

Review Article

Received on: 05-01-2018

Accepted on: 14-01-2018

Published on: 21-01-2018

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A Study on Demonetization and its effect on Indian Economy – Step towards Nation Building and inevitable transformation to Digital Economy

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ABSTRACT

Today, the word Demonetization is well known to people of India. The announcement of Prime Minister Mr. Narendra Modi on November 8th that India's two highest-denomination currency bills—1,000 rupees and 500 rupees—would immediately cease to be legal tender in most places. Holders have until the end of the year 2016 to deposit these bills into bank accounts. As replacements, the government has slowly rolled out a redesigned 500-rupee bill and a new 2,000-rupee bill. The long-term effects of India's demonetization strategy remain unclear, largely because no other major economy has attempted such an experiment except during a crisis. But with growth slowing and job losses rising, the short-term prognosis appears grim. Instead of factory openings or large new investments, the images that tell India's current economic story include snaking lines outside banks, distressed workers migrating back to their villages, and tax raids on jewellers and officials caught with hoards of allegedly illicit cash. From Jan 1, 2017 the scenario had changed. We find no queues in front of the banks and people are getting money to withdraw at the ATMs and banks. This researcher analysis the impact of demonetization on Indian economy and people of India with this article and draws conclusion based on the analysis.

Key Words: *Demonetization, GDP, Indian Economy, Citizens, Growth Rate*

Introduction

The Indian government declared the two largest denomination bills 500 and 1000 invalid, abolishing over 80 percent of circulating cash by value. On November 8, 2016, Indian Prime Minister Narendra Modi announced that the two largest denominations of banknotes could not be used for payments any more with almost immediate effect. The move aimed to curb black money in the financial system. Black money is one of the factors holding back the economy and Nullifying these FICNs (Fake Indian Currency Note) was also part of the demonetization move. This demonetization had shown short term impact on several businesses and people were caught up in the unprecedented cash crunch that has been caused. The present research study focuses on the impact of demonetization on general public and to know whether the government is really succeeded in declaring demonetization for eradication of black money.

Demonetization gave a good push on transparent transactions, higher accountability and reduction of black money through the push of digital payments. Most of the retail business started taking new dimensions due to the growth of the internet, the business models and the payment methods have all changed. Though, we can predict that this may lead to more positive effect in the long term of the Indian economy, but taking into consideration short term effects, it has been predominantly adverse for the customers and businesses.

Online transactions of money and digital payments are not as difficult as they were there before. This made easy to smartly tackle the situation and sudden ban of old bills. And online transactions do come with a lot of benefits. This is the right time to unleash the full potential of the debit cards, credit cards, e-wallets and net banking.

The present study is going to focus on how demonetization shown impact on India's transformation to Digital economy and to what extent these digital transactions lead to transparent transactions, accountability and reduction of black money. Apart from this, the Research study is going to focus on how these banks and companies were able to tackle the sudden demand of digital transactions and able to meet the customer expectations.

Review of Literature. This mainly focuses on literature review of Demonetization. Demonetization is the act of stripping a currency unit of its status as legal tender. It occurs whenever there is a change of national currency: The current form or forms of money is pulled from circulation and retired, often to be replaced with new notes or coins.

Ashish Das, and Rakhi Agarwal, (2010) states that Cashless Payment System in India- A Roadmap” Cash as a mode of payment is an expensive proposition for the Government. The country needs to move away from cash-based towards a cashless (electronic) payment system. This will help reduce currency management cost, track transactions, check tax avoidance / fraud etc., enhance

financial inclusion and integrate the parallel economy with main stream.

Alvares, Clifford (2009) states that “The problem regarding fake currency existence in India.” It is clearly said that the India's battle against fake currency is not getting easier and fake notes go undetected. It is also explained that counterfeiters hitherto had restricted printing facilities which made it easier to discover fakes.

Jain, P.M (2006) in an article stated that “E-payments and e-banking” opined that e- payments will be able to check black money”. An Analysis of Growth Pattern of Cashless Transaction System. Taking complete advantage of technology, quick payments and remittances will ensure optimal use of available funds for banks, financial institutions, business houses and common citizen of India. This article also pointed out the need for e-payments and modes of e-payments and communication networks.

Dalia Marin (2003) stated that the virtual economy argument for Russia suggests that barter allows the parties to pretend that the manufacturing sector is producing value added by enabling this sector to sell its output at a higher price than its market value. Based on the pricing data of 165 barter deals we find no systematic difference in the pricing behaviour in non-cash transactions across sectors. What appears to matter for the pricing behaviour is whether the firm is on the selling or buying end of the barter transaction? It offers a model that sees this pricing behaviour as a mechanism to deal with the absence of trust and liquidity in the economy.

Gao Jing (2007) stated that the function of gold as currency is gradually weakening after the demonetizations of gold. But other functions such as value reserve become more important. Countries around world are trying to adjust the volume of gold reserves they hold to fit the optimal structure of the international reserves.

Simon Clarke (1998) in his article “The Financial System and Demonetisation of the Economy” say that demonetisation, criminalisation and monopolisation of the economy, which has led to the deepest and longest economic depression in world history, has been a direct result of the government's monetary and financial policies.

Based on the review of literature and research works, the present study is going to extract the facts of implementing Demonetization and its impact on public and Indian economy growth and development in the short run and long run.

Conceptual Framework

The Conceptual Framework of the research study evolves within the framework of Demonetization introduced by the government of India. Demonetization enhanced the cashless system where most of the transactions will come into account. So that it will be easy to levy GST on transactions. Here are the few concepts which will be used in the research study.

Demonetization: Demonetization refers to an economic policy

where a certain currency unit ceases to be recognized or used as a form of legal tender. In other words, a currency unit still loses its legal tender status as a new one comes into circulation. Demonetization is the act of stripping a currency unit of its status as legal tender. It occurs whenever there is a change of national currency: The current form or forms of money is pulled from circulation and retired, often to be replaced with new notes or coins. Sometimes, a country completely replaces the old currency with new currency.

Demonetization can also be referred to as the process of moving people from a cash-based system to a cashless system (digital system).

Cashless System: Promoting the digital/payment devices including prepaid instruments and card. The term Cashless system or less cash society or cashless transaction economy indicate reducing the use and usage of physical cash for receipts and payments. Instead of cash, digital transactions are made to settle the receipts and payments.

The research study mainly explores the impact of Demonetization introduction in eradicating black money and whether the Indian government is really successful in digital payment system by making transparent transactions and higher accountability of the public.

Need for the Study

Due to Demonetization, India's previously booming economy has now ground to a halt. All indicators – sales, traders' incomes, production, and employment – are down. Former Prime Minister Manmohan Singh estimates that India's GDP will shrink by 1-2% in the current fiscal year. The present study is conducted to know how much it is going to really affect the Indian economy and people of India in getting adjusted to digital economy (cashless economy).

Importance of the Study

Demonetization of the 500 rupee note and 1,000 rupee note – the two highest currency denomination will hit the Indian economy hard in the short run. But it is very important to know to what extent the economy is going to be hurt with this move. So, this study is going to articulate how demonetization caused downfall in the growth rate in the Indian economy in the short run and how it is going to benefit India in the long run. And this article is also going to analyse the people view post-demonetization.

Objectives of the Study

The present research study focuses on the impact of demonetization on general public and to know whether the government is really succeeded in declaring demonetization for transparent transactions, higher accountability and reduction of black money through the push of digital payments. The other objectives are as follows

1. To study the impact of demonetization and its contribution to digital economy.
2. To study the performance and challenges of banks post demonetization.
3. To analyze the performance and growth rate of e-tailing companies online payment transactions after demonetization.
4. To analyze the performance and growth rate of banking transactions post demonetization.

Scope of the Study

The present study mainly focuses on demonetization and its impact on the Indian Economy and People of India. Scope of the study is limited to the period of 50 days after Post-demonetization. And the study is taken on the perceptions of the citizens of the India and based on Market research. The study is undertaken for banks, online companies and general public. Regional, sectorial, industry and economy wise analysis is done to appraise the gravity and magnitude of Indian industries in general and large enterprises in Particular. The general public, bankers and customers of the e-tailing companies from particular area are taken to know their perception levels.

Research Methodology

The study is based on a descriptive approach by surveying the preceding studies in the same area and based on the analytical approach, a questionnaire is developed to answer the study questions, and test hypotheses.

- Primary Data:** The primary data relates to opinions, perceptions and views of knowledgeable people who are either actively involved in the transactions on either side, as well as those who are interested in the issue are taken. The instrument used to collect the information is Questionnaire. The primary data will be collected through interviews schedule and personal interactions. These interviewees were essentially attempts to explore the views and judgements. The interviewees include general public, bankers and customers. This source of data enables where ever there exists information gap.
- Secondary Data:** The access to the data and the information for analysis is obtained in documented form and the data is predominantly secondary in nature. The main sources of information are : (i) Government Records (ii) R Industry Records (iii) Books, journals, e-journals, periodicals and other published data and information.

Data Collection

The study is made with respect to online companies belonging to e-tailing sector which were considered after examining the company's annual reports, websites from published sources.

The companies taken for the study are Flipkart, amazon, Paytm and ebay. And Banks like SBI, IDBI, ICICI and HDFC will be taken for collecting information. Questionnaire is used to collect primary source of data. The questionnaire is divided into two parts: First part of the questionnaire includes Questions measuring demographic features of the respondents, and the later part of the questionnaire consists of phrases that test hypotheses of the study which defines weights of the phrases. Likert scale will be used and this scale consists of the following options: strongly agree, agree, neutral, disagree and strongly disagree. The reliability coefficient of the questionnaire is to be established, depending on the scale of Cronbach's alpha. The phrases (1-15) in the questionnaire measure the implementing the Demonetization in India, the phrases (16-30) measure the relevancy and success of Demonetization in India

Research Study's Population

The study population consists of Indian nationals who involved in online transactions and banking transactions. Questionnaire will be distributed to the customers, employees of the e-tailing companies and banks

To answer the study's question and to test its hypothesis, the following statistical method will be used: Measurements of descriptive statistics is done by using SPSS to describe the characteristics of the study sample, one sample T test to examine the first hypothesis and one way ANOVA test the other hypotheses.

Study's Variables

The study aims at investigating the relationship between Demonetization (dependent variable) and achieving and sustaining transparent transactions, higher accountability and reduction of black money (independent variables).

Methodology

The present study even includes an explanatory and exploratory study on how Demonetization is used by Indian Government in assessing and achieving transparent transactions, higher accountability and reduction of black money. A case study method is chosen because:

- It highlights the complexity of a single case.
- It is a study of the particularity and it is not designed to optimize on generalizations.
- It traces uniqueness.
- It is possible to select cases which are distinctive of other cases.

Research Techniques & Tools

The present study will be done by using case study method and hence the following analysis should be undertaken. The case study analysis is based on PEST Analysis, SWOT Analysis, Porters Five forces model, Value chain analysis, Competitive advantage, Strategy analysis and Generic Strategies.

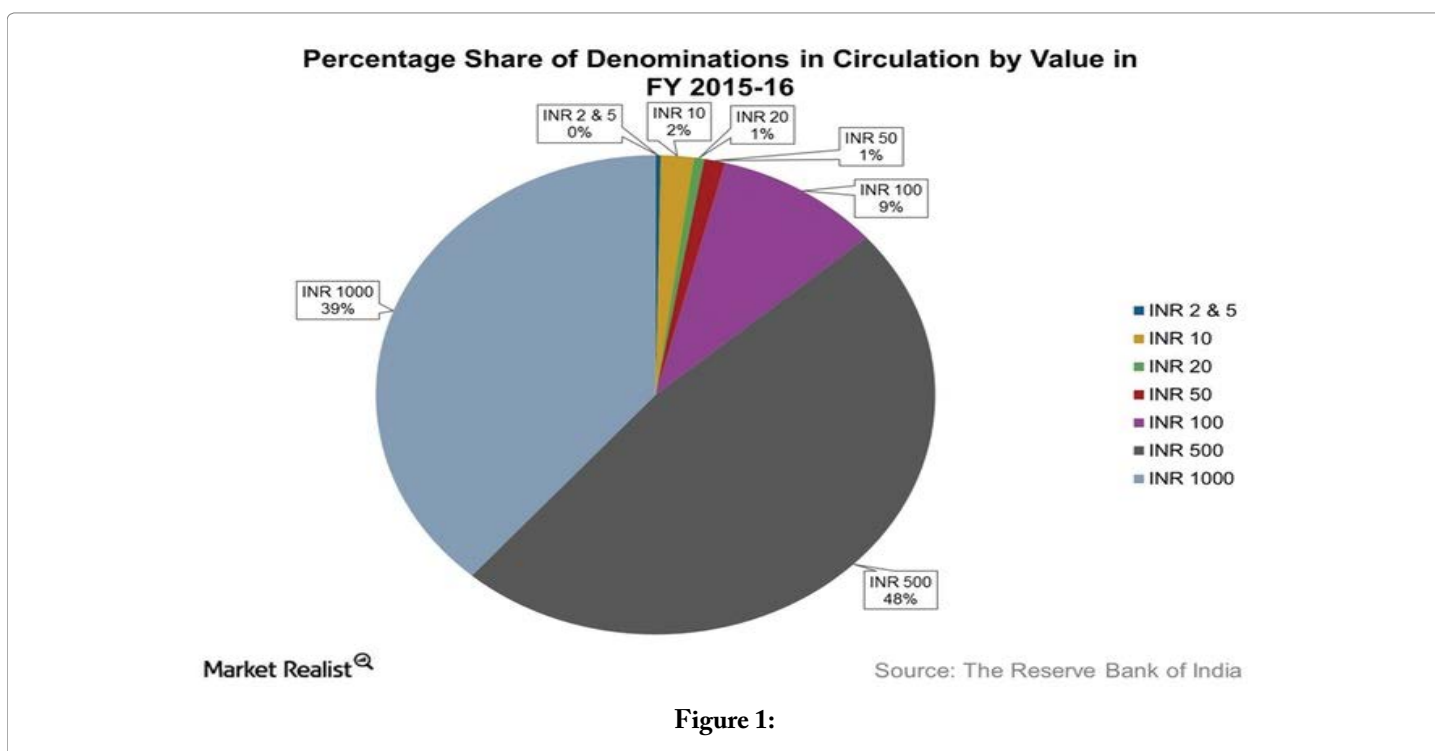


Figure 1:

Time Period of the Study

The time period taken for the research study is 2 years i.e., 2016-18. The previous year’s data and information is taken into consideration for analysing the country’s position and economy in the world. The time period taken for review of literature and past data sources is 6 months, field work is 7 months, Data/theoretical analysis is 5 months and Report writing is 6 months.

Limitations of the study

Demonetization primarily focuses on the RBI and government of India step towards nation building. Information is gathered based on interview schedule for primary source of data. However, research may lack exhaustive listing of reasons and strategies due to non-accessibility to some of the top officials who were directly associated with the Demonetization. Fixing the time frame of the study is a problem because Demonetization was implemented by the government of India recently. Only a portion of sample information is taken for analysing this research study.

Relevance, Anticipated Outcomes and Proposed Outputs from the Research

The findings are going to be based on the outcomes of the results on Demonetization. This research study is going to help policy makers in framing or modifying the policies accordingly based on the effect and impact of Demonetization. The outcomes will help the policy makers in changing the GST rates accordingly. Based on the findings of the research objectives and case studies, conclusions will be drawn and Recommendations will be made.

The main research problem is to trace whether Demonetization gave a good momentum on transparent transactions, higher accountability and reduction of black money through the push of digital payments. The research develops an understanding to enable companies, banks and general public to develop digital transactions that generates transparent transactions, accountability and helps the government in eradicating black money. Ultimately leads to nation building and economic growth & development of India.

The present research study helps to know the perception of the respondents in implementing demonetization and to what extent the government is successful in implementing it and succeeded in transparent transactions and higher accountability. This research determines to what extent respondents are willing to accept any future schemes of government of India in Nation building.

A brief Analysis of Demonetization

In an address to the nation on November 8, India’s prime minister, Narendra Modi, declared that the two highest denomination currency notes—the 500 rupee note and the 1,000 rupee note—won’t remain legal tender. The notes were demonetized at midnight on November 8. The move aimed to curb black money in the financial system. Black money is one of the factors holding back the economy. The demonetization was a surprise. Since the announcement, the media discussed the pros and cons for consumers and the banking system.

Lion’s share put out of circulation

According to the RBI’s (Reserve Bank of India) Annual Report

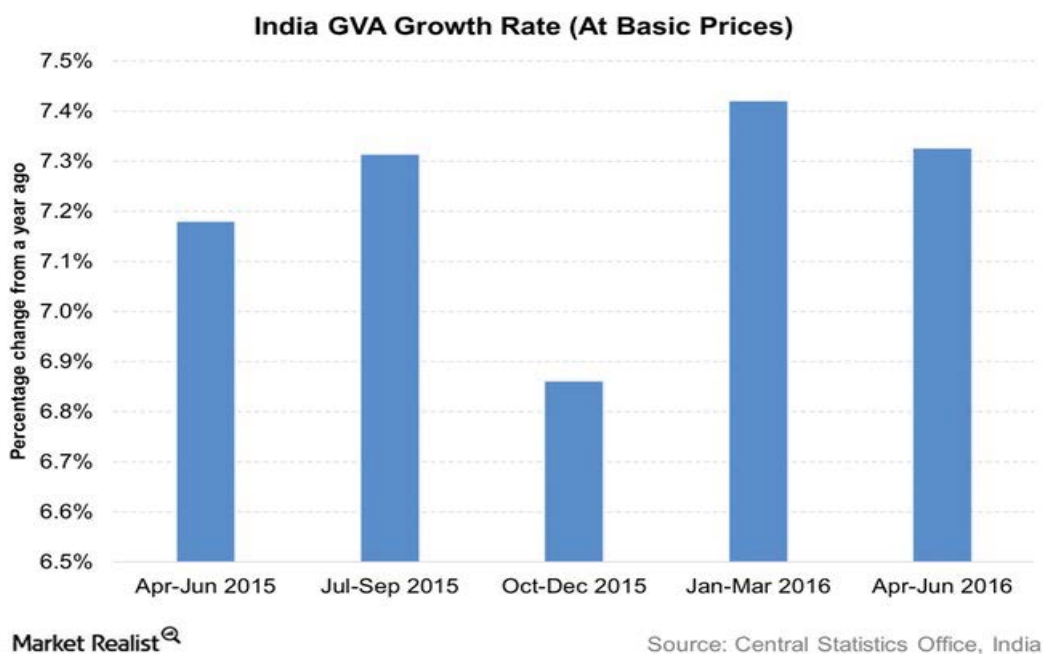


Figure 2:

for April 2015 to March 2016, the value of the currency notes at the end of March 2016 was 16.42 trillion Indian rupees. The 500 rupee and 1,000 rupee currency notes formed 86.4% of the value. In one stroke, the government removed 86.4% of the currency in circulation by value. In terms of volume, the currency notes of these two denominations formed 24.4% of a total 90.27 billion pieces. Also, RBI data showed that as of March 2016, 632,926 currency notes were counterfeit—known as an FICN (Fake Indian Currency Note). As a proportion of NIC (Notes in Circulation), the 1,000 rupee and 500 rupee notes were the highest. Nullifying these FICNs was also part of the demonetization move.

In this series, we'll look at the possible impact of the demonetization on the Indian economy. We'll discuss what it could mean for inflation, monetary policy, and financial markets (INDA) (PIN) (EPI). The series should help you assess what could transpire with your Indian investments in the short to medium term.

Let's start by looking at the broad impact that the demonetization had on the Indian economy.

Demonetization hit on the economy

The demonetization of the 500 rupee note and the 1,000 rupee note—the two highest currency denominations available in India—will likely hit the economy hard in the short term. The surprise move is expected to grind the consumption activity in the Indian economy to a virtual halt. The service sector, which dominates economic activity and involves a sizable chunk of cash transactions, will likely be hit the hardest.

India's economic growth

Growth in the Indian economy remained solid in the quarter from April to June 2016 (the latest available). In India, a financial year begins in April and ends in March of the following year. The previously mentioned quarter is the first quarter of fiscal 2016–2017. During that period, the GDP (gross domestic product) rose 7.1%, while the GVA (gross value added) rose 7.3%. The relationship between the GDP and GVA is:

$$\text{GDP} = \text{GVA} + \text{taxes on products} - \text{subsidies on products}$$

The base year for calculating the GVA is 2011–2012. The fall in economic activity due to demonetization could last from two to three quarters. As a result, GDP and GVA growth in the quarters from September to December 2016 and January to March 2017 could be significantly lower than previous years. Some bounce back should be seen in the first quarter of fiscal 2017–2018. In the medium term, the Indian economy can grow considerably after curbing the debilitation caused by counterfeit money and an increase in economic activity. A fall in discretionary consumption will hurt companies operating in this space. However, a rise in tax flow and lower interest rates, are expected to help the Indian economy grow stronger.

Conclusion

As the demonetization campaign progressed, its narrative gradually transitioned from being a measure to fight corruption to one to modernize a large swath of India's economy. Prior to this campaign, most of the country was firmly entrenched in the cash economy and there was very little incentive to break generations-old habits, get bank accounts, and go financially digital. But temporarily removing the society's access to cash pushed millions of people onto India's formal economic grid by all out fiat. Among the biggest criticisms of the demonetization campaign was that Modi and Co. simply did not take the lifestyle of the country's massive working class, poor, and subsistence-level agricultural population into account.

The providers of e-wallet and other digital payment systems have correctly viewed demonetization as a way to promote their services and to obtain new users. Since Modi's announcement, Paytm, a popular e-wallet, has seen a threefold increase in new sign-ups, while Oxigen Wallet's daily users spiked by 167%. "In the long run, this is nothing short of a revolutionary measure in moving a traditional cash centric economy to a fourth industrial revolution era. It's audacious, brash, and a future-centered decision, which has changed India, its people, politics, and money game forever," Prasad declared. "India will be 'before demonetization' and 'after demonetization,' BD and AD."

While the fundamentals of Modi's demonetization campaign appear sound — what government wouldn't want to curb corruption, clean out counterfeit currency, digitalized more of the economy, get a larger swath of the society into the formal market, and increase tax revenue? — the way that it was carried out appears to have been pointlessly rushed and under-planned, which resulted in a large amount of undue pain and inconvenience heaved upon hundreds of millions of people. However, the people of India for the most part steadfastly went along with their top leader's ambitious plan without any major protests, disruptions, or violence. "Given India is traditionally quite volatile and sensitive to certain aspects, this could have huge fiasco and embarrassment for Modi," said Prakhar Gupta, a resident of Lucknow. "But since no protests were there across India it means that there is a strong undercurrent of support for Modi as a person. But having said that, Modi has used up most of his goodwill and political capital with this move."

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