

A Critical Analysis on Demonetisation to Deify or Demonize

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Abstract: *Change is inevitable in the current global economic conditions and also for wealthy economy. Corruption and tax evasion are major impediments to the Indian economy which are caused to relatively poor of the country. Besides, India is one of the trillion GDP's countries. But tax payers are around 5 per cent only. In this context, the following headings give information on India's monetary scenario and consequences of demonetisation. This paper tries to presents the factors behind the sudden demonetisation in India, historical back ground of demonetisation, positive and negative consequences of demonetisation.*

Key words: payment system, pin-based debit cards, circulation

Introduction

Change is inevitable in the current global economic conditions and also for wealthy economy. Corruption and tax evasion are major impediments to the Indian economy which are caused to relatively poor of the country. Besides, India is one of the trillion GDP's countries. But tax payers are around 5 per cent only. In this context, the following headings give information on India's monetary scenario and consequences of demonetisation. The government has implemented a major change in the economic environment by demonetising the high value currency notes – of Rs 500 and Rs 1000 denomination. These ceased to be legal tender from the midnight of 8th of November 2016. People have been given upto December 30, 2016 to exchange the notes held by them. The proposal by the government involves the elimination of these existing notes from circulation and a gradual replacement with a new set of notes. In the short term, it is intended that the cash in circulation would be substantially squeezed since there are limits placed on the amount that individuals can withdraw. In the months to come, this squeeze may be relaxed somewhat. The reasons offered for demonetisation are two-fold: one, to control counterfeit notes that could be contributing to terrorism, in other words a national security concern and second, to undermine or eliminate the “black economy”.

Economic conditions of economy as on date of demonetisation

- **Size of GDP:** \$2.46 trillion (nominal; 2017)

- Currency GDP Ratio: 10.6 per cent
- Value of Total Bank notes: As on October 28, Value of total Bank notes Rs. 177.7 lakh million and
- Value of high denomination bank notes 141.8 lakh million (86 percent)
- Per capita income: \$ 1,852 ((Rs.1,20,380)

The figures shows that Value of high denomination bank notes i.e., Rs 500 and Rs 1000 was 141.8 lakh million equaling to 86 per cent to the total currency. Further, nobody is under poverty line as per the per capita income Rs.1, 20,380. Of course, economic inequalities are common due to mal-distribution of national income which caused to poverty in India.

Taxes payables are more than the actual taxpayers

S.NO	Class	Income (Rs.lakh)	Per cent Of population
1	Rich	10 & above	5.0
2	Middle	2 to 10 lakh	12-40%
	Total	-	45% (57.15 crore)

The above table shows that the income class people up to the Rs. 2 lakh is 45% (57.15 crore),. If we exclude the population below Rs. 2.5 lakh is around 99 lakh. About 1.95 crore showed income between Rs 2.5 lakh and Rs 5 lakh; 52 lakh showed income between Rs 5 lakh and Rs 10 lakh, and only 24 lakh

people declared income above Rs 10 lakh. Of the 76 lakh individual assesses who declared income of above Rs 5 lakh, 56 lakh are in the salaried class. The number of people showing income more than Rs 50 lakh in the country is only 1.72 lakh,.

Therefore, population who has capacity to pay tax is around 44%. But the actual **tax payers are 4.24% only. There is scope inclusion of population under tax payable is around 40 per cent which are under tax evasion.**

Major Possibility to tax evasion

- Liquidity as Store of value and exchange value: cash used for transactions could be black if it was earned through tax evasion and/or corruption.
- It is evidence that - Soil (too damaged) rate of currency notes are nearly to 50 % in other countries like in US. But in India soil rate of 33 percent per year. In contrast, the soil rate for the Rs 500 note is 22 percent and the Rs 1000 just 11 per cent. It is as estimate black money represents about 12 percent of GDP.

Hence, hoarding of currency is gradually increasing. Digitalization reduce storing currency

In this context, Demonetization is treated as a weapon to increase tax payes and treatment to several economic impediments

Demonetization

Demonetization is the withdrawal of a particular form of currency from circulation.” It is a process by which a series of currency will not be legal tender. The series of currency will not acceptable as valid currency

Historical perspective of demonetisation

Demonetisation is not a new concept to the world economies. The system was adopted in many countries like:

- Philippines, 1978
- Nigeria (1982)
- Ghana (1979&1981)
- Soviet Monetary Reform (1991)
- Russia 1993
- North Korea 2009
- Singapore, 1999 & 2014
- Greece 2015
- Australia , 2015 (first country - all series)
- Pakistan 2015

- Euro area 2016
- Venezuela 2016

This is not the First time, when Indian Currency is demonetized in India. Earlier it was done in 1946 with the complete ban of Rs. 1000 and Rs. 10000 Notes to deal with the unaccounted money i.e. Black Money. Second time, it was done in 1978 by Govt headed by Morarji Desai when Rs. 1000, Rs. 5000 and Rs. 10000 Notes were demonetized. Further, On 8th November 2016, Government of India had announced that from today onward rupees 500 and 1000 rupee note would cease to be legal tender from midnight. Means that 500 and 1000 rupee notes will not be accepted by anyone except the organization declared by the government. Public can deposit and change the currency from the banks and post offices till 30th December 2016.

Purpose of Demonetisation

- A parallel shadow economy corrodes and eats into the vitals of the country's economy resulting in
- **To curb corruption**
- **Counterfeiting/faking**
- **Forged cash** used to fund terrorist activities against India
- tax on all illicit/illegal activities,
- Include the earners in to tax payers
- Controlling **Inflation**
- • Infusion of new series bank notes will be monitored and regulated by RBI and
- **Major Aim of Demonetization is making India as a Cash less Society**

Progress of Demonetization

Up to 97% of the demonetised bank notes have been deposited into banks which have received a total of ₹14.97 trillion (\$220 billion) as of December 30 out of the ₹15.4 trillion that was demonetised. This is against the government's initial estimate that ₹3 trillion would not return to the banking system. A number of follow-up actions would minimize the costs and maximise the benefits of demonetisation. These include: fast, demand-driven, remonetisation; further tax reforms, including bringing land and real estate into the GST, reducing tax rates and stamp duties; and acting to allay anxieties about over-zealous tax administration. These actions would allow growth to return to trend in 2017-18, following a temporary decline in 2016-17

Digitalisation

- Digital transactions face significant impediments.
- They require special equipment,
- Cellphones for customers

- Point-Of-Sale (POS) machines for merchants,
- Internet connectivity
- e-payment firms need to recoup their costs by imposing charges on customers
- The poor, who are largely outside the digital economy of:
- Internet Banking
- Smart Mobiles
- Credit/debit cards
- There are approximately 350 million people without cellphones.

The government has taken a number of steps to facilitate and incentivize the move to a digital economy. These include: Launch of the BHIM (Bharat Interface For Money) app for smartphones. Launch of Aadhaar Merchant Pay, Aadhaar-Enabled Payments System (AEPS) aimed at the

350 million who do not have phones and payment wallets

IMPACT OF DEMONITISATION

Attack on Black Money Holders: People who possess huge amounts of black money in hard cash are at a complete loss now. Their black money in hard cash is now a pile of trash. Now if a black money holder wants to deposit money in bank account than he/she has to show ID. There will be 200 % penalty on income tax amount

Death Knell to Fake Currency Rackets

Most of the fake currencies used to be in the denominations of Rs. 500 and Rs. 1000 .

by banning RS. 500 and Rs. 1000 notes, Modiji has busted all these unethical rackets completely. Now there will no use of this money.

Factor	Impact	
	Short run	longer-term effect
Money/interest rates	Cash declined sharply	Cash will recover but settle at a lower level
	Bank deposits increased sharply	Deposits will decline, but probably settle at a slightly higher level
	RBI's balance sheet largely unchanged: return of currency reduced the central bank's cash liabilities but increased its deposit liabilities to commercial banks	RBI's balance sheet will shrink, after the deadline for redeeming outstanding notes
	Interest rates on deposits, loans, and government securities declined; implicit rate on cash increased	Loan rates could fall further, if much of the deposit increase proves durable
Financial System Savings	Increased	Increase, to the extent that the cash deposit ratio falls permanently
Corruption (underlying illicit activities)		Could decline, if incentives for compliance improve
Unaccounted income/black money (underlying activity may or may not be illicit)	Stock of black money fell, as some holders came into the tax net	Formalization should reduce the flow of unaccounted income
Private Wealth	Private sector wealth declined, since some high denomination notes were not returned and real estate prices fell	Wealth could fall further, if real estate prices continue to decline

Public Sector Wealth	No effect	Government/RBI's wealth will increase when unreturned cash is extinguished, reducing liabilities
Formalization/digitilisation	Digital transactions amongst new users (RuPay/ AEPS) increased sharply; existing users' transactions increased in line with historical trend	Some return to cash as supply normalises, but the now-launched digital revolution will continue

Impact on GDP

The standard way to do this is by employing the standard "quantity theory of money". Under this equation:

$MV = PY$, where

- M refers to the money supply
- V is velocity, the rate at which money turns over (the value of final sales [GDP] per rupee note)
- P, the price level
- Y, real GDP

The cash crunch must have affected the informal economy, which depends heavily on bank notes for its transactions and has been estimated to account for nearly half of the overall economy (Sen, 2016).

End of Terrorist Funding

- Huge sums of money especially in hard cash in the denominations of Rs. 500 and Rs. 1000 was used to fund Islamic terrorists, Naxalites.
- Now, these Organizations will suffer from shortage of funds.
- Most of These terrorist, Maoist Organization used these Funds for Buying Arms and Weapons.
- Buying arms is an extremely difficult task now after this ban.

Transparency

- Online transaction = More transparency = Financial Intelligence Unit Will track all online transactions. Now there will be more transparency in real estate sector

End of Huge Donations

- Huge amounts of donation that is taken in the private education and healthcare sectors would be stopped.
- Schools, engineering and medical colleges and hospitals (private ones) used to

take huge amounts of money as donations especially in the form of hard cash in the denominations of Rs. 500 and Rs. 1000.

- These money-minded people running these institutions won't be able to make any easy money now.
- Same applies to the real estate sector.

Towards A Cashless Economy

- While it is practically impossible to have a 100% cashless economy, the proportion of hard cash in the economy will decrease and our economy will get more digitized.
- This will result in greater transparency.
- Now government has put some limitation for Cash Withdraw from bank Accounts. People will go for online payments.
- They will use PayTM or other online payment to companies for Buying goods or Making payments.
- More Use of Debit and Credit Card
- **Hawala transactions ends:** Most Hawala transactions used to be carried out in the denominations of Rs. 500 and Rs. 1000. With this ban, Modiji has delivered a fatal blow to the unethical Hawala traders as they can't trade anymore using denominations of Rs. 500 and Rs. 1000.

Cons of Demonetization in India

- Major effect on agricultural sector
- Potato production faced price less and perished
- Onion and tomato yield unsold in AP
- NREGS works postponed
- Purchase of minimum necessities has also troubled
- Travelling became very costly
- Use of green cards declined while re-monetization (60% to 40% in February (21-2-2017))
- Indirect tax fallen
- No evidence of corruption control

- No cash transfer to poor as the govt. announced in the past
- Digitalization become costlier and have many impediments
- Banks will be extremely over-crowded by people .
- People will forget everything else and throng to the places where the banned notes are being officially exchanged leading to a tremendous chaos. Due to currency being sucked out of the market coupled with Trump's victory, the mood at the stock market was completely bearish .
- Sensex lost 1600 points at open . This can adversely have a negative effect on trade in general
- Many Indian housewives store money secretly so that they could be of help during times of financial crisis in their households .
- The accumulated money of our respected Indian housewives is of no use now until they exchange in the banks and post-offices
- Due to shortage of money in the market , a short-term cost push inflation will occur.
- The price of gold has already become sky high
- Prices of vegetables and fruits have also soared burdening the common man .
- Difficult For Those Families those have Weddings
- With the older 500 and 1000 Rupees notes being scrapped, until the new 500 and 2000 Rupees notes get widely circulated in the market, money supply is expected to reduce in the short run.
- To the extent that black money (which is not counterfeit) does not re-enter the system, reserve money and hence money supply will decrease permanently.
- However gradually as the new notes get circulated in the market and the mismatch gets corrected, money supply will pick up.
- The overall demand is expected to be affected to an extent. The demand in following areas is to be impacted particularly:
 - Price level is expected to be lowered due to moderation from demand side. This demand driven fall in prices could be understood as follows:
 - Consumer goods: Prices are expected to fall only marginally due to moderation in demand as use of cards and cheques would compensate for some purchases.
 - Real Estate and Property: Prices in this sector are largely expected to fall, especially for sales of properties where major part of the transaction is cash based, rather than based on banks transfer or cheque transactions
 - With cash transactions facing a reduction, alternative forms of payment will see a surge in demand.
 - Digital transaction systems, E wallets and apps, online transactions using E banking, usage of Plastic money (Debit and Credit Cards), etc. will definitely see substantial increase in demand
 - This Will Bring More transparency In System And You can Easily track Online Money Transactions.
 - Consumer goods
 - Real Estate and Property
 - Gold and luxury goods
 - Automobiles (only to a certain limit)
 - All these mentioned sectors are expected to face certain moderation in demand from the consumer side, owing to the significant amount of cash transactions involved in these sectors.

CONCLUSION

The advantages are much dominating and it will be in the long term interest of our country comfortably outweighing the disadvantages. Broadening the coverage of GST. Individual income tax rates and real estate stamp duties could be reduced. Reducing the corporate tax rate could be accelerated; Tax administration could be improved to reduce discretion and improve accountability. Government need to take all the necessary steps so as to ensure that there will be a smooth flow of currency exchanges.

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