

Demonetization in India- A Boon and Bane

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Abstract

Finance plays pivotal role for the success of economic development at large. The recent announcement of demonetization made tremendous impact in society. In this parlance, Demonetization refers to withdrawal of a specific form of currency from circulation. It considered as necessary whenever there is a change of national currency. The old unit of currency to be removed and substituted with a new currency unit. This move will help the government to track the black money. The currency was demonetized first time in 1946 and second time in 1978. The currency is demonetized as third time by the current Narendra Modi government on Nov. 2016. This is the bold step taken by the government for the betterment of the economy and country. The objective of this study is to discuss the impact of recent demonetization on the Indian system and also challenges of implementing demonetization in the

country. In the wake of demonetization, there have been multiple debates on whether the “radical” and “bold” step taken by the Central government was a judicious, well-thought out and well-implemented step. Besides this paper also focuses on pros and cons of recent announcement pertaining to the concept of demonetization.

Key words: Finance, tremendous impact, withdrawal, national currency.

I -Introduction and Evolution of Demonetization

Demonetization of currency means discontinuity of the particular currency from circulation and replacing it with a new currency. In the current context it is the banning of the 500 and 1000 denomination currency notes as a legal tender. The original objectives were stated as: eliminating fake currency; inflicting losses on those with black money; and disrupting terror and criminal activities. Later, new objectives were tacked on: enabling growth in bank credit, turning India into a cashless economy. The move will stop funding to the unlawful activities that are thriving due to unaccounted cash flow. Banning high-value currency will rein in criminal activities like terrorism etc.

Demonetization is a radical monetary step in which a currency unit’s status as a legal tender is declared invalid. In 1946, the currency note of Rs 1,000 and Rs 10,000 were removed from circulation. The ban really did not have much impact, as the currency of such higher denomination was not accessible to the common people.

However, both the notes were reintroduced in 1954 with an additional introduction of Rs 5,000 currency. Rs 500 and Rs 1000 notes were introduced in 1934 and after four years in 1938, Rs 10,000 notes were introduced. In 1978, the Prime Minister of India Morarji Desai announced the currency ban taking Rs 1000, Rs 5000 and Rs 10,000 out of circulation. The sole aim of the ban was to curb black money generation in the country. The note ban by Morarji Desai also aimed to drive away black money out of circulation in the economy.

Hence, The High Denomination Bank Notes (Demonetization) Act was implemented. Narendra Modi announced the currency ban in an address that was broadcasted across all news channels. Similarly, Desai announced the ban over the radio after which the banks were closed the following day. The Governor I.G. Patel believed that the ban was implemented simply to immobilize the funds of the opposition party. Patel also believed that people never store black money in the form of currency for too long.

In 2016, there is also a buzz that smaller denomination currency notes like Rs 50 and Rs 100 will also be replaced by incorporating new features and design. This reminds of an incident dating back to early 70s, when there were rumours of withdrawing Rs 100 note from circulation, and immediately hoards of people were seen rushing to banks to exchange their Rs 10 and Rs 20 currencies. In India, the move has been taken to curb the menace of black money and fake notes by reducing the amount of cash available in the system. It is also interesting to note that this was not the first time the Government of India has gone for the demonetization of high-value currency.

II - Reviews on Demonetization

Amartya Sen: Leading economist; Noble Laureate; recipient of the Bharat Ratna said “Only an authoritarian government can calmly cause such misery to the people - with millions of innocent people being deprived of their money and being subjected to suffering, inconvenience and indignity in trying to get their own money back”. He also said **that the government claims that unless proven otherwise, all are potential hoarders of black money:** “Telling the public suddenly that the promissory notes you have, do not promise anything with certainty, is a more complex manifestation of authoritarianism, allegedly justified - or so the government claims- because some of these notes, held by some crooked people, involve black money. At one stroke the move declares all Indians - indeed all holders of Indian currency - as possibly crooks, unless they can establish they are not”.

Dr. Manmohan Singh: Former Prime Minister; eminent economist; former RBI governor has called demonetization an “organised loot”, a “legalised plunder” and a “monumental mismanagement”. He even said that the National income would fall by 2 per cent, which in his mind was “an underestimate”. **Those who’d bear the biggest brunt will be those in the agriculture sector and other informal sectors:** “the way the scheme has been implemented will hurt agricultural growth in our country, will hurt small industry, and will hurt all those people who are in the informal sectors of the economy. And that the national income, that is the GDP, can decline by about 2 percentage points as a result of what has been done. After all, 90 per cent of our people work in the informal sector, 55 per cent of our workers in agriculture are reeling in distress. The cooperative banking system, which serves large number of people in the rural areas, is non-functional and has been prevented from handling cash... all these measures suggests that the way this scheme has been implemented is a monumental management failure.”

Kaushik Basu: Leading economist; Senior Vice-President and Chief Economist at The World Bank Cannot wipe out black money; hoarders have already found loopholes: “Anyone seeking to convert more than Rs 250,000 must explain why they hold so much cash, or failing that, must pay a penalty”. This requirement has already spawned a “new black market to service people wishing to offload: Large amounts of illicit cash are broken into smaller blocks and deposited by teams of illegal couriers”.

Arun Shourie: Former economist at the World Bank; recipient of the Padma Bhushan and Union Minister said that “the owners of black money have intelligently converted all that money into tangible and intangible assets: “This is not a strike on black money, and the reason for that is that those who hold this black money or who have black assets, they don’t hold them in cash. One percent of Indians own 53 percent of the total assets in India. 10 percent own 85 percent. Now these are the rich fellows, who would be having an even larger

proportion of black money. They are not going to put money under the mattress! They are holding it abroad-and there also it's not dollars in gunny bags, it's property! Maybe jewellery, maybe other assets, maybe stock markets.”

Arun Jaitley: Current Finance Minister of India; Senior Advocate, Delhi High Court, Eventually, the government will be able to invest more money in agriculture and social sector: “A lot of money that operates in the shadow economy will now become a part of the banking structure itself. Banks will have a lot more money to support the economy. Private sector investment, which was so far lacking, will now get back into the economy. The banks which were struggling because of the NPA problem will have a lot more money to lend for agriculture, infrastructure sector, social sector, trade and industry.”

Arvind Virmani: Leading economist; Former India's representative at IMF; Former Chief Economic Adviser, GOI, “This is a useful method of flushing out black money, given that a large percentage of cash holding is in these two denominations. The manner in which it was implemented is not surprising – such actions are always secret till announced, so that insiders do not take advantage of the information at the cost of the outsiders”.

Surjit Bhalla: Chairman, Oxus Investments, a Delhi-based economic research/advisory firm; Former Professor at Delhi School of Economics opines that “most of the spending of this black money is for expenditures on gold, purchase of foreign exchange, and purchase of real estate. Transfer of money abroad into ‘anonymous’ accounts is now a difficult exercise for all the world's black money residents. Gold purchases and hoarding are also becoming more difficult. So, the prime outlet for big-time black money use is real estate”.

III - Pros and Cons of Demonetization in India

(i Pros of Demonetization

1. Corruption free India

The demonetization policy will help India to become corruption-free. Those indulging in taking bribe will refrain from corrupt practices as it will be hard for them to keep their unaccounted cash. Corruption will also be automatically reduced by eliminating black money from economy.

2. It helps to create Digital India

It is a giant step towards the dream of making a Digital India. It helps to ensure that government services are made available to citizens electronically by improved online infrastructure and by increasing internet connectivity or by making the country digitally empowered in the field of technology. With the increasing adoption of digital currency, it will create a treasure trove of data in every industry. This kind of approach in future will see startups and big companies alike take advantage of these technologies to re-invent and innovate.

3. It makes cashless society

The ultimate objective is to make India a cashless society. A cashless society describes an economic state whereby financial transactions are not conducted with money in the form of physical banknotes or coins, but rather through the transfer of digital information (usually an electronic representation of money) between the transacting parties. The proportion of hard cash in the economy will decrease and our economy will get more digitized which will result in greater transparency.

4. It curbs black money

This move will help the government to track the black money. This move will help the government to track the black money. Those individuals who have unaccounted cash are now

required to show income and submit PAN for any valid financial transactions. The government can get income tax return for the income on which tax has not been paid.

5. It controls escalating price raise

Implementation of demonetization immensely supports in controlling the escalation of price. By this the consumer can clearly get to know about the fair price of the product. It helps in better allocation of economic resources by the government.

6. It stops flowing of funds to illegal activity

Moving towards demonetization will stop the circulation of fake currency. Most of the fake currency put in circulation is of the high value notes and the banning of 500 and 1000 notes will eliminate the circulation of fake currency. Most Hawala transactions used to be carried out in the denominations of Rs. 500 and Rs. 1000. This led to fatal blow to the unethical Hawala traders at large.

7. It makes people accountable for every rupee & proper filing of income tax return

The demonetization policy will force people to pay income tax returns. Most of the people who have been hiding their income are now forced to come forward to declare their income and pay tax on the same. All the monetary transaction has to be through the banking methods and individuals have to be accountable for each penny they possess. Despite deposits up to Rs 2.5 lakh will not come under Income tax scrutiny, individuals are required to submit PAN for any deposit of above Rs 50,000 in cash. This will help the income tax department to track individuals with high denominations currency. This move will help the government to track the black money. Through this method, the government was able to mop up a huge amount of undeclared income.

8. Myriad number of opening bank accounts

Government had urged people to create bank accounts under Jan Dhan Yojana. They were asked to deposit all the money in their Jan Dhan accounts and do their future transaction through banking methods only. This move has generated interest among those people who had opened Jan Dhan accounts under the Prime Minister's Jan Dhan Yojana. They can now deposit their cash under this scheme and this money can be used for the developmental activity of the country.

(ii Cons of Demonetization

1. Inconvenience to society

The announcement of the demonization of the currency has caused huge inconvenience to the people. They are running to the banks to exchange, deposit or withdraw notes. The sudden announcement has made the situation become chaotic. Tempers are running high among the masses as there is a delay in the circulation of new currency. Many poor daily wage workers are left with no jobs and their daily income has stopped because employers are unable to pay their daily wage.

2. Mad Rush at the Banks

Banks will be extremely over-crowded by people. People will forget everything else and throng to the places where the banned notes are being officially exchanged leading to a tremendous chaos.

3. Short-term Inflation

Due to shortage of money in the market, short-term cost push inflation will occur. The price of gold has already become sky high. Prices of vegetables and fruits have also soared burdening the common man.

4. Difficulty to Government

The government is finding it hard to implement this policy. It has to bear the cost of printing of the new currency notes. It is also finding it difficult to put new currency into circulation. The 2000 rupees note is a burden on the people as no one likes to do transaction with such high value currency. Some critics think it will only help people to use black money more easily in future. Further, many people have clandestinely discarded the demonetized currency notes and this is a loss to the country's economy.

5. Loss of Tax Payers Money

Rs 500 printing costs Rs 2.5 and Rs.1000 costs Rs 3, (approx). Multiply it by number of notes present in India now. Government has to pay this money from taxpayers.

6. Powerful Politician are converting black into white easily

In many areas they are distributing/giving loan of amount few lacs to each farmer/labour and later they will take their money back as poor man can't fight to those powerful peoples.

IV – Suggestions

In order to absolutely get rid of black money within a country, it is necessary to apply a huge plan to get back the money which is stack in neighbour country. Internet connection should be improved in all parts of the country for effective cashless inflow and outflow for mobile and other type of e-banking. By maintaining both withdrawal and deposit facility in all ATM's may reduce inconvenience among the people. In the way of introducing time intervals for withdrawing money in all banks can able to make people much more cozy for the society. For instance in all branches women and aged people are allowed to withdraw the money from 10.00 a.m to 1.00 p.m whereas the men can withdraw from 1.00 p.m to 4.00 p.m. Every bank need to provide swipe machine also apart from cash counter for deposits and withdrawals on permanent basis. Stringent law and regulations to be formulated and practiced for targeting our country to

be corruption free nation. To bring our nation in developed countries list, adopting the demonetization practices is need of the hour. As more number of fraudulent practices invading in real estate sector, government authorities to be cautious in all forms of scrutiny in this regard.

V - Conclusion

Economists are busy in listing out many more merits and demerit of this policy. The government is saying that there are only advantages of demonetization policy and this will be seen in the long term. Former Prime Minister Manmohan Singh who is a noted economist, former RBI governor and former Finance Minister of the country, dubs the demonetization move as an 'organized loot and legalized plunder'. However, by comparing the merits verses demerits, it will be safe to conclude that the former outweighs the latter. Even though there is suffering and agony among the masses right at the moment but the forecast is that its benefits will be seen in the long run. The government is taking all the necessary steps and actions to meet the currency demand and soon the trial and tribulations of the people will be over with the smooth flow of the new currency.

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