

Demonetization: A Step towards Cashless Economy in India

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Abstract

Cashless economy is considered as harbinger of transparency and economic growth by many economists. Many developed nations have implemented less cash economy in financial transactions. India, however has been largely been a cash transaction oriented economy. Move of demonetization by Prime Minister of India in 2016 has been a significant trigger for transformation to cashless economy. Current study analyzes cashless economy in Indian context with its advantages, disadvantages and hurdles faced by India in adapting to digital mode of transactions. This move has been like a shock treatment for many people in India, as whole economy was brought to stand still for some time owing to lack of capital. Initially portrayed as step to remove unaccounted money, finally it was switched towards implementation of cashless economy. People were forced to adopt a digital means of transactions. In hindsight, it has been a revolutionary move as it will lead to a modern India where transactions will be digital and will be accounted for. Ultimately it will be able to reduce corruption and limit black money and improve financial wellbeing all of each and every citizen.

Keywords: Cashless Economy, Demonitization, Digital Transactions.

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1. INTRODUCTION

As per the dictionary of economics, the cashless economy is “An economy that operates without notes and coins. When the concept was first introduced it was envisaged that checks and credit card transactions would steadily replace cash. This has not occurred, but the growth of electronic money has revived the possibility of the arrival of a cashless economy” [1]. The idea of a cashless society originated in United States around mid-1950s with hope that all traditional money exchange using currency bills, cheques and coins will be gradually taken over by electronic transfer [2]. No nation is truly cashless if this definition is faithfully followed. However, in most of economies of developed nations, majority of transaction are conducted without involving currency bills. Scenario is little different in India where cash is used in more than 90% transactions.

In an unannounced address to nation on 8th November 2016, Prime Minister of India announced that 500 and 1000 INR bills, which constituted 86% of currency in circulation, would no longer be legal tenders from same midnight. It sent shock waves throughout country with everybody trying to exchange currency. This was an audacious and very bold stand taken by chief executive of an economy where income tax is paid by less than 5% of population and which suffer from endemic corruption. Only radical move could change condition in a nation, plagued by so much dysfunctionality.

2. RESEARCH METHODOLOGY

2.1 Nature of Data: Secondary data: Already published work used for secondary data. It was both internal and external. Internal source: Originated from the specific field or institution where research was carried out e.g. published brochures, official reports etc.

External source: Originated outside the field of study, such as books, periodicals, journals, newspapers and the internet.

2.2 Data Collection and Analysis: Secondary data was used for this study, collected from articles, reports, journals, magazines, newspapers, reports prepared by research scholars, universities and internet. Simple analysis was made to find conclusion.

3. OBJECTIVES OF STUDY

- To investigate the conceptual issues related to cashless economy with their implication on Indian economy.
- To understand the benefits and disadvantages of move of demonetization, hurdles on path of cashless economy and prediction of futuristic scenario.

Cash dependency of Indian economy: In India, a high proportion of financial transactions are done using cash. It has one of the highest of currency notes to GDP ratio. It was 12.42% for India, compared to 4% for Brazil. By conducting its business in cash, India is plagued with old rigid system of finance and it is putting obstacles in its to path to modernity.

“No force on earth can stop an idea whose time has come”, said the great French author of 19th century, Victor Hugo. This is the time for India to change, to claim its position in world order. A growing economy and regional superpower of South East Asia, India needs to adapt to ways of modern world to realize its aspirations. There are many drawbacks with using cash for transaction. First there is cost involved in printing proof, paper bills, disbursing it in system and collecting it few

years to pump new currency in system. Even after using cutting edge technology and best efforts, forgers are able to make counterfeit bills and push it in financial system. Massive amount of counterfeit currency is used by terrorist groups and mafia syndicate in India, as revealed by intelligence reports from time to time. A cashless economy will put an end to such 'criminal' economy.

In a cashless economy, money is in possession of a third party, which could be government or banks. This money could be used for transaction whenever needed. Money not being used for transaction could be used by third party. This feature of cashless economy uplifts the overall economy.

People in India, don't love, they just worship cash bills. Before demonetization, 90% transactions were conducted in cash. Even in posh malls, which are frequented by upper middle class and upper class people, most of transactions are in cash. Many people in India have debit cards, but these are used only for withdrawing money from ATM. Using cash is not a big problem. Real issue is that it is intermingled with black economy. A shopkeeper dealing in cash can do without recording all dealings in his account books. Many small level businesses do not even maintain proper books due to lack of training and inability to hire an accountant. Even big businesses omit some deals and conduct operation in cash to avoid paying taxes. In India, only 5% of people pay taxes in their income and only 15% of national income is accounted by tax authorities (Economic survey of Government of India). It does not mean that every person is dishonest. Many people are patriotic and upright citizens. They want to pay taxes to contribute in development of nation. However, tax rate is very high and market is very competitive.

Many whole sale dealers do business at a narrow margin of 2-3% profit. They have to keep their rates minimum considering rates offered by their competitor. Now, if one of those businesses is diligently paying its taxes in regular manner, they need to increase the price to make profit. But, then their price will be higher than others and they will find it extremely difficult to do any business. Conversion of economy to cashless will force people to pay taxes regularly and accordingly set price to be able to make profit. In USA, reduction of corporate taxes in era of President Ronald Reagan saw a massive increase in economy. A similar move by Indian government is expected to boost Indian economy too.

4. ADVANTAGES OF CASHLESS ECONOMY

Implementing cashless economy has many advantages. It will boost tax collection as it will be difficult to hide transactions. The black money generation will be curbed as expenses will be tallied with income and investments and money trail will be impossible to bury. For real estate deals, major part of money was paid in cash due to avoid paying tax as well to hide source of income. Many deals used to be *benami*, so real estate purchase was a front for a rich person to stash his ill-gotten wealth and use someone else's name as front. All these factors resulted in enormous hike in prices of real estate in India in last 15 years. Affordable housing had become a distant dream for a major segment of population and those could fulfill it had to pay heavy EMI from their earning or sale ancestral properties or give up luxuries of modern society such as air travel, tourism, entertainment, dining out.

Demonetization will bring banking services at everyone's doorstep as no other than digital means, no other infrastructure is required. It will also promote a healthy environment as many

notes are soiled or stained with tobacco or germs. By removing compulsion to touch currency, germ spread will also be reduced. It will also increase speed of getting things done. No time will be wasted in counting money or standing in queue to withdraw money from ATM. People will keep money in bank which will increase tax revenue and banks will have more money to distribute loans at reduced interest rate. Government will be able to spend more money for welfare programs.

It is not just taxation which is affected by cash. In many organized sectors such as construction salary is paid in cash and employer avoid paying other facilities such as provident fund, medical and life insurance. A cashless economy will make employer more accountable and force them to provide all facilities for employee. Many businesses are planning to go complete cashless. There is no possibility of stealing money, no need to keep enough change to maintain smooth transactions, no need to tally balance at the end of day and clerks do not have to rush to bank to deposit the sales amount.

Kenneth S. Rogoff, the Thomas D. Cabot Professor of Public Policy at Harvard University and former chief economist of the International Monetary Fund, is a strong proponent of cashless economy. He is the author of bestseller book, 'The Curse of Cash'. According to him world is drowning in cash and it is making world poorer and unsafe place to live. An average American hardly touches a \$ 100 bill. Yet there are 42 of these bills in circulation for each US citizen. This surplus of cash is nourishing corruption, tax evasion, terrorism, narcotics business, trafficking of human beings for sex and labour, and promoting a parallel underground economy. He argues that by promoting a cashless system, the central banks replaces stacks of money with digital money and are in position to have full authority on monetary policies. He accepts that it is virtually impossible to have a perfect cashless system. So he advocates a less cash system. Demonetization move in India will lead to create such a 'less cash' system.

Move of demonetization has been a blessing in disguise for law and order for Indian cities. Central government has reported that since demonetization crime rates including robbery, extortion and burglary kind of crimes have reduced by half in capital Delhi and financial capital Mumbai. Moreover, it is more convenient. No longer had one need to carry wallet filled with money. It is not uncommon in India to see people carry money in airbags or sacks if they need to make huge transaction (say 30 lakh INR) for business or real estate deals or for paying tuition fee at a private college.

5. CRITICISM OF CASHLESS ECONOMY

- 1. Lack of confidence in internet banking** is a big deterrent in converting to a cashless economy. Many people in India are not even educated, not to talk about familiar it with internet and mobile transactions. Such people could be easily duped by others. Even personal computers could be hacked and important information could be stolen by hackers.
- 2. Critics of cashless economy state that dealings and transaction could be illegal and these give rise to black economy.** Currency is not black on its own and a cashless economy will not stop creation of black money. However, they forget that it was the availability of funds in form of cash which is conducive for dubious dealings, enable evasion from scrutiny by taxation authority and provide an environment conducive for parallel economy of black economy to thrive. Supply of black money will be greatly reduced by demonetization. It will

be immature to presume that demonetization move will bring back all black money (or black wealth) to the financial system. A large chunk of that is stashed in offshore accounts, tax heavens, real estate or jewelries. However, it will be able to pull back some of it into system and lower the rate of creation of further transfer of money in black economy.

3. **For a cashless economy to thrive and be viable, there are few prerequisites.** These are financial literacy, digital integration and strong security infrastructure. India has a good cell phone network, thanks to telecommunication of previous decades. Government has recently introduced digital transaction app; BHIM which could be accessed in various regional languages.
4. **Security is a big concern for cashless system in India.** In US, all financial institutions have a strong cyber security force, which keep close eye on all transactions and intervene if it suspects any wrong doing. Even if somebody loses money due to false transaction or hacking of bank account, bank takes full responsibility and refunds the money to customer without much hassle. Such provisions create confidence in customer. In India, somebody's card had been wrongly charged or somebody intentionally withdraw money by hacking account or getting access to online account ID and password, it becomes nightmare for customer to get his money back. He has to run to higher officials, lodge FIR with police and pursue his case for long time. He may not get his money back even after all efforts.
5. **Move of demonetization had an adverse effect on economy in initial run.** India's GDP had a growth rate of 7.6% in first two quarters of 2016. Rating agency ICRA (owned by Moody's) predicted this to have lessened to 7.2%. Another agency S & P predicted the rate to have been reduced by 17% in first quarter of 2017. Small businesses did not have sufficient cash in hand to purchase raw materials and pay to their employees.
6. **This resulted in job loss of 30-50% of workforce for small to medium size ventures in manufacturing, agriculture, construction and retail.** For two months, India growth story seemed to be going in reverse mode, bringing bad reputation for ruling party and its head, PM Modi. Slowly as more and more cash was available and new means to perform cashless transaction became popular, things started coming to be normal.

In ordinary conditions, it would have taken nation 30-40 years to be able to move to cashless mode. Demonetization has been like a long waited fast track surgery, which will propel country towards growth and prosperity.

6. GROUND REALTY OF CASHLESS ECONOMY IN INDIA

Internet connectivity is poor, mainly in small cities and rural area. It is said that there are two nations in India. One is Bharat (poor rural section) and other is India (affluent and modernized section). Same goes for internet and mobile banking. Cyber security is another big issue. India does not have strong cyber workforce to thwart hacking and cyber laws to prosecute the wrong doers. Only 50% population has access to banking facility. In a nation, where half of their population does not have access to clean drinking water, toilets and roads, internet banking is a big thing. Internet penetration rate is 27%, much below the other developing nations such as Kenya, Indonesia and even Nigeria. Ideally it should be about 67% for effective internet

transactions. Only 15% people have smartphones with internet connections and internet speed is very slow compared to global standards. There only 856 point of sales machines per million people, required for debit/credit card transactions, compared with 4000 per million people in China. To sum up, India do not have infrastructure needed for cashless economy at the moment. Government is taking steps to address these issues and increase internet banking and cyber security to enhance public confidence.

7. CONCLUSION

Rogoff argues that by replacing cash with a digital store of value, central banks are able to take full control over monetary policy. By move of demonetization, government pulled money from circulation and it took around 4 months to replace it by new bills partially. Left in a limbo, people were forced to adopt measures of cashless transaction. After passage of this revolutionary time period, things are getting to normalcy in India. Businesses are thriving as earlier and all activities are undergoing as earlier. Thus, demonetization has been a blessing in disguise for Indian economy.

India of this day is undergoing an overall transformation in the way financial transactions are made. More and more people are able to open bank account, rapid growth is seen in terms of use of e-services, cash transaction has reduced to a great extent, online shopping for all kind of merchandise and digital options of payment are mushrooming. The share market is soaring again, foreign exchange is amassing and INR is becoming stronger in comparison to USD. All these factors will contribute in achieving higher growth rate. Current regime in India came in power with promise of make economic development within reach of even the weakest person of society. Cashless economy in India will be large leap to come closure to this goal.

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