



## The impact of Demonetization on various aspects

Dr. Anuradha Alluri  
Reader in Economics, B.V.K. College,  
Visakhapatnam

**Abstract:** After Modi's announcement, the Governor of the Reserve Bank of India, Sri Urjit Patel, and Economic Affairs secretary, Sri Shaktikanta Das explained in a press conference that one purpose of the action was to fight terrorism funded by counterfeit notes, while the supply of notes of all denominations had increased by 40 percent between 2011 and 2016, the ₹500 and ₹1,000 banknotes increased by 76 percent and 109 percent, respectively, owing to forgery. In terms of volume, the report stated that 24% of the total 9026.6 crore banknotes were in circulation. In June, the Government of India had devised an Income Declaration Scheme, that and lasted till 30 September 2016, providing an opportunity to citizens holding black money and undeclared assets to avoid litigation and come clean by declaring their assets, paying the tax on them and a penalty of 45% thereafter. The plan to demonetize the rupee 500 and rupee 1000 bank notes began prior to six months, and was kept highly confidential with only limited people aware of it completely. The processes and primary preparations for printing the new 500 and rupee 2000 bank notes began in early-May. The cabinet was informed about the demonetization on 8 November 2016 in a meeting called by the Prime Minister of India Sri Narendra Modi which was followed by Modi's public announcement about the demonetization in public media of television. In Malda, a district believed to be a transit-point for fake Indian currencies, a large sum of cash deposits in dormant accounts was also reported. According to The Economic Times, more than 80 per cent of fake currency in India originates from Malda district in West Bengal.

**Key words:** fake currency, demonetization, Hawala

### Introduction

The previously the then governments try to demonetization, though similar one well happened 70 years back, i.e., on January 12, 1946 and 16<sup>th</sup> January, 1978, on the same plea what the present government to do. Coming to the present, on 8 November 2016, Prime Minister of India Sri Narendra Modi announced the demonetization in an unscheduled live televised address to the nation at 20:15 hrs. In the announcement, Sri Modi declared circulation of all ₹500 and ₹1,000 banknotes of Mahatma Gandhi Series as invalid effective from the

midnight of the same day, and announced the issuance of new ₹500 and ₹ 2,000 banknotes of Mahatma Gandhi New Series in exchange for the old banknotes. The aim behind the government action was to combat tax cheating counterfeiting and corruption.

### ANALYSIS

#### Human trafficking

Nobel laureate Kailash Satyarthi and others working to fight human trafficking said that the note ban had led to a huge fall in sex trafficking. Sri Satyarthi said the demonetization would



be effective in combating exploitation of children as well as corruption and would be a great obstacle to traffickers. However, 2 months later he expressed his disappointment on Rs 2000 notes being pushed into human trafficking in absence of other concrete steps.

### **Radical groups**

The Demonetization has badly hit Maoist and Naxalites as well. The surrender rate has reached its highest since the demonetization is announced. It is said that the money these Organizations have collected over the years have left with no value and it has caused them to reach to this decision. The move also reportedly crippled Communist guerrilla groups (Naxalites) financing through money laundering. According to Chhattisgarh Police, demonetization has affected the Naxalite activities. It is reported that insurgents have stashed more than ₹70 billion in the Bastar region. While Sri Manohar Parrikar claimed that the move has also helped in reducing the incidents of stone-pelting in the Kashmir valley, his claim has been later disputed.

### **Hawala**

Mumbai Police reported a setback to Hawala operations. Hawala dealers in Kerala were also affected. The Jammu and Kashmir Police reported the effect of demonetization on hawala transactions of separatists.

### **Railways**

As of November 2016, Indian Railways did not have the option to make payment with cards at the counters. After the demonetization move, the government announced to make card payment options available at railway counters in

the country. The railways placed an order for 10,000 card reader machines in January 2017.

### **Cash Shortage**

The scarcity of cash due to demonetization led to chaos, and most people holding old banknotes faced difficulties exchanging them due to endless queues outside banks and ATMs across India, which became a daily routine for millions of people waiting to deposit or exchange the ₹500 and ₹1000 banknotes since 9 November. ATMs were running out of cash after a few hours of being functional, and around half the ATMs in the country were non-functional.

The cash shortage was still ongoing in the month of April 2017, i.e., five months after the demonetization.

### **Deaths**

Around 250 people were reported to have died from standing in queues for hours to exchange their old banknotes. Deaths were also attributed to lack of medical help due to refusal of old banknotes by hospitals.

### **Stock market crash**

As a combined effect of demonetization and US presidential election, the stock market indices dropped to an around six-month low in the week following the announcement. The day after the demonetization announcement, BSE SENSEX crashed nearly 1,689 points and NIFTY 50 plunged by over 541 points. By the end of the intraday trading section on 15 November 2016, the BSE SENSEX index was lower by 565 points and the NIFTY 50 index was below 8100 intraday.



### Transportation disruption

After the demonetization was announced, about 800,000 truck drivers were affected with scarcity of cash, with around 400,000 trucks stranded at major highways across India were reported. While major highway toll junctions on the Gujarat and Delhi-Mumbai highways also saw long queues as toll plaza operators refused the old banknotes.

Sri Nitin Gadkari, the Minister of Transport, subsequently announced a suspension of toll collections on all national highways across India until midnight of 11 November, later extended until 14 November and again until midnight of 18 November, and yet again till 2 December.

### Agriculture

Transactions in the Indian agriculture sector are heavily dependent on cash and were adversely affected by the demonetization of ₹500 and ₹1,000 banknotes. Due to scarcity of the new banknotes, many farmers have insufficient cash to purchase seeds, fertilisers and pesticides needed for the plantation of rabi crops usually sown around mid-November.

### Fall in Prices of Food Products

The demonetization led to unavailability of cash to pay for food products. The reduction in demand that arose in turn led to a crash in the prices of crops. Farmers were unable to recover even the costs of transportation from their fields to the market from the low prices offered. The prices dropped as low as 50 paise per kilo for tomatoes and onions. This forced the farmers across the country to dump their products in desperation. Some farmers resorted to

produce in protest against the government.

### Business

By the second week after demonetization of ₹500 and ₹1,000 banknotes, cigarette sales across India witnessed a fall of 30–40%, while E-commerce companies saw up to a 30% decline in cash on delivery (COD) orders.

**Real Estate:** The most of Indian business environment has been tremendously shaken up by the demonetization of the currency. The real estate sector will definitely be affected by the demonetization exercise as it has traditionally seen a very high involvement of block money and cash transactions. The poor sales leading to almost flat and plot prices and high sold inventory have all colluded to keep real estate sector away from fulfilling its potential and provide necessary residential stability to average citizens.

### Digital transactions

Several e-commerce companies hailed the demonetization decision as an impetus to an increase in digital payments, hoping that it would lead to a decline in COD returns which could cut down their costs.

The demand for point of sales (POS) or card swipe machines increased. E-payment options like PayTM and Instamojo Payment Gateway, PayUMoney also saw a rise. According to data of Pine Labs, the demand for its POS machines doubled after the decision. The company stated that the debit card transactions rose by 108% and credit card transactions by 60% on 9 November 2016.

After peaking in December 2016, digital transactions declined from January 2017



onwards, thus thwarting the objective of increasing digital payments through demonetization.

### **Forecast of GDP growth rate**

Global analysts cut their forecasts of India's GDP growth rate due to demonetization. India's GDP in 2016 is estimated to be US\$2.25 trillion, hence, each 1 per cent reduction in growth rate represents a shortfall of US\$22.5 billion (Rs. 1.54 lakh crores) for the Indian economy. According to Society Generale, India's quarterly GDP growth rates would drop below 7% for an entire year at a stretch for the first time since June 2011

### **Drop in industrial output**

There was a reduction in industrial output as industries were hit by the cash crisis. The Purchasing Managers' Index (PMI) fell to 46.7 in November from 54.5 in October, recording its sharpest reduction in three years. The growth in eight core sectors such as cement, steel and refinery products, which constitute 38% of the Index of Industrial Production (IIP), was only to 4.9 percent in November as compared with 6.6 percent in October.

### **Job losses**

There was a loss of jobs due to demonetization, particularly in the unorganised and informal sector and in small enterprises. Labour union jobs were crashed

### **Municipal and local tax payments**

As the use of the demonetized notes had been allowed by the government for the payment of municipal and local body taxes, it led to people using the demonetized ₹500 and ₹1,000 notes to pay large amounts of outstanding and

advance taxes. As a result, revenue collections of the local civic bodies jumped. The Greater Hyderabad Municipal Corporation reported collecting about ₹1.6 billion in cash payments of outstanding and advance taxes, within 4 days.

The tax collection by local bodies have surged over 260% and more than 15000 crore more after 14 days of demonetization. The total indirect tax collection rose to 14.2% only in the month of December according to Finance Minister Sri Arun Jaitley

### **Gold purchases**

In Gujarat, Delhi and many other major cities, sales of gold increased on 9 November, with an increased 20 to 30% premium surging the price as much as ₹45,000 from the ruling price of ₹31,900 per 10 grams. Income Tax officials raided multiple branches of Axis Bank and found bank officials involved in money laundering acts, exchanging old notes for gold.

### **Donations in temples**

In India, the cash deposited into *hundis*, or cash collection boxes in temples and gurudwaras are exempted from inquiry by the tax department. This exemption is sometimes misused to launder money. After the note ban, there was a spike in donations in the form of the demonetized notes in temples. Authorities of Sri Jalakanteswarar temple at Vellore discovered cash worth ₹4.4 million from the temple hundi in the form of defunct notes.

### **Multiple bank transactions**

There have been reports of people circumventing the restrictions imposed on exchange transactions by conducting



multiple transactions at different bank branches and also sending hired people, employees and followers in groups to exchange large amounts of banned currency at banks. In response, the government announced that it would start marking customers with indelible ink. This was in addition to other measures proposed to ensure that the exchange transactions are carried out only once by each person

### **Railway bookings**

As soon as the demonetization was announced, it was observed by the Indian Railways authorities that a large number of people started booking tickets particularly in classes 1A and 2A for the longest distance possible, to get rid of unaccounted cash. A senior official said, "On November 13, 42.7 million passengers were nationally booked across all classes. Of these, only 1,209 were 1A and 16,999 for 2A. It is a sharp dip from the number of passengers booked on November 9, when 27,237 passengers had booked tickets in 1A and 69,950 in 2A."

The Railways Ministry and the Railway Board responded swiftly and decided that cancellation and refund of tickets of value ₹10,000 and above will not be allowed by any means involving cash. The payment can only be through cheque/electronic payment. Tickets above ₹10,000 can be refunded by filing ticket deposit receipt only on surrendering the original ticket. A copy of the PAN card must be submitted for any cash transaction above ₹50,000. The railway claimed that since the Railway Board on 10 November imposed a number of restrictions to book and cancel tickets, the number of people booking 1A and 2A tickets came down.

### **Backdated accounting**

The Enforcement Directorate raided several forex establishments making back dated entries. Money laundering using backdated accounting was carried out by co-operative banks, jewelers, sellers of iPhones, and several other businesses.

### **Accepting deposits without PAN**

In March 2017, it was alleged that more than 1 lakh crore (in high value deposits of more than 2.5 lakh) were deposited without any record of PAN

### **Income Tax Raids**

The Finance Ministry instructed all revenue intelligence agencies to join the crackdown on forex traders, hawala operators and jewellers besides tracking movement of demonetizncy notes. Income Tax departments raided various illegal tax-evasive businesses in Delhi, Mumbai, Chandigarh, Ludhiana and other cities that traded with demonetised currency large sum of cash in defunct notes were seized in different parts of the country. In a period of four months from 9 November 2016 to 28 February 2017, CBDT claims to have detected an undisclosed income of over ₹93.34 billion through more than 2,362 search, seizure and survey actions by Income Tax department.

**Seizures of ₹2000 notes** : Huge amounts of cash in the form of new notes were seized all over the country after the demonetization.

### **CONCLUSION**

The decision on demonetisation met with mixed reactions of praising and as well as allegations & criticism from several



heads/chair persons/CEOs of different banks, Businessmen, Founders of Software, Politicians, Chief Ministers of various states, former Chief Election Commissioner and Social Activist.

The opinion of the masses varied both ways on social media sites like Twitter

and face book. By and large, international response was positive which saw the move as a bold crackdown on corruption. However, the recent election results of UP, Uttarakhand, Manipur and Goa proves that the Demonetization has given positive result.

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