

Preliminary Effect of Demonetization on Financial Inclusion in India

Varun Singh Yadav^{1*} Deepika Gupta²

¹ Assistant Professor, Govt. PG College Sector 1, Panchkula

² Research Scholar, School of Management Studies Panjabi University, Patiala

Abstract – Financial inclusion aims to take banking services to the doorstep of everyone to meet their entire savings, credit and remittance facilities. When the poor have access to credit and savings facilities, so they can grow larger businesses, manage consumption and household expenses better and plan for shocks. Their standard of living improves and poverty falls which allowing people to contribute more to the economy as well. Indian government adopted demonetization in November 2016, to tackle with black money and make India a cashless digital economy. This paper is descriptive in nature. The objective of the paper is to examine both positive and negative effects of demonetization on financial inclusion. The positive effects of demonetization include operationalising of Jan Dhan Yojna accounts, making India a cashless digital economy, improving account usage and saving behavior of individuals and contributing to wealth of nation through conversion of dead capital into live capital whereas the negative effects of demonetization include the adverse effect on ordinary individual, rural population, women, informal sector and NBFC-MFIs. The findings concluded that demonetization has turned out to be positive for financial inclusion, but negative for common man, rural population, informal sector, women in low income groups and NBFC-MFIs.

Keywords: Black Money, Cashless Economy, Demonetization, Financial Inclusion.

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INTRODUCTION

Financial inclusion is defined as “the process of ensuring access to appropriate financial products and services needed by all sections of the society in general and vulnerable groups such as weaker sections and low income groups in particular, at an affordable cost in a fair and transparent manner by regulated mainstream institutional players. In order to achieve financial inclusion, variety of tools like financial literacy drives, microfinance, leveraging technology have been adopted from time to time by Government of India. One of the most important tool that Government of India has encouragingly adopted for achieving financial inclusion is **Demonetization**. Indian Government had demonetized bank notes twice – once in 1946 and then in 1978. Both the time the aim was same that was curbing black money, corruption, counterfeiting currency and tax evasion.

On 8 November, 2016 Prime Minister Narendra Modi announced the demonetization of all 500 Rs. and 1000 Rs. bank notes of Mahatma Gandhi Series. He declared that use of all 500 Rs. and 1000 Rs. bank notes of Mahatma Gandhi Series would be invalid. Such specified bank notes, valued at ` 15.4 trillion, constituted 86.9 per cent of the value of total currency in circulation. He further announced the issuance of

new 500 Rs. and 2000 Rs. bank notes of Mahatma Gandhi Series in exchange for the old ones. The Specified Bank Notes Ordinance, 2016 was issued by the Government of India on 28 December 2016 ceasing the liability of the government for accepting the banned bank notes, and also imposing a fine upto Rs. 10,000 or five times the amount of the face value of the bank notes, whichever is higher, for people transacting with them after 8 November 2016. However, Petrol, CNG and gas stations, government hospitals, railway and airline booking counters, state-government recognized dairies and ration stores, and crematoriums were allowed to accept the banned Rs.500 and Rs. 1,000 bank notes until December 2, 2016.

DEPOSIT AND EXCHANGE OF OLD BANK NOTES

The Reserve Bank of India opened a window for fifty days until 30 December 2016 to deposit the demonetized banknotes. The banknotes could also be exchanged over the counter of bank branches upto a limit that varied over the days.

- Initially, the limit was fixed at Rs. 4, 000 per person from 8 to 13 November.

- This limit was increased to Rs. 4,500 per person from 14 to 17 November.
- The limit was reduced to Rs. 2,000 per person from 18 November.

All exchange of banknotes was stopped from 25 November 2016. This demonetization move was implemented as a tool to measure the stock of black money hoarded, counterfeiting currency and to make India a cashless digital economy. The government aims to bring the unaccounted money back to the formal banking sector by allowing limited exchange and unlimited deposit of old notes in bank accounts till the end of 2016. However, the biggest problem is that initially Prime Minister Narendra Modi move was supported from several bankers but later criticized by members of opposition parties, word media. His move further met by protest and strikes by people.

NEED AND OBJECTIVE OF THE STUDY

As we know that, demonetization move was implemented as a tool to measure the stock of black money hoarded, and to make India a cashless digital economy, therefore it becomes imperative to study the effect of demonetization on the financial inclusion. Thus, the broad objective of the study is to examine both positive and negative effects of demonetization on financial inclusion.

EFFECT OF DEMONETIZATION ON FINANCIAL INCLUSION IN INDIA

Demonetization has created both positive and negative effects towards financial inclusion which included as follows:

Positive Effects

Operationalized the Jan-Dhan Bank Accounts:

After demonetization, 23.3 million new accounts were opened under Pradhan Mantri Jan Dhan Yojna. Out of which 53.6 % were in urban areas and 46.4 % were in rural areas. Deposits of Public sector banks (in million) under PMJDY has increased from 203.6 as on November 9, 2016 to 222.9 as on 1 March, 2017. Out of which increase in rural areas are from 114.3 to 122.1 during November 9, 2016 to 1 March, 2017 and increase in urban areas are from 89.3 to 100.8 during November 9, 2016 to 1 March, 2017. Deposits of Regional Rural banks under PMJDY has increased from 43.1 as on November 9, 2016 to 46.4 as on 1 March, 2017. Out of which increase in rural areas are from 37.1 to 40 during November 9, 2016 to 1 March, 2017 and increase in urban areas are from 6 to 6.4 during November 9, 2016 to 1 March, 2017. Likewise, deposits of Private Sector Banks under PMJDY has increased from 8.4 as on November 9, 2016 to 9 as on 1 March, 2017. Out of which increase in rural areas

are from 5.3 to 5.4 during November 9, 2016 to 1 March, 2017 and increase in urban areas are from 3.1 to 3.6 during November 9, 2016 to 1 March, 2017. Likewise, deposits of Scheduled Commercial Banks under PMJDY has increased from 255.1 as on November 9, 2016 to 278.4 as on 1 March, 2017. Out of which increase in rural areas are from 156.7 to 167.5 during November 9, 2016 to 1 March, 2017 and increase in urban areas are from 98.4 to 110.9 during November 9, 2016 to 1 March, 2017. Jan Dhan Accounts contribute 4.6 percent in aggregation of deposits of commercial banks after demonetization.

Deposits under Pradhan Mantri Jan Dhan Yojna (PMJDY): Number of Accounts (in million)

	As on November 9, 2016			As on March 1, 2017		
	Rural	Urban	Total	Rural	Urban	Total
Bank Group						
Public Sector Banks	114.3	89.3	203.6	122.1	100.8	222.9
Regional Rural banks	37.1	6	43.1	40	6.4	46.4
Private Sector Banks	5.3	3.1	8.4	5.4	3.6	9
Scheduled Commercial Banks	156.7	98.4	255.1	167.5	110.9	278.4

Source: "Macroeconomic Impact of Demonetization- A Preliminary Assessment", RBI, 2017

- Account usage and savings behaviour has significantly improved.
- Those who have cheque books have started making active use of them.
- Wealth produced and saved by the poor can be brought into the formal banking system. Thus, the dead capital which was not available in the formal economy is now being turned into live capital.
- The demonetization promotes cash-less economy and increase in use of digital financial services.
- E-Wallet companies experienced a rapid increase in the number of transactions and traffic on their web, but these were mostly by urban and metropolitan parts of the country.

NEGATIVE EFFECTS

ORDINARY INDIVIDUAL

The ordinary individual has had to bear a lot as 90 percent of all transactions are paid in cash. Millions of people are crowding the banks and queuing

outside ATM centers to deposit their cash. In spite of expanded digital access to bank accounts, a very small percentage of the population has been able to operate without withdrawing cash or visiting the bank regularly. This is due to lower level of digital financial literacy.

• **INFORMAL SECTOR**

Informal Sector comprising of contract labourers, daily wage workers, farmers, fishermen, micro-entrepreneurs etc. who runs almost entirely on cash. These groups of people typically do not have a formal bank account. Cash is their only means of receiving income and making payments. The demonetization has created a huge disruption on work and daily lives of these people with severe adverse impacts on their livelihoods. The small service providers like auto-rickshaws, road-side eateries, local kirana stores etc. were also suffered a lot. The demonetization has led them to compromise on their work and stand in long queues outside banks for their own hard-earned cash.

• **RURAL POPULATION**

The effect of demonetization had been more worrying in the rural parts of the country where visiting physical bank branches still remains a time consuming and costly exercise for many. Digital financial services like ATMs and POS machines at shops are limited in number and suffered with infrastructural issues which placed ordinary rural residents were in great stress.

• **WOMEN**

Women particularly in rural areas often save in the form of cash stored in their homes in secret cabins away from the eyes of men of the household. The government announcement of banning notes put women in an extremely vulnerable position.

• **NBFC-MFIs**

Micro finance companies comprising of individuals such as women, daily wage workers, farmers, fishermen, micro-entrepreneurs etc. who runs almost entirely on cash. Loan installments from such customers are usually collected on a weekly and sometimes on daily credit basis. Demonetization adversely affected their daily businesses /lives which in turn affected timely repayment of loans taken by them from NBFC-MFIs. It further leads to temporary increase in Non- Performing Assets.

• **Demonetization results in Inflationary pressure in the economy**

CONCLUSION

Demonetization has turned out to be positive for financial inclusion, but negative for common man, rural population, informal sector, women in low income

groups and NBFC-MFIs. According to financial inclusion insights Survey, 49 % of Indian adults are digitally included. However usage of these accounts remains debatable. Moreover, there is increase in the use of digital financial services through urban and metropolitan parts of the country only. In rural areas, low level of digital financial illiteracy founded.

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Corresponding Author

Varun Singh Yadav*

Assistant Professor, Govt. PG College Sector 1,
Panchkula