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Post Impact of Demonetisation on Indian Economy

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ABSTRACT

Indian Economy is an emerging economy and has grown the fastest amongst other economies in the world. Money plays a significant role in the Economy. GDP ratio and economic growth depend on money circulation in the country. Demonetisation impacts all sectors of the Economy like Primary. Manufacturing, Tertiary sector of the country. The paper aims to discuss the post-impact of demonetisation on the economy of India. The paper is based on descriptive research and secondary data collected from the RBI report, newspaper, magazine, research paper, websites from the internet, and books.

Keywords: Indian Economy; Demonetisation; Impact; Growth

INTRODUCTION

Demonetisation is referred to as the stripping of existing currency as a legal tender.

Demonetisation is a process by which the demonetized notes cease to be accepted as legal currency for any transaction. The new currency notes replace the old currency notes. The legal status of a currency unit has an impact on the transactions in an economy.

Demonetisation causes unrest in an economy or helps stabilize the Economy from existing problems. A country usually takes Demonetisation for various reasons.

Demonetisation in India

Demonetisation in India has occurred three times until now, namely in 1946, 1978, and 2016.

Demonetisation in 1946

The first time demonetisation happened was in 1946. In this denomination of Rs.1000 and Rs.10000 were removed from circulation of the economy. The impact of the demonetisation as the higher denomination currencies were not available for common people.

In 1954, these notes were re-introduced with a different denomination of Rs5000

Demonetisation in 1978

The second time demonetisation in India took place in 1978; the Prime Minister was Morarji Desai. During the second demonetisation, Rs1000, Rs5000, Rs10000 were taken out of circulation from the economy. The motive for demonetisation was to reduce the circulation of black money in the country's economy. Morarji Desai made the announcement.

Demonetisation in 2016

Demonetisation was announced on November 8, 2016, by Shri Narendra Modi (Prime Minister of India). During this demonetisation, the notes taken out of circulation were the denominations of Rs500 and Rs1000 and introduced a new currency of denominations Rs500 and Rs2000.

Objectives:

1. Removal of black money that is circulating in the country
2. For curbing the interest rates of the prevalent banking system
3. To assist in the creation of a cashless Economy
4. To formalize the informal Indian Economy.

5. To remove counterfeit notes from the market.
6. To help reduce anti-social activities and their finance

Demonetisation - Other countries

Demonetisation is not a fresh concept that has been implemented in the world. During the period between 1850-1855, the French used the word Demonetize which was the first time by any country. Also, other countries have initiated demonetisation in the past. As per the below Table 1, the details of demonetisation by other countries is provided.

Table 1: Demonetisation - Other countries

Country	Years of Demonetisation	Reasons for Demonetisation
GHANA	1982	Tackle tax evasion
NIGERIA	1984	Curb black money
MYANMAR	1987	Curb black money
SOVIET UNION	1991	Curb black money
AUSTRALIA	1996	Stop currency counterfeiting
NORTH KOREA	2010	Banish the black market
ZIMBABWE	2015	Solve the problem of hyperinflation
VENEZUELA	2016	Curb the inflation rate
PAKISTAN	2016	Curb the flow of black money

LITERATURE REVIEW

Dr. G Ganesan and B Gajendranayagam(2017). This paper will examine the issues associated with demonetization and its implications in the Indian Economy during pre and post-demonetisation.

Dr. Dimpal Vij(2018). The study was done on both negative & positive impacts of demonetization on the economic dimensions. To determine whether government objectives of demonetization have been fulfilled. The present study is descriptive. The paper's primary focus is to suggest measures to reduce negative impacts and increase positive effects.

Dr. S. PreethiT and Mrs. V.M. Sangeetha(2017). s. This paper is aimed towards the analysis of the impact of demonetization on different in the economy. Demonetisation is seen as a financial reform in the country and it has its positives and negatives.

OBJECTIVES OF THE STUDY

1. To study post-impact of demonetisation on Gross Domestic Product
2. To study post-impact of demonetisation on various sectors of the economy.
3. To study post-impact of demonetisation on the rise in inflation level in the Indian economy.

RESEARCH METHODOLOGY

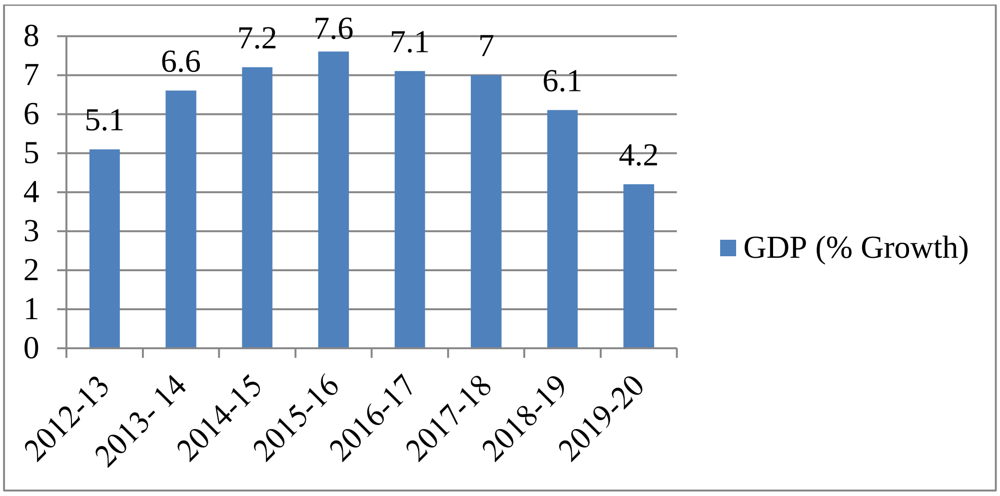
The paper is based on descriptive research & secondary data is collected from RBI reports, newspapers, magazines, research papers, websites from the internet, and books.

POST IMPACT OF DEMONETISATION ON GROSS DOMESTIC PRODUCT

Gross Domestic product – GDP is the value of final goods & services produced in all sectors during a specific year provides the total production in all the sectors in the current year. And the total of production combined in all three sectors given the GDP.

Indian Economy is a rapidly growing economy and is the fifth-largest economy in the world by nominal GDP. As per Figure 1, the GDP was 5.1% in 2012-13 and grew steadily at 7.6% in 2015-16. However, demonetisation in 2016 impacted the growth and reached a low level of 4.2% in 2019-20.

Figure 1: GDP %Growth



Source: Central Statistical Officer (CSO

Table 2: Growth Rates and Composition of Real Gross Domestic Products (At 2011-12 Prices)

(Per cent)

Sector	**Growth rate**				**Share**		
	Average 2013-14 to 2019-20	**2017-18**	**2018-19**	**2019-20**	**2017-18**	**2018-19**	**2019-20**
1	2	3	4	5	6	7	8
Expenditure side GDP							
1. Private Final Consuption Expenditure	7.0	7.0	7.2	5.3	56.0	56.6	57.2
2. Government Final Consumption Expenditure	7.9	11.8	10.1	11.8	10.2	10.6	11.3
3. Gross Fixed Capital Formation	4.8	7.2	9.8	-2.8	30.8	31.9	29.8
4. Change in Stocks	16.4	76.0	22.5	1.9	1.6	1.9	1.9
5. Valuables	-1.0	27.2	-11.9	13.5	1.5	1.2	1.3
6. Net Exports	-17.1	-257.7	11.8	29.2	-3.6	-3.0	-2.0
a) Exports	3.2	4.6	12.3	-3.6	19.7	20.9	19.3
b) Less Imports	1.5	17.4	8.6	-6.8	23.4	23.9	21.4
7. Discrepencies	-58.4	65.1	-73.9	-25.6	3.5	0.9	0.6
8. GDP	**6.8**	**7.0**	**6.1**	**4.2**	**100.0**	**100.0**	**100.0**

Source: National Statistical Office (NSO), Reserve Bank of India

POST IMPACT OF DEMONETISATION ON DIFFERENT SECTORS OF THE ECONOMY

Indian Economy

Indian economy is categorized into three sectors i.e., primary sector, secondary sector & tertiary sector. Considering employment, the Indian economy is divided into organized and unorganized sectors. While considering the ownership, it is divided into private sector and public sector.

Classifications of sectors of the economy:

1. **Based on ownership**

- Public sector – In this sector, the ownership of major assets is in the hands of government & it is responsible for providing all the services to the public.
- Private sector – In this sector, private individuals or companies have the ownership of assets and delivery of services.

2. **Based on employment**

- Organized sector – In this sector, the people have assured work, and an employee-employer relationship exists between them.
- Unorganized sector – In this sector, the government doesn't have control, and it consists of scattered and small units. Also, the employment opportunities are not fixed and are unsecure.

Demonetisation impact on various sectors of the Indian economy

1. **Agriculture Sector** - Agriculture sector is a crucial part of the Indian economy and has a major contribution towards the GDP. However, there is a decline in its share in recent years and is currently at 14% in 2019. More than 50% of India's population is dependent on the agriculture sector. Considering the priority of this sector, the Union Budget in 2017-18 prioritized the agriculture sector and projected farmers' incomes to be doubled by the fiscal year 2022.

The agriculture sector receives major subsidies every year and is at an all-time high, and various factors positively impacted this sector.

- The farming system has shifted in favor of cash crops like rubber and sugar-cane etc.
- Co-operative farming e.g., e-choupal
- Growth of Self-Help Group like Lijjat Papad etc.
- Various export sectors were opened for agricultural products

In the agriculture sector, cash currency plays the important role in money circulation. Demonetisation is bound to cause temporary stress due to dependency on cash currency for various transactions. Transport, marketing & distribution of ready produce goods to wholesale centers is cash-dependent and disruptions break in the supply chain led to lower sales, increased wastage of perishables, lower revenues that end up as trade dues instead of cash in hand.

2. Industrial sector

Industrial Sector is an essential part of the Indian economy. Requisite reforms like abolition of the 'Permit Raj' and opening of economic barriers are greeted with optimism & positivity. Due to these changes in the sector, the potential of industrial sector has increased since 1991 in the economy.

The industrial sector included iron and steel, jute, and automobile industries, and various factors positively impacted this industry.

- Automation in production, distribution and marketing
- Reduction in red-tapism.
- Private funding were encouraged and supported for both the domestic industry and Foreign Direct Investments (FDIs)
- New technology adaption and research & development
- Encouragement in various investment types such as public-private partnerships, joint-ventures and setting up of new Multi-National Companies (MNCs) in the country
- End of government monopoly in sectors where Private players were barred to enter.

This sector plays an essential contributor to growth, accounting for 23.4% of the total gross value added in 2017-18. A robust industrial and manufacturing sector helps in-country development, exports, and employment. Demonetisation hit this sector hard, especially the manufacturing and construction industries. However, its share has decreased since demonetisation and stands at 22.4% in 2019-20.

3. Services Sector

The services sector had the biggest impact as per the new economic policy. Service sector witnessed double-digit growth, which involved Financial services, Business Process Outsourcing, Business, IT service industry. Indian tech companies like WIPRO, TCS, Infosys, etc., are recognized around the world.

- Around 60 percent contribution towards Gross Domestic Product (GDP) is made by the services sector in India.
- India has stood up as the Information Technology hub of the world with its demographic dividend potential.
- Fresh employment opportunities are created due to the high potential for recruitment.
- Opening of sectors like transportation, medical and tourism activities led to growth in the service sector.
- The RBI transformed itself from being a banking regulator to a facilitator in the country.
- Wide product variety for financial funding

- Wider reach of services like banking, stock market, and insurance, etc.
- Foreign exchange reserves have considerably improved

The services sector plays an essential role in India's economic growth contributing almost 61.4% of its Gross Value Added Growth in 2017-18 and its share increased to 62.9% in 2019-20. However, the sector's growth has been affected post demonetisation, as the sector was growing at 6.7% in 2017-18 and declined to 5% in 2019-20. The impact on the industry was not immediate; however, the construction, real estate, hotels industry suffered the most due to demonetisation and the slow down resulted in an overall decline in the services sector.

The construction sector suffered the most and fell from 5% in 2017-18 to 1.3% in 2019-20 due to demonetisation, as this particular sector was mainly dependent on cash currency.

Table 3: Real GVA Growth

(2011-12 Prices)

(Percent)

Sector	**Growth Rate**				**Share**		
	Average 2013-14 to 2019-20	**2017-18**	**2018-19**	**2019-20**	**2017-18**	**2018-19**	**2019-20**
1	2	3	4	5	6	7	8
GVA at Basic Prices (Supply side)							
1. Agriculture, forestry and fishing	**3.6**	**5.9**	**2.4**	**4.0**	**15.1**	**14.6**	**14.6**
2. Industry	**6.4**	**6.8**	**4.5**	**0.8**	**23.4**	**23.1**	**22.4**
of which:							
a) Mining and quarrying	4.6	4.9	-5.8	3.1	3.0	2.7	2.7
b) Manufacturing	6.6	6.6	5.7	0.0	18.1	18.1	17.4
c) Electricity, gas, water supply and other utility services	7.1	11.2	8.2	4.1	2.3	2.3	2.3
3. Services	**7.4**	**6.7**	**7.5**	**5.0**	**61.4**	**62.3**	**62.9**
of which:							
a) Construction	4.1	5.0	6.1	1.3	8.0	8.0	7.8
b) Trade, hotels, transport, communication and services related to broadcasting	7.5	7.6	7.7	3.6	19.1	19.4	19.4
c) Finacial, real estate and professional services	8.2	4.7	6.8	4.6	21.6	21.8	21.9
d) Public Adminsitration defence and other services	8.1	9.9	9.4	10.0	12.7	13.1	13.9
4. GVA at base prices	**6.5**	**6.6**	**6.0**	**3.9**	**100.0**	**100.0**	**100.0**

Source: National Statistical Office (NSO), Reserve Bank of India

4. **Inflation**

In economic terms, inflation is a gradual increase in the price level of an economy over a specific period. During a general rise in the price-level, lower goods & services are bought by each unit, so as a result, due to inflation, the purchasing power of money reduces. So, there is a loss of real value in the unit of account and medium of exchange.

There are two categories of Inflation

Demand-pull inflation

Demand-pull inflation is caused due to rise in aggregate demand in the economy.

The following are the causes for this kind of inflation.

- Rise in the money supply & growth - When there is a rise in money flow in the economy the consumers intend towards more spending and taking extra debt. So as a result, there is rise in demand for a particular product/service, which results in price increase.
- Increase in foreign exchange reserves or Asset's inflation – A unexpected rise in exports forces depreciation of the currency in particular country.
- Deficit financing or excessive spending by government – This occurs when the government spends more freely, there is a gradual increase in prices.
- Due to policy measures like reduction of taxes to boost economic activity
- Increased borrowing or excess debt
- Depreciation of currency
- Unemployment rate at a low level

Demand-Pull Inflation has its effects on the economy:

- Inadequate supply or reduced supply of products or services
- Higher prices of the goods (inflation).
- Higher Cost of living

Cost-Push Inflation can occur due to the following reasons:

- Rise in price of inputs
- Hoarding & speculation of commodities
- Defect in supply chain
- Gradual increase in indirect taxes
- Depreciation of currency
- Crude oil prices fluctuation
- Defect in food supply chain
- Slower growth in agriculture sector
- Rise in prices of food products
- Rise in interest rates

Amongst the two inflation types, the Cost-push inflation is considered harmful as due to reduction in supply, the national income reduces as well.

As per RBI report on Inflation, as shown in Table 4, the Wholesale Price Index for all commodities increased from 1.7% in 2016-17 to 4.3% in 2018-19 due to the demontisaton impact faced in the country.

Even the inflation for manufactured products increased from 1.3% in 2016-17 to 2.7% in 2017-18 and its effect continued in 2018-19 with an increase to 3.7%. The manufacturing sector dealt a huge blow due to demonetisation, as small-scaled industries primarily relied on cash currency.

Table 4: INFLATION, MONEY & CREDIT									
(Per cent)									
Inflation									
Consumer Price Index (All India)	**Rural**			**Urban**			**Combined**		
	2017-18	**2018-19**	**2019-20**	**2017-18**	**2018-19**	**2019-20**	**2017-18**	**2018-19**	**2019-20**
1	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**
General Index (All Groups)	3.6	3.0	4.3	3.6	3.9	5.4	3.6	3.4	4.8
Food and beverages	2.4	0.7	4.8	1.8	0.7	8.1	2.2	0.7	6.0
Housing	…	…	…	6.5	6.7	4.5	6.5	6.7	4.5
Fuel and light	6.5	6.0	1.1	5.6	5.2	1.7	6.2	5.7	1.3
Miscellaneous	4.3	6.3	5.1	3.1	5.4	3.7	3.8	5.8	4.4
Excluding Food and Fuel	4.7	5.7	4.1	4.6	5.9	4.0	4.6	5.8	4.0
Other Price Indices	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**2019-20**
1. Wholesale Price Index (2011-12=100)									
All Commodities	8.9	7.4	5.2	1.3	-3.7	1.7	2.9	4.3	1.7
Primary Articles	9.8	9.8	9.8	2.2	-0.4	3.4	1.4	2.7	6.8
of which : Food Articles	7.3	9.9	12.3	5.6	2.6	4.0	2.1	0.3	8.4
Fuel and Power	14.0	10.3	7.1	-6.1	-19.7	-0.3	8.2	11.5	-1.8
Manufactured Products	7.3	5.4	3.0	2.6	-1.8	1.3	2.7	3.7	0.3
Non-Food Manufactured Products	7.3	4.9	2.7	2.7	-1.8	-0.1	3.0	4.2	-0.4
2. CPI- Industrial Workers (IW) (2001=100)	8.4	10.4	9.7	6.3	5.6	4.1	3.1	5.4	7.5
of which : CPI- IW Food	6.3	11.9	12.3	6.5	6.1	4.4	1.5	0.6	7.4
3. CPI- Agricultural Labourers (1986-87=100)	8.2	10.0	11.6	6.6	4.4	4.2	2.2	2.1	8.0
4. CPI- Rural Labourers (1986-87=100)	8.3	10.2	11.5	6.9	4.6	4.2	2.3	2.2	7.7

Source: Reserve Bank of India (RBI)

CONCLUSION

Demonetisation is having an unfavorable impact on all the sectors of the economy, & its impact will be carried over a long period. However, it has resulted in negative growth in the economy for the last three years, and citizens have witnessed problems in money circulation.

Sectors like real estate, construction and other small sectors heavily relying on the cash currency faced a significant impact. Various construction sites across India faced a huge financial loss as people were left with low currency for money circulation. This resulted in the developers defaulting the loans/debts taken from banks and other financial institutions.

Even the agriculture sector, which heavily relied on the cash currency faced a negative impact as small farmers depended on cash for their daily livelihood.

India's population is mainly involved in employment opportunities in the small and unorganized sector. Demonetisation caused a ripple in this sector and maximum people lost their jobs. Many small industries like cottage industries dealt a massive blow due to high dependency on cash currency. Even after a few years, the cottage industries face an uphill task to get back to an earlier situation, and the employment is still not up to the maximum limit.

However, if the government successfully addresses all the drawbacks associated with demonetisation. In that case, this demonetisation will be considered as an economic revolution in India and we can expect a better tomorrow with increasing economic growth and lower corruption levels.

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