

“Demonetization” - A Dead End for Shadow Economy: A Critical Analysis in Indian Context

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Abstract

The demonetization process has captivated many people's interest, and the system will face some serious resistance as a result of the decision. The present study intends to examine the effects of Currency devaluation and Indian economy's future prospects in light of the choice made. The study not only explores and navigates the topic of grafting, but it also covers a number of other topics that may have a direct or indirect impact on the Indian financial system as a whole. Every national interest triggers a well-established economy and planned infrastructural financial set up. The move to demonetize has however to some extent has met some sort of it. The black shadowed paper money required to be vanished off and this needs to be done keeping the fiscal deficit in row. Various available literatures were reviewed to know the impacts and effects of the move in this study. The statistical trend has a variety of long-term implications for the Indian economy on a global scale. The theme of the article also corresponds to prior demonetization choices in the past. As a result of this choice, a number of prominent sectors have suffered, and the research systematically attempts to assess their future performance. The outcomes of this study are, the move will plant innovative seeds such as elimination of Black Money, Tax Evasion and consequently, provides the Digital Platform and Cashless Economy. The change in the setup of traditional buying and selling of items would be changed forever, this in turn, would stagnant the dependency on Paper Money. Demonetization has a significant advantage in this regard. Income tax authorities will trace the money that is deposited. As a result, people will be hesitant to engage in tax evasion. In addition, the financing deal will be scrutinized and will be initiated through proper channel that will enhance the accountability. As a result, the flow of taxes would grow and the government would be forced to take more public welfare measures.

Keywords: Black Money, Tax Evasion, Demonetization, Digital Platform, Cashless Economy

1. Introduction

India, a country with many communities that inhales the strong odor of discrepancy in its financial connectedness, may add value to their financial situation as an undiscovered and immovable currency that may be in use after the decision is made. The immediate rationale, effects, and many critical assessments of the Indian government's decision to demonetize the currency notes of Rs. 500 and Rs. 1000 as of midnight on November 8th will certainly be drawn. The hasty withdrawal of notes from the active economy will have long-term implications and will effectively add more immovable, stagnant currency to the mainstream, eliminating the threat of inflation at its margin.

The decision should be viewed in an attempt to neutralize the stagnant currency and hidden currency that may hamper the national interest and the black money so collected in various banks abroad. There may be various reasons for different countries but in Indian context, corruption, black money, tax evasion and largely the depressed mood of the consumer towards using digital platforms for money transfer and fund manipulation seems to be on target.

2. Review of Literature

Ali Zaidi et al. (2017) in the research entitled “The Dilemma of Demonetization and its Impact on Indian Economy” carried out to determine the fundamental motivations, benefits, and impact of the demonetization policy on India's socio-economic situation. The study uses secondary data and is descriptive and exploratory in nature. The fundamental goals of demonetization are to protect and facilitate public funds, scrutinizing and preventing money laundering through the real estate sector, NGOs, and educational institutions by assuring transaction traceability across the banking system.

J. Bansal (2017) sought to analyze the impact of democratization on various sectors of GDP and the Indian economy. This study was quantitative in nature and secondary data were used for the analysis. As a result, GDP has declined slightly compared to the previous year, but not in the long run.

S. Chauhan, N. Kaushik (2017) tried to analyses in their research “Impact of Demonetization on Stock Market: Event Study Methodology” the impact of the Demonetization event on stock of S&P BSE 100 companies. In this study, In this research, the abnormal returns were calculated, OLS Market Model, Market adjusted return model and Mean adjusted Return Model were used. A fall in stock prices can affect several other external factors. And found in her study that there is no significant impact of the demonetization on the stock market and the short-term drop in stock prices could be attributed to other unrelated issues.

3. Statement of the Problem

Based on the review of available literature, it has been observed that the significant limitations of the studies being made as it delimits the overall scenario of the demonetization in context of such as long-term economic stability and many more. Impact of going to be on entire Indian economy would react to the demonetization. Hence, it was my curiosity to study the critical analysis of the demonetization on various aspects.

4. Objective of the Study

The main objectives of the study are as follows:

1. To ascertain the result of demonetization on various sectors in Indian context.
2. To know that, how far the demonetization has been effective in curbing the practice of black money and tax evasion.
3. To know the long-term impact of the demonetization. Futuristic trend of cashless economy and digital payment interface that may result the use of paper money to its minimum.

5. Research Methodology

For the present study, we have used the secondary data to collect the necessary information's. Secondary data are collected from peer reviewed journals, books and relevant websites. Tools such as theoretical analysis of the available literature are used in this study.

6. Analysis and Interpretation

Historical Reference

Demonetization was enacted to combat the threat of a shadow or parallel economy resulting from the proliferation of counterfeit notes and undeclared illicit money. The last time India took such a step was under Morarji Desai's Janta Party government, when the Rs. 1,000 note was removed from circulation. The government took nearly two decades to reintroduce bigger denomination currencies. The decision to demonetize Rs. 500 and Rs. 1,000 currency notes overnight is not a new one. In January 1946 and 1978, Rs. 1,000 and higher value currencies were demonetized. The Rs. 10,000 note, produced between 1938 and 1954, was the biggest denomination note ever printed by the Reserve Bank of India. As per the RBI Figures and data, these notes were demonetized in January 1946 and January 1978. The Rs. 1,000 and Rs. 10,000 banknotes were in use prior to January 1946. Higher denomination bank notes of 1,000, 5,000, and 10,000 rupees were reintroduced in 1954, but they were all demonetized in January 1978. The only indication of all these previous demonetize stunt put forward a strong commitment of financial institution towards neutralizing the corrupt practices such as fake circulation and unaccountable currency.

A Surgical Encounter to Shadow Economy

The bold decision of devaluing Rs. 500 and Rs. 1000 notes must be a heart attack for the rackets that centrally aims to devastate the progress of India by fake generation of notes. Shadow or Parallel economy is worth to understand in a way to realize the significance of demonetization and what this decision brings for a common man that struggle to achieve some immediate assignment for nation. Shadow economy can be defined as "Unidentified economy that is generated as a result of unaccounted circulation of currency under the table and is liable to be used for developmental process". The opposition has put forwarded many allegations on the contrary side but it seems nothing strong then mere gaining a political edge out of it.

The shadow flow of money, undoubtedly, A real challenge for many of developed and under developing countries that hampers the growth of economical circulation and smooth financial functioning. As addition to demonetization, the Financial Intelligence Unit is gathering evidence from banks on major cash transactions, which will be shared with the Income Tax Department in the future. This will not only help to uncover concealed assets, but it will also contribute to greater tax compliance in the future.

Strengths and Weaknesses of the Move

Strengths

Diminishing Fraudulent Practices: The most significant benefit of demonetization is the reduction in fraudulent activity in the country. People holding black cash would be afraid of being penalized for these crimes while storing funds for exchange with banks because they would be unable to swap black money with banks during the process. As a consequence, it is an optimal method to counter-terrorism or other illicit behaviour requiring currency counterfeiting.

Carry a Charge System: The banking system will significantly improve as a result of demonetization. In the long run, if the economy evolves toward a cashless economy, it will open the way for better credit access in the economy. The remainder of the white cash will be handled by the government. Banks and financial organizations can now use the newly legalized money to grant loans to deserving applicants while also generating income for the banks.

Liability Reduction: Allowing demonetization reduces the risks associated with handling liquid currency. All issued notes are a liability for the government, and individuals who choose to turn in their earnings will forfeit the value of the present notes. As a result, in the format of demonetization, the government has a lot easier time managing the country's economy.

Reduced Instances of Tax Evasion: If carried out correctly, the abrupt severe relocation can substantially lower tax avoidance. The Indian economy might benefit significantly from tax avoidance. The government may be able to implement public welfare initiatives as a result of greater tax revenue.

Increased GDP: Higher tax collection allows for lower interest rates on bank loans; hence, misinforming tax avoidance can introduce clean money into the currency stream and enhance the country's economy's disposable income.

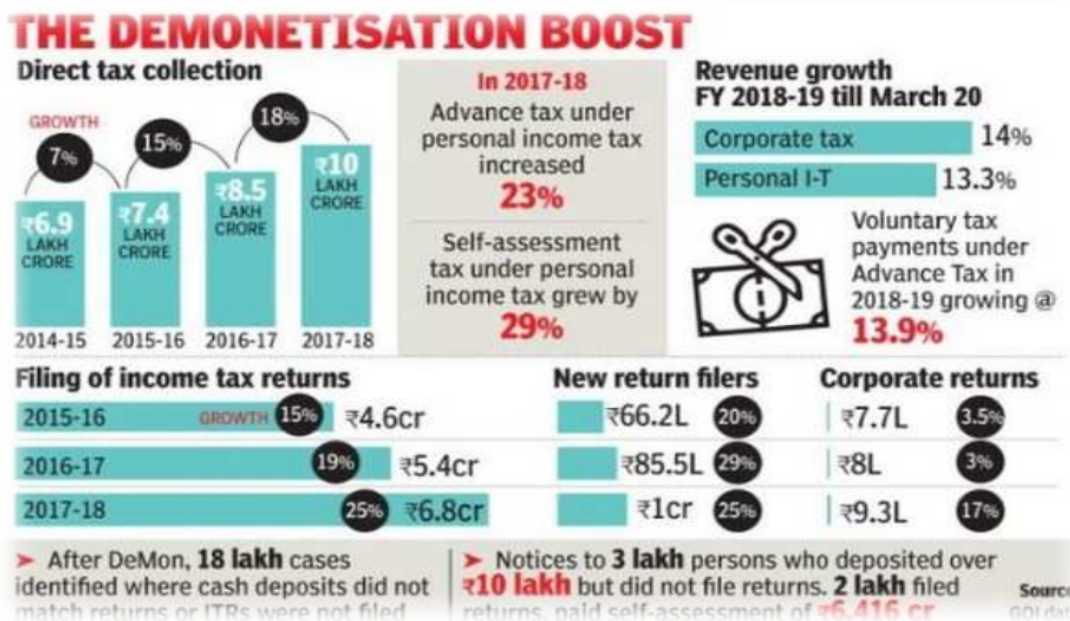
Weaknesses

According to a study published by the Reserve Bank of India in 2018, nearly 99.3% of the demonetized notes worth Rs. 15.30 lakh crore were deposited in the bank. Only Rs. 10,720 crores were spent on banknotes that were not deposited. As a result, analysts concluded that the attempt to combat the threat of black money in the market had fallen short of its goals. Furthermore, not only did this rash choice reduce industrial output, but it also had an impact on GDP growth. Demonetization has also resulted in the loss of 50 lakh employment, according to a report by Azim Premji University. Following the announcement, we've noticed that many people have burned their cash and thrown it away, causing a loss to the economy. The government is responsible for the costs of creating and circulating new currency. When the advantages of demonetization are greater, it makes sense. One of the major downsides of de-monetization is the cost of currency printing, which is a burden on taxpayers. Subsequent IT raids and the discovery of crores of unaccounted money in national currency demonstrate a gap in the decision's execution. Most bank employees who are involved in money exchange with high-net-worth persons, making it impossible to fulfil the goal and causing a cash shortage in the economy by not making a new currency available to the common man, who is the engine of the economy. Because of criticism from well-known economists and neutral parties, people began speculating on a currency crisis and began hoarding their money (no matter how tiny) rather than spending it, exacerbating the issue. If not spent appropriately, the fiscal stimulus that the government is projected to receive could lead to fiscal indiscipline. The government took advantage of this opportunity to promote electronic payments so that black money can be curtailed to some extent and traders cannot avoid paying indirect taxes once the transaction is digital, hence raising state revenue and lowering the fiscal deficit.

Inherent Disadvantages in Demonetization

We still have a long way to go toward being a cashless society, particularly in terms of digital transaction security. Even if a person is willing to conduct a digital transaction, most sellers are not. This is due to a lack of understanding on the part of the vendors. Because of their illiteracy, the rural poor may find it difficult (without assistance) to transition to the digital economy.

Statistical and Tabular Report of the Income Tax Collection Post Demonetization



“The revenue growth trends continued in the 2018-19 fiscal year, more than two years after demonetization, with corporate income tax growing at 14% and personal income tax at 13%. Voluntary tax payments under advance tax are also growing at a healthy rate of 14% which, if seen along with increasing digitalization, points to a cleaner economic system.” (Source: <https://timesofindia.indiatimes.com/business/india-business/direct-tax-collection-up-sincededemonetisation/articleshow/69077749.cms>)

Statistical Implication on Various Sectors and its Interpretation

Post-Demonetization Implications of Tax Collection

The total number of income tax returns filed in March 2014 was 3.8 crores. This value increased to 6.86 crores in 2017-18. When the impact of demonetization and other measures is considered, income tax returns have climbed by 19% and 25% in the last two years. This is a remarkable increase. In the two years since demonetization, the number of new returns filed has climbed by 85.51 lakhs and 1.07 crores. For the 2018-19 fiscal year, advance tax increased by 44.1% for personal income tax assesses and 17.4% for corporate tax assesses in the first quarter. Income tax receipts climbed from 6.38 lakh cores in 2013-14 to 10.02 lakh cores in 2017-18. In the pre-demonetization two years, income tax revenues grew by 6.6% and 9%, respectively. In the two years following demonetization, collections grew by 15% and 18%. In the third year, similar pattern was seen. After demonetization, the GST was imposed on July 1, 2017. The number of assessors registered climbed by 72.5% in the first year. The initial assessment of

66.17 lakhs has been enhanced to 114.17 lakhs. Demonetization has had a good effect in this way. Subsequently in the first two quarters, the wealth has become more formalized, with more money in circulation, higher tax returns, higher expenses, and higher growth. (Source: <https://pib.gov.in/newsite/PrintRelease.aspx?relid=183178>)

The following year, FY18, the number of tax filings filed increased by 23.1% to 68.7 million. According to Income Tax interpretation which followed the government's campaign against black money, had supported this spike, as well as the economy's constant expansion. From 6.4% in FY14 to 8.2% in FY17, the Indian economy grew steadily. Despite the fact that economic growth slowed to 7.2% in FY18 from 8.2% the year before, tax return registrations increased by 23.1%. Return filings, on the other hand, did not maintain the enthusiasm over the next fiscal year, falling roughly 2% to 67.4 million in FY19 from the previous year's strong natural as economic growth slowed to 6.8%. (Source: <https://www.livemint.com/politics/policy/economic-downturn-dents-growth-in-tax-returns-seen-after-demonetisation-11573190535672.html>)

Post-demonetization implications on Black Money

Is demonetization's goal of eradicating dark money being met? According to data from the Reserve Bank of India, practically all of the money that was invalidated was restored to the banking system (more than 99%). Out of the Rs. 15.41 lakh crore in notes that were invalidated, Rs. 15.31 lakh crore in notes were returned. In February 2019, then-finance minister Piyush Goyal told Parliament that numerous anti-black money actions, including demonetization, had resulted in the recovery of Rs. 1.3 lakh crore in black money. (Source: <https://www.moneycontrol.com/news/business/after-5-years-of-demonetisation-black-money-is-very-much-around-7695611.html>)

Post-demonetization Implications on the use of UPI and Digital Payment Interfaces

The quantity of notes in circulation increased by Rs. 2,28,963 crore on October 29, 2021, compared to Rs. 26.88 lakh crore on October 30, 2020. The year-over-year increase was Rs. 4,57,059 crore on October 30, 2020. According to the report, the rise in NIC from the previous year was Rs. 2,84,451 crore on November 1, 2019. According to the latest Reserve Bank data, the value of the notes in circulation climbed from Rs. 17.74 lakh crore on November 4, 2016, to Rs. 29.17 lakh crore on October 29, 2021. The value and volume of banknotes in circulation increased by 16.8% and 7.2%, respectively, in 2020-21, compared to 14.7% and 6.6% in 2019-20. (Source: <https://www.businessstandard.com/article/economy-policy/post-demonetisation-notes-in-circulation-on-rise-so-are-digital-payments-1211107004041.html>)

Terror Funding ban after Demonetization

While illegal financial cash transfers to terrorists and separatist elements in Kashmir, which were mostly in denominations of Rs. 500 and Rs. 1,000, have ceased, Maoist groups, particularly in states like Bihar and Jharkhand, are finding it difficult to capitalize on ransom money that has been piled up as "legal tender." According to Intelligence report regarding tracking terror funding in Jammu and Kashmir, the scrapping of the Rs. 500 and Rs. 1,000 notes caused hawala networks to dry up. Due to a lack of illegal funds to support violence and protests, the valley's top troublemakers have been forced to go undercover. Since they can no longer afford to pay local kids to throw stones and conduct violent protests, they have

run out of money. (Source: <https://economictimes.indiatimes.com/news/defence/demonetisation-effect-funds-tap-turns-dry-for-terror-and-maoist-groups/articleshow/55448082.cms>)

Findings and Conclusion

The demonetization has overall positive impact on various sectors of the economy, but it was not planned move and created some sort of financial hassle to one section of the society. It has not been able to achieve the results for which it is launched and failed to achieve the desired results of the move. After this historical move one thing can be said that it has been proved to be birth giver to the Cashless Economy to a greater extent. Now, most of the population transacts cashless by using digital interfaces, which in turn, the use of paper currency to its minimum.

Conclusion

Demonetization was enacted to combat the threat of a shadow or parallel economy resulting from the circulation of counterfeit notes and undeclared illicit money. The last time India took such a step was under Morarji Desai's Janta Party government, when the Rs. 1,000 note was removed from circulation. The government waited over two decades to reintroduce higher-denomination currency. Moreover, the immediate beneficiaries of this decision will be the country's startups operating mobile wallets and online payment platforms, as submitted by many most of top entrepreneur that positively such a move will encourage people to use digital platform for all trading. Use of E-wallets and E-transactions will ensure a supervised, safe and controlled flow of currency and thus it will help stakeholders to check upon black perpetrators and their black earning. Terrorists' unlawful purchases of weaponry and ammunition, banned substances, counterfeit currency rackets, and recruiting foreign hands to destabilize the country's integrity and security, among other crises, will be dealt promptly. In the next days, the introduction of digital transactions and the concept of plastic money will assure a transparent economic activity. The unreported and unregulated currency will begin to circulate in the system and can be used to fund a variety of pipelined initiatives, giving hope to the impoverished and underprivileged masses at large, and ensuring that economics is a top-scoring topic in the Indian curriculum. Following the study to a favourable climax, it adequately solves numerous security threats to the country not only on physical boundaries, but it has also prepared the path for a stronger and more transparent economy.

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