



Impact of Demonetisation on Indian Economy

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Abstract:

Indian Demonetisation has impacted the economy remarkably and lots of repercussions were recorded, few sectors of the economy are hoping to get positive impact whereas few fear to get hard hit. On 8th November, 2016 our Hon. Prime Minister Shri Narendra Modi, announced demonetisation decision. Sudden announcement of demonetisation has resulted in to insecurity and fear among peoples. There were huge crowds outside ATMs across the country as people lined up to withdraw currency of smaller denomination. Media- news channels and newspapers were projecting suffering of people as well as benefits of demonetisation. This research article therefore, is an attempt to find out ground reality and how demonetisation had impacted the different sectors of Indian Economy.

Keywords: *Indian Demonetisation, Indian economy*

1. Introduction

Demonetization is an established practice in monetary policy to tackle black money. It was meant to be suddenly implemented. In the past, demonetization has taken place twice but it failed. It's a radical monetary step in which a currency unit's status as a legal tender is declared invalid. This is usually done whenever there is a change of national currency, replacing the old unit with a new one. For example a step was taken by European Monetary Union nations, when they decided to adopt Euro as their currency. However, the old currencies were allowed to convert into Euros for a period of time in order to ensure a smooth transition through demonetisation. In India's case, the move has been taken to curb the menace of black money and fake notes by reducing the amount of cash available in the system. It is also interesting to note that this was not the first time the Government of India has gone for the demonetisation of high-value currency. It was first implemented in 1946 when the Reserve Bank of India demonetised the then circulated Rs 1,000 and Rs 10,000 notes. The government then introduced higher denomination banknotes in Rs 1000, Rs 5000 and Rs 10000 in a fresh avatar eight years later in 1954 before the Morarji Desai government demonetised these notes in 1978.

2. Review of Literature

Katke et al (2015) studied the impact of demonetisation on Indian Automobile Industry with special reference to Car Industry. The study focused on only two dimensions of demonetisation impact- impact on sales and impact on consumer behaviour of car buyers. His study focused on short term results only. The study concluded that socio-economic factors are determinants for car purchase, demonetisation not only posed economic problem but also penetrated psychological fear. The study also concluded that car is no more luxury for Indians; it is necessary due to improper commutation facilities provided by many states across the country.

Undale and Gaggad (2016) studied the impact of demonetisation exactly after one month of demonetisation. Study is based on quantitative research approach, a structured questionnaire was developed and survey was conducted from the respondents. The study also attempted to capture gender wise, income wise and education wise differences in opinions towards demonetisation. The study concluded that people supported the demonetisation irrespective of their age, gender and income. Study was observed that daily wage worker affected very badly by the decision.

Kaur (2017) studied the impact of demonetisation on cashless payment system. The study is based on secondary data/ information and journals. The study concluded that cashless transaction system is reaching its growth day by day, as soon as the market become globalised and the growth of banking sector more and more the people moves from cash to cashless system.

Chowdhry (2017) studied the impact of post demonetisation on economy. The study focused on deposits growth, currency circulation, SLR security and credit growth. The study also concluded the impact of demonetisation on RBI balance sheet and different sectors of economy.

3. Objective of the Study

The study aims at:

- To study the Role of Demonetisation
- To examine the impact of Demonetisation on Indian Economy.

4. Research Methodology

The study is based on secondary sources of data/ information. Different books, newspapers and relevant websites have been consulted in order to make the study effective one. The study attempts to examine the impact of demonetisation on Indian Economy.

5. Demonetisation of Currency

Demonetization is the act of stripping a currency unit of its status as legal tender. It is the process of ceasing to produce and circulate particular forms of currency. This is necessary whenever there is a change of national currency. The old unit of currency is retired and replaced with a new currency unit. Legal tender is a medium of payment recognized by a legal system to be valid for meeting a financial obligation. It can be anything which when offered in payment extinguishes the debt. Coins and banknotes are usually defined as legal tender whereas personal cheques, credit cards, and similar non-cash methods of payment are not considered legal tender as debt obligations is not relieved until the payment is tendered. The higher denomination banknotes in Rs 1,000, Rs 5,000 and Rs 10,000 were reintroduced in the year 1954 and these banknotes were again demonetized in January 1978. So the last time demonetisation was done in India is almost 36 years ago. (Kaur, 2017)

6. Impact of Demonetisation on Indian Economy

Demonetisation impacted to every area in Indian Economy. Daily routine of people has changed a lot due to not exchange. Many peoples face difficulties due to sudden decline in the money supply. Even this decision lowered the GDP of the country and sever impact on cash based sectors like MSME, and downfall in stock market as well. Major impact of demonetisation on various fields is as follows:

Effect on GDP: The sudden decline in money supply and simultaneous increase in bank deposits was adversely impacted consumption demand in the economy in the short term. This, coupled with the adverse impact on real estate and informal sectors may lead to lowering of GDP growth (based on facts, 2016)

Effect on Bank: As directed by the Government, the 500 and 1000 Rupee notes, which at that time cease to be legal tender were to be deposited or exchanged in banks (subject to certain limits). This would automatically lead to more amounts being deposited in Savings and Current Accounts of commercial banks. This, in turn, would enhance the liquidity position of the banks, which would be later utilized further for lending purposes. (based on facts, 2016)

Effect on Parallel Economy: The currency of the aforementioned denominations constitutes around 86% of the total value of the currency in circulation. It was expected to remove black money from the economy as they would be blocked considering the holders would not be in a position to deposit the same in the banks, temporarily halt the circulation of large volumes of counterfeit currency and curb the funding for anti-social elements like smuggling, terrorism, espionage, etc. (based on facts, 2016)

Effect on ATM Withdrawals: In initial days, ATM which were not recalibrated had limit of withdrawal up to Rs 2000/- per day, whereas which were recalibrated had limit of withdrawal up to Rs 2500/- per day. (based on facts, 2016)

7. Sectoral Impacts of Demonetisation

On top Six Sectors:-

1. Auto & Auto Ancillary
2. Consumption
3. Banking
4. Hospitality and tourism
5. Oil & Gas
6. Real Estate

1. AUTO & AUTO ANCILLARY: Negative impact.

On passenger vehicles: short term impact due to purchase deferment, but demand will be revive in medium term. On tractors: demand to be materially impacted; plus questionable trade practise link over –invoicing to moderate. High impact on two wheeler sales as large percentage of rural two wheeler transactions are in cash. Commercial vehicles sales negatively impacted, 2nd hand truck sales, which had higher percentage of cash transaction will declined (both number of transaction and pricing)

2. CONSUMPTION: Neutral impact

Consumer Staples: Demonetisation benefited organised retail and hamper the market for local counterfeit goods. Consumer Durables: sales through online retails picked up relatively but sales of durables likely to be hampered over short-term, especially through unorganised channels as cash purchases.

3. BANKING: Marginally Positive Impact

Increased share of savings moving to banks; high CASA ratio (lower cost of funds). Lower bond yields resulting in high treasury gains (particularly PSU Banks). Government's moves to remove higher value banknotes from circulation would lead to a surge in deposits, allowing lenders to eventually lower landing rates and lower costs to service the sector's debt. With any sharp infusion of deposits and relatively limited avenues to lend, the credit deposits ratio for bans became unfavourable, and thus impact margin.

4. HOSPITALITY AND TOURISM: Negative Impact

Major gain for online forex marketplace companies like BookMyForex that have introduced online forex and have been promoted plastic money (forex travel cards) against online or electronic payments. Hotels demand impacted due to slow down in Domestic Travel and bad impact on Corporate Travel whereas inbound demand remained unaffected.

5. OIL & GAS: Neutral Impact

Temporary picked up in demand due to significant pre-buying of auto fuels. Refiners are to benefit from robust refining margins, capacity expansions and higher fuel marketing margin. Over medium term, demand, especially for personal transportation could be somewhat negatively impacted due to high proportion of cash transactions. City Gas; largely unimpacted , the demand for CNG got slightly hurt where cash transactions are high.

6. REAL ESTATE: Negative Impact

Demonetisation smashed the real estate market and it will result in 50% drop down and it will remain further 5 to 6 months. While the short term impact is negative, Experts are hoping that rates cut in coming months would boost sales. Demonetisation also coupled with Real Estate Regulation Act, Benami Act and GST, will transform the Real Estate sector in longer term. Key positive expected – increased transparency, improved investor confidence, better access to funding, higher FDI likely. Higher revenue for government in terms of higher registration cost.

8. Conclusion

The present study based on descriptive analysis examined the impact of Demonetisation on Indian Economy. The analysis revealed that different segments of the economy were influenced differently with the demonetisation move. Further, various sectors viz auto & auto ancillary Consumption, banking sector, hospitality and tourism, oil & gas and real estate sector were also affected differently. Negative impact of demonetisation was observed in case of hospitality and tourism and real estate sector. Neutral impact was observed in case of Oil and Gas and auto & auto ancillary sector. Whereas, in case of banking sector, marginally positive impact was observed due to the demonetisation.

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