

## **Demonetization And Its Impact: An Overview**

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**ABSTRACT:** *Demonetization refers to the withdrawal of a particular form of currency of the nation from circulation. Demonetization is necessary whenever there is a change of national currency. The old unit of currency must be removed and substituted with a new currency unit. The study attempts to analyze the impact of demonetization on the Indian economy. The study is based on secondary data. The required data has been extracted from the various sources like research papers, published sources like reports, magazines, journals, newspapers and the authenticated websites. The study found that, by demonetization, black money will be taken out of Indian system; corruption will also be automatically reduced. Thus, we can conclude that this is a historical step taken by Narendra Modi and should be supported by all. This decision of Indian government will definitely fetch good results in the long run.*

**Keywords:** *Demonetization, Impact, Jan Dhan Accounts, Corruption.*

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### **I. INTRODUCTION**

Demonetize is nothing but “To deprive 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 process of removing the legal status of currency unit. 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. Process of removing a currency from general usage or circulation is known as demonetization.

Money is the life blood of every economy. With the growth of civilization and mankind, the needs of human beings increased. Barter system was emerged to fulfill the needs of human beings; the invention of money became a stronger pillar to build the economy. Money exchange facilitates ease of doing business, facilitates taxation and national integration. All activities like manufacturing, exchange, distribution, services etc. form an economy, it is known as formal economy. An informal economy is one where neither taxed nor monitored by government. Presence of corruption, black money, counterfeit currency, poor governance etc. promotes and establishes parallel economy. Parallel economy is nothing but functioning of unsanctioned sector in the economy whose purpose is to evade tax. This is popularly known as illegal economy, unaccounted economy; tax evaded economy or black economy. In order to mitigate parallel economy or to redefine formal economy government takes many initiatives like demonetization, voluntary income declaration scheme, economic liberalization, reducing tax rates.

The Indian Government had demonetized bank notes on two prior occasions once in 1946 and then again in 1978 and in both the cases, the objective was to combat tax evasion by black money held outside the formal economic system. There are multiple reasons why nations demonetized their local units of currency. To combat inflation, to combat corruption and crime, to discourage a cash depended economy and to facilitate trade. On November 8, Indian Prime Minister Narendra Modi announced in a broadcast to the nation that 500 and 1000 currency notes would no longer be recognized legally currency. This is the bold step taken by the government of India for the betterment of the Indian economy.

Demonetization is one of the government's bold steps towards transformation of Indian economy. It is one of the biggest big bang reforms undertaken by government after a long time. India had an experience of demonetization of its currency twice before. The first was when Rs. 1000, Rs. 5,000 and Rs. 10,000 notes were taken out of circulation on 12<sup>th</sup> January, 1946. The highest denomination note ever printed by RBI in India was Rs. 10,000 note introduced for the first time in the year 1938. However all three of Rs. 1000, Rs. 5,000 and Rs.10,000 notes were again reintroduced in 1954. The second phase of demonetization was done on 16<sup>th</sup> January, 1978 when an ordinance was promulgated to phase out notes with demonetization of Rs. 1000, Rs. 5,000 and Rs.10,000. On 12<sup>th</sup> 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 16<sup>th</sup> 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.

On 8<sup>th</sup> November, 2016 the government announced the demonetization of Rs. 500 and Rs.1,000 notes with immediate effect, giving little time for hoarders or small time savers to convert their stock of illegal tender money into legal tender money. This was followed by subsequent policy announcement from RBI to ease the hardships faced by the citizens. However, even after 50 days of the announcement, the long queues of people outside ATMs to withdraw their savings continue. Small traders, especially in the informal sector are facing a tough time with a decline in sales and small units have shut down, unable to meet their working capital expenditure. Setting aside the hardships faced by the common man, how much black money or unaccounted money was disclosed or turned into white money.

Prior to the demonetization announcement, under the income declaration scheme 2016, the government was able to unearth 65,250 crores of undisclosed income through 64,275 declaration upto 30<sup>th</sup> September, 2016. More such undisclosed income would be made public with the income tax department identifying 67.54 lakh potential non files on income tax, who had conducted high value transaction in 2014-15 but have not files their returns.

## II. OBJECTIVES OF THE STUDY

1. To study the overview of demonetization.
2. To study the Deposits under PMJDY.
3. To study the measures to sustain demonetization.
4. To study the effect of demonetization on different sectors.

## III. RESEARCH METHODOLOGY

The study is based on secondary data. The required data has been extracted from various sources like Research Papers, various bulletins of RBI, published sources like Reports, Magazines, Journals, Newspaper articles and the authenticated websites.

## IV. REVIEW OF LITERATURE

- ★ **Dr. S. Parthiban and S. Krishnakumar (2016)** the article entitled “Impacts on Demonetization in Organized and Unorganized Sector”. In this paper an attempt has been made to examining the impact of demonetization in organized and unorganized sector. The study found that, demonetization is a historical step and should be supported by all. One should look at the bigger picture which will definitely fetch results in the long term. The study also found that, demonetization will likely result in people adopting virtual wallets as Paytm, Ola Money, Net banking, mobile banking and transaction through other apps will increase, this behavioral change could be a game changer for India.
- ★ **Dr. S. Balamurugan and B. K. Hemalatha (2016)** the article entitled “Impacts on Demonetization: Organized and Unorganized Sector”. In this paper an attempt has been made to elucidate the impact of demonetization on the availability of credit, spending, level of activity and government finances. The study found that, the demonetization drive will affect some extent to the general public, but for larger interest of the country such decisions are inevitable. Also it may not curb black money fully, but definitely it has major impact in curbing black money to large extent.
- ★ **Vedashree Mali (2016)** the article entitled “A step towards modified India”. In this paper an attempt has been made about the move of demonetization taken by central government of India on 8<sup>th</sup> November, 2016 with respect to its reasons and effects on different sectors in India. The study found that, demonetization though it has created some positive and some negative impacts on different sectors but in long run it definitely will have positive impact in controlling black money and fake money.
- ★ **Anil I. Ramdurg and Dr. Basavaraj C. S. (2016)** the article entitled “Demonetization: Redefining Indian economy”. In this paper an attempt to assess how the tool of demonetization can be used to eradicate parallel economy, pros and cons of demonetization and measures needed to sustain demonetization benefits. The study found that, the demonetization is a general measure to mitigate the problems of black and counterfeit notes, though there are specific measures to tackle the same menace.

## V. MEASURES TO SUSTAIN DEMONETIZATION

Parallel economy was erased after a lot of efforts made by the government. Following are the measures are taken to sustain the demonetization:

- ❖ **Implementation:** The problem is not the existence of parallel economy to curb it, but it is implementation of all those measures to overcome menace of parallel economy. If government takes initiation in implementing at least majority of the measures available before government, then this problem finds solution on its own.
- ❖ **Linking of Aadhaar:** Linking of Aadhaar must be made mandatory to get civil benefits. All multiple bank accounts must be linked with Aadhaar. Various departments like Income Tax, Sales Tax, VAT, Excise,

Customs, Service Tax and Licensing Department etc. must be linked with Aadhaar number. This not only creates awareness among the people but also as controlling mechanism.

- ❖ **Reduced Tax Rates:** The main reason for tax evasion and tax avoidance is high tax rates. Tax rates are to be brought down to such an extent that cost of compliances must be lower than the cost of tax evasion.
- ❖ **Mechanized System:** In generating revenue to government there are leakages due to corruption. If we plug those leakages, government can reduce its tax rates. Reduced human interference in the system will reduce corruption.
- ❖ **Declaration of Assets:** It must be made mandatory to declare every persons asset to government. If undeclared assets found, then the same assets can be seized by government. This prevents mobilization of black money in the form of gold, land, house property etc.
- ❖ **Simplified Tax Structure:** Many people are finding it difficult to understand various taxes and its calculation. Simplify the tax calculation mechanism. Removal of various tax mechanisms in direct tax like surcharge, education cess, short term capital gains etc. may be removed.
- ❖ **Uniform Property Registration Software:** Uniform software should be developed to register properties throughout the country. That should be linked with Aadhar to overcome holding of benami properties. This can be made without disturbing the state government power to generate revenue of stamp duty, just as a control technique.
- ❖ **Good Governance:** People must believe in good governance and support for it. Winning public faith in good governance is very much essential to build strong economy. Control on holding of cash and physical money both in India and outside India, must be brought under the legal framework.

## VI. MAJOR BENEFITS OF DEMONETIZATION

- ✚ Fake Currency: 100% fake currency out of circulation in one stroke.
- ✚ Hawala Sources Dried Up: Funding stops to Terrorist, Naxalites Maoists, Jihadis and underworld.
- ✚ Kashmir moving back to Normal: Blow to insurgency, no more schools being burnt and no stone palters to be found.
- ✚ Reduction in fiscal deficit: Fiscal deficit of India set to reduce.
- ✚ Use of Apps and Card: Small vendors have started using apps and card machines.
- ✚ Gold Stock: All Jewellers are being issued forms to declare their gold stock on day to day basis.
- ✚ Banks have started mobile ATM for Hospitals.
- ✚ Jan Dhan account is full with money.
- ✚ 55 lakh money disputes settled in one day in Lok Adalat.
- ✚ More than 3 lakh crore cash already deposited in accounts.
- ✚ All business men are depositing cash lying with them as current year income with advance tax.
- ✚ Defaulters of Banks, property tax, electricity bills, telecom bills are clearing their long pending dues.
- ✚ Defaulters of all kind of government taxes are clearing their dues.

## VII. DEMONETISATION - MEASURES TO MITIGATE HARDSHIPS

- ❖ **Calibrated adjustment of limits for exchange of specified bank notes (SBNs):**

The exchange facility of specified bank notes (SBNs) which was initially allowed up to Rs. 4,000 was increased to Rs.4,500. It was reduced to Rs.2,000 (effective 17<sup>th</sup> November, 2016). This facility was subsequently discontinued effective 25<sup>th</sup> November, 2016 at banks, but was available at RBI counters up to 30<sup>th</sup> December, 2016.
- ❖ **Withdrawal limit from ATMs:**

The limit for cash withdrawal from ATMs, which was initially set at Rs. 2,000 per day, was enhanced to Rs. 2,500 per day and further to Rs. 4,500 and Rs.10,000 and was withdrawn from 1<sup>st</sup> February, 2017.
- ❖ **Gradual Relaxation of limits on withdrawal from Bank Accounts:**

The limit of withdrawal from saving account, which was initially stipulated at Rs. 20,000 per week, was revised to Rs. 24,000 and further to Rs. 50,000 per week (effective 20<sup>th</sup> February, 2017). Effective 13<sup>th</sup> March, 2017, there will be no limit on cash withdrawals from savings accounts. Current account withdrawal of Rs.50,000 per week was enhanced to Rs. 1,00,000 per week effective 16<sup>th</sup> January, 2017. Limit on cash withdrawals from current accounts was removed effective 30<sup>th</sup> January, 2017. Cash withdrawal from the bank deposit accounts up to Rs. 2,50,000 were allowed from 21<sup>st</sup> November, 2016 to meet wedding related expenses.
- ❖ **Deposit of SBNs:**

Deposits of SBNs in bank accounts were permitted up to 30<sup>th</sup> December, 2016. The facility for exchange of SBNs for the residents, who could not avail the facility from 9<sup>th</sup> November to 30<sup>th</sup> December, 2016 on account their absence from India during the aforementioned period, was made available at the RBI up to 31<sup>st</sup> March, 2017 and for non- resident Indian citizens up to 30<sup>th</sup> June, 2017.

❖ **Other Measures**

- ✓ Banks were advised to waive ATM charges on withdrawals between 10<sup>th</sup> November and 30<sup>th</sup> December, 2016.
- ✓ The limit for cash withdrawal at POS (for debit cards and open system prepaid cards issued by banks in India) was made uniform at Rs. 2,000 per day across all centers for all merchant establishments enabled for this facility and customer charges were not be levied on such transactions from 18<sup>th</sup> November, 2016 to 30<sup>th</sup> December, 2016.

**VIII. FACTS AND FIGURES**

Up to 97% of the demonetized bank notes have been deposited into banks which have received a total of 14.97 trillion (\$220 billion) as of 30<sup>th</sup> December, out of the 15.4 trillion that was demonetized. This is against the government initial estimate that 3 trillion would not return to the banking system. Of the 15.4 trillion demonetized in the form of Rs. 500 and Rs.1000 bank notes of Mahatma Gandhi series 9.2 trillion in the form of 500 and 2000 bank notes of the Mahatma Gandhi new series has been recalculated as of 10<sup>th</sup> January, 2017.

After demonetization of Indian currency on 8<sup>th</sup> November, 2016, rupee had become stronger than currency of 143 countries. Out of 161 countries' currency, rupee has become weaker than 17 currencies and is at same exchange rate with 1 currency. Indian Rupee has become stronger by 0.95% against US\$ from 66.78 INR per unit US\$. Indian Rupee has become stronger against some popular currencies like Euro, Australian dollar, Swiss France, Singapore Dollar, Japanese Yen,, British Pound, Pakistani Rupee, Sri Lankan Rupee, Bangladesh Taka, Canadian Dollar and Hong Kong Dollar. Indian Rupee has become weaker than Russian Ruble and South African Rand. In Modi Government, Indian rupee has become stronger than 107 currencies.

PERIOD	STRONGER	WEAKER	SAME
After Demonetization (8 <sup>th</sup> November, 2016 to 14 <sup>th</sup> March, 2017)	143	17	1
In Modi Government (26 <sup>th</sup> May, 2014 to 14 <sup>th</sup> March, 2017)	107	53	1
In Modi Government Before Demonetization (26 <sup>th</sup> May, 2014 and 8 <sup>th</sup> November, 2016)	93	67	1

**PRADHAN MANTRI JAN DHAN ACCOUNTS (PMJDY)**  
**Table 1: DEPOSITS UNDER PMJDY (NUMBER OF ACCOUNTS)**

(Rupees in Millions)

Bank Groups	As on 9 <sup>th</sup> November, 2016			As on 1 <sup>st</sup> March, 2017			Variation		
	Rural	Urban	Total	Rural	Urban	Total	Rural	Urban	Total
Public Sector Banks (PSBs)	114.3	89.3	203.6	122.1	100.8	222.9	7.8 (6.8)	11.5 (12.9)	19.3 (9.5)
Regional Rural Banks (RRBs)	37.1	6.0	43.1	40.0	6.4	46.4	2.9 (7.8)	0.4 (6.8)	3.3 (7.7)
Private Sector Banks (PSBs)	5.3	3.1	8.4	5.4	3.6	9.0	0.1 (1.3)	0.5 (16.8)	0.6 (7.0)
Scheduled Commercial Banks (SCBs)	156.7	98.4	255.1	167.5	110.9	278.4	10.8 (6.9)	12.59 (12.7)	23.3 (9.1)

**Note:** Figures in parentheses are percentage variation

**Source:** Pradhan Mantri Jan Dhan Yojana (PMJDY) website

The above table reveals that, during post demonetization 23.3 million new accounts were opened under the Pradhan Mantri Jan Dhan Yojana (PMJDY), bulk of which (80%) was with public sector banks. Of the new Jan Dhan accounts opened 53.6% were in urban areas and 46.4% in rural areas. Deposits under PMJDY accounts increased significantly post demonetization. The total balance in PMJDY deposit accounts peaked at Rs. 746 billion as on 7<sup>th</sup> December, 2016 from Rs. 456 billion as on 9<sup>th</sup> November, 2016 an increase of 63.6%. As there were reports regarding the use of these accounts to convert black money into white, the government issued a warning against the misuse of such accounts.

**Table 2: DEPOSITS UNDER PMJDY (AMOUNT MOBILIZED)**

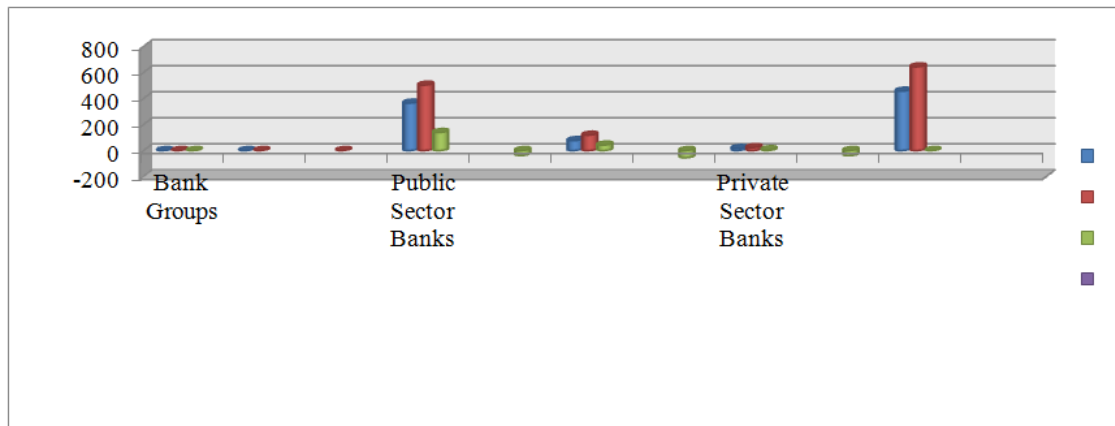
(Rupees in Billion)

Bank Groups	As on 9 <sup>th</sup> November, 2016	As on 1 <sup>st</sup> March, 2017	Variation	Variation in aggregate Deposits of Scheduled Commercial Banks (17 <sup>th</sup> February, 2017 over 11 <sup>th</sup> November, 2016)	Accretion in PMJDY Deposits as Percentage of Accretion aggregate Deposits*
Public Sector Banks (PSBs)	364.0	502.5	138.5 (38.0)	2733.0 (3.9)	5.1

Regional Rural Banks (RRBs)	76.3	118.1	41.8 (55.0)	616.0 (18.0)	6.8
Private Sector Banks (PSBs)	16.0	22.3	6.3 (39.0)	778.0 (3.5)	0.8
Scheduled Commercial Banks (SCBs)	456.4	642.9	186.5 (41.0)	4098.0 (4.1)	4.6

**Note:** Figures in parentheses are percentage variation  
**Source:** Pradhan Mantri Jan Dhan Yojana (PMJDY) website  
 \*The ratio pertains to Jan Dhan deposits as on 15<sup>th</sup> February, 2017.

The above table reveals that, the government also capped deposits into PMJDY accounts at Rs. 50,000 on 15<sup>th</sup> November, 2016. Although deposits declined to Rs. 643 billion as on 1<sup>st</sup> March, 2017, they were still higher by 41% over the level of 9<sup>th</sup> November, 2016. Jan Dhan accounts contributed 4.6% in total accretion of aggregate deposits of Scheduled Commercial Banks in post demonetization period.



### IX. EFFECTS OF DEMONETIZATION ON DIFFERENT SECTORS

- **Real Estate:** Real estate will be one of the most affected sectors. Everyone believes the same and hence the Nifty Reality Index closed at 175.2 down 11.60%. It is a popular bet in the fresh and resale market dominated by black money holders. The number of buyers will come down and low demand will bring about lower prices in the short term. However, it will subsequently help in improving the sector's prospects. Unorganized builders will be most affected and the sector will drag down cement and ceramic sectors also along with it.
- **Gold Prices:** As investors rushed to invest in safe havens gold futures touched a high of Rs. 31,376 and was trading at Rs. 30,500 up 2%. Local shops have stopped selling gold in exchange of old notes. It will create havoc for a little while and the economy will also destabilize. But overall it is going to be good for the country.
- **Banks:** Banks are the back bone of this entire process and also the biggest beneficiaries. Post complete exchange of currencies, banks should benefit from higher deposits and transaction volumes lower cash handling costs and greater acceptance of digital channels. There are likely to be secondary benefits for the insurance, asset/ wealth management companies through higher financial savings.
- **Entertainment/Restaurants:** One of the most common areas where undisclosed income is utilized is the entertainment and restaurant industry. There are plenty of restaurants out there that accept credit and debit cards. Since a majority of the transactions are in cash from in here, it will be exciting to see how people reach to it. Will they continue to opt for entertainment at the same scale that they did earlier.
- **Beauty Parlours:** This has been a booming industry that works largely on cash. In the past few years, beauty parlours have mushroomed on almost every street of urban and semi urban India. Although a few of the larger, organized parlours do accept credit and debit card payments, most parlours transact mainly in cash because it is often seen as a luxury spending fuelled by unaccounted income.
- **Tourism:** Favorite foreign tourist destinations of Indian people like Thailand, Singapore, Malaysia, Maldives, Hawaii, Vietnam, Sri Lanka, Nepal, China, Indonesia and Dubai will see negative impact in tourism revenues all black money sponsored trips will come to a halt. Indian local tourism will also get affected as they lose large chunks of the pay-in-cash only clientele. Illegal foreign currency conversion is also reported to be badly hit, because they were big acceptors of Rs. 500 and Rs.1,000 denomination currency.

- **Luxury items:** will have a drastic negative impact. Majority of the people spend their undeclared income on such products. After the decision, it is likely that all luxury segments like clothing, electronics, luxury car, furnishing and allied business will take a hit. Media and hospitality industries are also likely to get affected.

Sectors that we feel will not be affected are Pharma, FMCG, Education, Agriculture, Hospitals, Energy and Telecommunication.

#### **X. REASONS WHY DEMONETIZATION IS A MASTERSTROKE BY MODI**

- ★ Boost deposit base and savings.
- ★ Improve monetary transactions and reduce lending rates.
- ★ Create room for further monetary accommodation.
- ★ Ready steady, now go: financial inclusion via Jan Dhan account.
- ★ Support Government finance.
- ★ Positive impacts from a bond market perspective.
- ★ Rise in GDP growth potential

#### **XI. IMPACT OF DEMONETIZATION ON THE UNORGANIZED SECTOR**

- ✓ **Cash Economy:** Nearly 2/3 of India's GDP is cash economy which is heavily dominated by the unorganized sector. Most of the transactions in this sector happen through cash, some even daily wages. Sudden liquidity crunch hit both employers and merchandise and wages respectively.
- ✓ **Banking Penetration:** Banking penetration in India is close to 53% but since the co-operative banks, which have a massive presence in rural areas is missing from the ambit. Most of the employers in the unorganized sector are illiterate they are not tech savvy and may not be completely aware of banking procedures. Also many unorganized jobs are in rural areas gives them less access the banks and ATMs.
- ✓ **Savings and Trade:** Since most of the savings and trade are done in the form of cash, the new move has brought them to a standstill.
- ✓ **Future Trade Flow:** No cash made them impossible to carry on buying products for next cycle of selling. This could be clearly evidenced in agriculture sector, where farmers are not able to buy seeds, fertilizers. Being a sowing season for Rabi crops, it is taking a toll on farmers.

#### **XII. MEASURES TAKEN FOR ENSURING BUSINESS AS USUAL**

- Permission to farmers to withdraw up to 25,000 a week.
- Agri -traders registered with marketing committees can withdraw up to Rs. 50,000.
- Extension in payment of crop insurance premium.

#### **XIII. FINDINGS OF THE STUDY**

1. The demonetization drive will affect some extent to the general public, but for larger interest of the country such decision are inevitable.
2. The demonetization may not curb black money fully, but definitely it has major impact in curbing black money to large extent.
3. Small farmers, sellers, merchants, daily wage laborers and traders are suffering because of lack of proper planning, intelligence and foresight such as recalibration of ATM machines.
4. Majority of Indian unorganized sector have no knowledge about cashless transaction and resources also limited. When a poor farmer is unable to repay his small loan 5, 6% of the amount deducted in every digital transaction as service charge.
5. Temporarily unorganized sector buying capacity i.e. purchasing of raw materials, fertilizers will decrease.
6. After demonetization the demand for gold and other precious metals rise greatly, because people are trying to invest their black money in gold to make it white in short period. But demand for gems and jewellery to decline in the next two or three quarters.

#### **XIV. SUGGESTIONS**

1. Most of the cashless transactions are connected through internet which demand proper network that is still inadequate in some parts of India.
2. Many illegal agents (Dalals) are emerged who are indulged in exchange of notes with a huge commission resulting in moral degradation.
3. Government is promoting the cashless transaction and in this direction, government has taken initiative with some incentives such as insurance, e-payment discount offer etc. and recently lucky winners for each week using e-payment.

4. Central government as well as State government has made efforts to make their offices cashless that deal with public.
5. The government has put its very big efforts through PMJDY accounts so that every citizen could be connected to banking services and really this effort has been providing fruitful in the Demonetization move.
6. Proper tracking of people is must so that needy could be provided money and commission agents could be arrested.
7. There must be efforts to equip each government office with cashless machine so that people can make their e-payment smoothly.
8. Government must put its best efforts to train the people at ground level even up to small villages and for such purpose contributions of government officials, teachers, sarpanchs and panchs can be availed.

## **XV. CONCLUSION**

Demonetization is not new to India or to the outside world. Various governments across the world have decided to ban currency note in circulation, rendering huge amount of cash useless overnights due to plethora of reasons. These reasons include fighting counterfeiting, stopping terror activities, battling black money etc. Many countries have adopted this process of demonetization to overcome hyperinflation, to curb black money, to bring economic stability, to remove counterfeit currency etc. Demonetization is a historical step and should be supported by all. One should look at the bigger picture which fetches results in the long run. This is what the people have been asking for a long time which has finally happened. Demonetization will likely result in people adopting virtual wallets such as PAYTM, OLA Money, Net Banking, Mobile Banking, and transaction through other apps will increase; this behavioral change could be a game changer for India. "When we expect an honest government with no corruption and malpractices, we also have to be honest. Honesty is not one way road"- Prime Minister Narendra Modi. Demonetization though it has created some positive and some negative impacts on different sectors but in long run it definitely will have positive impact in controlling black and fake money.

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