



DEMONETIZATION: BLACK MONEY CORRUPTION IN INDIAN ECONOMICS

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Abstract

The demonetization of Rs. 500 and Rs. 1000 bank notes was a sudden and swift process that took the nation by surprise. In a move that has been lauded majorly by most of the sections of society, Prime Minister Narendra Modi on an unscheduled live TV address to the Nation on November 8, announced that the notes of Rs. 500 and Rs. 1000 would be deemed invalid as legal tender from the midnight of November 8, 2016.

Demonetization means to the suspension of current currency units and reinstate those currency units with new currency units. In this paper researchers aim to study the advantages and disadvantages of demonetization and its impact on Indian banking sector, Despite major developments in paperless currency over the past decade, physical cash remains widely used throughout the world. Therefore one of the main motivating factors for this study is to find out the alternatives of physical cash payments such as online bank transfer, e- clearing, e- KYC, digital locker and Unified Payment Interface. In an attempt to curb the black money in the financial system PM Modi has announced some bold moves. Denomination of Rs 500 and Rs 1000 will cease to exist as legal tender. Experts in the mutual fund industry are optimistic towards this bold step.

Keywords: *Demonetization, Cash Crunch, Cashless, e-money, Black Economy, Corruption.*

Introduction

After November 8, 2016 which was declared to be a bank holiday, the old demonetized INR 500 and INR 1,000 notes could be deposited, with proper identification, in bank or post office accounts, without any limit, until December 30, 2016. These could also be exchanged for new INR 500 or 2,000 notes, or old INR 5, 10, 20, 50 and 100 notes, but initially only up to INR 4,000. This limit was increased to INR 4,500 since November 14, before such direct exchange was completely stopped from November 25, 2016.

After 38 years again India witnessed demonetization of bank notes in November, 2016 and this time government demonetized Rs. 500 and Rs. 1000 notes and replaced it with new designed 500 notes and for the first time Indian government introduced 2000 value note.

The decision of the Government and the Reserve Bank of India (RBI) to withdraw the legal tender status of the pre-existing INR 500 and INR 1,000 currency notes beyond November 8, 2016 and the resulting cash shortage have been matters of intense debate, e.g. in Rajakumar and Shetty (2016) and Banerjee (2016). The measure, according to the Government, was motivated by the twin objectives of curbing the menace of fake Indian currency notes and for eliminating black money.

On 8 November 2016, the Government of India announced the demonetization of all 500 (US\$7.40) and 1,000 (US\$15) banknotes of the Mahatma Gandhi Series. The government claimed that the action would curtail the shadow economy and crack down on the use of illicit and counterfeit cash to fund illegal activity and terrorism. The sudden nature of the announcement—and the prolonged cash shortages in the weeks that followed—created significant disruption throughout the economy, threatening economic output. The move was heavily criticized as poorly planned and unfair, and was met with protests, litigation, and strikes.

Prime Minister of India Narendra Modi announced the demonetization in an unscheduled live televised address at 20:00 Indian Standard Time (IST) on 8 November. In the announcement, Modi declared that use of all 500 and 1000 banknotes of the Mahatma Gandhi Series would be invalid past midnight, and announced the issuance of new 500 and 2000 banknotes of the Mahatma Gandhi New Series in exchange for the old banknotes.

The BSE SENSEX and NIFTY 50 stock indices fell over 6 percent on the day after the announcement. In the days following the demonetization, the country faced severe cash shortages with severe detrimental effects across the economy. People seeking to exchange their bank notes had to stand in lengthy queues, and several deaths were linked to the inconveniences caused due to the rush to exchange cash.

Exchange of old notes

The Reserve Bank of India stipulated a window of fifty days until 30 December 2016 to deposit the demonetized banknotes as credit in bank accounts. The banknotes could also be exchanged over the counter of bank branches upto a limit that varied over the days:

1. Initially, the limit was fixed at 2,000 per person from 8 to 13 November.



2. This limit was increased to 4,500 per person from 14 to 17 November.
3. The limit was reduced to 2,000 per person from 18 November.

All exchange of banknotes was abruptly stopped from 25 November 2016.

International airports were also instructed to facilitate an exchange of notes amounting to a total value of 5,000 for foreign tourists and out-bound passengers.

Withdrawal Limits

Cash withdrawals from bank accounts were restricted to 10,000 per day and 20,000 per week per account from 10 to 13 November. This limit was increased to 24,000 per week from 14 November 2016.

A daily limit on withdrawals from ATMs was also imposed varying from 2,000 per day till 14 November, and 2,500 per day till 31 December. This limit was increased to 4,500 per day from January 1, and again to 10,000 from January 16, 2017. Limits placed vide the circulars cited above on cash withdrawals from Current accounts/ Cash credit accounts/ Overdraft accounts stand withdrawn with immediate effect. The limits on Savings Bank accounts will continue for the present and are under consideration for withdrawal in the near future. Limits vide the circulars cited above placed on cash withdrawals from ATMs stand withdrawn from February 1, 2017. However, banks may, at their discretion, have their own operating limits as was the case before November 8, 2016.

Facts and Figures

Up to 97% of the demonetized 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 demonetized. This is against the government's initial estimate that 3 trillion would not return to the banking system.

Of the 15.4 trillion demonetized in the form of 500 and 1000 bank notes of the Mahatma Gandhi Series, 9.2 trillion in the form of 500 and 2000 bank notes of the Mahatma Gandhi New Series has been re circulated as of 10 January 2017, two months after the demonetization.

Objective

1. To removing black money from the country in India
2. To stopping Illegal trading and curbing fake notes
3. To stopping corruption in Indian economy and Terror funds
4. To the election of various states in India

History of Demonetization

History: The French were the first to use the word Demonetize, in the years between 1850 -1855. Since then many countries have used the word and the policy with immense restriction and discomfort, for it disrupts economics and population at large. India has demonetized before: **First time** on 12 Jan 1946 (Saturday), **second time** on 16 Jan 1978 (Monday), **Third time** on 8th November 2016 (Tuesday).

First time: the measure did not succeed, as by the end of 1947, out of a total issue of Rs. 143.97 crores of the high denomination notes, notes of the value of Rs. 134.9 crores were exchanged. Thus, notes worth only Rs. 9.07 crores were probably 'demonetized', not having been presented. The results of the demonetization measure were summed up by Sir Chintaman, in his Dadabhai Naoroji Memorial Prize Fund Lectures, delivered at Bombay in February 1957, as under : It was really not a revolutionary measure and even its purpose as a minatory and punitive gesture towards black-marketing was not effectively served. In the end, out of a total issue of Rs.143.97 crores, notes of the value of Rs.134.9 crores were exchanged up to the end of 1947 as mentioned in the Report of the Board of Directors of the Reserve Bank. Thus, notes worth only Rs.9.07 crores were probably "demonetized", not having been presented. It was more of "conversion", at varying rates of profits and losses than "demonetization".

Second time: The Finance Minister H.M. Patel in his budget speech on 28 Feb 1978 remarked: The demonetization of high denomination bank notes was a step primarily aimed at controlling illegal transactions. It is a part of a series of measures which Government has taken and is determined to take against anti-social elements.

As the FM did not say anything about the success of the exercise, one can almost guess that it did not create much impact like in 1946.

In January 1946, banknotes of 1000 and 10000 rupee were withdrawn and new notes of 1000, 5000 and 10000 rupee was introduced in 1954. The Janata Party coalition government had again demonetized banknotes of 1000, 5000 and 10000 rupee on 16 January 1978 as a means to curb counterfeit money and black money.



Third time: The whole country was taken aback when Prime Minister Narendra Modi on November 8 announced that the currencies in the denominations of Rs 500 and Rs 1,000 will be invalid post midnight. However, the lower denomination –Rs 10, Rs 20, Rs 50, Rs 100 and coins –will be valid. He further announced that new notes of Rs 500 and Rs 2,000 would introduce shortly, Thus, giving millions of Indians a panic attack.

But what do you think was this the first time an Indian currency was banned of a sudden?

On Nov. 8, 86% of India's currency was nullified in a great demonetization effort that aimed to clean out the black market's cash supply and counterfeit notes which completely disrupted the social, political, and economic spheres of the world's second largest emerging market. All 500 and 1,000 rupee notes were instantaneously voided, and a 50 day period ensued where the population could (ideally) redeem their canceled cash for newly designed 500 and 2,000 rupee notes or deposit them into bank accounts.

India has done this before. In 1946, all 1,000 and 10,000 rupee notes were recalled. In 1978, 1,000, 5,000, and 10,000 rupee notes were demonetized.

Advantage and Disadvantage of Demonetization

It's has been over 60 days since government demonetized 500 and 1,000 rupees notes. It was a major decision which had its impact on all sections of the society. Demonetization has given a new direction to the way people do monetary transactions in India. Just like a coin has a flip side, demonetization too has its advantages and disadvantages. As one can see from the above that demonetization has both advantages and disadvantages. Demonetization alone cannot fight parallel economy and eliminate black money. Several other measures are required by the government to change the economy for good.

Advantages of Demonetization

1. A major advantage is that demonetization helped the government track black money. A large sum of black money was kept hidden by tax evaders. Demonetization helped government uncover huge amount of unaccounted cash. According to estimates made by RBI, people have deposited more than rupees 3 lakh crores worth of black money in the bank accounts. This has helped the government in slowing down the plague of parallel economy.
2. A major reason behind demonetization was that a big part of black money was being used for funding terrorism, gambling, in inflating the price of major assets classes like real estate, gold and other social evils. Demonetization is acting as an effective countermeasure against such activities. Now all such activities will get reduced for some time and also it will take years for people to generate that amount of black money again and hence in a way it helps in putting an end this circle of people doing illegal activities to earn black money and using that black money to do more illegal activities.
3. Another benefit is that due to people disclosing their income by depositing money in their bank accounts government gets a good amount of tax revenue which can be used by the government towards the betterment of society by providing good infrastructure, hospitals, educational institutions, roads and many facilities for poor and needy sections of society.

Disadvantages of Demonetization

1. The biggest disadvantage of demonetization has been the chaos and frenzy it created among common people initially. Everyone was rushing to get rid of demonetized notes while inadequate supply of new notes affected the day to day budgets of citizens. Banks and ATMs witnessed long queues while small businesses suffered temporary financial losses. The situation was even worse in rural India where people struggled to exchange and withdraw cash due to lack of enough number of banks and ATMs in their vicinity.
2. Another disadvantage is that destruction of old currency units and printing of new currency units involve costs which has to be borne by the government and if the costs are higher than benefits then there is no use of demonetization.
3. Another problem is that this move was targeted towards black money but many people who had not kept cash as their black money and rotated or used that money in other asset classes like real estate, gold and so on were not affected by demonetization.

Conclusion

The demonetization move could change the face of the Indian economy. This is a step which will make a positive difference, if the transition challenges get handled well by the administration, From the findings of this research it is evident that the impact of demonetization on society is highly debatable. Resulting disruption in the real economy stemming from this move is very significant and potentially fatal for some vulnerable sections of society. Whereas, on one hand proponents present its



bright side in terms of a revolutionary move, the opponents condemn its ugly side to be unfavorable for the economy at large. However, it can be said that demonetization can only be a component of an inclusive approach to confront black money and corruption, and is expected to enforce considerable discomfort due to its adverse effect on low-end employment and GDP. Advancements on these would only lead to an actual contribution to plummeting the generation of black money in future.

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