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SPECIAL ISSUE ON

**TAX REFORM FOR DEVELOPING
VIABLE AND SUSTAINABLE
TAX SYSTEM IN INDIA**

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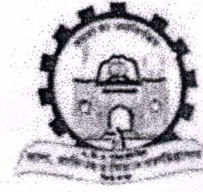


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Special Issue on "Tax Reform for Developing Viable and Sustainable Tax System in India"



Impact of Demonetization on Indian Economy

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Abstract-

Demonetization means that Reserve Bank of India has withdrawn the old notes Rs.500 and Rs.1000 as an official mode of payment. Demonetization is the act of stripping a currency unit of its status as legal tender. The Government of India declared that the old five hundred & one thousand rupees notes will no longer be legal tender from midnight, 8th November, 2016. Demonetization has impacted the Indian taxation system by making digitalization of payment & collection system. The RBI will issue 2000 rupees notes & new notes of 500 rupees which will be placed in circulation from 10th November, 2016. Notes of Rs 100,50,20,10,5,2,&1 rupee will remain legal tender & will remain unaffected by this decision. This measure has been taken by the PM in an attempt to address the resolve against corruption, black money and counterfeit notes.

Introduction-

Demonetization is an act of cancelling the legal tender status of current unit in circulation. Anticipation positive changes on the liquidity structure as a whole national often adopt Demonetization policy as a measure to counter balance the current economic condition. Countries across the globe have used Demonetization at some or the other point to control situations such as inflation & to boost economy. Money is the life blood civilization the needs of human beings increased. Money exchange facilitates ease of doing business, facilitates taxation & national integration. All activities such as exchange, production, distribution, services etc. from an economy it is called formal economy. Informal economy is neither economic activity that is neither taxed nor monitored by Government, contrasted with a formal economy.

Demonetization occurs when a particular type of currency is withdrawn from circulation. A situation the demonetized currency ceases to be recognized as a legal tender. Demonetization means stopping a form of currency from being legal tender. That means that this currency can no longer be legally used. It can not be used to buy things & if it is paid into the bank.

Bank manager should not accept it. In India Demonetization has occurred thrice. The first was on 12th January 1946, second on 16th January 1978 & the third was on 8th November 2016.

Demonetization proved that Indians can strive & adopt to any changes and made people financially aware about the different spending options. The government efforts to revamp the current system provided people with a boost to use the cash that was lying around and invest it in a more productive way. The return of almost all the demonetized currency to the banking system may create the false impression that the exercise was a failure benefits it such as the ability of income tax officials to track depositions & crack down on suspicious transactions could lead to long-term benefits.

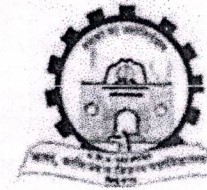
Impact of Demonetization in Indian Economy-

Demonetization is a generations memorable experience & is going to be one of the economic events of our time it's impact is felt by every Indian citizen. Demonetization affects the economy through the



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liquidity side its effect will be a telling one because nearly 86% of currency value in circulation was withdrawn without replacing bulk of it. As a result of the withdrawal of Rs. 500 & Rs. 1000 notes, there occurred huge gap in the currency composition as after Rs. 100 & Rs. 2000 is the only demonetization. Demonetization technically is a liquidity shock a sudden stop in terms of currency availability. It creates a situation where lack of currencies jam's consumption investments, employment, production following are the main impacts.

Not a Big Disaster- Demonetization is not a big disaster like Global banking sector crisis of 200% but at the same time, it will act as a liquidity shock that disturbs economic activities.

On Gross Domestic Product (GDP)- The Indian economy is a cash-driven economy & demonetization has largely affected its growth. The GDP growth rate of 8.01% in 2015-2016 fell to 7.11% in 2016-2017 after demonetization. This was largely due to less availability of cash in cash intensive industries like manufacturing and construction.

Impact on Bank money- Though only a small portion of black money is stored in the form of cash & majority is in the form of physical assets like land, gold & building. Demonetization of the rupee 500 & 1000 notes might take out a lot of black money from the economy.

Loss of Growth momentum- India risks its position of being the fastest growing longest economy reduced consumption, investment & income etc.

Consumption will be hit- When liquidity shortage strikes, it is consumption that is going to be adversely affected first consumption.

Over Financial inclusion- The inflow of cash into the banks will enable them to offer subsidized loans & other facilities to Jan Dhan account holder. The share of Jan Dhan Yojana account in total deposit base of the banking system is under 1%. Demonetization drive of higher denominated notes might proper cash deposits in Jan Dhan Yojana accounts.

Over Bond market- The ban currency notes will enhance the demand for government bond in the market. As we know it will improve cash deposits in the banks which will eventually lead to higher statutory liquidity ratio demand.

Over lending rates- Cash deposit base will enable banks to cut down the cost of funds because higher deposits will replace the high cost of borrowing & reduce overall costs of funds. It can be expected that banks can reduce deposit rates by 125 bps over the next 6 months. The new directives of marginal cost of funds based lending rate will instantaneously take into account in the lower cost. The way for a decline in lending rates, which will expedite the economic activity in the medium.

Impact on Bank deposits- Deposits in the short term may rise, but in the long term its effect will come down. The saving's with the banks are actually liquid cash people stored. It is difficult to assume that such ready cash once stored in their hands will be put into savings for a long term. They saved this money into banks just to convert the old notes into new notes.

Welfare loss for the currency using population- The daily wage earners, other labourers, small traders etc. who reside out of the formal economy uses cash frequently, these section will lose income in the absence of liquid cash. Cash stringency will complete firms to reduce labour cost & thus reduces income to the poor working class.

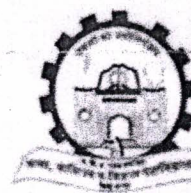


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Conclusion-

There are both impacts of Demonetization on different sectors. The demand of gold & luxury items was increased in the beginning period of demonetization. Demonetization is no doubt that is a great move for a better future of India & its economy. It will definitely influence many more shoppers to start using plastic money in the long term. If the money dissolves as some collectors would not like to be understood with their cash mound.

Demonetization in India is a great energy taken by Indian Government to battle with black money and corruption. It is a bold decision taken by Government. The main purpose of demonetization is eliminating the black money & decrease the corruption. Government of India has become success. The decision of demonetization will prove excellent in long run and our tax consultant will earn a huge profit because now the [people will appoint them for the returns & filling & the government can earn huge economic benefit.

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