Demonetisation - Impacts after an year

Why in news?

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November 8th marks the 1st year anniversary of the announcement of Demonetisation.

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What were the objectives?

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- 86% of the currency in circulation was withdrawn in one fell stroke.
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- This was done to achieve -\n
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  - a lower cash-to-GDP ratio
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  - subsequent reduction of black money
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  - cutting fake currencies
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  - curbing terror fundings
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  - pushing digital transactions
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  - increasing the tax net.
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What are the positive effects?

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- DeMo has rung in a climate of tax compliance, even if through coercive means.

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- Deposits worth nearly Rs.3 lakh crore are under the scanner.
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- According to the Finance Minister, an additional 9 million people have come under the tax net.
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- Over 200,000 shell companies have been deregistered.
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- Real estate shenanigans have been reined in.
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What are the negative effects?

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- **Growth -** Growth has been slowed down since DeMo.
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- GDP growth in Q1 of 2017-18 was at 5.7%, against 7.9% in 2016.
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- Rural sector was affected the most with 2.3% growth in Q1 2017-18, against despite record foodgrain output in 2016-17.
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- Earlier a rapid recovery from the slowdown was predicted. But the narrative has now been changed into ‘short-term pain for long-term gain’.
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- **Price -** Prices have crashed in major markets for kharif crops such as maize, green gram, groundnut, soyabean and sunflower despite their output being either flat or marginally lower than last year.
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- It is primarily because of the disruptive impact of the withdrawal of cash on supply chains and inventories. Click here to know more about Impact of DeMo on Prices
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- **Unemployment -** The rate of loss of jobs registered in the trade sector and industries was “almost” 55% in the two months after the note ban.
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- The job loss is significant in the middle-age group (40 to 50), among people with limited options.
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- Job creation was zero in November-December 2016.
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- It improved to a growth rate of 10%-15% in January-March 2017, and to 20%-25% in April and June, but again, between July and October, fell to

5%-10%.
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- **Return of cash -** Though cashless transactions prevailed initially, cash has returned.
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- The major reasons for this are connectivity issues with POS, the transaction charge and security concerns.
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- **Logical flaw -** To say that a 12% cash-to-GDP ratio for India is too high, when compared with other countries, is incorrect.
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- This comparison is not valid as India has a large informal sector.
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- So its cash needs are also higher.
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- A lower cash-to-GDP ratio could mean that the informal sector has shrunk due to demonetisation thereby needing lower cash.
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- This indicates rise in unemployment.
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- **Ignoring Other Factors –** Government projects that it achieved a lower cash-to-GDP ratio of 9% after demonetisation, from over 12% earlier.
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- This might be due to a combination of factors apart from a shift towards digital transactions.
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- It might be due to lower currency supply, shrinkage in cash-dependent enterprises due to the note ban, and shortage of cash in pockets of the economy.
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- **Terror Funding -** Since demonetisation, the number of infiltration attempts in the Valley has reached a high,.
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- The number of civilians killed has trebled.
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- In the theatres of Left Wing Extremism, more security personnel have been killed in Naxal attacks but in fewer incidents, which have dropped 21%.
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What should have been done?

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- Cash plays a significant role even in developed economies such as Japan.
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- So the criminalisation of the entire cash economy seems unfair.
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- Hence the debate on DeMo is about ends and means.
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- The same outcomes could have been achieved with less pain.
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- DeMo could have been implemented in a gentler way — with ‘nudging’ rather than bureaucratic diktat.
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Source: BusinessLine, Indian Express

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