



INDIAN ECONOMY-BEFORE AND AFTER DEMONETIZATION

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Abstract

India's demonetization movement was a surprise canon tactic to pull to bits the cash-centric market, to rinse the country of fake notes. This movement was to further digitize the economy and to get more of the population onto the formal and official taxable economic framework. Government planned to recall the canceled notes and they are to be replaced by new 500 and 2,000 denomination notes. But the efforts in circulation of replaced currency went vain and the most cash dependent country in the world gone throbbing due to lack of availability of cash to run the economy. Though a severe cash crunch hit the economy, almost 90% of the stock of 500 and 1000 denominations was recovered. The movement initially targeted to curb black currency, later extended to nullify corruption and cruising towards digital payments surprisingly without losing the growth.

Keywords: *Demonetization, Economy, Currency, Growth, Inflation, Banking.*

Introduction

A significant day has made the currency in the hands of the people go useless. Though people have money in their wallets, nobody was in a position to accept it. The decision taken by the government on 8th November 2016 can be considered as one of the biggest financial sector reform in the country. Demonetization is not new. But the consequences of demonetization have made people panic. A person who never visited the bank was also standing in the que to exchange the cancelled notes with the new currency.

According to the statistics of the government, 95% of the transactions taking place in India are cash based and only 5% transactions went cashless. In fact there was no such mechanism and infrastructure to accept the cashless transactions. Above all lack of awareness of people about cashless transactions and the significance of cashless transactions was also limiting factor. In the unorganized sector still, wages and salaries are paid in cash. Transactions with money has its gross roots in Indian economy.

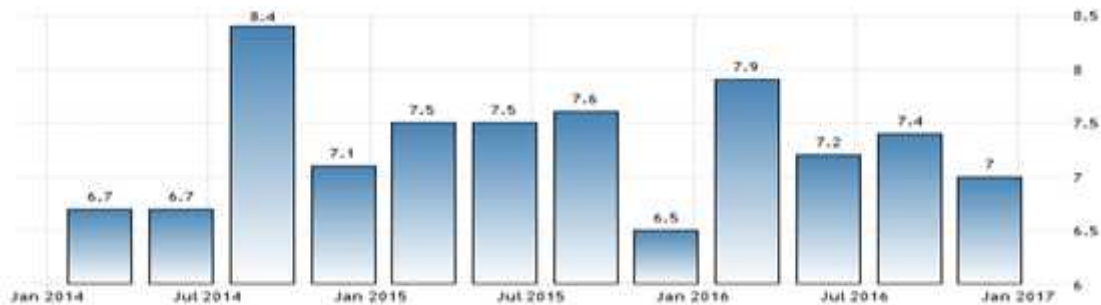
Stray thoughts on Demonetization

India is an economy with 125 crore population. Though there are over 125 crore people, only 3.65 crore individuals filing their tax returns. If people outside the tax brackets are exempted, only 1% people are paying taxes promptly. India's tax revenue as a percentage of its GDP was 16.7 per cent in 2016, compared with 25.4 per cent in the United States and 30.3 per cent in Japan. This is due to non-shown currency payments through official accounting systems. One of the major agenda could be to bring transparency in the transactions so as to make every one rupee shown in the account book. Counterfeiting of the existing currency notes was another biggest problem for the economy. According to the statistics of RBI, 250 fake currency notes per million were in circulation of in Indian economy. The value of fake currency in circulation was Rs 400 crore according to the study of Indian statistical institute. One of the best ways to control this fake system is demonetization. Because of flow of this fake currency, the unwanted activities are taking the bounds. Demonetization is a counter check for these activities. NRI remittances have been the non-taxed flow into the economy so far. Demonetization could put a check to that. Most importantly, making the economy as digital economy and making the economy a digital economy could be the biggest motive behind demonetization. Demonetization will seal the pocket of the common man which can control the expenditures which will reduce the retail inflation in the economy.

Growth of Economy and Demonetization

Though 86% of the currency is taken out from the economy, many external agencies believed that the conditions will drastically influence the GDP of the economy. When cash accounts for 78% of normal payments, the strident contraction in money supply brings spending to a crushing halt. People become more cautious as there is ambiguity as to how long the cash crunch will persist. Retail trade and transportation of goods got extremely impacted. This affect was on formers too as they were unable to pay for the fertilizers, seeds and the same time they were not paid for the crops what they have sold.

Many external agencies have predicted the growth during Q3 Of 2016-17 as negative and these negative speculations have made demonetization as negative phenomenon in Indian economy. It seems government has defend the game as it has recorded 7% growth in Q3 beyond the expectations of every one which is closer to the GDP of Q2. But still fears are there as the effect of demonetization can be in Q4 of 2016-17. Agriculture and Mining have given boost to the economy.



Source: Trading economics

Tax Revenue Acceleration

Year	Gross tax revenue(Rs. Trillions)	YOY Growth (%)
2012-13	10.36	16.54
2013-14	11.38	9.85
2014-15	12.44	9.31
2015-16	14.55	16.96
2016-17*	17.1	17.53

Source: Budget documents finance ministry-Live mint

According to Ministry of Finance the direct tax revenue has increased to 14.4% and it was only 8.3% during previous year. Surprisingly indirect tax revenue rose to close 27% after the demonetization. According to government nearly 50 cities in India reported a total 268% YOY increase in tax collection only in the month of November 2016. Demonetization has brought a large part of money into the formal banking system which has increased the ability of the banks to lend.

Banking Sector and Demonetization

The biggest beneficiary from demonetization is the banking sector. This is mainly due to the long standing queues of people depositing cash in the banks. These deposits result in substantial liquidity with the banks. As the deposits with the banks will increase the ratio of deposits in current and saving accounts. Banking sector in India has earned 14.5 lakh Crore deposits in just 2 months after demonetization. Many bank accounts which didn't have minimum balance have flooded with funds of thousands of crores. Rural banks also not exceptional to this. According to a study more than 10000 crores were deposited in rural banks. Majority of the bad debts were cleared with the black currency. This finally resulted in increased net interest income and the net earnings of the banks. This has increased the lending capacity of the banks and many banks decreased their base rates. On the flip side as the bankers have become busy beans during the exchange process of old notes, the pace of lending of loans has decreased which is a biggest revenue source for the banks. Other side Non banking finance companies (NBFCs) have faced tough time as the repayment capacity of the people almost become zero due to non availability of currency.

Gaining Popularity of E-Wallets

The period after November 8th'16 has been the golden period for e-wallets. E-wallet companies such as Paytm, Mobikwik, free charge were in the market over years. But many people came to know their significance only after demonetization. These e-wallets have seen a robust growth. Mobikwik have provided innovative cash pick up facility to its customers for some days. A person if click on 'cash pick up' on the Mobikwik app, a representative of the wallet will come to the person to exchange Rs500 and Rs1000 notes and will directly load it in their e-wallet. Nearly 2 billion customers are added to paytm after demonetization and nearly 1 billion for other e-wallet companies. People now have become confident that transactions through e-wallets is safe. More than 2 billion rupees worth transactions are taking place through e-wallets. A common vegetable vendor now accepts paytm, mobikwik payment options. This shows how these e-wallets are penetrated into the economy.



In addition to that Bheem app of government has further empowered people with many rewards in competition to the offers of Paytm, Mobikwik and free charge. On the other side transactions through NEFT, IMPS, Mobile banking, Debit and Credits were highly encouraged. A common man now make payment for gas cylinder through his debit card by entering the website of his company. Ola have asked its customers to go cashless by putting money in Ola money wallet so that they can pay directly without cash. Now everywhere we see "Paytm, Mobikwik accepted here". If this trend continues, e-wallet is the gateway for digital India.

Inflation and Demonetization

No doubt! Empty pocket buys nothing. The contraction of money availability in the economy will reduce the purchasing power of the people. When purchasing power decreased, the demand for many things will come down and finally the price will fall down. This leads to decrease in the interest rates. This relationship between inflation and demonetization is short term. But one should notice that the real income in the form of wages and salaries will make the common person psychologically strong.

Conclusion

The transactions made through online, e-wallets, debit and credit cards are under the official route of the Indian financial system. These transactions are taxable and transparent. Demonetization is just another step towards inclusive growth, towards sustainable growth with no room for corruption and black money. But the common man has suffered and has been suffering still due to the non-availability of the currency. India is the economy with major paper currency transactions and only 22% of the transactions have gone digital so far. But Demonetization has shown new avenues of transactions for the common man in the form of Electronic fund transfers and e-wallets. The aim of demonetization is to control black money, counterfeiting of currency and to make digital India. But if this decision is coupled with any policy reforms, would yield better results than bitter results. Every common man now wants to see a clean India not only through Swatch Bharat but also by supporting government in such decisions with patience without any protests.

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