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## DEMONETIZATION- IMPACT ON INDIAN ECONOMY

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### **Abstract:-**

For a common man demonetization mean withdrawal of 500 and 1000 rupees by Reserve Bank of India but this decision has taken by government because India has the highest level of cash on hand circulation. A significant portion of the cash on hand is generated by economic transactions that are not reported to tax authorities leading to the corruption. Demonetization of higher denomination will help in controlling all such illegal activities. Present paper focuses on the effects of demonetization in Indian economy and some of the benefits of going cashless in India.

Key Words:- Demonetization, Cash on hand, Indian economy ,Reserve Bank Of India

### **Introduction:-**

Demonetization for us means that Reserve Bank of India has withdrawn the old Rs 500 and Rs 1000 notes as an official mode of payment there is a tremendous interest among policy makers, academicians, and commercial enterprises to explore the possibilities of moving towards a cashless economy. It is widely believed that the movement from cash to cashless economy has significant benefits. In India, there are two major issues : the share of cashless - both in terms of transactions as well as value and the factors that affect them most. This provides a roadmap to increasing the share of cashless transactions in the economy. Economy consists of economic system of a country the labor, capital ,land resources, consumption of goods and services, all kind of professions, occupations, economic agents contribute to the economy. An informal economy is economic activity that is neither taxed nor monitored by a government , it is a dynamic process which

includes many aspects of economic and social theory including exchange, regulation, and enforcement. This is referred to as Parallel economy functioning of an unsanctioned sector in the economy whose objectives run parallel and in contradiction with the objectives of official sector. This Parallel economy' poses a serious threat to stability and growth of the official economy, surely it stems from the fact that the magnitude of 'black-money' is large and rigged deals are growing in volume and complexity at an alarming rate. Finally the time has come to deal with all these and strengthen the economy; therefore the PM of India on 8<sup>th</sup> November 2016 has made an historic decision called currency demonetization in order to deal with the :-

- Black money in India
- To reduce the cash on hand circulation which is the main reason for corruption
- Going Cash less transactions

- To remove the black money used in funding of terrorism and completely eliminate the terror groups in India.

**OBJECTIVES :-**

- 1. To study the causes and impact of black money on Indian economy
- 2. To study the impact of demonetization on Indian economy
- 3. To analyze the probable consequences of the demonetization on Indian economy

**Demonetization:-**

It is widely believed that the movement from cash to cashless economy has significant benefits. There are two major benefits of cashless payments on GDP growth: lower costs of storing and processing physical currency and increased tax collection. There are both direct and indirect benefits of going cashless for India. Some of them are

**Direct Benefits:**

- High maintenance costs:-

According to the Reserve Bank of India (RBI), the provisional estimates of the amount of currency in circulation (as of June 2016) stand at INR 16.61trillions, out of which only 5% of the currency is with the bank. From April 1994 to June 2016, currency has shown a yearly growth rate of 17%, while the share of bank currency has remained around 5%.<sup>2</sup> It was

estimated that, for 2009–2010, RBI incurred an annual cost of INR 2800 Crores for printing currency notes (Das and Agarwal2010). This is 0.4% of the total currency in circulation.<sup>3</sup> This cost does not include the cost of storage, transportation, security, detection of counterfeits, etc

- Financial records and tax collections:

It is difficult to obtain accurate estimates of the amount of “black money”. As a prevention strategy, the Government has recently announced an immediate demonetization of all high-value currencies. Economic Index of Freedom data estimates the tax burden in India (tax revenue as a percentage of GDP) at only at 17.6%, which is lower than the global average of above 25%. The lower tax burden is mostly due to low tax compliance, as well as a complicated tax structure. The effort is therefore to increase indirect tax collection. With cashless transactions, all transactions would leave digital footprints. In India, the two major benefits of going cashless are stronger i.e; promoting financial inclusion better targeting of benefits

**Indirect benefits:**

- Financial inclusion

The percentage of population covered by the banking system is still low in India (slightly above 60%), despite recent improvements. The push towards financial inclusion in India has emanated from the Pradhan Mantri Jan Dhan Yojana in August 2014, as well as the special thrust on financial inclusion by the Financial Stability and Development Council. As of July 2016,

approximately 228 million accounts have been opened under the PMJDY scheme. However, a quarter of them are zero-balance accounts. Most of the previous models in India have focused on how to make it easier for the individuals to access cash. The focus should be on how efficiently can they carry forth their financial transactions.

- **Stopping leakages**

A cashless economy could stop leakages. The use of computerized platforms to keep record of all transactions pertaining to government-to-person (G2P) payments can have a significant impact on the economy as a whole in terms of efficiency, safety, and transparency.

**CAUSES OF BLACK MONEY:-**

There are many ways for generating back money in India. Few of them are as follows:

- Quotas and licensing system
- Higher Rates of Taxes
- Ineffective enforcement of tax laws
- Funding of political parties with black money
- Second World War after influence - A favorable environment for black marketing making of marketing money out of shortages and not out of extension of the business activities.

- Inflation – Hike in prices of commodities like petrol, etc. in international market, boost in prices of commodities due to high increase in duties and taxes imposed by the government is the root of inflation creating black money
- Agricultural Income – reluctance of agricultural earnings in income tax has also contributed to creation of black money
- Privatization Transactions in Urban Real Estates
- The other factors like smuggling, bribery, kickbacks, commissions, etc are also responsible for the creation of black money

**Impact of Black Income and initiatives of government:-**

- Black income has been causing underestimation of GDP in India resulting in growing continuation of parallel economy of the country
- loss of revenue as a tax evasion
- transfer of funds from India to foreign countries
- parallel economy has totally distorted and disrupted the planning of the economy of the country
- The government has taken a number of steps to tackle the black money scrutiny of income tax returns are being done by the Income Tax Department
- The Government has floated various voluntary disclosure schemes to determine the black money.

- The income tax evasion penalties can help the government recover maximum amounts in the form of tax and utilize the money for the benefit of the common public.
- Introduction of economic liberalization has detached the regime of controls and regulations and thereby the extent of black economy would be reduced regularly (Lekhi, 2003, 196).
- Controlling the election expenses incurred by the candidates
- NRI foreign exchange remittance, issuing National Development Bonds in US dollars etc

### **Impact of demonetization on Indian economy:-**

The Indian markets have fallen a bit more than other emerging markets in Asia. The extra fall in the Indian markets compared to others could be due to many factors, including high valuations, but it's very likely that the demonetization effect is mainly responsible for the fall.

Some stocks such as DLF Ltd, jewellery companies, and BSE Realty index have also fallen down because a lot of gold purchases are through cash stocks of mid- and small-sized finance companies which collect payments in cash have fallen. Information technology stocks are down. While these companies will be unaffected by the demonetization process, this reflects a concern about a Trump presidency and a possibility of anti-outsourcing measures.

### **Probable consequences of the demonetization on Indian economy:-**

- Having closed the voluntary disclosure window for undisclosed money by limiting the deposits to Rs 2 lakhs would increase tax net, higher tax collection and a better tax to GDP ratio. As the money gets accounted and more taxes are collected, government might reduce tax rates going forward.
- One of the biggest impacts of demonetization would be high value transactions, especially land and gold resulting in lower inflation, tempting the central bank to reduce interest rates
- overall tightening of the cash-liquidity in the supply chain, consumer firms may be forced to offer easier credit terms to the distributors through which we can expect an increase in their receivables
- Demonetization comes at an important time as the country heads to a new tax regime with the implementation of GST. Along with GST, demonetization will lead to a higher tax/GDP ratio, says CLSA.
- The removal of these 500 and 1000 notes and replacement of the same with new 500 and 2000 Rupee Notes is expected to - remove black money from the economy and - curb the funding for anti-

social elements like smuggling, terrorism, espionage, etc.

### Observations:-

- Internationally, the government is likely to get thumbs up for the move and more countries could potentially see this as a viable option to curb black money and stem illegal financial activity
- The real estate sector is likely to see a significant negative impact in the medium- to long-term, particularly in the repurchase market
- There is likely to a reset of spending patterns as this move represents indirectly a significant push towards a cashless economy
- There is a positive impact on E-commerce, online retail, mobile wallets and fin-tech etc
- There is a negative impact on agriculture, luxury goods, consumer durables and non-durables.

In India amount of black money are increasing continuously which badly impacts the economic growth of the nation. Such money is a new challenge for Indian economy giving scope for Parallel economy which is a threat to Indian economy. This black money as it is underestimating GDP, increasing inequality of income, increasing illegal activities etc. Even though demonetization is a challenge faced by citizens it was a good move which will

reduce black money and have a large impact on India. The efforts will bring massive amounts of cash into the banking system – a benefit in itself. This is making India gradually migrate towards a cashless economy. The cashless economy involves network effects, certain enablers are identified as more payments are directly credited to the account, cashless payments increase significantly. Therefore, while in the short run a positive “shock” towards developing a critical network is important, in the steady-state equilibrium, cashless transactions increase only if accounts have steady inflows. Awareness about the advantages of cashless payments: A concerted effort to make individuals aware of the advantages of cashless payments is the starting point. Removal of e-payment costs: Merchant Discount Rates and convenience charges associated with e-payments must be reduced. Mobile banking as an extension of banking: Although mobile payments dominate the cashless scenario, loading the mobile wallet is currently allowed almost entirely through bank accounts. It will be more effective allowing individuals to directly deposit cash in the mobile wallet. Indeed, if this is allowed in the current demonetization exercise, it would have tremendous short- and long-term gains.

### CONCLUSION :-

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