

DEMONETISATION AND ITS EFFECT ON INDIAN ECONOMY

Amandeep Kaur

Assistant Professor

Department of Economics

Guru Nanak Khalsa College

Yamuna Nagar

Haryana

On 8th November 2016, the government of India announced the demonitisation of all Rs.500 and 1000 bank notes of Mahatma Gandhi series. In his announcement Prime Minister Mr. Narendra Modi declared that use of all the Rupees 500 and 1000 banknotes would be invalid past mid night and announced the issuance of Rs.500 & 2000 Bank Notes of New Series in exchange for the old Bank Notes. The BSE Sensex & Nifty 50 stock indices fell over 6% on the day after announcement. Due to Demonetisation, country faced severe cash shortages with severe detrimental effects across the economy. Where people have to stand in long queues for exchange of notes and several deaths were linked owing to the rush to exchange the currency. The most worst effect was on the growth rate of the economy which fell from 8.1% (2015-16) to 7.1% (2016-17).The present paper throws light on the worst effects of demonetisation done by Indian govt.

On 8th November 2016 at 8:15 p.m., Prime Minister of India, Mr. Narendra Modi in his unscheduled television address to the nation announced that the Currency Notes of Rupees 500 and 1000 denomination will not be a legal tender money from the same mid-night. Prime Minister told in his address that his government was taking this step of demonetizing the currency as a tool to fight against black money & corruption in the Indian Economy.

WHAT IS DEMONETISATION?

- Demonetization is the act of stripping a currency unit of its status as legal tender. It occurs whenever there is a change of National Currency. The current form or form of money is pulled out from circulation and retrieved to the National Treasury, often to be replaced with new currency notes or coins. Sometimes, a country completely replaces the old currency with new currency.
- In India , Rupees 500 & 1000 notes were completely withdrawn from the economy. It was replaced by new notes of 500 and 2000.
- SOURCE:www.investopedia.com
- In India 1st time Demonitisation was done in 1946 and after Independence, it was done in 1978 as well. Now, it is the 3rd time when Demonitisation is done. People were allowed to exchange their old currency notes with the new ones from ATM's and banks for a period of 60 Days.

- SOURCE: Indian Express

Demonitization in India

- It was January 1946, when notes of Rupees 500, 1000 and 10000 were demonitised. The old notes were being sold at 60 & 70 % of their actual Legal Price. The move was termed as a death blow to Black marketers. A rumour also went viral that Rupees 100 Notes were also being demonitised, leading to a panic and out of fear people discarded their Rupee 100 notes as well.
- In January 1978 notes of Rupee 1000, 5000 & 10000 were again demonitised to curb black money transactions. It was termed as an act done in the public interest for the demonetisation of certain high denomination bank notes and for matter connected there in India.
- People who forced these notes were given till January 24 the same year a highly denomination notes. The one big difference with the announcement Tuesday is the rupees 1000+ high value notes were almost impossible to possess then for the common man given the value of these amount then.
- It was not the first time when govt of India demonetised currency. Earlier to this India has witnessed demonetisation in 1946 and 1978. And it was the third time when govt. of India again demonetised Indian currency. This time Indian govt demonetised rupees 500 and rupees 1000 notes in the economy on 8th November 2016 in order to control black money in the economy.

IMPACT OF DEMONETISATION ON INDIAN ECONOMY:

- Govt of India demonetised the currency as a tool to fight against corruption and black money, which are the major problems of Indian economy . Demonetisation affects the economy through liquidity side. The present demonetisation effects shows that 86% of currency value in the circulation was withdrawn without replacing bulk of it. As a result of the withdrawl of rupees 500 and rupees 1000 notes, there occurred huge gap in the currency composition as after rupees 100 and rupees 2000 is the only denomination.
- Demonetisation technically is a liquidity shock, a sudden stop in the terms of currency availability. it creates a situation where lack of currency jams consumption, investment , production employment etc., in this context ,the exercise may produce following short term and long term impacts on Indian economy. The intensity of demonetisation effects clearly depends upon the duration of the liquidity shocks ,following are the main impacts :
- A disaster:--- demonetisation is not a big disaster like global banking sector crisis of 2007, but at the same time ,it will act as a liquidity shock that disturbs economic activities.
- Liquidity crunch---- it means people are not able to get sufficient volume of popular denomination especially rupees 500. This currency unit is favourable denomination in

daily life current reports indicate that all security printing press can print only rupees 2000 million units of rupees 500 notes by the end of this year. Some portion of this were filled by the new Rs. 2000 notes and towards end of march approximately 1000 million units will be printed and replaced. All this indicates that the currency will be in our economy for the next four months.

- Effect on GDP----India's GDP which grew at 7.6% in financial year 2015 -16 is likely to slow down by 0.5 to 1.5% due to the less availability of cash. Even the automobile industry which was growing rapidly earlier has seen a contraction in October –December 2016.purchasing power of the consumer is adversely affected because Indian economy is largely cash driven with more than 90% transaction taking place in cash and digital transactions accounting for just remaining 10%.
- Effect on households----according to estimates, about 80-85% transactions in the economy are done in cash right from paying for groceries or the maid to buying high ticket consumer durables, much of our transactions happen in cash .and if the the855 cash has been demonetised that means a severe disruption in consumption for some time until liquidity is infused.
- Effect on small enterprises---- needless to say, much of the micro and small unorganized and small organised sectors thrive in the cash business. Acoording to data micro, small and medium enterprises employ 80.5 million people and account for about 38% of the GDP. With limited liquidity and dip in demand, these firms will take a hit, even if temporary .some of these enterprises may also be stressed in the repayment of their loans and may hence impact the lenders ----be it NBFC/ banks or the unorganized lenders .Effect on non-tax payers----- among the small unorganized space—be it your saloon or kirana shop—a good chunk of these businesses could be non-tax payers . for them with little option than to become tax payers, many of their businesses could become unviable. even the slightly larger businesses, the GST would ensure that they are brought under the tax net. Hence, in the medium term there is a possibility that such businesses either go out of business or take a severe haircut in their profits .what it means is that employment could become a medium term concern.
- Effect on agriculture---- this is one sector where all transaction are done in cash. The withdrawal of the old currency notes put pressure on the mandis, farmers are having problems in selling their produce or both the parties have to agree on the mode of payment .acute shortage of rupees 500 and 1000 notes is found. Change for the highly denomination rupees 2000 notes not readily available with the vegetable and vendors. this is also taking the buyer away from the vendors to big retail markets. thus impacting the livelihood of the unorganised sectors.
- Effect on employment----since consumer's demand has slowed and consequently industrial production has declined ,employment generation has been adversely impacted by currency demonetisation drive. Since manufacturing sector which accounts for the

highest employment of skilled and semi skilled labourers is witnessing slow down in the production not only less jobs are being created but lay- offs are also taking place at a higher rate due to demonetisation as production gets hit ,especially in labour intensive sectors like textile ,garments, leather and jewellery . As many as four lakh people mostly daily wagers , may have either lost their jobs or shunned worth temporarily.

- Effect on black money---- most of the black income has been converted into white by depositing it Jan Dhan accounts ,depositing it individual s own accounts ,by breaking it into smaller chunks ,by exchanging for new currency notes through Hawala dealers ,by buying last minute luxury items like jewellery high priced mobiles ,by paying advance wages to the employees .the entire amount of rupees 14.18lac crores in rupees 500 and 1000 currency laying with the public has returned to the banks.

CONCLUSION

In the end I would like to say that in my opinion the decision of Indian govt to demonetise the currency was totally unprecedented and disaster for Indian economy which not only affected adversely the production, employment of the economy but it adversely affected the GDP growth rate which fell from 8.1% to 7.1%.presently it is 5.7%. This means that the Economy had been really hit by the process of Demonitization.

REFERENCES

www.investopedia.com on 10th October 2017

- 1) Some articles from Indian express
- 2) The tribune of 19th December 2016.
- 3) The tribune of 2nd jan 2017.
- 4) The tribune of 7th jan 2017.
- 5) Views of Mythili Bhusnurmath (a senior consultant at national council of applied economics.