating a new revolution in our country. This was brought in with a good intention which was to curb black money, choke the flow of funds to terrorists, eliminate fake currencies, etc. Though this brought a lot of hardships to business and to common it was brought in with good intention. Hence it is now the government's responsibility to bring the economy out of the slump also government should move towards removing all obstacles coming to the ineffective implementation of GST by being sensitive to businessmen problems, reduce taxes and stamp duties, giving booster dose to MSME and unorganized sector so that the people who have lost their jobs or businesses due to demonetization may join back the formal economy and live a dignified life.

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