

**Demonetization of Indian currency notes of ₹ 500 and ₹ 1,000 Notes: An
Analysis**

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Abstract: *In an important decision taken by the Government of India declared on 8th of November 2016 by honorable Prime Minister Shri. Narendra Modi that the five hundred and one thousand rupee notes will no longer be legal tender with effect from midnight of 8th November 2016. Soon after that it was declared by the Prime Minister of India that, RBI will issue new Two thousand rupee notes and Five hundred rupees note which will be placed in circulation from 10th November 2016. Notes of one hundred, fifty, twenty, ten, five, two and one rupee will remain legal tender and will remain unaffected by this decision. This measure has been taken by the Prime Minister of India with an intension to resolve the issue of corruption, black money and fake notes. This move is predicted to clear the formal economic system and disposal of black money from the same. The move by the government to demonetize ₹ 500 and ₹ 1000 notes by replacing them with new ₹ 500 and ₹ 2000 notes has taken the country with astonish. The move by the government is to tackle the menace of black money, corruption, terror funding and fake currency.*

Keywords: Demonetization, corruption, black money, currency issues, terror funding.

1.0 Introduction: Demonetization is a practice in which a series of currency notes will not be legal tender. The same thing happened with ₹ 500 and ₹ 1000 note demonetization. In history, previous Indian governments had demonetized bank currency notes. In January 1946, banknotes of ₹ 1,000 and ₹ 10,000 rupees were withdrawn and new bank notes of ₹ 1,000, ₹ 5,000 and ₹ 10,000 rupees were launched in 1954. The Janata Party alliance government had again demonetized banknotes of ₹ 1,000, ₹ 5,000 and ₹ 10,000 rupees on 16 January 1978 as a means of curbing counterfeit money and black money.

1.1 Research objectives:

1. To understand the process of demonetization
2. To find out the reasons for demonetization.
3. To analyze the outcomes of demonetization.

1.2 SCOPE OF THE STUDY

The scope of the study is limited only to demonetization in India effect from 8th November 2016 till date only.

1.3 LIMITATION OF THE STUDY

The study is limited to demonetization of Indian currency only. Other countries which initiated demonetization in their states are not taken into consideration while performing this study. Demonetizations occurred previously in India are also not included in this study. The data used is limited to extensively secondary form only.

1.4 RESEARCH METHODOLOGY

This research paper is based on the methodology in which pure secondary data is used from the secondary sources such as articles, research papers, annual reports, bank's websites, etc.

1.5 Review of Literature:

1. Ramdurg A. I., Basavaraj C.S. (2016) has emphasized on E-banking, E-commerce popularization to combat corruption and stock of black money.
2. According to Sharif Mohd. (2016) formal modes of payments such as debit and credit cards, net-banking and digital wallets should get a boost.
3. S. Harish Babu. (2016) says that citizens getting used to handling digital money, their trust in anything online and mobile will get a big boost to Indian Economy.

1.6 Process of Demonetization

Demonetization is an economic term which is used to signify the 'scrapping' of older currency notes and narrowing off their position of legal tender. There are two basic elements to this definition. One is 'scrapping of older currency notes' and 'position of legal tender'. prior to explanation of the same, what we require to identify is that a currency note or paper currency is fundamentally a legal document or a promissory note that merely suggests that the payee has 'promised' to pay that amount to the client. The similar note is printed on each currency note as well. This is authenticated by the chief of the Central Banks of the country and in case of India

the Governor of Reserve Bank of India is the signing Authority. This "status" of legal tender can be scrapped for a currency note, which shows that the currency note confiscates to be a "legal" form of monetary transactions and in effect loses the worth associated with that instrument. In other words, until and unless the old currency is legally exchanged at the designated centers, they are equivalent to nothing more than scraps of paper.

1.7 Reasons for Demonetizing

1. The extensive use of hard cash in high denominations has led to a fake rise in the price of goods and services.
2. A structural alteration plan which exhort against black money can bring about a variation in the intermediate term and the political gains.
3. Shifting towards a cashless economy with a larger focus on electronic transactions is being envisioned.
4. The elimination of hefty bills will compose several illegal and criminal actions more costly such as tax avoidance, drugs, human trafficking, extortion and terrorism.
5. Scaling back higher denominations will not finish the crime, but it will force the dissident economy to utilize riskier and less liquid payment systems.
6. In general elections malpractices such as distribution of black money through various sources as a part of campaign for sure shot victory of the candidates of certain political parties.
7. Drug, Smuggling, Terrorist and Maoists and other unlawful activities which harmed society in one or other way are also responsible for the break out of demonetization.

1.8 Impact of Demonetization

The effect of this decision is not going to be consistent across the economy. Sectors that have a larger cash constituent in their transactions will be hit harder, such as real estate, movie production, campaign finance, etc.

1.8.1 Short-term Impact

A. Negative Effect

1. Forthcoming orders as well as ongoing works in water, roads, railways and distribution and transmission sectors, too, will be hampered as compensations to labour is generally made in cash.
2. Remote areas with low number of bank accounts such as small villages would face supply-chain disruptions that could affect demand for consumer staples for a short period of time.
3. The demand impact of large consumer durable items such as clothing, home appliances, and the likes could also head south.
4. Procurement of agro inputs and agrochemicals; generally which is done via cash, too, could come down.
5. All metal businesses will be negatively impacted as a large part of trade in steel and other metals is carried on a cash basis at present.
6. The short-term debt servicing ability of small borrowers could be reduced, which may impact the asset quality as well as credit growth of microfinance companies.
7. Housing loan providing companies, too, could observe pressure on their credit value as well as growth, as fall in real estate prices would impact the loan against property (LAP) business.
8. Even e-commerce traders are also likely to feel the heat in the near- to medium-term. Cash on delivery forms anywhere between 70 and 90 per cent of e-commerce traders' revenues and, hence, can impact valuations of retail e-commerce traders.
9. Impact on purchase and sales of day to day used products of FMCG.
10. Immediate impact on public in general.
11. Impact on daily wage earners, other unorganized labourers and small traders.

B. Positive Effect

- Banks are supposed to gain meaningfully from implementation of demonetization, but over a period of time.
- Demonetization would also have the effect of lowering down deposit and lending interest rates further with no cut in the repo rate by RBI. An increase in deposit base will permit banks to lower the blended cost of funds.
- Growing use of plastic notes *viz.* credit/debit cards, net banking and other online payment mechanisms will be another positive, as these would not only lessen transaction costs but some of these could help earn some free income as well.
- In the nearby future, we are likely to eyewitness larger bank deposits, price corrections and better tax collection possibilities in the economy.
- Another sector which is likely to be benefited is mining from this move as this will harm illegal/unauthorized mining activities, supporting organized players such as Coal India, NMDC, among others.

1.8.2 Long Term Impact

- In the long run, this is an important positive surprise to the Indian economy and society.
- This will send a strong signal about India's anti-corruption drive if executed considerably; also it is very much likely to develop the country's reformist pose.
- It also provides an enhancement to the government's *financial inclusion drive*, making more and more households approach towards competent banking and secured payment systems.
- Tax revenue generation will rise.
- Bank deposits will increase which would support the economy. Demonetization will boost the growth of country's economy as it will enlarge and sanitize the formal gross domestic product.

1.8.3 Impact across sectors

1. New job opportunities would be created for the poorer sections of the society along with middle class and neo middle class communities.
2. Higher education, Healthcare and Real Estate would be brought into reach of the common man.
3. Terror funding shall be curbed.
4. Huge amount of counterfeit money would be brought into end circulation.
5. Due to demonetization black money would come under scrutiny of Income Tax department.

1.8.4 Effect on parallel economy

The elimination of these 500 and 1000 notes and substitution of the same with new 500 and 2000 Rupee Notes is projected to eradicate black money from the economy as they will be barren since the owners of the currency notes will not be in a position to deposit the same in the banks.

9.0 Conclusion

In spite of having many positive outcomes such as rise in tax to GDP, increased GDP growth, decreased inflation, increased financial savings; due to demonetization the root cause of black money move may not curb but would substantially reduce the illegal trades.

“This initiative deals with the ‘stock’ of black money but not essentially the manufacturing of black money unless some system is established to track the movement of the new high denomination currency notes.

However, such an abrupt and severe march by the government might discourage some, if not all categories of the society from creating new black money reserves.

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