



## Four Years of Demonetisation

---

 [drishtias.com/printpdf/four-years-of-demonetisation](https://drishtias.com/printpdf/four-years-of-demonetisation)

### Why in News

---

**8<sup>th</sup> November 2020** marked the **four year anniversary of demonetisation**, when Rs. 500 and Rs. 1,000 notes were withdrawn from the system in 2016.

**Demonetisation:** It is the act of **stripping a currency unit of its status as legal tender**. It occurs whenever there is a **change of national currency** and the current form or forms of money is **pulled from circulation and retired, often to be replaced with new notes or coins**.

### Key Points

---

- **Objectives of Demonetisation:**

- To **discourage the use of high-denomination notes for illegal transactions** and thus **curb the widespread use of black money**.
- To **encourage digitisation of commercial transactions, formalise the economy** and so, **boost government tax revenues**.

The **formalisation of the economy** means bringing companies under the regulatory regime of government and subject to laws related to manufacturing and income tax.

- **Operation Clean Money:**

- It was launched by the **Income Tax Department (CBDT)** for **e-verification of large cash deposits** made during the period from 9<sup>th</sup> November to 30<sup>th</sup> December 2016.
- The programme was launched on 31st January 2017 and entered into the second phase in May 2017.
- It aimed to **verify cash transaction status** (exchange/savings of banned notes) of taxpayers during the demonetisation period and to **take tax enforcement action** if transactions do not match the tax status.

- **Impact of the Move:**

- Currency with public stood at **Rs. 17.97 lakh crore on 4<sup>th</sup> November 2016 and declined to Rs 7.8 lakh crore in January 2017** after demonetisation.
  - **Currency with Public:** As per the Reserve Bank of India (RBI) definition, currency with public is arrived at after deducting cash with banks from total currency in circulation.
  - **Currency in Circulation:** It refers to cash or currency within a country that is physically used to conduct transactions between consumers and businesses.
- **Demands fell**, businesses faced a crisis and gross domestic product (GDP) **growth declined nearly 1.5%**, with many **small units and shops being shut** down and it also **created a liquidity shortage.**

Liquidity shortages or crises arise when financial institutions and industrial companies scramble for, and **cannot find the cash they require to meet their most urgent needs or undertake their most valuable projects.**

- **Current Trends:**

- **Currency with Public:** On **23<sup>rd</sup> October 2020**, the currency with the public stood at a record high of **Rs. 26.19 lakh crore, up 45.7%** from November 2016.
  - The **pace of rise in currency with the public has been very sharp over the last 10 months** as it has risen from Rs. 21.79 lakh crore as on 3rd January 2020 to the current number in October 2020.
  - The hike was mainly **driven by a rush for cash by the public between March and May amidst the stringent lockdowns** to tackle the spread of the **Covid-19 pandemic**.
  - It shows that the **cash in the system has been steadily rising**, even though the government and the RBI had pushed for a less-cash society, digitisation of payments and slapped restrictions on the use of cash in various transactions.
- **Digitisation:** According to an **RBI study on digital payments**, although digital payments have been growing gradually in recent years, both in value and volume terms across countries, **currency in circulation to GDP ratio has increased in consonance with the overall economic growth**.
- **Tax Revenues:** Along with demonetisation, the introduction of the **Goods and Services Tax (GST)**, the **Insolvency and Bankruptcy Code (IBC)**, **Real Estate (Regulation and Development) Act 2016** and **Benami Transactions (Prohibition) Amendment Act, 2016** encouraged compliance such that the **number of income tax returns and the number of income tax filers grew** at a healthy rate in 2017 and 2018.
- **Counterfeit Currency:** In the year **2015-16**, more than **4 lakh fake notes** of Rs. 500 and Rs. 1,000 were captured. This number **reduced to 45,400 fake notes** of Rs. 500 and Rs. 2,000 in **2018-19**. However, the number of fake notes among the new design notes of Rs. 500 **more than doubled** with an increase of 121% whereas those of Rs. 2000 increased by 21.9% over the previous year during 2018-19, according to the annual report of RBI.
- **Terrorism:** It was believed that **stopping the high-value currency from circulating will restrict funds used for terrorist activities** which will gradually decrease the terrorist activities in the country. But, on the contrary, the number of such **incidences rose in the years 2016, 2017, and 2018, compared to 2015**.
- While 728 people died in terrorist activities in 2015; the number of casualties rose to 905, 812, and 940 in such activities in 2016, 2017, and 2018, according to the **South Asia Terrorism Portal (SATP)** data.

## Way Forward

---

- Demonetisation was an expeditious move to boldly counter the black money and parallel economy (illegal economy, such as money laundering, smuggling, etc.) threat with visible impact on how the government's policies are perceived in international circles of economic power.
- This move by the government achieved larger significance for a globally connected India as it showed boldness in tackling an issue which has remained a thorn in the growth success story of this generation.

**Source: IE**