

Impact of demonetization on Indian economy

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Abstract:

Objectives: The impact for demonetization has been mentioned, illustrating how similar events have had an historical analogy. The experts estimate has been used to support reasonable arguments made in context of requirement of monetary policy change.

Methods/Statistical analysis: Demonetization is a monetary policy which functions to remove currency of higher denomination which is currently in circulation. Reasons for its execution are restricted to each government and the need of the people. Although in best interest of the country and stabilizing the economy, demonetization reaches to sectors both organized and unorganized.

Findings/Results:Its effects are socio-economic which results in the desired outcome planned before, while bringing the policy in effect. Measures by the Government of India to demonetize with effect from 8th November 2016 will redefine business and investment in India and will lead this country to where it really belongs, in a league of developing nations contributing to the development of the entire world. The outcomes post demonetization has been discussed and its future implications have been mentioned in this manuscript. The assumptions made while applying policy change regarding the creation of urge to learn and implement smart IT solutions have also been mentioned illuminating desire for technological growth in the country. The article also follows through both advantages and disadvantages of demonetization.

Applications: Monetary Policy change, establishing business in a new economic environment.

Keywords: Demonetization, Policy, business, economics, currency in circulation, black money, cashless economy.

1. Introduction:

This paper attempts to explain demonetization in effect in the Indian economy. It is the process of stripping a currency unit of its legal tender status. It is a necessary tool for National currency change wherein the old currency units are retired and replaced with new currency units, while Re-monetization is restored as legal tender.

There are multiple reasons for nations to demonetize their national currency units; some of the few reasons are to combat inflation, corruption and to encourage cashless system. The process of demonetization involves either introduction of new notes/coins of same currency or replacing the old currency notes /coins with the new currency. On November 8 2017 when PM Narendra Modi came out with his masterstroke on corruption counterfeit currency, terrorism, black money by announcing demonetization and stopping of Rs. 500 and Rs. 1000 notes as part of legal tender in India [1].

The reasons given by Indian Prime Minister for demonetization were:

1. To check black money
2. To take the country from the cash economy to less cash if not cashless
3. To eliminate fake currency, to check embezzlement in the form of fake currency and dodgy funds kept, misused by terrorists to spread and fund anti national activities in India [2].

2. Historical account:

Demonetization has been an economic transition mechanism that is now new to the Indian economy. Even in the past, there have been events where rulers in pre modern India had means to control currency in circulation using demonetization. It has been noted in the past that certain measures are not without consequences, but they have never been investigated in the light of right or wrong unless prior to their effect over the civilization. The first act of demonetization was taken by Muhammad bin Tughlaq in the 14th century. There was famine in his kingdom and he could not easily maintain the supply of gold and silver coins named dinars and adlis respectively. He introduced copper and brass coins that could be exchanged for fixed amounts of gold as well as silver. One of the most interesting

personalities of medieval India, Muhammad Bin Tughlaq ruled over the northern parts of the Indian subcontinent and the Deccan from 1324 to 1351 AD. A learned man with an open mind and a unique streak of intellectual creativity, Tughlaq was well versed in poetry, astronomy, religion and philosophy [3].

A ruler whose real expertise shone in the times of war, Tughlaq took some very bold and strong measures to reform the administration during his chequered reign as the Sultan of Delhi. In 1329 AD, he shifted his capital from Delhi to the more centrally located Devagiri in Maharashtra, which was renamed Daulatabad. He had many motives for doing so – other than saving his capital from recurring Mongol raids, the move would cement his control over the rich fertile lands of the Deccan and ensure access to the busy ports on the Gujarat and the Coromandel Coast. While there was nothing fundamentally wrong with a Tughlaq's pragmatic decision, his blunder lay in ordering the entire population of Delhi to move to the new capital (instead of just shifting his official court). Despite many arrangements that were made for the convenience of the travellers, the suffering of the people was terrible and many people died on the way.

However, no sooner had the Sultan reached Daulatabad when trouble broke out in Bengal as well as on the northwestern frontier. Tughlaq realized that while his new capital was distant enough to be safe from Mongol invasions, it was also too far away to protect northern India.

So, the mercurial ruler re-ordered his people to return to Delhi. Thousands died in the punishing 1500 km return march to Delhi. While Tughlaq did try to make amends by abolishing multiple taxes and organizing relief measures, the financial loss was immense and the consequences for Delhi grave.

Not only had the imperial city lost many of its people, it had also lost its former prosperity and grandeur. The widespread public resentment against the Sultan also led to revolts and bitterness that rankled the Sultanate for years to come. Though Tughlaq invited many scholars and artistes to settle in the city, the impact of this incident had far-reaching consequences; Ibn Batuta, the famous traveller who came to Delhi in 1334 (during Tughlaq's reign), wrote in his memoirs that he found certain parts of the city still deserted.

Muhammad Bin Tughlaq, ruled Delhi from 1324-51 AD, was known for taking very bold decisions. He was also clearly nick named "Man of Ideas", he shifted his capital from Delhi to Daulatabad for a much easier administration of the Deccan region of the country, a pretty wealthy province.

One of the most notable bold decisions taken by him was to demonetize Gold and Silver coins and to replace them with copper and brass coins.

According to Ziauddin Barani's Tarikh-i-Firuz Shahi, this hasty decision was fuelled by Tughlaq's ambition to conquer the world. To fuel his ambition, basically copper and brass coins were introduced as token currency, which would then replace the gold and silver coins used earlier. However, in his enthusiasm, Tughlaq forgot to retain the right to issue the currency with the State which wasn't appropriate. This made forging of the coins very easy. People learned in the art of forging turned their houses into "mints". The simplicity in the design made it pretty simple for fake coins to be forged. This led to the token coins becoming valueless. This led to hyperinflation. Local Kings and many village headmen became very rich at the cost of government. Coins issued by government lost its value as it became difficult to distinguish them from the fake ones. The damage was clearly done to the government.

The king as a final resort allowed for the exchange of the copper and brass coins with that of the gold and silver coins. Delhi was flooded with people waiting to exchange their copper coins and one could see piles of copper coins in the State treasury! He soon had to scrap the idea to bring order back into the currency system. Tughlaq's 'bold' decision ended as a failure. This has served as a guide for the future policy makers. In the year's 1946 and 1978 the Indian Government had demonetized notes learning from the past experiments of demonetization by Tughlaq. The cause for demonetization was to penalize Indian businessmen who were then believed to have been storing wealth from the masses which was needed to help allies during World War II. This has never been done by the Government of India to implement demonetization against Indian businessmen. In 1946 Government India Act of 1935 had given power to the cabinet parliament which was under British Raj. Till 1950 India was a dominion state and later on became the Republic of India. In another attempt by the government in the year 1978, the news about the demonetization spread like a wildfire thereby reducing the element of surprise, unlike the way it was done in the year 2016. Muhammad Bin Tughlaq could have implemented demonetization in a better way, but his hurry to realize his dreams punished his people. He took a very hasty decision rather than spending some time chalking out a plan. This move was simply an administrative disaster. He should have realized the difficulties that could have occurred during his bold move. But then his experiment was an utter failure causing widespread confusion. The historians refer to Tughlaq as the 'wise fool'. Another attempt of demonetization was done by Nadir Shah in the year 1735AD. He devalued his own currency, making a certain double paisa coin into a single paisa coin.

Ghana in the year 1982 demonetized their 50 Cedi currency notes in order to monitor money laundering and corruption. They too chucked this out of the system. Nigeria in the year 1984 demonetized their currency to curb the black money in the African country. 80% of the currency of Myanmar in the year 1987 was made illegal tender. This

move led to massive protests. North Korea demonetized its currency in the year 2010. This led to an economic breakdown and the people starved.

The citizens of the Soviet Union experienced a very difficult situation when its currency became too undervalued. People were seen carrying sacks full of currency notes to buy their groceries and other commodities. RBI being as a regulator of currency in India derives its functioning role from RBI Act of 1934, as per which they removed a series of Rs 500 bank notes that was in circulation from November 8th 2016 and added Rs 2000 into circulation. The act of demonetization is not new to the Indian economy, earlier it has been done in January 1946 and in January 1978 thereby by demonetizing Rs 10k notes which were printed by the RBI in 1938 and again in 1954 as per RBI data. This did not have an evident impact on the Indian Economy because less than 5% of the population and very few banks had access to such notes.

3. Impact on Indian economy:

This move will help boost the Digital India and Jan Dhan campaign, which in-turn will yield fruitful results in making direct benefit Schemes a success (wherein the Govt. will directly deposit scholarship, compensatory amount in the poor people's accounts). People will realize the importance of using technology, even for bank transactions. Smaller queues post demonetization will be the evident as more and more people would be educated in the digital payment methods.

The Government's attack on the black money compelled the black money holders to deposit their money into banks. The Government came up with a scheme for tax dodgers to deposit their money with the 50% taxation and 85% taxation if not. The rest of the money will be deposited in accounts of various welfare schemes under the Prime Minister.[4] It is a courageous reform that'll bring substantive benefits to such schemes. The taxable amount would be used for the welfare of the poor in the India [5].

Demonetization had many objectives amongst them one was dislodging black money out of circulation. Although this does not appear to be a problem for middle range real state pricing, which are mostly affordable residential properties in various cities. Residential properties that deliver value for money, those that have always been part of important and critical financial transactions in the economy are beyond the range of the real estate property that can get affected. Values of high-end (market price of INR 2 crore, and above) residential properties in non-metro cities and nearby towns are likely to get affected due to the unorganized exchange of cash and mostly all the transactions are relied on cash. Sufficing to say that as long as transactions are done in transparently, property values would not be affected, and primary sales of such residential properties will definitely not be upset. Focus on recovering action kept people involve and avoided the stress arising from situation to develop [6] [7].

The real estate usually had large transactions that remained in darkness and out of circulations, the demonetization will channel the necessary and required amount to desired sectors and proper tax and policy follow up will ensure that economy is functioning for the citizens by the government in the right direction. The sudden change in monetary policy and recent adaptations to daily changes has left the citizens experiencing variations in market but it will come to rest and all prices will get restored as we go forward with right usage of these recent changes that have been made. Government has led the real estate where early signs look recoverable but hold potential of the market that was hidden will get untapped as now citizens will freely involve with using the right means to purchase any residential or farming complex. The investment by the people of the country will inculcate growth and it will be sooner or later reflected in our GDP and will be evident from the recovery of the real estate sector in metropolitan cities as well as nearby towns and villages.

As per the articles that came in soon after the demonetization such as Bloomberg predicted a decline estimated for the FY2017 and FY2018 earnings per share (EPS) at Rs. 1420 and Rs.1729, According to Bloomberg it was at Rs.1435 and Rs.440.15. Bloomberg report came in December 2016 that relied on estimates, the recent article by Bloomberg on demonetization was published on 11 January 2017 showed that the estimates were not as bad as feared. Now current data indicate a growing economy and signs of recovery. Kotak expects a 23% net income growth.[8] Which is another indication of growth. The early belief that was given by estimates were broken down as the data what presents with the current change in the system reflects that effect is not as bad as feared. The recent change depicts that estimates that were predicted in December post demonetization are now broken as the current real time data does not behave as per the estimate [9].

The demonetization is taking India forward and the impact is clearly positive. The outcome shows that there is only positive increment that lies ahead and by analyzing several data shows the evidence of the current direction of decisions taken on 8 November have turned out in the right turn of events. The demonetization aftermath was imagined to be a very unstable and highly volatile market, but it didn't proved to be that way, although there were

lows and decrements which led to an integral factor while estimating that effects in the following economic quarter of FY2017 could turn out pretty bad, but just after there were a certain drop in percentage rates there was steady and positive increment this reflects that estimates were wrong.[10]

As per the live mint article in the newspaper's it quoted several instances through which aspects that involved any form of doubt were eliminated and there was a much clearer picture .The quoted text are from the live mint report and other such articles which provide deep and exact information about effects of demonetization and they can be viewed in the light of such events where it is clearly evident that demonetization played out correctly and worked its way cleansing the problems associated with the Indian and economy and disappearing as its effects do not remain constant and are not part of the upcoming business domestic or international activity [11].

ICICI Securities Limited predicts the revenue of the SENSEX firms to grow 2.1% year on year, while the net profit is expected to grow 12% [8]. As Sensex seeks to grow with the above stated information the amount of investment that can come and attract investor's increases, a growing market reflects healthy investment which shows the capability to manage risk. Investments done for the FY17 and FY18 the EPS estimates were Rs.453 and Rs.540 respectively. This estimate came in January of the year 2017 and early predictions had an element of uncertainty "Nifty firms according to Edelweiss could expect a growth in revenue and net profit growth of 8% year to year and 18% year on year respectively. The estimates for the FY17 and FY18 are Rs.453 and Rs.540 respectively.

The impact of demonetization will be on a lot of consumption companies. Another company Emkay Global Financial Services said it expects a 0.6-2.7% quarter on quarter growth amongst big MNC's like HCL Technologies Ltd.

The earnings of 55 of 94 firms were much better than expected. [8] Mint investigation reports effects not as bad as it was feared to be .The financial results for the 3 months ended 31st December for around 58% firms exceed the estimates [8]. MINT had analyzed 94 of the BSE 500 companies the estimates show that 55 have reported earnings that were much better than estimates. Ultratech cement Ltd. reported December quarter profits rose to 51.3% since one year, which were pretty good estimates.

BioCon Ltd profits rose to 65% to Rs.171.3 crore The profit for ITC Ltd grew to 5.7%the sales and profit for {According to the analysis of 243 BSE companies} rose 0.59% and 7.76% respectively. There will be a direct boost to the Industrial Growth as the labor will get cheaper, the land will become cheaper. This has a proportional impact on the GDP of the country which will rise. Demonetization is an Investor Friendly move.

Arundhati Bhattacharya (Chairwoman of SBI) recently told CNBC managing Asia that most things have turned back to normal [12]. The odds have been managed within the time span of January to March. A Research report by Moody's says that the impact of demonetization will yield positive results [13].

4. Advantages:

One of the biggest advantages of this move would be to check the practices of the corrupt. It has also put gold manipulations to a halt. People possessing black money in the form of cash won't be able to exchange that freely because of the fear of getting exposed, penalized and prosecuted by the authorities. The enemies of India were in the practice of circulating fake currency that would terribly damage our own economic cycle.

The boost for a cashless economy will help the government track transactions and will be able to catch the defaulters who do not pay taxes. This will lead to much better transparency in the cash flow. Terrorist organizations were funded by cash. Cleansing of the banking system in India where in maximization of white money, minimization of black money were being facilitated by promotion of " cashless society " wherein individual would be held accountable for every new single paisa spent by him.

Hence, government would have more clearer picture regarding white money possession of an individual which would be kept in bank, which in turn could be put on loan and interest can be earned from it, which in turn would result in fall of interest rates and which will make path for deflation (fall in inflation) .

In the form of new legal money (base money) banking system will get a boost. The new legalities will uplift the banking system in India, however it needs to be seen how much money remains with the bank, once the cash withdrawal limits are eased.

As soft money is safer than hard money the risk and cost of cash handling would be considerably reduced, which in turn will reduce government liability as old currency will become a piece of paper for those individuals who opt not to disclose their income hence this will remove, government's liability [14]. It's expected that approx. Rs. 5 lakh crore may come to government extinguished RBI Liabilities, taxes and penalties. This is enough to take care of the entire fiscal deficit of India for one or more years. It will also result in friction of cash avoidance by authorities hence those people will be extra conscious during this period of demonetization.

Especially sectors like real state and jewelry and others entering into loan transactions may also undergo tax scrutiny by IT department. This will result in the search and seizure activities. This will also increase search activities to curb such malpractices.

Importantly, in the longer run tax and interest rates on loans are expected to decrease because of higher income tax collection arising from better compliance. In comparison to current, future taxation level would be much higher, which could enable the Government of India to impose taxes at reasonable rates. Which in turn will boost up disposable income which might leave a positive impact on consumption demand in the long run. Demonetization has severely affected the consumption of Cigarettes, in the India.

Most of the smokers prefer buying loose cigarettes rather than the entire pack. And almost all of these transactions are in cash. One of the main reasons for this is the shortage of the change. The vendors find it difficult to provide customers with change as stated by various leading newspaper [15].

The cigarette distributors have estimated the consumption to have gone down by around 40% [19].

Times of India interviewed a kiosk owner Kishan Kumar. He said, "In the first four days after the demonetization was announced, I did not sell a single cigarette. Gradually, sales picked up, but it is still nowhere close to what it was before November 8. My estimate is that the sale of cigarettes has gone down by at least 40%."

Rohan another kiosk owner said, "The sudden announcement has slashed cigarette sales at my stall by almost half. Even big manufacturers are not selling to us on credit basis. So, it is very difficult to extend credit facility to customers. This is a major reason for sales dipping".

Cash facilitates crime because it is anonymous and big bills are easy to carry. So going less-cash is a fine balance between maintaining ease of financial transactions and curbing malpractices. Besides, the new Rs.2,000 bills have been designed with enhanced security features, so this is not just new money replacing old money in the system.

5. Disadvantages:

Reduced liquidity(cash) might lead to a negative impact on sectors involving high level of cash transaction. Sectors like jewelry, real estates, hotels, restaurants, logistics, luxury brands, FMGs. Some in retail, supplier markets might face shortage in lending money. Company with high level of debt might face more heat and could face loan defaults. Furthermore the wall between Government and RBI must not be breached [16].

Demonetization could pull own initial GDP growth [17]. It is a serious attempt in the ongoing process of achieving the goal on "Achhe Din" under the Narendra Modi Regime. People are terming this as a surgical strike on Black Money. Despite initial shortcomings, this will act as a shot in the arm of the black money holders in the country. In this serious attempt of cleansing the country we stand united as one backing the bold decision of PM Narendra Modi.

6. Benefits of cashless society:

Cashless societies are, generally corruption free. There are lots of benefits for being cashless (doesn't mean being poor). Cost of handling cash is high, it is in the favor of economies to go cashless. There would be increased cost of replacing the currency operation of banking systems like frequent refilling of ATMs and the overburdening of banking staffs in assuaging this impact. It is almost next to impossible to create India a cashless economy as more than 50% of the Indian population is not familiar with various forms of Soft Transactions.

Hence it is a cumbersome task to educate such a huge amount of population to the technology regarding cashless transactions in such a short period of time. Lately the government is seen taking various steps in improving liquidity in the systems by promoting cashless transactions through incentives. The government now values if a citizen makes efforts to be a part of the cashless society by giving special discounts.

Another concern among all individuals and citizen regarding technological capacity to suffice cashless needs must also be addressed considering current events that have caused severe inability in terms of access not just of goods and services but also sharing wealth in the form of physical currency, there are more than likely chances of accelerating the acquisition of knowledge for the use of cashless transactions.

The transition demands new skills which have been developing as a result of our coherence with fourth modern Industrial Revolution. The use of protected, encrypted devices and software held privately by individuals which will serve as payment devices is the step to cashless economy. The primary function which will take place firstly, is a huge awareness for technology that is applied in making payments. Such as Paytm, E-banking and other such modes of mobile payments. The difference which will take place is sudden increase in users and doing it outside the confines of their homes and offices.

Not only the process of being aware about cashless payments would make masses, technology friendly, it will also make them risk averse. We know the benefits of being risk averse is a combinations all kinds of health and social benefits.

Chances of thefts would also be eliminated, which will result in movement of masses within the remote urban infrastructure which will unlock the held potential in the local markets as they might have been prone to illegal activities. The advancements in computer vision and neural network has made mass based use of services of any kind without the need of cash. The challenge for rural India remains.

The recent Amazon Go stores are using AI (Artificial intelligence) to identify customer and deduct cost of the product taken by the customer wirelessly [18]. They identify the customer via computer vision and which is interfaced with server record of inventory and associated dynamics that work in loops to evaluate customer purchase by acquiring the meaning of his gesture and respond with required intelligence to process payment involved in the purchase. The customer walks in the store, picks what is needed and walks out. The concept introduced by Amazon Go will be effective in markets in the coming months.

But this is one of many initiatives that will pull the citizen from the cycles of useless effort required to support living and perform daily routine actions. The citizens can now benefit from the time and effort saved given their remains more secure and easily accessible.

After the bold move by prime minister Modi crime rates has fallen from sky to deep inside the sea. Union defense minister of India claimed that after demonetization the crime rates in Mumbai reduced to half. Crimes with a financial motive have dipped sharply in Delhi since the government pulled out high-value banknotes, police data show.

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.

The number of robberies, burglaries, extortions and vehicle thefts has fallen in the week beginning November. Cases of drug abuse and peddling have come down to nil while gambling cases have halved. People are carrying less money, so the vulnerability of victims in snatching or robbery is less. Security of e-wallets has increased and use of e-wallets have also increased [19].

7. Conclusion:

Cashless drive reshaping Indian Economy to become technologically friendly and will help to achieve greater heights in matter of civilization on a global level. It is not only a unique event in the history of the world, it's a process redesigning business, relations and social aspect which binds the functioning of any human using currency in circulation. The qualitative view of the article is inclined towards developing the implications of monetary policy change. The advantages discussed and disadvantages that were prevalent are based on assumptions that monetary policy change is required for IT driven economy where cashless transactions could become a major driver for any monetary exchange, which is monitored and secure. Absence of such characteristics from our economy in the past has made the country experience vulnerability and poor immunity from misuse and abuse of legal norms laid in the citizen's benefit. The impact mentioned derives its backing from the historical action following demonetization in those times.

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The Publication fee is defrayed by Indian Society for Education and Environment (www.iseeadyar.org)

Cite this article as:

Siddharth Choudhary, Ashish Jacob, Ayush Trivedi, D.K. Singh. Impact of demonetization on Indian economy. *Indian Journal of Economics and Development*. Vol 5 (4), April 2017.