

DEMONEZITIZATION: PROS AND CONS

Dr Ajoy Mitra
Dept of Finance
Dispur College
ajoy444@gmail.com

Abstract

The demonetisation of high value currency denominations featuring Rs 500 and Rs 1,000 notes were banned effective 8th November 2016 was a bold step by Indian government. Demonetization of currency means discontinuity of the said currency from circulation and replacing it with a new currency. It has deeply impacted Indian economy in various ways. But it has been widely acclaimed as positive decision taken for the benefit of the citizens. But India may be successful this time because all other countries tried it before the age of digitalization. Modi tried this with immense care and preparation beforehand and not it was ever an act just on spur of moment. He has been working very hard for the last two years to create bank accounts for all-the ranks and the common folk. This paper discussed about the history of demonetisation and its various pros and coons

Keywords—Government of India, demonetize, discontinuity, new currency.

Introduction:

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.

To understand demonetization, we have to understand currency. Currency is a legal tender guaranteed by sovereign. It also demonstrates authority of a sovereign. In olden days it was representative of the king and his authority as sovereign. Higher the number of state accepting the currency of a king, higher was his stature among kings.

This hasn't changed since then. Today currency, apart from being the means of transaction represents the identity and independence of a country. Universal acceptance of dollar/ pound and euro as international currency shows the clout that these countries have on businesses worldwide. So, every time, a king acquired a new state, or a new king inherited the throne, he resorted to demonetized the coins of previous kings. In modern world, after the paper currency was introduced, the demonetization has been a routine phenomenon primarily to take currency, which is no longer in use, out of circulation like lower or exceptionally higher denomination currency. 2nd most common reason for demonetization is counterfeit currency. New currency which better demonstrates the spirit of sovereign nation usually keeps replacing the old currency.

Currency demonetization is almost as old as the currency. The biggest demonetization phenomenon of modern currency was introduction of Euro, when all EU nations demonetized their currency and started using Euro.

In modern world many countries including developed and developing countries have done it like US, Australia, USSR, India, Pakistan, Myanmar multiple African nations like Nigeria, Zimbabwe and Ghana. Except USA and Australia all other countries failed miserably due to various political reasons.

Country: – **United States of America**

- Step Taken: – 1969
- Due to black money existence in the nation, the country was losing its sheen built on Silicon Valley and the so-called even today existent American Dream. In 1969, US President Richard Nixon announced all bills above \$100 null and void.
- Status: – Success. Even today \$100 bill is the maximum available for circulation.

Country: – **Australia**

- Step Taken: – 1996
- The government to the curb black money crisis and improve security features on the notes, they withdrew all paper-based notes and replaced them with long life polymer-based notes of the same denomination.
- Status: – Success. This improved the life of the bills and helped in making Australia a business friendly country, despite the initial costs incurred to manufacture polymer-based notes.

Indian Scenario:

The demonetisation of high value currency denominations featuring Rs 500 and Rs 1,000 notes were banned effective 8th November 2016 midnight by Prime Minister Narendra Modi in a televised announcement. This step may have shocked the nation, but the prime minister's move was hardly unprecedented. India has pulled select denominations of its currency twice before. The first was when Rs1,000, Rs5,000, and Rs10,000 notes were taken out of circulation in January 1946, a year and a half before the country won independence from the British. 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. Then, in 1977, the Janata Party coalition government came into power. A year into the government's term, the then Prime minister Mr. Morarji Desai was more bullish about cracking down on counterfeits and black money. The High Denomination Bank Notes (Demonetisation) Act, instated by the ruling party on Jan. 16, 1978, deemed the Rs1,000, Rs5,000 and Rs10,000 notes illegal for the second time.

But India may be successful this time because all other countries tried it before the age of digitalization. Modi tried this with immense care and preparation beforehand and not it was ever an act just on spur of moment. He has been working very hard for the last two years to create bank accounts for all-the ranks and the common folk. With an estimated half of our population having bank accounts as of now, this seems right that every family has at-least one bank account for making online transactions possible for the family.

.Here is a list of the major events of the demonetisation months i.e. November & December:

Date	What happened
Nov.08	Modi declares the Rs500 and Rs1,000 notes invalid. Exchange of currency up to Rs4,000 allowed at banks, ATM withdrawal limit set at Rs2,000.
Nov.10	Banks reopen after a day. Massive queues ensue as millions line up to deposit or exchange old currency.
Nov.12	Deaths attributed to waiting in queues begin to be reported. The Sensex registers the biggest single-day fall in nine months.
Nov.13	Currency exchange limit raised to Rs4,500 and ATM withdrawal to Rs2,500.
Nov.15	Banks asked to use indelible ink marks on those exchanging money, election commission raises concerns.
Nov.16	Parliament session begins; opposition parties corner the government over the sufferings of the poor.
Nov.17	Currency exchange limit lowered to Rs2,000.
Nov.18	India's supreme court says many are "frantic" over demonetisation.
Nov.22	RBI says banks have received Rs 5.3 lakh crore in deposits since Nov. 08.
Nov.24	Old notes can now only be deposited at banks and not exchanged.
Nov.27	RBI governor Urjit Patel justifies demonetisation, says the new notes are difficult to counterfeit.
Nov.30	RBI limits the withdrawals from Jan Dhan accounts to Rs10,000 per month.
Dec.08	The Modi government announces incentives to initiate people into digital payments. Offers discounts on digital payments.
Dec.19	The RBI says deposits above Rs5,000 in old currency to be permitted only once until Dec. 30, the last date for depositing old notes.
Dec.21	The RBI withdraws the restrictions on depositing cash above Rs5,000. Allows multiple transactions until Dec. 30 provided they are know your customer-compliant
Dec.31	Narendra Modi thanks Indians while addressing the nation on new year's eve. Says "firm resolve" and "infinite patience" characterises 125 million Indians.

Meanwhile, the government's stated objective changed. In the past few weeks, rather than harping on the curbing of black money, it has increasingly used demonetisation to push India towards becoming a cashless economy. Asia's third-largest economy has one of the world's highest cash-to-GDP ratios—nearly 12% compared to around 3.9% in Brazil and 3.7% in South Africa.

On Dec.08, the Modi government offered a slew of incentives to push Indians towards digital payments. This included discounts on the purchase of fuel, railway tickets, and insurance policies. It later launched the Bharat Interface for Money (BHIM) app for “fast, secure and reliable” cashless payments. “It's a part of our campaign to incentivise people, to persuade people,” Arun Jaitley, India's finance minister, said during a press conference. “I think incentivising people to go digital and shed cash, to the extent it is possible, is a good development for the economy.”

Impact on economy:

Fast-moving consumer goods (FMCG) firms have reported lower sales, especially in rural areas. Some 90% of the FMCG market in India comprises small mom-and-pop stores, heavily reliant on cash sales. And 60% of small traders have already seen a drop in sales post-demonetisation, according to market research firm Nielsen.

In rural areas, where internet penetration is limited, cash is often the only mode of payment. People in the hinterlands have struggled to access cash—there are 7.8 bank branches per 100,000 persons in rural India—and this, in turn, has affected wage and loan disbursal in these areas.

Besides microeconomic headwinds, the overall Indian economy, too, has seen some effects. GDP growth in the world's fastest-growing major economy is estimated to take a hit in the coming quarters. Most analysts, apart from the RBI itself, have revised their GDP estimates. The Indian central bank, too, has lowered its forecast for 2017 by 0.5% to 7.1%.

In fact, brokerage Ambit Capital slashed its estimate for India's GDP growth to just 3.5% for fiscal 2017. Demonetisation, it said, would badly hit the informal economy which forms 40% of India's GDP.

Certain sectors, especially the cash-intensive ones, would suffer more than others. For instance, real estate, manufacturing, and small and medium-sized businesses are already seeing a major drop in activity. Realty demand has slumped and diamond cutters and polishers have stopped operations.

Here's how demonetisation has affected the various sectors:

Sectors	Impact
FMCG	Sales dropped, rural demand hit.
Auto	Sales down in November, consumers postpone purchases, impact seen more in rural areas.
Banking	Deposits rise, lenders could cut interest rates.
Real estate	Short-term demand falls, transparency could increase in the long run.
Diamond cutting & polishing	No wages for workers, industries in Surat hit with temporary halt in operations.
Manufacturing	The November purchasing managers index for manufacturing dropped as production, buying activity, and new orders were hit.

Pros: Since the decision to ban high value currency notes was taken in early November, the government has tried to portray the brighter side of the note ban and its benefits on the economy in the long run. The decision to ban high value notes was taken to weed out black money and counterfeit notes from the system which has been deep-rooted in the economy for the past many decades.

With 86 percent of the total money circulation wiped out from the system, the government plans to keep a tight leash on the corruption front. According to Ambit Capital report, the share of the informal economy in India could shrink from 40 percent to 20 percent and the formal organised sector will gain market share.

The sustained crackdown on black money will also prevent people from parking their savings in physical assets such as gold and real estate, and instead boost the flow of savings into the financial system. With the quantum increase in financial savings, the cost of debt capital in India should fall. Further, as saving rate increases, lending rates are likely to fall in the line. Through the demonetisation exercise, the government has been pressing hard to become a cashless economy and is encouraging more and more people to adopt the digital payments system for their transactions. The government wants people with smartphones to use the United Payments Interface (UPI) app for a cashless transaction. Besides banks, online wallet companies including Paytm, MobiKwik and Free-Charge, too, are promoting their online products and wooing customers to get away from cash-based transactions.

In the aftermath of demonetisation, reports also suggest that housing prices in 42 major cities across India could drop by up to 30 percent over the next 6-12 months.

Cons: Although several advantages of demonetisation rolling into the economy could be far-fetched, there are immediate challenges the economy is already staring at. Following the decision to ban the currency notes, the government's lack of preparedness to deal with cash availability has hit the common man really hard. Despite the government's assurance to improve cash availability on a daily basis, several banks and ATMs across the country continue to dispense little or no cash.

People in villages and semi-urban areas are worst hit as majority of the transactions are done through cash. The government's constant flip-flops on withdrawal and deposit limits at bank branches and ATMs have put people in complete disarray. With one month past the note ban move, the problem doesn't seem to be fully resolved as banks continue to face cash crunch.

The bigger threat arising out of demonetisation is the impact on the country's economic growth. While brokerage Ambit Capital created shock waves by predicting that GDP growth will fall to 5.8 percent in 2017-18 from 7.3 percent estimated earlier, former Prime Minister Manmohan Singh, also an economist, echoed concerns by suggesting that demonetisation could contract the GDP by as much as 2 percent.

According to CPM's Sitaram Yechury, since 8 November, four lakh jobs have vanished, and more than 31.9 million people employed in the textile sector or "government" sectors have not been getting wages. Construction and allied sectors, jewellery, textiles and real estate are some sectors where job losses, if not already happening, are imminent.

Similarly, 20-25 percent of the roughly 2.5 lakh workers in the leather industry have been adversely affected as they are daily wage workers. The industry has been hit particularly hard as 90 percent of the units are small and medium enterprises. In the jewellery sector, 15-20 percent of workers, who are paid daily, too, have been affected.

Economist Pronob Sen has also warned that a virtual shutdown of India's informal sector could spell doom for employment.

Recently, the July-September growth numbers of 7.3 percent also came below analysts' estimates. A day before, the Reserve Bank of India in its policy statement cut down growth forecast to 7.1 percent from 7.6 percent earlier for the current fiscal year.

In order to understand demonetization better let's look at advantages and disadvantages of demonetization

Advantages of Demonetization

1. The biggest advantage of demonetization is that it helps the government to track people who are having large sums of unaccounted cash or cash on which no income tax has been paid because many people who earn black money keep that money as cash in their houses or in some secret place which is very difficult to find and when demonetization happens all that cash is of no value and such people have two options one is to deposit the money in bank accounts and pay taxes on such amount and second option is to let the value of that cash reduced to zero.
2. Since black money is used for illegal activities like terrorism funding, gambling, money laundering and also inflating the price of major assets classes like real estate, gold and due to demonetization 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 is that once people in the country gets to know about it than initially for few days there is chaos and frenzy among public as everybody wants to get rid of demonetized notes which in turn sometimes can lead to law and order problem and chaotic situation especially in banks and ATMs which are the only medium to change the old currency units to new currency units.
2. Another disadvantage is that destruction of old currency units and printing of new currency new 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 majority of times this move is targeted towards black money but if people have not kept cash as their black money and rotated or used that money in other asset classes like real estate, gold and so on then there is no guarantee that demonetization will help in catching corrupt people.

Looking Ahead:

Traditionally Indian people have a very stereotyped mindset. We the educated suppose that the uneducated cannot do online transactions. Uneducated people to the tune of crores do ATM transactions and WhatsApp today because they need it or they want to. If they are persistent, they will be able to do online transactions too. What the government should ensure is to circulate very easy -to -use and yet safe apps in the market and that's it.

Fake currency is as old as the beginning of first coinage in Greece. It means that even the earliest coin in our recorded history was also faked. Today easy printing technology has made the job really very easy. But possibly India encounters the problem in a much greater dimension than any other countries. There is sustained and unabated flow of fake currency from at-least two countries bordering us and they cannot be stopped as that is motivated by jihad which is perennial and as stable as the rocks and the mountains. Hence for India at least fake currency is a real great issue undermining public confidence on our very money system. A single fake note is detected and a thousand good currency notes are naturally brought into suspicion.

True, it is a real tough job to make all people go online but the benefits are innumerable great and were certainly worth trying. May be India will be successful and many other countries will follow in footsteps by courtesy of the immense efficacy and prospect of digitalisation

Conclusion:

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 get income based on their daily work and those who don't have the digital transaction culture. Overall economic activities will be dampened in the short term. But the unmeasurable benefits of having more transparency and reduced volume of black money activities can be pointed as long term benefits.

As one can see from the above that demonetization has both advantages and disadvantages and it is up to the government to see and analyze all the pros and cons and then decide whether it is beneficial to go ahead with more demonetization in future or not.

At the end of day we have to keep in mind the fact that what the government is doing is for the people and to make a corruption free India. We all know one thing that to what extent corruption exists in India so to clean this mess up a revolutionary step had to be taken and that's what is being done and it will take some hardships to clean the mess (corruption) that already exists in India

Data Source:

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