

## **DEMONETIZATION: IMPACT ON INDIAN ECONOMY**

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### **ABSTRACT:**

Demonetization for us implies that Reserve Bank of India has pulled back the old Rs 500 and Rs 1000 notes as an official method of payment. Demonetization is the demonstration of stripping a currency unit of its status as lawful tender. In an important move, the Government of India announced that the five hundred and one thousand rupee notes will never again be lawful tender from midnight, eighth November 2016. The RBI will issue Two thousand rupee notes and new notes of Five hundred rupees which will be set available for use from tenth November 2016. Notes of one hundred, fifty, twenty, ten, five, two and one rupee will remain legal tender and will stay unaffected by this decision. This measure has been taken by the PM trying to address the purpose against debasement, black money and counterfeit notes. This move is required to wash down the formal economic system and dispose of black money from the same. Its reasons are as under: This article has made an endeavor to evaluate how the device of Demonetization can be utilized to annihilate parallel economy. Demonetization is one of the enormous advances started by Government in tending to the different issues like black money, fake currency, corruption, fear mongering and so forth then again on the off chance that we discuss the Indian industry on a more extensive way it can be classes in three parts Manufacturing sector, Service sector and Agriculture sector. After demonetization just Agriculture sector demonstrates some positive change while on the off chance that we discuss the manufacturing and service sector both were smashed down and these will influence the entire Indian market in 2017 moreover.

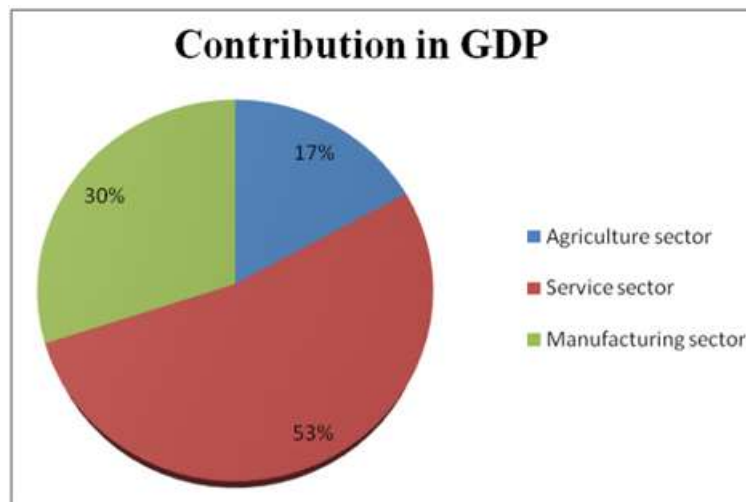
**KEYWORDS:** Demonetization, Indian economy, Black money, Government of India, Manufacturing sector, Agriculture sector, Tax evasion, Swiss bank.

**INTRODUCTION:**In popular parlance, the informal economy goes by the name of black money and the authority of white money. Black and white are likewise differently substituted by number two and number one, unaccounted and accounted, unreported and revealed, unrecorded and recorded et cetera... It is stripping a currency unit of its status as legal tender. Demonetization is the old unit of currency must be resigned and supplanted with a new currency unit". Money is the backbone of every economy. With the growth of development and humankind, the necessities of human beings expanded. With a specific end goal to fulfill humans boundless needs bargain framework rose. In any case, over some undefined time frame, the creation of money turned into a solid column to construct an economy. Money exchange has all the earmarks of being more helpful than bargain since it hinders the "twofold fortuitous event of needs" and is equipped for maintaining generally complex economy. Money exchange encourages simplicity of doing business, facilitates tax assessment and national joining. All exercises, for example, creation, exchange, distribution, services etc. shape an economy. It is called formal economy. An informal economy is neither economic activity/activities that is neither saddled nor monitored by Government, diverged from a formal economy. Nearness of debasement, black money, fake currency, poor governances, advances and builds up parallel economy.

With impact from eighth Nov. 2016 Tuesday Midnight PM Shri Narendra Modi Ji Banned the Currency notes of 500 and 1000. It is a strict choice of prohibiting customary 500 and 1000 rupee notes from flow which is a result of finding 1.25 lakh crore black money. As per the RBI's (Reserve Bank of India) Annual Report for April 2015 to March 2016, the estimation of the currency notes toward the finish of March 2016 was 16.42 trillion Indian rupees. The 500 rupee and 1,000 rupee currency notes shaped 86.4% of the esteem. In one stroke, the legislature evacuated 86.4% of the currency available for use by esteem. As far as volume, the currency notes of these two denominations framed 24.4% of an aggregate 90.27 billion pieces. Likewise, RBI information demonstrated that as of March 2016, 632,926 currency notes were fake—known as a FICN (Fake Indian Currency Note). As an extent of NIC (Notes in Circulation), the 1,000 rupee and 500 rupee notes were the most astounding. Invalidating these FICNs was additionally part of the demonetization move. Presently we discuss the effect of Demonetization on Indian Economy Sector. First economy can be bifurcated in three wide portions Agriculture Sector, Manufacturing

Sector and Service sector all these three sectors contributed in Indian GDP.

- Agriculture Sector Contribute 17% in GDP
- Manufacturing Sector Contribute 30% in GDP
- Service Sector Contribute 53% in GDP
- After Demonetization all the three sectors faces negative impacts



**REVIEW OF LITERATURE:** Demonetization is not new to India or to the outside world. Various Governments crosswise over the world have chosen to boycott currency note available for use, rendering huge amount of cash useless overnights, because of plenty of reasons. These incorporate battling forging, halting dread exercises, doing combating black money and so forth. Many countries have received this process of demonetization to beat hyperinflation, to control black money, to bring economic stability, to expel fake currencies. Truly outstanding and late cases of demonetization is that of appropriation of Eurocurrency among the nations of European Union so as to change to the Euro currency, authorities first fixed exchange rates for the shifted national monetary standards into Euros. At the point when the Euro was presented, the old national currencies were demonetized. However, old currencies remained convertible into Euros for some time so a smooth change through demonetization would be guaranteed.

The dictionary meaning of DEMONETIZE is "To deprive (a metal) of its capacity as a monetary standard" or "To pull back from utilize as currency" So, demonetization is the demonstration of stripping a currency unit of its status as legal tender. It is the demonstration or procedure of

evacuating the legal status of currency unit. A currency on which Governor of RBI for the benefit of Central Government ensures by making explanation "I guarantees to pay the carrier, the entirety of cash ... " which enables it a lawful status. From the date of demonetization, all old currencies which are demonetized will stop to be a lawful delicate. Such currency cannot be utilized as money to do any exchange hereafter, however to supplant with a newcurrency.

**Reasons of Demonetization:** As per my study Following is the main reasons behind Demonetization.

**Black Money:-** A recent study had pegged India's black market economy at over Rs 30 lakh crore or about 20 % of total GDP. This is even bigger than the GDP of countries like Thailand and Argentina. So now after this Decision black money holders are left with just two options – either route this money through banks, declaring it to be their income or burn the stashed file.

**Fake Currency & Terrorism:** -Terrorism is a frightening thing. But have you ever thought about how these terrorists get their money? Enemies from across the border have run their operations using fake currency notes. This has been going on for years.¶

**Economy:** - The Major impact of this decision is on the economy because it gives highly positive impact on the economic Stability in near future. The coming six to seven months are expected to witness a considerable level of deflation. Sectors like real estate, construction material, Gold, unorganized trade and services will see significant pain in the near time.

**Election:** - We all know how much black money is used by political parties. It will be a very tough task to use trucks of money at least for the upcoming five state elections. Now in upcoming UP election which was held in January neither of the parties can purchase the vote of poor people and Some drastic change in the elections going to be seen by everyone.

**Unorganized Trading:-**

- 1.) Prices hike in Real estate sectors is mainly because of the involvement of black money, but after taking this decision the prices of property will surely come down to their real value.
- 2.) Unorganized dealing in share market will also be eliminated after this decision and this will gain positive result in the economic condition of the country.
- 3.) The problem of inflation will get solved with this step as the government will get more money in its pocket in form of taxes and undisclosed income.

4.) Banking system will also get strengthened as banks will be flooded with huge amount of money. This will also result in more economic development in the nation as the money will be channelized properly through banks.

**Less Cash Economy:** - It is not possible to make India Cash-Less economy, but for the development and making transparency in the economy we can say use of less Cash is possible. So for making people familiar with E-Payment and use of plastic currency.

**Principles of Tackling Black Money:** The first principle is that remove the systemic pain that leads to creation of black money in the first place. Blame lies with the tax department. Black money is nothing but money generated in legitimate transactions which are hidden from government so as to avoid paying the transaction cost (usually tax) in the legitimate economy his is usually done by using physical cash. This cash thereafter must be processed to convert into consumption or investment. Black economy refers to various activities, transactions etc. that help process this physical cash, create returns on this cash, facilitate consumption using this cash etc.

The second principle has two parts. First, not all cash transactions are necessarily black money transaction. They become black money transactions only if they are hidden from the legitimate economy. Thus, a shopkeeper who does not give receipt but declares the sale (it's only hypothetical) does not create black money. Conversely, a shopkeeper who gives a receipt but discloses other receipt book to the tax authorities (happens all the time) creates black money transaction. Second, the black money must at some time or other be plugged into legitimate economy. Thus, it cannot be done using user created currency that cannot be exchanged with local currency. So it depends on legal tender. It means somewhere down the chain there must exist a person for whom part of this black money is legal cash income which he can use for his own consumption in legitimate channels. Usually, this is the construction worker, or other poorest of the poor who will give certain services and his income will remain under the government radar. It can also be illegal traders in gold or diamonds etc. who can convert this into precious items that have quasi legal tender status.

The third insight is that black economy is continuously fed by parts of white economy that go underground. Quite a few people who do not want to promote black money contribute to it. They are either coerced say developer forcing buyer to pay him in cash or government officer seeking

bribes in cash. Therefore, preventing white money from becoming black the starting point. The recommendations of Report titled Measures to tackle Black Money in India and Black economy depends on black money financiers. These are money lenders earning like 2% per month on their investments for financing the activities in black money friendly sectors. Film financing, construction financing, retailers, dance bars, alcohol, etc. These financiers also need enforcement mechanism to ensure their money is safe. Naturally they ally with criminal elements. Al Capone, the famous Chicago mobster, was previously an enforcer but later a financier.

**Other Black Money Creators:** There are other critical elements in black money chain or black economy. These elements represent turning smaller amount of white money into black by aggregation and misrepresentation. For example, take NGOs. Some of the NGOs existing only on paper. Their model is thus. These NGOs collect legitimate amounts from citizens and push it into causes like animal shelters, girl child, medical aid to needy etc. The main problem is that the costs of these NGOs is unreasonably high. They also commit fraud by misrepresenting number of animals and kind of facilities etc. creating a source of black money for the promoters who get salary and or benefits like cars and drivers from the NGOs. Cooperative banks are another piece of the puzzle. These accept smaller deposits from individuals and loan to founders and directors. The process is illegal and escapes the law only because it is not regulated by the RBI but by Politicians who are themselves directors in such institutes.

Government aided/recognized schools, colleges and institutions which look innocuous and have no actual teachers, students or infrastructure but simply using approvals from complicit education officers create a chain wherein legitimate money turns into black money. Others institutes have proper systems but use management quota to pool students' money into black money pools for the founders. Some use both mechanisms. Such entities are inherently different from SMEs which exist to service the needs of a wealthy black money holder or create black money through banks. These elements will be hit substantially by the demonetization and their promoters will be forced to declare these amounts or destroy them. However, the issue is that they can continue to create black money sources since their model has not been dismantled.

**Impact of Demonetization on Agriculture Sector:-** Agricultural growth in India contracted 0.2% in 2014-15 and grew no more than 1.2% in 2015-16, largely because of back-to-back droughts. It

was expected to grow at 4% in this year as per CRISIL Report, but due to Demonetization this forecast is proven wrong because Farmers are running out of Cash to buy Seeds, Fertilizer, Equipments, and Wages payment to workers and Commission to Agents etc. Because of Cash shortage daily supply transport system has also suffered which was result in 25 to 50 % reduction in sales. Following is the main reasons;

**I.** Farmers are not educated and aware about how to work on E-Payment System, Recent study by RBI Says 78% of the population do not use internet in which almost 80 to 85 % are Farmers.

**II.** In most of the Villages Proper Banking system is not Developed yet and Villagers are need to go to the cities for the same because of that Farmer's most of the time is engaged in exchanging the old notes in Banks.

**Impact of Demonetization on Business sector:-** As per the study IPP says Growth in Business sector 0.7% in October 2016 but after 8th Nov.2016 Demonetization shows a different picture because of this decision labour turnover is also increased as lack of Production because of low demand of products people were purchase only if it necessarily required, for this I have studied on following business sector

**I. Textile industry :-**Most of the Brands and Retailers Report 40 to 60 % drop in sales after Demonetization in first few weeks but from December onwards this drop is slightly decrease, but still we can say the impact of this decision has affect the industry in 2017 also for at least 3 to 4 months.

**II. Real Estate: -** Demonetization smashed the real estate market and it will result in 50% drop down and it will remain for further 5 to 6 months. While the short-term impact is negative, Experts hoping that rate cuts in the coming months would boost home sales.

**III. FMCG Products:-** Consumer expenditures also affected by that decision now only those products are purchased which was necessary for daily consumption and mostly the small traders like '\_kirana store', '\_small bodies', '\_thelawala' etc. they all have done their daily transactions only in cash and because consumer has less cash in his pockets the daily sells of these traders drop down by 20 to 30 %.

**Impact of Demonetization on Service Sector:-** Service sector is hit very hard by Demonetization decision in November 2016 worst Slump in nearly three year is noted. The Nikkei India Services

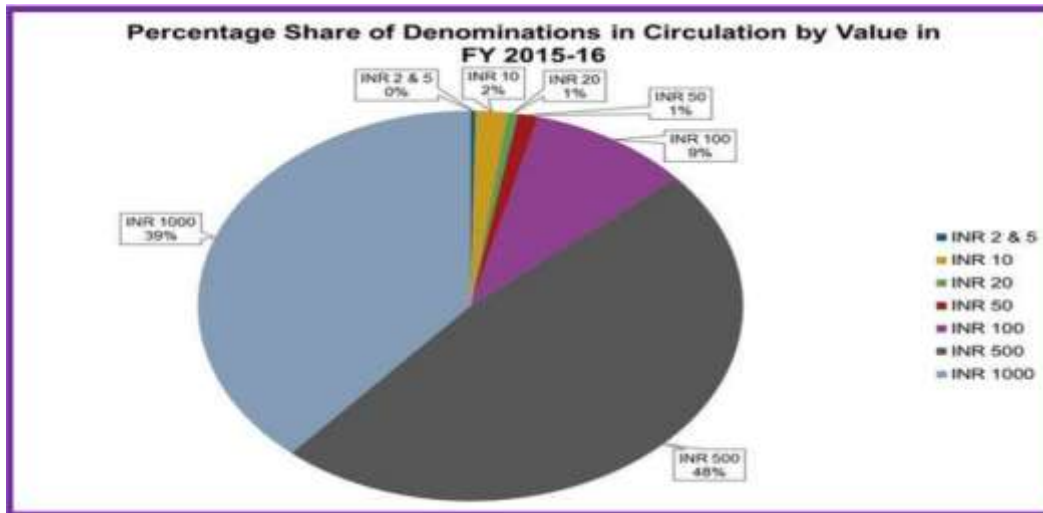
Purchasing Managers' Index (PMI), which tracks services sector companies on a monthly basis, stood at 46.7 in November, down from 54.5 in October. The Index slipped into contraction territory for the first time since June 2015 and pointed to the sharpest reduction in output for almost three years. On other hand if we talk about Banking Sector this is the only sector which was benefited by that decision in many aspects, this move will pull a large chunk of first time users to banks, who will have to use the system at least once to exchange their old notes for new ones. According to a study conducted by Moody's, people tend to continue using banking services once they have crossed the 'first-time user' mark. This development will increase bank deposits by 1 to 2 percent compared to what they were before the demonetization scheme.

**Semantics of the current Demonetisation:** Demonetisation is the mechanism by which the government states to withdraw the money which is current legal tender. The government being sovereign can take such decision. The effect of this announcement is that the currency notes in circulation will now cease to be valid tender and can only be exchanged at the banks. Demonetisation of higher denomination notes as an idea has been around. There are two important issues with respect to the present demonetization. Government aided/recognized schools, colleges and institutions which look innocuous and have no actual teachers, students or infrastructure but simply using approvals from complicit education officers create a chain wherein legitimate money turns into black money. Others institutes have proper systems but use management quota to pool students' money into black money pools for the founders. Some use both mechanisms. Such entities are inherently different from SMEs which exist to service the needs of a wealthy black money holder or create black money through banks. These elements will be hit substantially by the demonetization and their promoters will be forced to declare these amounts or destroy them. However, the issue is that they can continue to create black money sources since their model has not been dismantled.

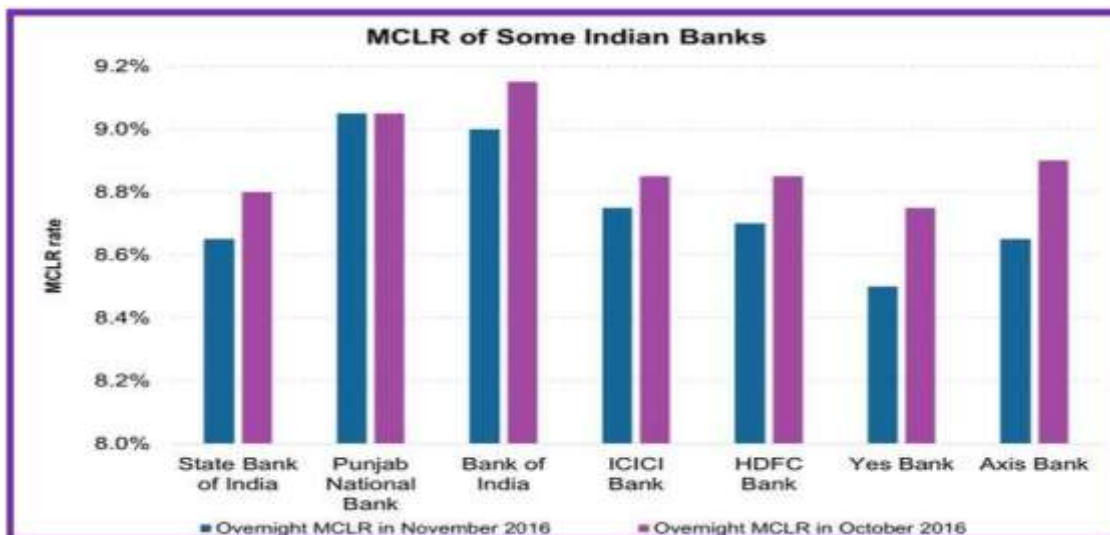
**Impact of demonetization on Indian economy:** The demonetization somehow reduced consumption activity in economy of India. But it increased the money in banks. At the time of demonetization the consumption had reduced and the market become slowdown, but the increase in the deposition in the bank would be better for economy in future. After demonetization announcement deposition in Indian bank has increased, According to reserve bank India, deposits



crossed 5 trillion rupees from 10th November to 18th November. Due to this many banks like SBI, ICICI, and HDFC PNB reduced their deposits rates.

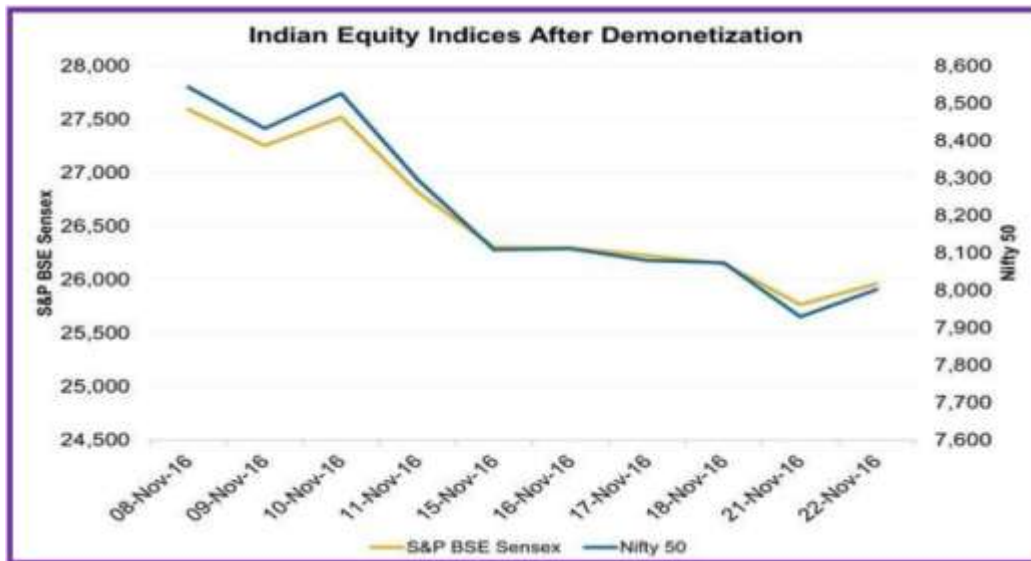


Impact of demonetization on Indian economy



MCLR means (Marginal Cost of Landing Rates)

**Impact of demonetization on Indian financial market:**After demonetization Indian financial market has been followed just like secular falling trend. Nifty 50 fell approx. 6.3% and S&P BSE Sensex Fell 5.9% from 8 November to 22 November.



**CONCLUSION:**The present study shows the impact of Demonetization on Indian economy's different sectors. GDP of Country slightly decreases as compare with the previous year but we cannot say it will be same in future also. —This intervention is a one-time draining of this current stock of black money but unless the root causes of corruption are removed, corruption will continue. It is sort of like a dialysis, more of a short term cleaning up than a solution of the problem. Central government's recent decision to demonetize the high value currency is one of the major steps towards the eradication of black money in India. 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. 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. And anybody knows if the bank has more deposits then bank become stronger. The country in which bank is strong then that county is more financially strong. In future banks will able to do more and more loans to the individual and to the industrial sectors sot that production will grow in our country, employment will be generate, and our country can develop at very fast rate. But this is only future perfections; upcoming few months will show the actual economic condition of our country.

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