

# Impact of Demonetization: Short Run Vs Long Run effects

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## Abstract

Demonetization is the act of stripping a currency unit of its status as legal tender. The old unit of currency will be replaced with a new currency unit. The currency was demonetized for the first time in 1946 and second time in 1978. Third time on Nov 8th 2016 the 500 and 1000 rupee note currency is demonetized and replaced with new 500 and 2000 rupee note by the present Modi Government.

This is the bold step taken by the Government for the betterment of the economy and country. In this paper I would like to discuss the impact of recent demonetization in the short run as well as Long run effect in India. The move was targeted towards to put a check against Fake currency, Black money, Corruption and Terrorism. Unbanked villages, small businesses badly hit as currency crisis continues.

## Introduction

The Government of India announced that the 500 and Rs. 1000 denominated currency notes will not cease to be legal tender from 8th November 2016 midnight 12.00 pm. The move was targeted towards tackling black money, corruption and terrorism. After initial euphoria, questions began to emerge. How does this demonetization affect the economy? How does GDP get affected with this move? What is its effect in the short run as well as Long run? Will the Black Money be completely eradicated? Does the Black turns into White? Is the pain of Demonetization worth the gain we get from it? Is it a unplanned decision of central Government? Is it a process of cleaning up the country's financial system.

## History

Demonetization took for first time in the year 1946 January of 1000 and 10000 rupee notes which were reintroduced again in the year 1954 in 1000, 5000 and 10000 denomination. Subsequently in the year 1978 Government demonetized 1000,5000 and 10000 notes from economy.

## Objective of the Study

The main objective of this Paper is to know the effect of Demonetization on 8th November by the present government in the Short Run as well as Long Run.

## Methodology of the Study

Data has been collected from various secondary sources. It was collected from various published sources like News Gazette, magazines, journals, newspapers and Media etc.

## Short Run Effects

Sudden decline in paper Cash in the Economy which effect demand of Goods and Services as the flow

Black money comes down which is directly linked to GDP will also come down in short run. Demonetization resulted in short-run disruptions in economic activity in cash-intensive sectors like Retail, Trade, Hotels, Restaurants, Transportation and the unorganized sector. Hit on Hotels, Restaurants and Food joints which do not have swipe machines. Tourism and Travel Industry hit as bookings has come by 7% to 80% and plans cancelled. Shortage of Working Capital was majorly felt by small and Medium Entrepreneur.

Diesel and petrol use, which account for more than half of India's oil demand, has slowed down during the first quarter of Demonitisation. Several Corporate Hospitals refused to accept banned notes and instead asked patients to extend their stay during first two weeks of post demonetization. No money and No Medicines for some.

Anakapalli Jaggery market which has annual turnover of 150 crore has shut down temporarily during demonetization due to crunch of Hard cash. Lost 2 crore just in two days. During the period of Nov 10th to Nov 30th 1.77 lakh borrowers has repaid loans over 25lakhs using old currency repayment which added upto nearly 50000 Crore.

Income earning departments like Registration, Excise & Prohibition, Commercial taxes and other Tax collecting wings are reporting a steep fall in revenue. When Government said no Black money through Demonetization people started converting it into Gold Overnight in Crores which resulted in inflated increased demand for Gold. Nearly 1.5 lakh Small and Medium industrial units like Plastics, Manufacturing, Steel and Cement along with the Hyderabad City's belt have now stopped production due to severe Cash Crunch. While some are operating 10% to 20% of its Capacity.

- Small traders and Kirana store owners have witnessed a huge drop in Business. People stuck to minimum purchase even when it comes to basic necessities. People surviving on daily wages got affected badly
- Activities of Naxals and Terrorists has come down due to non availability of Cash
- Temporary suspension of Toll in Major Highways
- Limit on number of withdrawals in ATMs have been waived temporarily during this period
- SBI has waived charges on Rupay cards which usually range from 0.75 % to 2.95% during this period to subside the problems faced due to non available of cash.
- Many of the Banks and ATMs running out of cash by forenoon.
- A lot of Entrepreneurs are sending out employees to exchange cash and some of Labourers were paid in old currency even after demonetization.
- 90 people lost their life standing in queues near Banks and ATMs for cash and some committing suicide due unexpected move of central Government.
- Entertainment Industry is no escape as Movie theatres being empty in the initial days of Demonetization.
- Some People postponed weddings due to non-availability of cash though Government gave limit of 250000 to withdraw.

### Effect on Auto Industry

The Government decisions to ban 500 and 1000 notes have crippled sales of Cars and Two

## Management of Demonetization: Challenges and Opportunities Ahead



- Boost in demand for consumer durables and automobiles.
- Increase in Point of Sale machines.
- Increase in micro ATM's in rural areas

Though the market goes down in the short run it will move to positive side in the long run which will build confidence of overseas investors in Indian Stock Market.

The Sectors or Schemes expected to affect severely are Major & Medium irrigation, Mission Kakatiya, Mission Bhagiratha, Roads and Building, Housing, Social Welfare schemes such as Aasara Pension, Shaadi Mubarak, Kalyana Lakshmi, Pre & post matric scholarships, Fee reimbursement, Partial Waiver of farm loans, Power Subsidy for Farm Sector, release of funds for Panchayat Raj and Urban local bodies, interest payments & servicing of debts etc.

## Conclusion

It's a Remedy and not a tragedy!!! Though its hurting common man hard. It's a process to clean up the country's financial system. Demonetization will have a "negative" impact on growth in the short run but for the full fiscal, the GDP decline would be "relatively moderate", the impact on GDP growth is clearly going to be negative in the short run and depends to a large extent on how long the cash crunch is going to take. Demonetization was done for a "long term structured transformation" it's a step towards organizing the Economy. It's a short-term pain but long term gain. Its Boom time for swipe machine makers. Transaction fee on debit and credit cards should be waived off to encourage digitalization.

Digitalization is going to happen, Cyber security is a major concern in transactions we should take measures to avoid cyber crime like Pharming (fake website that seems similar to original) Keystroke Logging, Malware etc. One of the challenge to the Government is 76% of Indians are not on Internet.

In any value chain, the last link is mostly cash. There has been slowdown in the off take of the Goods because cash has not been immediately available. But the fact is its temporary in nature. Demand still exists in the country. As there is demand still people will readjust their models, come back and do their business. The amount that is coming into the bank will not remain fully with the bank, around 10% to 15% of it will remain in the bank and rest will have to go back in the Economy not as cash but as transfer transactions.

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