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Demonetization – It's impact on Common Man

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ABSTRACT

*On 8th November, 2016 Modi government brought a prominent reform - Demonetization to eliminate the "black economy"**.** It is the process where the old unit of currency is replaced with new currency having both pros and cons in the Indian economy. It can be used as a tool to curb corruption, terrorism, drug menace and smuggling. Though demonetization is a good idea to resolve various money related issues but common people of the country had faced several incommodiousness for a short period of time. There was a great chaos and disruption as maximum currency in circulation was pulled out at one stroke from the economy. It had brought a sense of justice among honest tax payers and this would be further strengthen if money recovered is used by the government in an efficient and leak-proof manner for infrastructure and social schemes. Due to demonetization the common people have made an entry to increase the use of digital payment system and it is an excellent move to destroy the corruption to a greater extent. Once India take forward steps to digital economy, short term challenges will be at an end and transparency will increase and the ability to tackle money laundering and money flow will become easier.*

*The reasons for demonetization are to control counterfeit notes that could be contributing to terrorism, and to undermine or eliminate the "black economy"**.** In the other words, the rest would be available only as electronic money. The objective of this paper is to study the impact of demonetization on common man and Indian economy.*

Keywords: Demonetization, common man, black economy, electronic money, transparency

Introduction: Demonetization is the most important and necessary when there is a change of national currency. The old unit of currency replaced with new currency. Demonetization is the process where government declares the currently running currency notes illegal to be tender after the declaration is made. There are both pros and cons of demonetization in the Indian economy. The reasons for demonetization are to control counterfeit notes that could be contributing to terrorism, and to undermine or eliminate the "black economy"

Demonetization in India: 1946: Rs1,000, Rs5,000, and Rs10,000 notes were taken out of circulation in January 1946. The Rs10,000 notes were the largest currency denomination ever printed by the Reserve Bank of India, introduced for the first time in 1938. All three notes were reintroduced in 1954 . Historically, previous Indian governments had demonetized bank notes. In January 1946, banknotes of Rs1,000, Rs5,000, and Rs10,000 notes were taken out of circulation. The Rs10,000 notes were the largest currency denomination ever printed by the Reserve Bank of India, introduced for the first time in 1938. In the year 1945 all three notes were reintroduced. In 1977 Wanchoo committee (set up in 1970s), a direct tax inquiry committee, suggested demonetization as a measure to unearth and counter the spread of black money. On 28 October 2016 the total banknotes in circulation in India was Rs.17.77 trillion (US$260 billion). In terms of value, the annual report of Reserve Bank of India (RBI) of 31 March 2016 stated that total bank notes in circulation valued to Rs.16.42 trillion (US$240 billion) of which nearly 86% (around Rs.14.18 trillion (US$210 billion)) were Rs.500 and Rs.1,000 banknotes. They were taken out of circulation from 2016.

Review of Literature: Arpit Guru and Shruti Kahanijow (2010) researcher analysed the black money income? Need for amendment in DTAA &ITEA and analysed that black money is spread everywhere in India up to a large extent International Journal of Interdisciplinary Research in Arts and Humanities (IJIRAH) Impact Factor: 4.675, ISSN (Online): 2456 - 3145 (www.dvpublication.com) Volume 2, Issue 1, 2017 10 which continuously stashed towards abroad in a very large amount. The researcher also identified how black money had caused menaces in our economy and in what ways it is used. Sukanta Sarkar (2010) conducted a study on the parallel economy in India: Causes, impacts & government initiatives in which the researcher focused on the existence of causes and impacts of black money in India. According to the study, the main reason behind the generation of black money is the Indian Political System i.e. Indian govt. just focused on making committees rather than to implement it .The study concludes that laws should be implemented properly to control black money in our economy. Tax Research Team (2016) in their working paper stated in favour of demonetization Its main objective is to analyze the impact of demonetization on Indian economy.

Objectives of the Study:
- To study the impact of demonetization on common man
- To study the effects of demonetization on Indian economy

Research Methodology:
This paper is based on secondary data. Data is collected from various secondary sources such as Journals, Newspapers, magazines, online journals.
The impact of this move on the common man includes:
a. Financial/business impact
- People with large amount of black money used unscrupulous means to convert it into legitimate currency
- A taxpayer has to stand in queues to withdraw his hard-earned money
- Small/medium sized business relying on cash transactions are seeing a total demand collapse
- Gem and Jewelry business were hard hit.
- Second-hand car market will crash badly
- Banks had a tough time flooded with cash culture

b. Social impact
- Low-income people have been impacted as their payments are delayed
- Some people had commited suicide
- Marriages to become cheap. Death of dowry
- All medicines in white money
- Big blow to gambling
- Death of drug mafia and terror networks
- People now know moral status of their peers and neighbours better

Pros:
- Purchasing power will be improved, directly correlated with inflation (Rise in prices) i.e. controlled prices will directly impact on common man and had much purchasing power
- Banks Interest rates will be reduced making it easy for common man to avail fresh loans
- Govt. had scope of introducing new schemes for welfare of common man
- Lesser TAX Liability, Boost for savings and consumption, New Employment opportunities

Cons:
- Currency crunch in market having its direct impact on demand and supply for common man Current currency exchange restrictions made life difficult for common man, Although Govt. is regularly changing rules for better adherence
- Difficulty in cash deposits / exchange of Old currency notes for ones with no bank a/cs
- Frequent changing currency rules getting day to day activities affected both for common man and banking institutions
- Promotion of illegal activities till OLD Currency completely stopped in system
- Higher cash deposits in Nov & Dec-16 attracted income tax authorities for verification even it is earned through proper taxable income disclosures and same needs to be justified else additional tax levied

- Dealings in cash adversely effected for small retailers /dealers etc
- Fear of unemployment in MSME and other small manufacturing/ unrecognized sectors where majority is cash dealings as same is largely affected /Temporary closed due to liquidity crunch.
- Although it benefits E- mode of payments but it largely for educated people, No specific provision for uneducated / village people living in interior areas of cities / villages

Impact of Demonetization on Indian Economy

Demonetisation may not be a huge disaster like the global banking sector crisis of 2007; but at the same time, it will act as a liquidity shock that disturbs economic activities.

- ***Liquidity crunch (short term effect):*** Liquidity shock means people are not able to get sufficient volume of popular denomination especially Rs 500. This currency unit is the favourable denomination in daily life. It constituted to nearly 49% of the previous currency supply in terms of value. Higher the time required to resupply Rs 500 notes, higher will be the duration of the liquidity crunch.
- ***Duration of Currency Crunch:*** Current reports indicate that all security printing press can print only 2000 million units of RS 500 notes by the end of this year. Nearly 16000 million Rs 500 notes were in circulation as on end March 2016. Some portion of this were filled by the new Rs 2000 notes. Towards end of March approximately 10000 million units will be printed and replaced. All these indicate that currency crunch will be in our economy for the next four months.
- ***Welfare loss for the currency using population:*** Most active segments of the population who constitute the 'base of the pyramid' uses currency to meet their transactions. The daily wage earners, other labourers, small traders etc. who reside out of the formal economy uses cash frequently. These sections will lose income in the absence of liquid cash. Cash stringency will compel firms to reduce labour cost and thus reduces income to the poor working class. There will be a trickle up effect of the liquidity chaos to the higher income people with time.
- ***Consumption will be hit:*** When liquidity shortage strikes, it is consumption that is going to be adversely affected first.

Consumption ↓→ Production ↓→ Employment ↓→ Growth ↓→ Tax revenue ↓

- ***Loss of Growth momentum:*** India risks its position of being the fastest growing largest economy: reduced consumption, income, investment etc. may reduce India's GDP growth as the liquidity impact itself may last three -four months.
- ***Impact on bank deposits and interest rate:*** Deposit in the short term may rise, but in the long term, its effect will come down. The savings with the banks are actually liquid cash people stored. It is difficult to assume that such ready cash once stored in their hands will be put into savings for a long term. They saved this money into banks just to convert the old notes into new notes. These are not voluntary savings aimed to get interest. It will be converted into active liquidity by the savers when full-fledged new currency supply take place. This means that new savings with banks is only transitory or short-term deposit. It may be withdrawn by the savers at the appropriate time. It is not necessary that demonetisation will produce big savings in the banking system in the medium term. Most of the savings are obtained by biggie public sector banks like the SBI. They may reduce interest rate in the short/medium term. But they can't follow it in the long term.
- ***Impact on black money:*** Only a small portion of black money is actually stored in the form of cash. Usually, black income is kept in the form of physical assets like gold, land, buildings etc. Hence the amount of black money countered by demonetisation depend upon the amount of black money held in the form of cash and it will be smaller than expected. But more than anything else, demonetization has a big propaganda effect. People are now much convinced about the need to fight black income. such a nationwide awareness and urge will encourage government to come out with even strong measures.

- ***Impact on counterfeit currency:*** The real impact will be on counterfeit/fake currency as its circulation will be checked after this exercise. Demonetization as a cleaning exercise may produce several good things in the economy. At the same time, it creates unavoidable income and welfare losses to the poor sections of the society who gets income based on their daily work and those who does not have the digital transaction.

Pros:

- Fake currency and terrorism funding will be controlled
- Hit on black money / parallel economy currently having adverse impact on economy
- Banking Sector will be benefited with cash inflows / higher deposits which directly had impact on lending rates and acts as economy booster in log run
- Country's Trade deficit will be reduced i.e. higher GDP (Gross domestic product) growth indicator of future growth prospects
- Currency Transactions will be more transparent and identifiable
- Expansion of Govt. Tax structures and reach to every earning individual which not only acts as generation of additional govt. revenues but also simplifies future tax regime
- Country's overall rating in global scenario given by recognized rating agencies like CRISIL etc will be improved, criteria for FIIs (Foreign Institutional investors – imp for Banks /NBFCs/Mutual funds etc as it is additional mode of sourcing funds)
- Banks Lending % will be enhanced with lower cost of capital and interest rates, key contributor of economy growth.

Cons:

- Cash / Liquidity crunch in market. If this is not controlled in near term will had adverse impact on economy in short term viz. higher inflation, Mismatch of demand and supply as dealings /exchanges would be in recognized currency notes only etc
- New currency flows needs to be improved in village / interior areas of cities / villages effecting life of both common man and economy as a whole
- Banking reforms required when deposits are withdrawn once new currency circulated / Withdrawal limits raised else had adverse effect on both market liquidity and lending rates
- There are other forms of Black Money also Eg: Investments in Real Estate, Cash funding to Election parties with no proper records etc this needs to be duly monitored and regulated if we need to attain sole objective of complete erosion of black money from Indian economy as demonetization of 500 Rs and 1000 Rs notes alone will not erode black money completely
- After demonetization closure, Govt. reforms required in Real Estate sector and MSME else it will had adverse impact on both employment and economy.

CONCLUSION AND FUTURE SCOPE

The move will hence "short-term pain" but growth gains in the long term; it is beneficial for both Indian economy and common man. Boost for savings and consumption, New Employment opportunities .It may not control the amount of black money in the nation directly, but nonetheless, it is beneficial for the Indian economy in the future. This process would also forcibly bring in huge amount of money from the informal sector, which was unaccounted for. This will help in the growth and therefore GDP would not face a negative impact. Lesser TAX Liability, Boost for savings and consumption, New Employment opportunities

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