

# Effect of Demonetization in India

## Abstract

It is current form of money that is pulled from circulation and it is often replaced with new notes or coins. Sometimes a country completely replaces the old currency with new one. Demonetization in India is a great effort taken by Indian government to combat with black money and corruption. Most of the black money has been crushed. Amount of cash liquidity increased in the bank day by day. It is bold decision taken by government. The main purpose of demonetization is eradication the black money and reduces the corruption

**Keywords:** Demonetization, Consumers, Cashless System.

## Introduction

Demonetization is the act of stripping a currency unit of its status as legal tender. It occurs whenever there is a change in national currency. It is current forms of money that is pulled from circulation and it is often replaced with new notes or coins. Sometimes a country completely replaces the old currency with new one. India has carried out demonetization exercises twice before, in 1946 and 1978. In January 1978, 1.7% of total notes in circulation was demonetized. In 1946 the first demonetization took place and Rs. 1000 and Rs. 10000 notes were demonetized. Later in 1978, Rs. 1000, Rs. 5000 and Rs. 10000 were demonetized. The value of demonetization was very small in 1978 and that is only 0.1% of GDP. However in 2016 demonetization efforts covers 86% of total currency in circulation (11% of GDP). This is the third time demonetization has taken place. 78% Indian customers transactions are in cash. In this conditions bank line outside ATM and bank increase. New currency is different in size or specification so re-calibration of ATM is require. Government also restricted withdrawal limit, create problems for some days to the civilians. It is effecting more to the small business and daily wages workers.

## Objective of Demonetization

The main objective of demonetization are-

1. Removing black money from economy.
2. Stop funding for terrorism in India by other countries.
3. Reducing fake notes.
4. Increase cashless transaction
5. Control the Inflation
6. Reduce the Rate of Interest
7. Make it Digital India through E-transactions
8. Transparent money transaction
9. Increase the Tax Revenue

## Objectives of the study

1. To estimate the consequences for future of the note ban decision.
2. To know the impact of note ban decision on the Indian economy.

## Collection of Data

Secondary data has used for the study. It is collected from library, text books, and journals, articles from news papers and from relevant websites available on internet.

## Review of Literature

**Ansari (1982)** examined the impact of real per capita GDP, the size of overseas trade and density of population on the tax revenue by making an inter country comparison. Data was collected for the period 1972 to 1976 from IMF publications, earlier studies and World Bank publications relating to 79 62 countries. The author employed regression analysis on the basis of two equations. In the first equation real per capita

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GDP and size of trade were taken as independent variables and tax revenue as dependent variable. In the second equation population factor was also included as independent variable to assess the impact of all three factors (GDP, size of overseas trade and density of population) on tax revenue. The study concluded that real gross domestic product and foreign trade were positively correlated with tax revenue, whereas density of population was negatively correlated with tax revenue.

**Arpit Guru and Shruti Kahanijow (2010)** researcher analysed the black money income? Need for amendment in DTAA & ITEA and analysed that black money is spread everywhere in India up to a large extent which continuously stashed towards abroad in a very large amount. The researcher also identified how black money had caused menaces in our economy and in what ways it is used.

**Sukanta Sarkar (2010)** conducted a study on the parallel economy in India: Causes, impacts & government initiatives in which the researcher focused on the existence of causes and impacts of black money in India. According to the study, the main reason behind the generation of black money is the Indian Political System i.e. Indian govt. just focused on making committees rather than to implement it. The study concludes that laws should be implemented properly to control black money in our economy.

**Tax Research Team (2016)** in their working paper stated in favour of demonetization Its main objective is to analyze the impact of demonetization on Indian economy. This paper shows the impact of such a move on the availability of credit, spending, level of activity and government finances.

#### **Positive Effects of Demonetization**

There is a great impact of demonetization in the Indian society. Its effect on society are as follows.

#### **Black Money**

At one stroke the Prime Minister has choked the supply of black money stacked inside the country. Of the Rs 17 lakh crore of total currency in circulation in the country, black money is estimated at mind-boggling Rs 3 lakh crore. Black money is nothing but a plunder of the nation. Black money operators run a parallel economy which shakes the very foundation of the Indian economy. With Modi's demonetisation move, all domestic black money will either be deposited into the banks with heavy penalty or be simply destroyed.

#### **Economy**

Demonetisation will have a huge resultant effect on the Indian economy. The clean-up of illegal cash will help turn around the economy. First, it will bring more borrowings to the exchequer, improve inflation outlook and increase India's gross domestic product (GDP). Second, it will revive investment opportunities and give a fillip to infrastructure and the manufacturing sector. Third, it will help reduce interest rates and lower income tax rate.

#### **Note Bank Politics**

In the run up to the crucial assembly elections in Uttar Pradesh, Punjab, Goa and Uttarakhand, Prime Minister Modi's demonetisation

announcement has come as a shock and awe for the political parties and politicians for whom black money is a lifeline. The pulling out of the old Rs 500 and Rs 1,000 currency notes will help make the election process clean and transparent. But it has brought tough times for the political parties and politicians who believe in the idea of purchasing votes in exchange for notes. That is precisely the reason a rainbow coalition of a galaxy of regional parties and the Congress is building up against Modi, because their political interests are badly hurt.

#### **Real Estate Cleansing**

It is said that real estate is an industry built on black money. The extent of black money floating around in the sector is huge. According to an estimate at least 40 per cent of real estate transactions in Delhi-NCR are in black. Modi's demonetisation move will curtail the flow of black money into the real estate sector. This will help in making the much needed correction in the sector. The impact: An unexpected dip in land and property prices.

#### **Hawala Transactions**

Demonetisation has crippled the hawala rackets. Hawala is a method of transferring money without any actual money movement. Hawala route is used as a means to facilitate money laundering and terror financing. Hawala rackets run again on black money. With black money suddenly being wiped out of the market, thanks to demonetisation, hawala operations have come to a grinding halt. According to an India Today report, one of the hawala operators in Mumbai has destroyed currency notes worth about Rs 500 crores.

#### **Counterfeit Currency**

Demonetisation has dealt a death blow to the counterfeit Indian currency syndicate operating both inside and outside the country. Counterfeit currency seriously devalues the real worth of Indian currency. A study conducted by Indian Statistical Institute, Kolkata on behalf of the National Investigation Agency (NIA) suggests that fake Indian currency notes (FICN) amounting to Rs 400 crore are in circulation in the country at any given point of time and around Rs 70 crore fake notes are pumped into Indian economy every year. The estimation is based on recovery and seizure made by various agencies. But the actual figure could be much larger. A One India report, quoting an Intelligence Bureau dossier, says fake Indian currency worth Rs 12 lakh crore has pumped into Indian financial system over the years. Needless to say that most of the fake currencies circulated in India are of Rs 500 and Rs 1000 denominations. It is also pertinent to mention that the fake currency floating inside the Indian financial system is not counted within the Rs 17 lakh crore of total currency in circulation in the country. This is an open secret that Pakistan has been printing fake Indian currency at its government printing press in Quetta and its security press in Karachi. The enemy nation funnels the counterfeit currency through the frontier at Jammu & Kashmir and via India's porous border with Bangladesh and Nepal. With Prime Minister Modi's decision to pull out the old Rs 500 and Rs 1,000 notes and replace them with new Rs 500 and Rs 2,000

series has completely stalled the circulation of counterfeit Indian currency. Experts say the new currency notes have come with advanced security features which are almost impossible to replicate. So Pakistan has no option but to shut shops of its fake Indian currency.

#### **Terror Financing**

Terror financing is sourced through counterfeit currency and hawala transactions. This is how terror financing works. Fake currency circulation is routed through a multi-layered network of hawala operators which are closely linked to satta (gambling) and smuggling of drugs, opium and arms. Indirectly, they all end up financing terrorism. In addition, the terrorists collect huge donations and then route the money through hawala transactions. With the circulation of counterfeit Indian currency completely stalled and hawala transactions stopped, all windows for terror financing are closed.

#### **Maoism**

Maoist sympathisers call Modi's demonetisation move an "undeclared financial emergency". There are reasons to it. Demonetisation has hit the Maoists and their movement hard. Black money is the oxygen for Maoists. According to an estimate, Maoists manage to raise Rs 300 to Rs 400 crore annually through donations, levy and extortions. The illicit money is used to purchase arms and ammunition, food and medicine and daily essentials, apart from distributing it among the ranks and the cadre. Police sources in both Chhattisgarh and Odisha have told the writer that the Maoists have stashed old high denomination notes to the tune of over Rs 10,000 crore at their dumps in the dense jungles of Odisha- Chattisgarh boarder. No wonder, with Modi's demonetisation drive, all those illegal money are reduced to paper scrap. Maoists are in a state of coma and Maoist activities see a crippling blow. Ever since the demonetisation announcement was made, no major violence was reported from the Maoist infested states like Chhattisgarh, Odisha, Andhra Pradesh and Telangana.

#### **Kashmir Unrest**

The four-month-long unrest in Kashmir valley is on a backburner, thanks to demonetization. No stone pelting on security forces has been reported in Kashmir ever since the demonetisation announcement was made. An intelligence estimate suggests that Pakistan sends Rs 1,000 crore annually to the separatists for fuelling unrest in Kashmir. The money is transferred through hawala route. With hawalatransactions completely choked up, the separatists are now clueless. It won't be wrong to say that "stone pelter" Modi completely shattered the Kashmir unrest with his stone called demonetization.

#### **North-East Insurgency**

Demonetisation has severely affected the multiple militant groups operating in the North-East. According to intelligence estimate the north-eastern insurgent groups together have a corpus of Rs 400 crore annually. The insurgents source their funding in two ways. They raise funds through levy and extortions like the Maoists do. But unlike Maoists, the leaders of North-East militant outfits do not live in the

jungle. Their English speaking high ranking leaders run operations from their dens in Myanmar, Bangladesh and Nepal.

#### **Negative Effect of Demonetization**

1. As everyone is in rush to change their money there is a situation of Chaos which lead to law and order problem and chaotic situation as these money can be exchanged from banks and ATMs only.
2. Destruction of old currency and printing of new currency involve costs, these cost has to be born by the government, if the cost is higher than benefit, then there is no use of demonetization.
3. If black money are not kept in terms of liquid cash and it will be kept as real estate or gold then there will be no use of demonetization.
4. Normal life has been impacted very much because of demonetization.
5. Fiscal deficit come down as housing prices will come down. Real estate market went down for certain period and dealers bare the loss due to the effects of demonetization.

#### **Conclusion**

Indian economy is saving economy. It leads to stable in Indian economy in all times. Whenever there is any economic meltdown in the world, there had been no changes in Indian economy. Demonetization in India is a great effort taken by Indian government to combat with black money and corruption. It is a bold decision taken by government. The main purpose of demonetization is eradicating the black money and reduces the corruption. Government of India has become success to some extent. Most of the black money has been crushed. amount of cash liquidity increased in the bank day by day. Whilst Indian government and all the stakeholders are trying to grapple with the implementation of demonetization announcements from the government, there has been certainly increased participation by Indian citizens through digital payment gateways, internet banking, mobile and digital wallets and so on. There is broader consensus amongst the most of the economists in India that there will be at least 1-2.5% drop in GDP over the next two quarters in India. Also there is broader commentary that not enough cash will be pumped to replace the old notes before May 2017 to replace amount of cash taken of the circulation. There is also expectation from the broader markets in India that the Indian government may come up with more relevant measures to reduce black money and also encourage digital transactions in the country. We believe some of these insights that we collected and assembled for the readers of this report gives an insight into current challenges and opportunities that prevail in the Indian economy and also explains the Indian government's longer term aspirations to achieve a cashless economy in the country.

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P: ISSN NO.: 2321-290X

RNI : UPBIL/2013/55327

VOL-6\* ISSUE-5\* January- 2019

E: ISSN NO.: 2349-980X

## **Shrinkhla Ek Shodhparak Vaicharik Patrika**

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