

## **Demonetization is a Boon or Curse to the Nation? An Independent Thinking.**

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### **ABSTRACT**

Demonetization has been the biggest financial outbreak India saw in this decade. The sudden ban of 500 and 1000 rupee currency notes on November 8, 2016 shook the Indian economy and surprised its citizens. An abrupt monetary measure taken by the Government to curb black money and its aftermath has flashed in news headlines for days and weeks. But what actually is the big picture behind demonetization? Has it become a Government flaw? Or is there a shrewd reality India is going to see in the coming months? An independent thinking.

**Keywords:** Demonetization, currency, money, bank, cash.

### **INTRODUCTION**

#### **Why Demonetization?**

Demonetization is considered as a crucial step in clamping black money. A formidable tool to clean the entire economy. Precedently, India has witnessed demonetization of higher denominated currencies twice before in 1946 and 1978. In 2016, Prime Minister Narendra Modi's bold move was greeted with positive feedback all around the country. Let's see what his intentions were.

#### **Reasons for Demonetization:**

1. India is a cash-based economy according to RBI stats. The total physical cash transactions are 98% by volume and 65% by value. Maintaining a clear track record of these transactions is practically impossible. Hence there is a high probability of malpractices in money

circulation and usage. Demonetization is the only means to bring all this money to banks where RBI could get a clear picture of monetary records.

Volume and value of notes in circulation, March fiscal year-ends, 2014-16

Denomination	Volume ( in mn)			Value (Rs bn)			% shares in total volume			% shares in total value		
	2014	2015	2016	2014	2015	2016	2014	2015	2016	2014	2015	2016
Rs 2 and 5	11,698	11,672	11,626	46	46	45	15.1	14.0	12.9	0.4	0.3	0.3
Rs 10	26,648	30,304	32,015	266	303	320	34.5	36.3	35.5	2.1	2.1	1.9
Rs 20	4,285	4,350	4,924	86	87	98	5.5	5.2	5.5	0.7	0.6	0.6
Rs 50	3,448	3,487	3,890	172	174	194	4.5	4.2	4.3	1.3	1.2	1.2
Rs 100	14,765	15,026	15,778	1,476	1,503	1,578	19.1	18.0	17.5	11.5	10.5	9.6
Rs 500	11,405	13,128	15,707	5,702	6,564	7,854	14.7	15.7	17.4	44.4	45.9	47.8
Rs 1,000	5,081	5,612	6,326	5,081	5,612	6,326	6.6	6.7	7.0	39.6	39.3	38.5
<b>Total</b>	<b>77,330</b>	<b>83,579</b>	<b>90,266</b>	<b>12,829</b>	<b>14,289</b>	<b>16,415</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>

Source: RBI, Kotak Institutional Equities

- India has been a country prevalent with fake currency menace. The fake currencies are forged in higher denomination notes and used all over the country without being brought in to light. Preventing such a mishap could immensely reduce inflation hikes and corruption.
- Intelligence reports have pointed out that black money is being used for terror funding and illegal arms supply. Eliminating the prospects of black money from circulation can eventually put an end to years of terrorism in the country.
- Government reports portray generations of black money lying unused in locked secret rooms and houses of the super-rich. These stacked up currency bundles have not been put into circulation for decades. As a result, the general price hike, GDP growth, Stock markets, currency exchange rates are all being affected adversely.
- Income Tax Department of India eyed the amount of tax they could get as a result of people bringing old notes of unrevealed income to banks. Hence, from a revenue perspective it was a positive move for the Government as they could collect both tax and fines for unrevealed income.
- Lastly, the Modi Government also put their focus in building a cashless economy where everything goes digital. In such a scenario, people no longer require physical currencies, and daily transactions could be done through online or mobile banking and the like. This is the ideal economy as there would be no scope for black money, corruption, fake currencies or any such social evils.

Demonetization drastically impacted the day to day affairs of businesses, persons and the overall economy. People were stranded and cash-strapped. Long queues in front of ATMs and banks became the order of the day. Although the entire purpose was Legitimate, there are both negative and positive results.

#### **Impact of Demonetization on Banking Sector:**

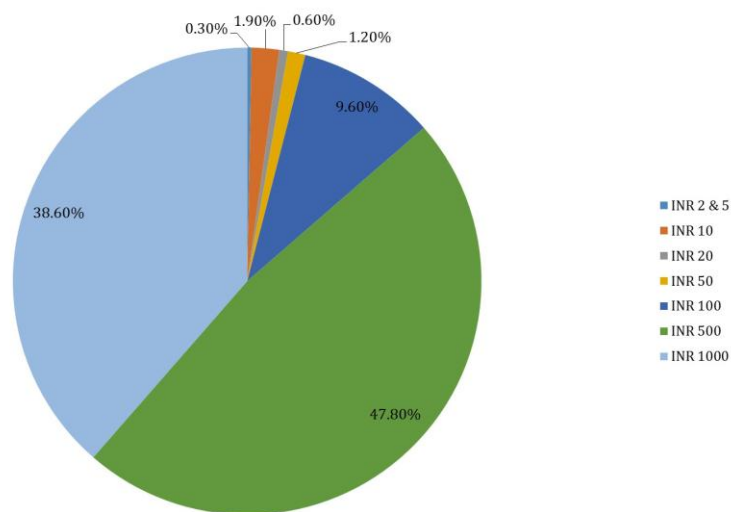
- As demonetization hit money stackers badly enough, people were forced to deposit money at banks. Banks were flooded with piles of currency notes just after demonetization. RBI

announced that banks have collected around three lakh crores more money through deposits. This was an immense relief to banks that faced liquidity issues and depended on RBI liquidity reserves to have enough cash to rise up. Hence demonetization has been positive in enhancing the banking sector.

2. It shouldn't be surprising that as more deposits flow into banks, the deposit rates naturally gets cut down. This is because banks could not provide deposit interest at the prevailing rates when there is no equivalent increase in lending credit. Therefore investment in banks is not a good viable option after demonetization.
3. Banks follow Marginal Cost of Funds based Lending Rate, (MCLR). This means loans would be available at lower interest rates when deposit rates drop. Add to that, the dropped inflation rates due to demonetization is another factor for RBI to consider cutting down loan rates.
4. Bank employees were made to work tirelessly and non-stop. For weeks, banks were flooded, many banks functioned for extra hours, security measures had been multiplied and chaos were filled everywhere when ATMs were out of cash.

### Impact of Demonetization on People and Society:

Percentage Share of Denominations in Circulation by Value in FY 2015-16

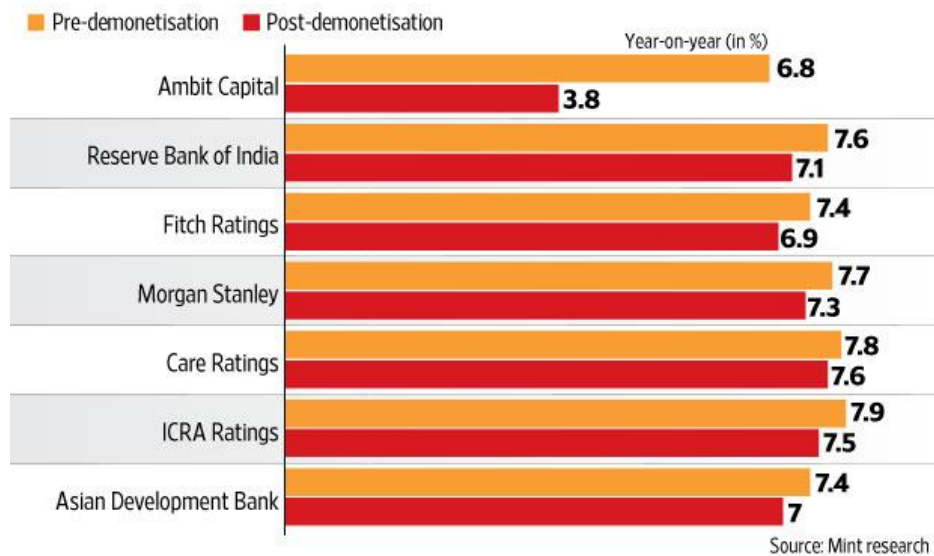


Source: The Reserve Bank of India

1. After PM's announcement of demonetization, ATMs were accompanied with long queues. People collected lower denomination notes as much as they could. The focus was on collecting money rather than spending. Hence money circulation was made stagnant just after demonetization.

2. The impact on people was highly negative. For days, daily wagers were jobless and those who carried cash in higher denominations suffered even more. They could transact only after standing for hours to get money exchanged.
3. Chaos even worsened when banks and ATMs went out of cash. For days, people were immobile. Shopping rates immensely plunged down, businesses had dull days, and everything came to a standstill.
4. People were forced to take leave for a day each week just for the sake of standing in queues as cash withdrawal was limited per person per week. This made them lose even part of their current salary. Some people even capitalized on it by exchanging money for someone else and getting commission in return.

### GDP GROWTH PROJECTIONS FOR INDIA IN FY17



#### Impact of Demonetization on Overall Indian Economy:

1. The Asian Development Bank (ADB) forecasts India's GDP growth to be cut down to 7% from a healthier 7.4% post demonetization. Industrial production, agricultural and livestock economy, foreign investment, foreign currency exchangers have all gone down.
2. Stock markets crashed up to 6% the day after the demonetization announcement. Real Estate business was in big loss due to the cash crunch. Many foreign corporates became disheartened to invest in India.
3. Modi's concept of cashless economy was successful to a certain extent. Digital shopping through card payments increased up to 400%. Online shopping businesses blossomed and brick and mortar shops faded. Part of the society has already shifted to a digital lifestyle.

4. PM's Pradhan Mantri Jan-Dhan Yojana Scheme collected huge deposits of around 65,000 crores. Around 88% accounts were opened in November alone as a result of demonetization. Banks received a real boost in terms of deposit collection.
5. Frequent raids conducted by tax authorities all over India have claimed and captivated around 3000 crores so far as black money. Legal fear has also made big corporate officials surrender illegal money.

As of now, one could only see the cons overthrowing the pros of demonetization. A deeper statistical analysis could even point out an economic collapse in the foreseeable future which even top economists have agreed upon. But once things come back to normal, everything will melt down to the real truth. Till that point, it is better not to decide upon the situation. Only time can prove whether Demonetization was a real boon to India in years to come or not. Let's hope for the best.

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