



Impact of Demonetization on Indian Economy

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Abstract

Demonetization is act of stripping a currency unit of its status as legal tender. Fastest growing economy India is hit by the demonetization of the 500 and 1000 rupee note. Its impact is felt by every citizen of India. The Indian currency three times demonetized in 1946, 1978 and latest in Nov. 2016 by the Modi government. It's a historical decision taken by government for the betterment of Indian economy. So in this paper we study how recent demonetization impact on Indian economy.

Keywords

Demonetization, corruption, black money , fake currency

Objectives

Main objectives of this paper to study the impact of demonetization on Indian economy and what are pros and cons of Nov 2016 demonetization in India.

Methodology

This study is purely based on secondary data. Data is collected from various magazines , newspapers , journals and internet.

Introduction

Historical decision taken by Modi Government on 8 Nov 2016 announced discontinue of Rs 500 and 1000 notes with effect from same day midnight , making these notes invalid a major step to check undeclared black money. Apart from tackle with black money , the stated purpose is check fake currency circulation in Indian economy and used to finance terrorism . A new designed series of Rs 500 and new denomination of Rs 2000 is in circulation since 10 Nov 2016

Earlier to this two times demonetization was done in India in 1946 and 1978. The highest denomination note ever printed by the RBI of India was the Rs 10,000 banknote in 1938 and again in 1954 but these banknote demonetized in 1946 and again in 1978 as per RBI

History of Demonetization in India

First demonetization in 1946

In 1946, the currency note of Rs 1000 and Rs 10000 banknote is withdrawal from circulation. But this withdrawal of currency don't have much impact on common people because higher denomination was not accessible to the common people. However these ban currency of Rs 1000 and Rs 10000 reintroduced in 1954 and additional new currency of Rs 5000 is introduced.

Rs 500 and Rs 1000 notes were introduce in 1934 and after four years in 1938, Rs 10000 notes were introduced.

Second demonetization in 1978

In 1978, Prime Minister of India Morarji Desai announced the currency ban taking Rs 1000, Rs 5000, Rs 10000 out of circulation. The main aim of this ban was to stop black money generation in country.

Third and recent demonetization in 2016

On 8 November 2016, Indian government announced to demonetization of all Rs 500 and Rs 1000 banknote of the Mahatma Gandhi series. The government claimed that the action would check the parallel economy and fake currency used to fund illegal activity and terrorism. The sudden nature of announcement and due cash shortage created significant disruption throughout the economy. This step was criticized as unplanned and unfair and was met with protests , strikes and litigation.

The BSE SENSEX and NIFTY 50 stock index fell over 6% after the demonetization announcement by Modi government. Due to this hard step country GDP and industrial production is reduced. This step is criticized by many economists and by media

However demonetization have positive long term results could accelerate financial deepening , foster financial inclusion and increase transparency said by WORLD BANK.

World bank said the changes in the use of specific digital payment tool over the last few months suggest that permanent change might taken place.

For boosting the digital payment system many app recently launched by government like BHIM, UPI Unified payment interface, BharatQR code.

Impact of demonetization on Indian economy

Liquidity crunch

Liquidity crunch means people are not able to get sufficient volume of popular denomination Rs 500. Due to this shortage their daily needs were badly hit and this currency constitute 49% of the pervious

currency supply in terms of value. Higher time required to resupply Rs 500 so there was higher liquidity crunch.

Impact on black money

One of the main target of demonetization is to check black money. Due to currency become invalid black money holder unable to replace there Rs 500 and 1000 notes. They cant deposit in bank due to lack of valid source of income. In this way black money holders affected in great way.

Fall in prices of real estate

Due to lesser cash transaction in real estate sector there is great reduction in prices and become cheap.

Increase in bank deposit

Due to demonetization Rs 500 and 1000 become invalid people who hold currency for household purpose, business and emergency purpose started deposit currency in current and saving account .in this way there is great increase in bank deposit.

Fake currency

Dealers of counterfeit currency affected most because if they come to bank for replace their fake currency there racket will exposed. So they have only option to destroy their notes and make losses.

Stock market

In short term market hit badly fell 6% after demonetization announcement but in long term Indian market still a attractive destination for overseas and domestic investors. But after demonetization news, market have great down fall for three months.

Fall in GDP

Due to its GDP forecast for 2016-2017 to 6.8% from 7.8% earlier and stating demonetization erosion of Rs 1.5 trillion this fiscal.

Lower inflation

Reduction on inflation rate is possible because of demonetization. As the black money goes out of the system the money supply will shrink to some degree.

Gold and silver

Demand of gold and silver rises sharply because black money holders want to invest their black money in gold and silver to make their money white.



Cashless payments

Due to shortage of money supply common people started using plastic cards and digital payment for paying payments. This will boost the cashless economy.

Conclusion

So far as we discussing Impact of demonetization on Indian economy. It's a historical decision taken by Modi Govt. and some supported or some criticized the decision. Majority of decision taken are negative effect but they all are short run in nature and solved after new currency widely circulated in the economy. Most benefited sector during demonetization is banks and some sector suffer like real estate, luxury items, gold and silver but they suffer near to medium term. This step lead to improved taxation system. It will check corruption, fake currency and funding to terrorism. This step help sustained economic growth in the longer term.

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