International Journal of Business and Management Invention (IJBMI)
ISSN (Online): 2319-8028, ISSN (Print):2319-801X
www.ijbmi.org || Volume 9 Issue 1 Ver. I || Jan. 2020 || PP 47-52

Indian Banknote Demonetization

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Abstract: *Demonetisation is withdrawing the units of money in a legal form. Demonetisation refers to change in use of currency notes, coins used by the country. The government take the step of demonetisation with an attempt to clear black money and to have transparency in the economic system. It involves the introduction of new notes, coins of same denomination. The currency has been demonetised thrice in India. The details are as follows :*

- *12th January 1946*
- *16th January 1978*
- *8th November 2016*

The study is descriptive nature and all data have been taken up from various journals and websites.
Keywords: *India, economics, demonetization, money*

Date of Submission: 18-01-2020 Date of Acceptance: 06-02-2020

I. INTRODUCTION

Demonetization is a measure of monetary policy where the circulation of all or part of the pieces of the monetary cone is declared illegal. It usually occurs when there is an economic, political and social crisis that leads to a change of national currency by replacing the old monetary unit with a new one; front high levels of hyperinflation that generate recurrent updates of the monetary cone through the abandonment of the pieces of smaller denomination and its replacement by new notes of greater nominal value; the falsification and money laundering processes; the excessive storage of foreign currencies and national currency in cash; and the recurrent acts of corruption. The announcement of demonetisation of currency notes of Rs 500 and Rs 1000 took place on 8th November 2016. The main motive of demonetisation was to curb corruption, black money, terrorism funding. Along with that aimed to make India as Digital India, where transaction can be done cashless using internet and other positive development such as adoption of faster technology, increase in tax base and possibility of lower tax rates. The government believed that currency ban is required to control inflation to fight against corruption and to discover the cash transaction. India has to find solutions to the problems like this for betterment of the country.

Objectives

- To study present scenario of black money in India
- To understand meaning and reasons of demonetisation
- To study positive and negative impact of demonetisation

Research Methodology

RESEARCH METHODOLOGY:

- This study is of descriptive nature and tells about the meaning and reasons of demonetisation along with the
- sector-wise impact of demonetisation and positive and negative impacts of demonetisation on Indian economy.
- Hence makes use of secondary data. The entire study is based only on observation and documentary analysis.
- Furthermore, the required & relevant secondary data are collected from various Research Papers, Journals, &
- Publications, websites and many others. Books have also been referred for theoretical information on the topic
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- ❖ **Scope**

The study covers the concept of demonetisation which refers to change in currency used by the country. The main motive is to cope with the challenges of corruptions, black money, high inflation, funding to terrorist and fake currency. The demonetisation initiated on 8th November 2016, by making currency notes of Rs 500 and Rs 1000 not as legal tender.

❖ Limitation

The study is basically limited to secondary data and only discusses the one aspect of financial inclusion. It does not take into consideration all the factors or determinants of Financial inclusion.

❖ Present scenario of Black Money

The root cause for the increasing rate of black money in the country is the lack of strict punishments for the offenders. The criminals pay bribes to the tax authorities to hide their corrupt activities. Thus, they are rarely punished by the judge. The criminals who conceal their accounts from the government authorities include big politicians, film stars, cricketers, and businessmen. Some Indian corporations practice transfer mispricing, by under-invoicing their exports and over-invoicing their imports from tax haven countries such as Singapore, UAE, and Hong Kong. Thus the promoters of the public limited companies who hold rarely more than 10% of share capital, earn black money abroad at the cost of majority share holders and tax income to the Indian government. By the year 2008, the cumulative Illicit Financial Out flows from the country touched US$452 billions.

Political organizations, corrupt politicians and government officials take bribes from foreign companies then park or invest the money abroad in tax havens for transferring to India when needed. In addition, locally earned bribes, funds and collections are often routed abroad through hawala channels in order to evade Indian tax authorities and consequent legal implications.

The unlawfully acquired money kept abroad is routed back to India by the round tripping processes. Round tripping involves getting the money out of one country, sending it to a place like Mauritius and then, dressed up to look like foreign capital, sending it back home to earn tax-favoured profits.

Foreign direct investment (FDI) is one of the legal channels to invest in Indian stock and financial markets. As per data released by the Department of Industrial Policy and Promotion (DIPP), two of the topmost sources of the cumulative inflows from April 2000 to March 2011 are Mauritius (41.80 per cent, US$54.227 billions) and Singapore (9.17 per cent, US$11.895 billions). It is not plausible that the small economies of Mauritius and Singapore are the true origins of such huge investments. It is apparent that the investments are being routed through these jurisdictions in order to conceal from revenue authorities the identities of such tax evaders; In many cases they are Indian residents who have invested in their own companies.

Gold imports through official channel and smuggling is a major conduit to bring back the black money from abroad and convert into local black money as the gold commands high demand among the rural investors particularly. Also fictitious high value round trip transactions via tax haven countries by diamonds and precious stones exporters and importers is a channel for to and fro transactions outside the country. Fictitious software exports can be booked by software companies to bring black money into India as tax exemptions are permitted to software companies

❖ Meaning and Reasons of demonetisation

Black money is money earned through any illegal activity controlled by country regulations. Black money proceeds are usually received in cash from underground economic activity and, as such, are not taxed. Recipients of black money must hide it, spend it only in the underground economy, or attempt to give it the appearance of legitimacy through money laundering.

Demonetization has been used as a tool to stabilize a currency and fight inflation, to facilitate trade and access to markets, and to push informal economic activity into more transparency and away from black and gray markets.

❖ Positive Impact of Demonetisation

Demonetisation and Indian Financial Sector

As per the monetarist view, the effect of demonetisation on economic activities and stock market is related to the fall in interest rates. However, the real side impact of any demonetisation move will also depend upon the relative share of connected and unconnected sectors of the economy. Demonetisation has led to increase of cash flows in the banking system. An event study utilized the daily data of BSE 200 stock index and revealed a 9 percent reduction in the shareholders' wealth during eight trading days immediately after the announcement of demonetisation. The market perceived the move negatively. The short-run impact of demonetisation on creating volatile markets is intuitive. However, the long run impacts are well aligned to economic theories.

Abolish black money:

Before demonetisation, according to White Paper on Black Money in India report, published in May 2012, Swiss National Bank estimates that the total amount of deposits in all Swiss banks, at the end of 2010, by citizens of India were CHF 1.95 billion (INR 92.95 billion, US$2.1 billion). After demonetisation according to annual report giving a balance-sheet of demonetisation implemented 21 months ago. Of Rs 15.41 lakh crore demonetised currency notes of Rs 500 and Rs 1,000 denominations, only Rs 10,720 crore did not reach to the banks or the RBI. This step would abolish black money from the economy as the owners will not be in a position to deposit the same in the banks and which generally used to create chaos and terror or is lying with terrorists, Maoists, naxalites, scrap.

Elimination of Counterfeit Currency:

Counterfeit currency is generally circulated in highest denomination notes to impact most. So, by demonetizing the highest currency notes India could almost eliminate 100% fake currency out of circulation in one stroke. A noteworthy growth was also seen in the number of counterfeit currency reports (CCRs) which increased from more than 4.10 lakh in 2015-16 to over 7.33 lakh in 2016-17, which has been attributed to the demonetisation exercise. The annual spike registered in 2016-17 is the highest since 2012. The Reserve Bank of India's annual report for 2016-17 told a similar story. "At the Reserve Bank's currency verification and processing system, during 2015-16, there were 2.4 pieces of FICNs of Rs 500 denomination and 5.8 pieces of FICNs of Rs 1000 denomination for every million pieces notes processed; which rose to 5.5 pieces and 12.4 pieces, respectively, during the post-demonetisation period

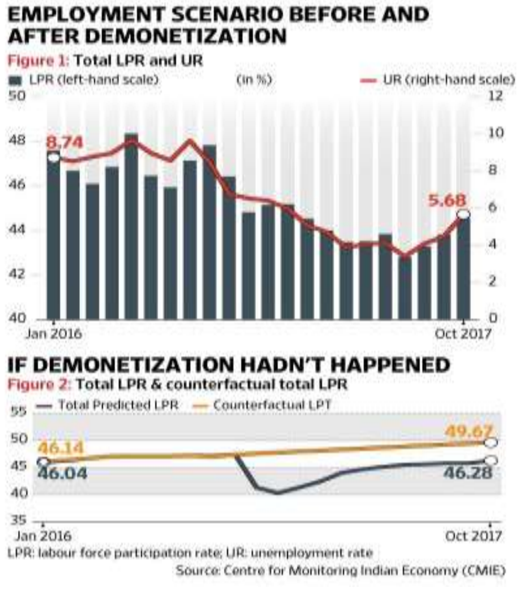
Higher Tax Collection:

This led to higher tax collection as business men are depositing cash lying with them as current year income with advance tax. Defaulters of bank, property tax, electricity bills and telecom bills are clearing their long pending bills and thus utilizing their old currency notes. In March 2014, the number of Income Tax returns filed was 3.8 crores. In 2017-18, this figure has grown to 6.86 crores. In the last two years, when the impact of demonetisation and other steps is analysed, the Income Tax returns have increased by 19% and 25%. This is a phenomenal increase. The number of New Returns filed post demonetisation increased in the past two years by 85.51 Lakhs and 1.07 crores. For 2018-19, advance Tax in the first quarter has increased for personal Income Tax Assesses by 44.1% and in the Corporate Tax category by 17.4%. The Income Tax collections have increased from the 2013-14 figure of `6.38 Lakh crores to the 2017-18 figure of `10.02 Lakh crores. The growth of Income Tax collections in the Pre-demonetisation two years was 6.6% and 9%. Post-demonetisation, the collections increased by 15% and 18% in the next two years.

Digital banking :

Digital banking got a push post demonetisation with private sector banks taking the lead armed with cutting-edge technology and full government backing to ensure that transactions move online. Promotion of digital transactions is one of the major achievements of the demonetisation implementation. Earlier in India there were fewer digital transactions as most of the Indian population depended upon the cash for day to day purchases and bill payments. With the crunch of cash in the market and various other incentives that were announced by the government, there was a surge in the digital transactions in India. More digital transactions meant visibility of money held by citizens to the government agencies to track tax evasions.

❖ **Negative Impact of Demonetisation**



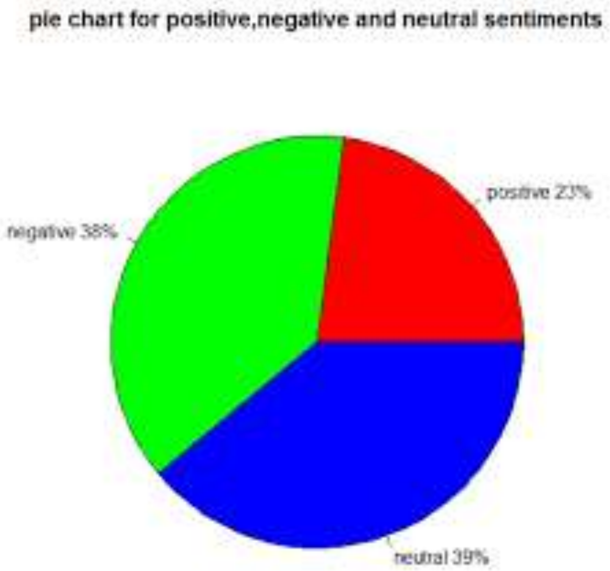
Jobseekers' market

Demonetisation uncertainty has made employers cautious. Fresh hiring has nearly stopped, increments are likely to go down and attrition has come to a grinding halt. This has created an employer's market, taking away not only new job opportunities but also the bargaining power of an employee. All this has led a negative impact on job seeker and leading them to de-motivation.

Business Impact Analysis

- **Liquidity** – The immediate impact will be on liquidity. Businesses dealing with a large amount of cash can no longer use the currency to drive business.
- **Loan Demand** – To fill up the gap and run the business smoothly the demand of loans or funding from the bank and other financial institutions will increase.
- **Loan Dis-approval** – Businesses dealing with cash will have difficulty in getting funding as the Balance sheet will give a different story, making them unqualified for loans. Banks will be reluctant and extremely cautious as they would want to avoid NPA's.
- **High Cost** – Even if one can avail funding through other institutions, the cost of lending will be much higher.
- **Small businesses were vanished** worst hit by demonetisation implementation in India. Cash payments to workers and employees is still a practice in small scale businesses. So as India faced cash crunch, small business units were not able to pay its workers. Workers also had to stand in long queues to withdraw / exchange money in ATMs / Banks which had reduced effective working hours of business operation. Thus, small businesses had to limit their business activities and many of the small businesses suffered great losses with the demonetisation process.

Below Poverty Line Families affected by DEMONETISATION



As small businesses shut down / limited their activities, many BPL (Below Poverty Line) Indians lost their jobs temporarily and got into trouble. Lack of bank accounts and limited resources, poor and needy people of India were the most affected ones. People had to stand in queue to get the money exchanged, for which they have to wait for hours which was very hectic. Many people got psychological disappointed due of the situation as they were suffering mentally and physically.

GDP Came Down

GDP of India has slowed down after implementation of demonetisation move as small industries were finding it difficult to carry out business. Due to decrease in consumption, demand for products in domestic market sharply fell down. GDP also rallied downwards from 9.2 in January 2016 to 7 in December 2016. GDP continued to fall and had finally came down to 6.1 by March 2017. However Indian government has maintained that GDP will increase soon and no one should worry about it.

Implementation of GST (Goods and Services Tax) is also one of the reasons for GDP fall down.

III. CONCLUSION

Demonetization of old currency notes surely has had some positive impact like reducing the cash flow to terror organizations, dismantling of counterfeit currency infrastructure, better income tax and indirect taxation, boost to digital economy. However, it has come at a huge social and economic cost. Central government's recent decision to demonetize the high value currency is one of the major steps towards the eradication of black money in India. The demonetization drive will affect some extent to the general public, but for larger interest of the country such decisions are inevitable. Also it may not curb black money fully, but definitely it has major impact in curbing black money to large extent. Along with that it has some negative effects as well line reduction in employment ratio, reduction on GDP ratio. Demonetisation period created a frenzy in the digital money space, companies like pay tm and other mobile wallets had got a tremendous boost and their penetration level has been improved. Tax payer base has been improved.

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Sheetal V Bhatavdekar. "Indian Banknote Demonetization." *International Journal of Business and Management Invention (IJBMI)*, vol. 09(01), 2020, pp 47-52