
DEMONETIZATION'S EFFECT ON INDIAN ECONOMY: A REVIEW PAPER

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ABSTRACT

Demonetization refers to the return of a country's lawful currency. Demonetization has occurred in numerous countries throughout history, including Ghana, Nigeria, Australia, the Soviet Union, and Pakistan. Demonetization occurs in India at various periods. The most recent demonetization occurred on November 8, 2016. The primary goal of demonetization is to reduce corruption, as well as black money and counterfeit money. My primary objective in this research paper is to examine the historical context of demonetization in the globe and in India, as well as the impact of demonetization on the Indian economy, including the impact on the value of the Indian currency, the stock market, the impact on India's gross domestic product, the impact on inflation, the impact on various sections of society, the impact on various sectors, and the impact on India's inflation. The main result is that demonetization has a beneficial impact on certain aspects of the Indian economy while simultaneously having a negative impact on others.

KEYWORDS: *Demonetization, Economy, Impact, Indian Currency.*

1. INTRODUCTION

1.1. Demonetization:

Demonetization refers to the process of removing a currency unit from its legal tender status. Whenever there is a change in the national currency, demonetization is required. The old currency unit must be decommissioned and replaced with a new currency unit. Remonetization is the polar opposite of demonetization, in which a form of payment is reinstated as legal money(1). The declaration of 86 percent of paper currency as unlawful money in a matter of seconds on the eve of November 8, 2016 necessitated an instant disruption in people's lives(2). This movement shocked everyone since it was a significant and unexpected decision that was announced without prior notice in the evening at 8:15 p.m. by our esteemed Prime Minister Shri Modi. Demonetization is not a new idea(3). This effort is aimed at draining "black money" out of our economy and making it legal, banked, and taxed so that it can get to be a part of it(4). When looking at the microeconomic effects, it appears to be beneficial: first, uncollected revenue at various Nagar Nigams increased; second, it was also apolitical because it was a surgical strike on terror financing; and third, the circulation of forged notes can be restricted(5).

1.2. Impacts of the Demonetization on Indian Economy:

There are several causes of Demonetization such as Black money, corruption, GDP, increase of unemployment there are many people that became jobless. It will take 2 or 3 quarters to get things back on track. The process of demonetization will take time. Small and medium enterprises have suffered resulting unemployment in unorganized sector, The Indian government believes that huge amounts of liquid cash are a major source of corruption and black money(6). The risk of fraud will be reduced as a result of digital payments and other transparent methods of payment. In the quarter

after demonetization, the rate of increase of economic activity was reduced by at least 2 percentage points(7). Following demonetisation, cash availability in banks and post offices increased dramatically, and banks now have adequate liquidity. As a result, the Reserve Bank of India (RBI) has the option of lowering key policy rates(8). This will give rise to the expectation of a low interest rate. The government has employed demonetization as a macro-economic strategy to control or alter the country's economic affairs with the goal of addressing problems such as a parallel economy, counterfeit money in circulation, terror funding, corruption, hawala transactions, and so on(9). The government makes an effort to evaluate the economy as a whole and to identify methods to enhance its overall performance. Demonetization has had a variety of economic and societal consequences that were not anticipated before to its introduction (10–12).

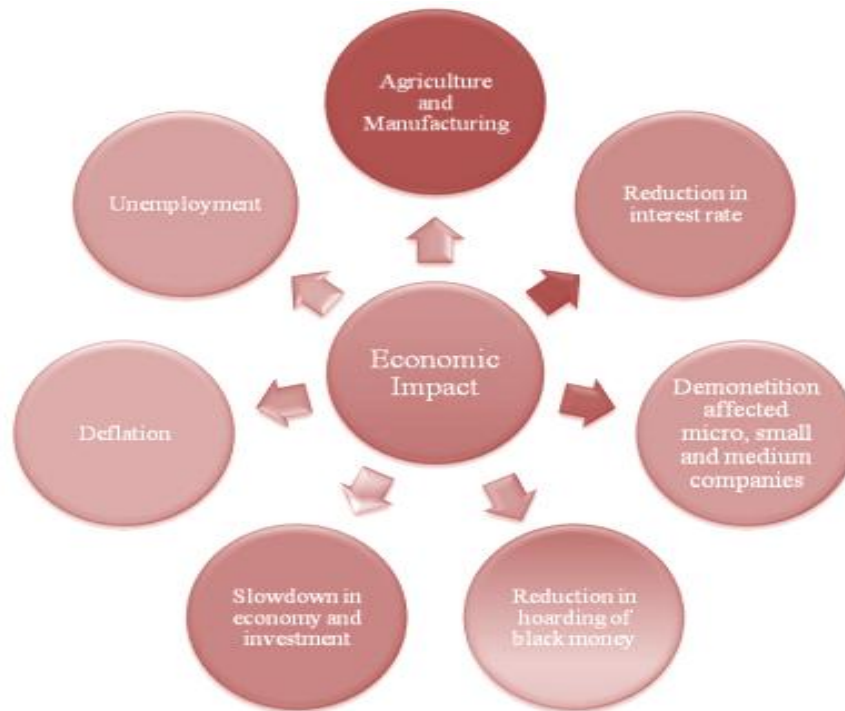


Figure 1: Illustrates the economic impacts of the demonetization.

At 12.1 percent of GDP, India has one of the highest levels of currency in circulation. Cash on hand is estimated to be around 3.2 percent of household assets, which is higher than equity investment, which is around \$220 billion. 87 percent of the cash is in the form of Rs 500 and Rs 1,000 notes, totaling about Rs 14 lakh crore (\$190 billion)(13). Economic transactions that are not reported to tax authorities or that are generated through corruption account for a significant portion of the household cash on hand. If the higher denomination money is scrapped, it will either be reintroduced into the system or it will simply vanish(14). The economy will not benefit if the money vanishes because some hoarders do not want to be seen with their cash. However, if the money makes its way into the economy, it could have a significant impact. However, the move was one of a series that failed to fix a debt-ridden and inflation-ridden economy, as evidenced by different countries' experiences (11,15).

The current study is entirely reliant on secondary data because it is essentially a review of previous literature. A secondary source of data was collected from a variety of periodicals including issues of the Indian Economic Survey. To conceptualise the issue, the first portion includes a brief overview of previous investigations. After then, the impact of demonetisation on the Indian economy was investigated using secondary data. The study's main variables are the tax-to-GDP ratio and GDP growth rate. The impact of demonetisation on various areas of the economy is also examined using GDP growth rates per sector. The study tells about the meaning and reasons of

demonetisation along with the sector-wise impact of demonetisation and positive and negative impacts of demonetisation on Indian economy. Hence makes use of secondary data. The entire study is based only on observation and documentary analysis.

In long run, there are some positive and some negative impact of demonetization but negative impact does not outweigh the positive impact of it. After the demonetization some sectors not affected like Pharma, FMCG, Education, Agriculture, Hospitals, Energy and Telecommunication From an equity market perspective, this move would be positive for Banking and Infrastructure sector in the medium to long term. This would be negative for Real Estates, Customer durables, Luxury items in the near to medium term. Demonetization can lead to elimination of fake currency and corruption, it can be said that this is a historical step by the Modi Government and should be supported by all. This decision of Government will definitely fetch results in the long term this is the stepping stone towards/ for sustained economic growth in long run.

India had an experience of demonetization of its currency twice before. The first was when Rs. 1000, Rs. 5000 and Rs 10000 notes were taken out of circulation on 12th January 1946, a 1 ½ year before the Independence(16). The highest denomination note ever printed by RBI in India was Rs. 10000 note introduced for the first time in the year 1938. However all three of Rs. 1000, Rs 5000 and Rs. 10000 notes were again reintroduced in 1954. The second phase of demonetization was done on 16th January 1978 when an ordinance was promulgated to phase out notes with denomination of Rs. 1000, Rs 5000 and Rs. 10000. On 12th January 1946 demonetization was resorted to but the Direct Tax Enquiry Committee in its interim report observed, "Demonetization was not successful then, because only a very small proportion of total notes in circulation were demonetized in 1946 and its worth was Rs. 1,235.93 crores". On 16th January 1978, demonetization of high denomination notes was introduced. The high demonetization notes as on that day amounted to Rs. 146 crore and total notes tendered to RBI amounted to Rs. 125 crore as per data available till August 1981.

Demonetization refers to withdrawal of a particular form of currency from circulation. It is necessary whenever there is a change of national currency; the old currency must be remove and substituted with the new currency unit. The currency was demonetizing first time in 1946, and second time in 1978. On 8th Nov. 2016 the currency is demonetized third time by present Modi Government. The chaos was created in every strata of the society whether upper, middle or lower. Where some welcomed the move as it was seen for curbing black money, many are suffering by this movement. In this paper analyze the current and immediate impact of demonetization on Indian economy and work out the probable consequences of the demonetization.

The paper is based on the secondary data. The secondary data was collected from various published sources like reports, magazines, journals, newspapers etc. The dictionary meaning of DEMONETIZE is "To deprive (a metal) of its capacity as a monetary standard" or "To withdraw from use as currency" So, demonetization is the act of stripping a currency unit of its status as legal tender. It is the act or process of removing the legal status of currency unit. A currency on which Governor of RBI on behalf of Central Government guarantees by making statement "I promises to pay the bearer, the sum of money" which empowers it a legal status. From the date of demonetization, all old currencies which are demonetized will cease to be a legal tender. Such currency cannot be used as money to do any transaction henceforth, but to replace with a new currency. The Government of India on the 8 November 2016 announced demonetization of high denomination currency notes Rs 500 and Rs1000. This means that 500 and 1000 rupees notes will be accepted by anyone except the organization declared by the Government. A new redesigned series of Rs 500 and Rs 2000 banknote is in circulation since 10 November 2016.

Impact on Black Money and Corruption: 'Black Money' or 'Dirty Money' is the money on which not tax is paid to the Government and it goes unaccounted in the duration of country tax

assessment period which causes revenue loss to the government. It is argued that steps taken by the government of demonetization can help curbing black money in the country. Corruption will also be automatically reduced by removing black money from economy.

SBI Research, RBI The Table depicts the public holding of high denomination notes worth Rs. 9926 billion as on march 2016. There are 3 scenarios in table. In scenario 1 and 2 it is assumed that 50% of the notes of higher the denomination do not return to the system. It is also reasonable to expect that 60% of Rs. 500 notes and 40% of Rs. 1000 notes would be exchanged at banks/ post offices and RBI before March 31, 2017. Based on such estimates, roughly round Rs. 4.5 lakh crore of money could disappear from the system.

The Biggest positive impact of the demonetization will be on the counterfeit/fake currency as it currently thrown out of the system fully. GDP become down because circulation of currency is less because of cash crunch in the country. The GDP formation could be impacted by this measure, with reduction in the consumption demand. Moreover, this expected impact on GDP may not be significant as some of this demand will only be deferred and re-enter the stream once the cash situation becomes normal. Inflation arises due to higher liquidity in the market. Because of demonetization there is less liquidity and less cash flow in the market that's why inflation becomes down. As the black money goes out of the system the money supply will shrink to some degree. This will reduce inflation rate in the Lower absence of any open market interventions by the Reserve Bank of India. Inflation is of four types.

The move of demonetization has affected the purchasing power. This is mainly affect those assets that are used as long term investments like Real Estate, Vehicles and core sectors of cement and steel. The stock prices of the companies of these sectors will have a negative impact. Purchasing power of consumer is also affected due to the shortage of cash because 90% transactions taking place in cash in the Indian economy. Demonetization smashed the real estate market and it will result in more than 50% drop down and it will remain for further 5 to 6 months. While the short-term impact is negative, Experts hoping that rate cuts in the coming months would boost home sales. The demonetization effects on banks will be both on the positive side and the negative side. However, In the long run it will be more on the positive side. As per directions of Government people have to deposit their money with the banks which will increase the liquidity of the banks for short term. This liquidity can be used by banks for lending purpose for long run.

2. DISCUSSION

The grounds for demonetization are as follows: Money in circulation that isn't legal. Demonetisation was a brave and innovative move by India's government to combat black money, and it would have a significant effect on the country's parallel economy. This maneuver may be used to identify pockets and people with black money. Property dealers, jewellers, foreign currency dealers, and private money lenders are among the companies that retain large sums of undeclared money in the form of currency notes. A parallel economy has developed in the nation as a result of the undeclared money. Through indirectly or directly routes, such illicit funds have made their way into bank accounts. Demonetisation has resulted in the squandering of fake currency notes. Withdrawing the highest value notes from the economy would have a significant influence on fake currency syndicates, thereby ending terror financing in Jammu & Kashmir, Naxalite-affected regions, and the North-eastern states. The false money used by racketeers has been abandoned, and new currency notes with great security have been introduced, making counterfeiting impossible.

Demonetization was a surgical strike against a circulating counterfeit money. Demonetization has reduced those counterfeit money notes to nothing more than a piece of paper. The goal of demonetization was to promote a cashless/digital economy. As more and more transactions become cashless or less cash, more revenue will be disclosed, resulting in an increase in direct tax

receipts. Alternative means of payment will become increasingly popular as cash transactions decline. Electronic modes of payment, such as online transactions, payments through apps, E-wallets, E-banking, and the use of payment cards, will undoubtedly see a significant rise in demand. Demonetisation has already had a negative effect on real estate and property, construction, and household spending in general, the long-term advantages for GDP growth are expected to exceed the short-term transitory impact. Demonetization has put a stop to the bulk of builders' companies since a large percentage of their transactions rely on cash rather than bank transfers or cheque transactions(17–19).

Marginal builders, like other industries, are negatively affected by the significant cash component in payment in their industry. Builders who are disorganized have been the most hit. Builders will suffer a financial constraint as a result of the unexpected decrease in sales, so they will need to provide attractive incentives and other advantages to entice customers. Because cash plays such a large part in these transactions, demonetisation would have a direct effect on the resale and land sector. Demonetisation has removed the majority of the accounted cash from the system. Pharma, Education, Farming, Hospitals, Electricity, and Telecommunications were not affected by demonetization. This decision would be favorable for the Banking and Construction sector in the medium to long term. In the short to medium term, this would be bad for real estate, consumer durables, and luxury goods. Demonetization has the potential to eliminate counterfeit money and corruption; thus, it can be stated that the Modi government has taken a historic move that should be applauded by everyone. This government action will undoubtedly provide long-term benefits, since it is a stepping stone toward/for long-term economic development (20).

3. CONCLUSION

The move to demonetize high-denomination currency notes was both daring and risky. It will have a significant effect on the Indian economy in many sectors, with far-reaching repercussions in many areas. Due to the excess cash created by the demonetisation campaign, prominent banks throughout the nation have been able to reduce their lending rates. Real estate, consumer goods, luxury products, jewelry, and related industries may be affected. A drop in economic activity due to currency restrictions during the demonetization phase, Within the 2 months the RBI could have properly replaced up to 75 percent of the demonetized currency with the new 500 and 1000 notes. People in India are very adaptable, as shown by the widespread acceptance for the switch to e-wallets. Even in the first week after demonetization, certain sectors of the economy grew, while others, such as the impulse purchase sector (biscuits, soft drinks, etc.) declined. Farmers and Rabi sowing seem unaffected, as shown by an increase in sowing area. The Indian economy is now forming a 'V' shape as a result of demonetization. Following demonetization, digital payments are on the rise. Everyone is attempting to embrace digital payment. The amount of black money in the Indian economy has decreased. In India, corruption has decreased. The value of a bank deposit may increase in the near term, but it will decline in the long run. India's gross domestic product would fall as a result of demonetization.

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