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A STUDY ON IMPACT OF DEMONETISATION IN INDIA

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ABSTRACT

On 8th November, 2016 Indian PM Mr. Narendra Modi announced in broadcast to the nation that Rs. 500 and Rs.1000 currency notes will no longer be recognized legally as currency this is known as Demonetization. The high denomination currency notes make about 85% of the total cash circulated in India. In the announcement, PM Narendra Modi declared that use of all 500 and 1,000 banknotes would be invalid after midnight of that day, and announced the issuance of new 500 and 2,000 banknotes of the New Series in exchange for the old banknotes. This measure has been taken by PM to resolve the problem of corruption, black money and counterfeit notes. Demonetization had a great significant and immediate impact on the state of the Indian economy. This paper makes an attempt to do an in-depth analysis of the impact of Demonetization and also described the effect of demonetization on different sectors of the economy.

KEYWORDS: *Demonetization, Black money, cashless economy Corruption, Digitalization, Counterfeit currency, Indian Economy.*

INTRODUCTION

Objectives

- To describe the demonetization concept in India.
- To describe the impact of demonetization adopted in 2016 by present government on Indian economy and system.
- To work out the probable consequences of the Demonetization.

Research Methodology

This paper is based on secondary data. The data was collected from the various published sources like reports, magazines, journals, newspapers etc.

What is Demonetization?

Demonetization is a act by which the currency will not be legal tender. The currency will not be valid, the government states to withdraw the money which is

legal tender. The government has the right to take such decision. After demonetization the money can only be exchange at the banks. The Government of India has implemented a major change in the economy by demonetizing the currency notes of Rs.500 and Rs. 1000. They announced that the currency notes will cease to be legal tender from midnight of 8th of November 2016. People have given the option to exchange the money held by them up to 30th December 2016. The government replaced these notes with the new notes of Rs.2000 and Rs.500. There are different effects of demonetization. The reasons given for demonetization are to control the counterfeit notes that contributing in terrorism, to eliminate black money, corruption, there are agent in the economy who are holding cash which they cannot explain the mode of earning hence they cannot deposit into the banks . This

part of currency can be exhausted which cannot be replaced in any manner. The government choose to replace the money which was in circulation in cash and force a cashless economy and promoted electronic money. Demonetisation have short term and long term effects.

History

First time demonetization took place in 1946, Rs. 1000 and Rs.2000 notes were demonetized. Later it happened in 1978, Rs. 1000, Rs. 5000 and Rs. 10,000 notes were demonetized. These two demonetization affected very high value of money into circulation which formed a very small part of currency notes into circulation. The highest value note printed by RBI was Rs. 10,000 notes in 1938 which is demonetized in January 1946 and again printed in 1954 but demonetized in January 1978 according to RBI data. Demonetized bank notes of Rs.1000, Rs.5000 and Rs.10,000 were reintroduced in 1954 and again demonetized in January 1978 all of them.

CURRENT DEMONETIZATION IN INDIA

The Government of India has implemented a major change in the economy by demonetizing the currency notes of Rs.500 and Rs. 1000. It means Rs. 500 and Rs. 1000 note will not be accepted by the organization declared by the government. They announced that the currency notes will cease to be legal tender from midnight of 8th of November 2016. People have given the option to exchange the money held by them from banks and post office till 30th December 2016. The government replaced these notes with the new notes of Rs.2000 and Rs.500. There was a huge impact of this on Indian Economy because Rs. 500 and Rs. 1000 notes contribute more than 84% of money value circulated in the economy. People who have huge amount of black money in cash faced complete loss now. If the person want to deposit the black money into the bank then they have to show there ID. There would be 200% Penalty on income tax amount.

BENEFITS OF DEMONETIZATION

- **Increased Savings** – When currency is demonetized, people tend to deposit their cash with a bank and store less physical currency at home. This helps them save more.
- **Lower lending rates** – With currency demonetization, money moves from people to banks and financial institutions. Therefore, there is a better circulation of money. Further, banks and financial institutions have a lower cost of funds which translates into lower lending rates.
- **Better economy** – Since demonetization induces people to deposit their cash with the banks, there is a higher circulation of money in the

economy. The government receives more taxes and can undertake more development projects. Eventually, this leads to a better-performing economy.

- **Curbing anti-social activities** – Usually, anti-social elements like smugglers or terrorists use cash as a mode of transaction. When the government decided to demonetize 500 and 1000 rupees notes, they were the highest denomination notes in circulation. By demonetizing them, the government forced these anti-social units to find ways to get rid of the old notes. This allowed the government an opportunity to get a better control over the unaccounted money in the economy and curb anti-social activities.
- **Reducing counterfeit currency notes** – During demonetization, people deposit all old notes with banks who check if the notes are genuine or counterfeit before accepting them. Therefore, this allows the government to weed out counterfeit notes circulating in the market.
 - It makes the economy cashless and reduces the use of physical cash as well. If the economic transactions is digitalized it will reveal the expenditure of individual to the tax authorities.
 - It will spread the attitude against black money. It can eliminate the mentality that deal with black money. Awareness and conscience can reduce the transaction with black money. Due to digitalization the economy could be more transparent.
 - Demonetization will increase the number of tax payer. Online transaction may clear the business transaction in more transparent manner. It will increase the revenue of government
 - Unaccounted monies held as cash which was not productive will become productive as it enters the legal system.
 - Funding of terrorism and other illegal activities will be reduced and money with the political parties is flushed out.

EFFECTS OF DEMONETIZATION

- **Effects on parallel economy:** Parallel economy is the economy where unaccounted money exists. The demonetization of these 500 and 1000 notes and replacement of it with new 500 and 2000 Rupee Notes may remove black money from the economy that is blocked with the owners they will not in the position to deposit in the banks. The depository has to prove the source of income and tax paid details to the government. Circulation of large volume of counterfeit currency has been stalled . It

would help to remove the funding for anti-social activities like smuggling, terrorism, espionage, etc.

- **Effects on money supply:** Demonetisation reduces the money supply from the economy in short run until the new currency circulated in the economy. Removal of Rs. 500 and Rs.1000 notes reduced the money supply to the extent the new currency re-entered in the system. Gradually the new currency will enter in the economy the mismatch gets corrected and supply will increase. To the extent of black money the money will reduce from the economy.
- **Effects on Demand:** Demonetization reduced the level of demand in the economy to some extent. The overall demand is affected like demand of consumer goods has been reduced; demand of real estate and property is postponed with the expected low price. People mainly invest their black money in real estate and with this demonetization this sector affected the most. Demand of gold and luxury goods has been reduced due to lack of money with the people.
- **Effects on prices:** Demonetization affects the pockets of buyers. Due to demonetization of notes there is lack of hard money because of shortage of exchange sources, lack of plastic money and conditions of the government on withdrawal amount. This tends to reduce the demand of goods and services in the markets and leads to increase the prices of the products.
- **Effects on Real estate:** the real estate business is expected to fall. More the transaction is held in cash. People use the black money to purchase the property. They use the money which is unaccountable. So, shortage of cash money reduces the real estate business and force to fall in the prices of the property.
- **Effect on GDP:** Demonetizations adversely affect the consumption demand in the economy this leads to fall in the GDP of the economy. For example- Goa is famous tourist place to celebrate Christmas and New Year but because of shortage of cash their business has been affected this affect the overall GDP of the country.
- **Effects of Banks:** it enhance the liquidity of the banks as directed by the government the 500 and 1000 represented notes cease to be legal tender are to be deposited or exchanged

in the banks. It will automatically lead to increase the deposits with the banks in the saving and current accounts. This hiked the deposits of the banks.

Effect on Stock market: The Indian markets have fallen more than other markets in Asia. The S&P BSE SENSEX is down 3.8%, which is more than other Asian stock markets. BSE Realty index is fall by 15%. Some other stocks like DLF Ltd is down by 20%. Stock of Jeweler companies fallen by 11%.

Will demonetization eliminate black money?

Demonetization cannot eliminate the black money by itself. This is just one step taken by the Modi's government. This effect bring massive amount of cash into banks. The government can use it in an effective manner. Black money can be eliminated only if we change the mentality of the public. Demonetization may bring a social shake up in the country by destroying this mentality. The attitude of people should change against black money. The awareness of the drawback of black money can eliminate it.

CONCLUSION

Demonetization was the biggest shock to the Indians. This step is taken by the government for several reasons such as Black money, cashless economy, Corruption, Digitalization, Tax evasion, counterfeit currency and funding illegal activities. This is the historical step by the Modi government and supported by the public. The effect of this decision will be fetch in the long run. This may lead to improve tax compliance, better balance of payment (BOP), lower inflation and corruption. Common men are finding it difficult to buy consumption goods with no money in their pocket. They are wasting hours in queues it could be avoided if planned in advance.

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