



DEMONETIZATION- ITS RAMIFICATIONS ON INDIAN ECONOMY

CMA R .Venkatavarahan
Assistant Professor in Management
Srimad Andavan Arts and Science College Trichy 620005

ABSTRACT

Demonetization is defined in the dictionary as the act of stripping a currency unit of its status as legal tender. The Government of India decided to cancel the Legal Tender Status of Rs.1000 and Rs.500 denomination currency notes on 8th November 2016 with several objectives:

(i) flushing out black money, (ii) eliminate Fake Indian Currency Notes (FICN), (iii) to strike at the root of financing of terrorism and left wing extremism, (iv) to convert non-formal economy into a formal economy to expand tax base and employment and (v) to give a big boost to digitalization of payments to make India a less cash economy. Demonetization was initiated with a wide array of motives like stripping the Indian economy of its black money, push people to pay taxes for the unaccounted pile of cash, curb terrorism, promote the digital India movement and make India a cashless economy.

This move will help the government to track unaccounted black money or cash on which income tax has not been paid. Individuals who are sitting on a pile of cash usually do not deposit the amount in the bank or invest anywhere as they would be required to show income or submit PAN for any valid financial transactions. They would hide it somewhere and use it as and when necessary. Banning high-value currency will impact people who will have no option, but, to declare income and pay tax on the same or destroy the cash somehow. Now, it is not possible to hide the money as the notes have been declared invalid.

From slowing down the economic growth in various sectors to giving people nightmares of the long queues and the inability to spend liquid cash freely, the hullabaloo created by demonetization is remembered by one and all on its first anniversary. Demonetization began as a way to curb the black money from our economy was later addressed as a means of making India cashless and giving digital India a boost.

Banning high-value currency will halt illegal activity as the cash provided for such activities has no value now. Black money is usually used to fund the illegal activity, terrorism, and money laundering. Fake currency circulation will come to a halt in a single shot. Corrupt officers, money launderers are under threat as Income tax department is taking all the measures to track such people.

Most of the businessmen who have been hiding some income are ready to pay advance tax as current year's income. Tax payers who have been hiding some income can come forward to declare income and pay tax on the same. Individuals are required to submit PAN for any deposit above Rs 50,000 in cash, which will help tax department to track individuals with high denominations. Also, deposit up to Rs 2.5 lakh will not come under Income tax scrutiny.

It is important to remember that the demonetization move was intended more as a political move than as an economic one. analysts claim that the economic benefits will emerge over time. The demonetization campaign clearly contributed to economic slowdown, reflected in poor GDP figures in April-June. In hindsight, this can be deemed a failure from an economic point of view. assuming that demonetization is complemented by efforts to enhance tax compliance, then some success can be salvaged and lead to higher government revenue. This means that the government can expect to see the benefits of taxation on previously hidden black money over the coming months and years.

India's finance ministry says it is probing 1.8 million bank accounts where cash inflows during the demonetization period "did not appear in line with its tax profile," meaning it can expect some belated tax payments. There are also long-term benefits from demonetization in terms of increasing income tax payments going forward and encouraging the use of digital payments over cash, a means of encouraging better tax compliance among businesses. Traditionally, other governments have only embarked on demonetization schemes in times of extreme need, such as hyperinflation, political upheaval and wars.

DEMONETIZATION AND PERSONAL FINANCE

Piggybanks have been transformed to savings accounts as people turn towards increasing bank balances instead of stashing emergency cash in different corners of the house. People finally began to trust the digital payment systems; because that was the only option they were left with. Demonetization proved that Indians can strive and adapt to any changes and made people financially aware about the different spending options. The government's efforts to revamp the currency system provided people with a boost to use the cash that was lying around and invest it in a more productive way. The more native and conservative people also opened up towards the era of plastic cash and made several Indians tech friendly.

DEMONETIZATION AND BLACK MONEY

One of the most important points that pushed people to support demonetization was its associating with bringing an end to the black money problem in India. However, almost 99% of the money was deposited back to RBI. The statistics revealed that either the hoarders found a way to legitimize their black money or did not hold them in the form of cash. But this was known by many before the RBI reports as well. Black money hoarders do not hold the money in cash according to several finance experts and when this point was highlighted time and again, other important effects of demonetization were publicized by the government, like the role of demonetization on curbing terrorism.

DEMONETIZATION AND TERROR FUNDING

The second reason to support demonetization was its role in curbing terrorism by increasing the obstacles in terror funding. Terrorist organization were known to use fake Indian currency notes for funding their projects and the government believed that this could be contained with the help of demonetization. The Income Tax department seized Rs. 474.37 crore in new and old currency from November 9, 2016 to January 4, 2017 (the demonetization period). However, there are no reports if the money seized had any association with terror funding. In spite of these numbers, there is no doubting that the cash reserves of several terror groups were severely hit in the early days of demonetization.

DEMONETIZATION AND DIGITAL INDIA

Pushing India towards becoming a cashless economy was another reason that demonetization was publicized for. People turned towards digital transactions for everything from buying groceries from a road side vendor to paying utility bills during the time of

demonetization. However, as the flow of cash into the economy began to increase, the use of these apps and digital wallets saw a slide once again.

DEMONETIZATION AND TAX PAYMENTS

Pushing Indians to deposit and account the cash lying in their house also meant a rise in the tax payments for the country. According to government reports the income tax payers saw a record increase in the post demonetization era. 9.1 million New taxpayers were added to the slab which was an 80% rise over the typical yearly rise. This increase in the number of taxpaying citizens in the country has been credited to demonetization. This increase was also resonated in IT returns filing and advance tax payment.

Demonetization and GDP

The ban on old notes is being cited as one of the key contributors to the economic slowdown. With the gross domestic product (GDP) for the April-June quarter slipping to 5.7%, the reality of the economic slowdown could not be ignored. The World Bank has reduced the India GDP growth forecast to 7% for 2017-18 owing to demonetization and GST (Goods and Service tax). The slowdown is being cited as a delayed consequence of demonetization by the World Bank and while there are various other reasons at play, the steep decline has been credited to be an effect of demonetization.

DEMONETIZATION AND MSMES

Demonetization had a lasting effect on Indians MSMEs (Medium, Small and Micro Enterprises). Various medium and small enterprises turned towards digitalization, however, the micro industries were affected by the worst of its wrath. The micro industry owners were not a part of the black economy and they were clearly unprepared for the effects of demonetization. Many micro industry workers returned back to villages and the growth rate of these companies went as low as 1%. The MSME sector has been recovering from the drastic changes and its impact on the revenue, but demonetization forced the MSME sector to be friendlier and more accommodating towards the digital arenas and made them more accommodating towards change.

While these are some of the effects of demonetization on the national and economic front, demonetization gave individuals several lessons that have changed the way we look at managing finances. Demonetization made sure that we monetize our earnings to get the best returns possible whether it is by turning to monthly investment schemes to save better or by turning our safe cash pile into an easy withdrawal FD (fixed deposit). The government's revenue

will see an increase because of demonetization and its initial effects are already prevalent in the income tax filings post note ban. Demonetization has played a crucial role in bringing digitalization and financial planning into the forefront for many. India has withstood the immediate chaotic impacts of demonetization and it is evident that the returns of the hardships will begin to show in the coming months.

The good news starts with the widening of the tax base. The number of income tax returns filed for 2016-17 year grew by 25%, which is crucial to ease pressure on public finances in a country that has well over 1.25 billion people but less than 30 million file tax returns. The Economic Survey put the number of new taxpayers at 5.4 million, or just 1% of all individual taxpayers. Digital transactions have surged, too. More efficient than paper money, digital money is expected to bring in transparency into the system. Innovation emerged as well, such as the government-backed payment app BHIM, which facilitates easy electronic transfers between bank accounts. But digital payments haven't substituted the use of paper money as India still remains a cash economy.

Demonetization wrecked the primarily cash-reliant rural economy, adding distress to mounting debts. The agricultural sector, which is behind in reforms and investment, worsened due to cash shortages, plunging demand and collapsing prices. Prices of potatoes, onions and tomatoes were half of what they had been a year before in January-February. The outcome was widespread suffering and farmer unrest in the states of Madhya Pradesh, Maharashtra, Gujarat, Tamil Nadu and Rajasthan.

The downturn spilled over to other sectors. A survey by India Development Foundation found that production took a hit, accompanied by fall in employment, wages and job losses in the two months after demonetization. In Mumbai, more than 50% of the power loom units were shut down, impacting around 300,000 workers. Around 1.5 million jobs were lost in the first four months of this year.

Surveys done by the Punjab Haryana Delhi Chamber of Commerce and Industry, All India Manufactures Association and State Bank of India showed that the impact was between 50% and 80% on small and unorganized sectors. The Reserve Bank of India's Annual Report (RBI) stated that industry slowed down. The economy is also still coping with aftermath. In the first quarter of fiscal 2017-18, growth slumped to 5.7% compared to 7.1% in the same quarter of the previous year.

Although there is no way to be absolutely certain that the cause of all this is demonetization, there are some telltale signs: Rural loans increased by only 2.5% between October 2016 and April 2017; the growth in industrial output in April was 3.1%; and the construction sector registered negative gross value added growth. On top of this, little black money has been brought to light. Of the \$240 billion USD worth of the notes removed from circulation, the government estimated that as much as a third wouldn't be deposited in banks, implying that black marketeers would junk their undeclared cash than risk being found out. But this didn't happen. According to RBI's report, banks received around \$220 billion USD, or 99% of the money.

Even as RBI stated that there has been a significant increase in the rate of fake currency note detection, the government's freshly minted 2,000-rupee notes, issued after demonetization, are already being counterfeited. If this was not enough, the RBI suffered a loss printing new currency notes -- the cost of printing notes was nearly \$900 million in 2016-17, which is double the \$450 million spent a year prior.

DIGITIZATION

A vanguard of digital payment providers have benefited from PM Modi's move. The biggest player is Paytm which has seen its customer base surge since November. Demonetization also triggered record domestic inflows into mutual funds, which have gushed into the equity market and pushed the key indexes to multiple records. While overall digital transactions have dipped as cash returns to the economy, the government points to relatively lower levels of currency in circulation as a win. If it wasn't for demonetization, India would have had some Rs. 18 lakh crore in high-value bills today -- instead it has Rs. 12.5 lakh crore. So the potential of storing black money is so much reduced.

TAX EVASION

Widening the tax base is probably where analysts are most optimistic about demonetization. The government has said it will scrutinize the deposits that have flowed into banks since the cash ban to detect any tax evaders. Success in widening the tax base would ease pressure on public finances in a nation where less than 5 percent file tax returns. The exercise changed the public's perception of what the government can, and will do to root out corruption,.

The Reserve Bank of India (RBI) has reported in their Annual Accounts that Specified Bank Notes (SBNs) of estimated value of Rs. 15.28 lakh crore have been deposited back as on 30.6.2017. The outstanding SBNs as on 8th November, 2016 were of Rs. 15.44 crore value. The total

currency in circulation of all denominations as on 8th November, 2016 was 17.77 lakh crore whereas total currency in circulation as on 4th August, 2017 was 14.75 lakh crore. The Government had expected all the SBNs to come back to the Banking system to become effectively usable currency. The fact that bulk of SBNs have come back to the Banking system shows that the banking system and the RBI were able to effectively respond to the challenge of collecting such a large number of SBNs in a limited time. At the same time, the effective currency in circulation today is only 83% with full demonetization having taken place.

A significant portion of SBNs deposited could possibly be representing unexplained/black money. Accordingly, 'Operation Clean Money' was launched on 31st January 2017. Scrutiny of about 18 lakh accounts, prima facie, did not appear to be in line with their tax profile. These were identified and have been approached through email/sms. More than 9.27 lakh responses were received giving information on 13.33 lakh accounts involving cash deposits of around Rs.2.89 lakh crore. Advance data analytics tools were deployed which further identified 5.56 lakhs new cases and about 1 lakh of those cases in which either partial or no response was received in the earlier phase. Besides, about 200 high risk clusters of persons were identified for appropriate action. The Income Tax Department (ITD) conducted searches on various entities, leading to seizure of cash and admission of undisclosed income. Since November 2016 and until the end of May 2017, a total of Rs. 17526 crore has been found as undisclosed income and Rs. 1003 Crore has been seized. The investigation/scrutiny is going on.

CONCLUSION

Demonetization immensely beneficial to Indian Economy and People

As a result of demonetization drive, there is a substantial increase in the number of Income Tax Returns (ITRs) filed. The number of Returns filed as on 05.08.2017 registered an increase of 24.7% compared to a growth rate of 9.9% in the previous year. Advance tax collections of Personal Income Tax (i.e. other than Corporate Tax) as on 05.08.2017 showed a growth of about 41.79% over the corresponding period in F.Y. 2016-2017. Personal Income Tax under Self Assessment Tax (SAT) grew at 34.25% over the corresponding period in F.Y. 2016-2017.

Transactions of more than 3 lakh registered companies are under the radar of suspicion while one lakh companies were struck off the list. The government has already identified more

than 37000 shell companies which were engaged in hiding black money and hawala transactions. Around 163 companies which were listed on the exchange platforms were suspended from trading, pending submission of proof documents. The Income-tax Directorates of Investigation have identified more than 400 benami transactions up to 23 May, 2017 and the market value of properties under attachment is more than Rs. 600 crore.

As a result of demonetization of SBNs, terrorist and naxalite financing stopped almost entirely. No high quality FICN was found / seized by intelligence operations, including at the Indo-Bangladesh Border since demonetisation. Further, it also adversely affected the hawala operators and *dabba* trading venues.

Demonetization drive led to significant change of saving habits and formalization of assets market. Considerably more funds came into the organized financial markets, whereas earlier households were parking much of their savings in unproductive physical assets. The savings in the form of investment in equity mutual funds, life insurance premia etc., increased. The total assets under management (AUM) of Mutual funds (MFs) rose by 54% by the end of June 2017 from March 2016. As on 16 August 2017, the number of Pradhan Mantri Jan Dhan Yojana (PMJDY) accounts stands at 29.52 crore with rural accounts comprising 60% of it. Thanks to demonetization led efforts, zero balance accounts under PMJDY declined from 76.81 % in September 2014 to 21.41% in August 2017.

The impressive revenue collection under GST is also partially attributable to demonetization drive. The total revenue of GST remitted upto 29 August, 2017 is Rs.92,283 crore that too with only 64.42% of assesses having completed the payments. The number of *new* taxpayers who have registered with the GSTN upto 29 August, 2017 is 18.83 lakhs.

As part of fillip to digitalization, about 52.4 crore unique Aadhaar numbers have been linked to 73.62 crore accounts in India. As a result, every month now, about 7 crore successful payments are made by the poor using their Aadhaar identification. The government now makes direct transfer of Rs. 74,000 crore to the financial accounts of 35 crore beneficiaries annually, at more than Rs. 6,000 crore per month. Now with the BHIM App and the Unified Payments Interface (UPI), a secure and seamless digital payments infrastructure has been created so that all Indians, especially the poor can become part of the digital mainstream. Digital payments have increased by 56% from 71.27 crore transactions in October 2016 to 111.45 crore transaction till the end of May, 2017. Within reach of the country is what might be called the 1 billion-1 billion-

1 billion vision i.e. 1 billion unique Aadhaar numbers linked to 1 billion bank accounts and 1 billion mobile phones. Once that happens and it would happen quite soon, all of India will become part of financial and digital mainstream. Some people had expected a very large shock to economic growth on account of demonetization. Their expectations have been belied.

India has continued to be on path of one of the strongest growths in the world. The two big measures of demonetization and introduction of GST were humongous measures which had changed structural and ethical foundations of Indian economy. Government has been able to manage the transition extremely, effectively and with the least pain. With demonetization's short term effects having played out completely, it is the long term positive impacts which will be still working its way to contribute beneficially to India's economy and well-being of its people.