

DEMONETISATION: A SWOT ANALYSIS

Dr. D.Anbugeetha, Mr. R.Mahaveer Jain
Department of Business Administration
Thiagarajar College
Madurai - 9
E-mail: d.anbugeetha@gmail.com

ABSTRACT

The demonetisation of Rs500 and Rs 1,000 banknotes was a policy enacted by the Government on 8 November 2016, ceasing the usage of all Rs 500 and Rs 1,000. The announcement was made by the Prime Minister of India Mr. Narendra Modi in an unscheduled live televised address at 20:15 Indian Standard Time (IST) on 8 November.

The government claimed that the demonetisation was an effort to stop counterfeiting of the current banknotes allegedly used for funding terrorism, as well as a crack down on black money in the country. The move was also described as an effort to reduce corruption, the use of drugs, and smuggling. However, in the days following the demonetisation, banks and ATMs across the country faced severe cash shortages. People seeking to exchange their notes had to stand in lengthy queues, and several deaths were linked to the inconveniences caused due to the rush to exchange cash. Also, following the announcement, the BSE SENSEX and NIFTY 50 stock indices crashed for the next two days.

This conceptual paper presents the back ground and the SWOT Analysis of Demonetization.

Key Words: Demonetization, SWOT Analysis,

INTRODUCTION

The demonetisation of Rs 500 and Rs 1,000 banknotes was a policy enacted by the Government on 8 November 2016, ceasing the usage of all Rs 500 and Rs 1,000 banknotes of the Mahatma Gandhi Series as legal tender in India from 9 November 2016. The announcement

was made by the Prime Minister of India Mr. Narendra Modi in an unscheduled live televised address at 20:15 Indian Standard Time (IST) on 8 November. In the announcement, Mr. Modi declared that use of all Rs 500 and Rs 1,000 banknotes of the Series would be invalid after midnight of that day, and announced the issuance of new Rs 500 and Rs 2,000 banknotes of the Mahatma Gandhi New Series in exchange for the old banknotes. However, the banknote denominations of Rs 100, Rs 50, Rs 20, Rs 10 and Rs 5 of the Mahatma Gandhi Series and Rs 2 and Re 1 remained legal tender and were unaffected by the policy.

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BACKGROUND OF DEMONETISATION

Historically, previous Indian governments had demonetised bank notes. In January 1946, banknotes of 1,000 and 10,000 rupees were withdrawn and new notes of 1,000, 5,000 and 10,000 rupees were introduced in 1954. The Janata Party coalition government had again demonetised banknotes of 1,000, 5,000 and 10,000 rupees on 16 January 1978 as a means of curbing counterfeit money and black money.

In 2012, the Central Board of Direct Taxes had recommended against demonetisation, saying in a report that "demonetisation may not be a solution for tackling black money or economy, which is largely held in the form of benami properties, bullion and jewellery". According to data from income tax probes, black money holders keep only 6% or less of their ill-gotten wealth as cash, hence targeting this cash may not be a successful strategy.

On 28 October 2016 the total banknotes in circulation in India was Rs17.77 trillion (US\$260 billion). In terms of value, the annual report of Reserve Bank of India (RBI) of 31 March 2016 stated that total bank notes in circulation valued to Rs16.42 trillion(US\$240 billion)

of which nearly 86% (around Rs14.18 trillion (US\$210 billion)) were Rs500 and RS1,000 banknotes. In terms of volume, the report stated that 24% (around 22.03 billion) of the total 90266 million banknotes were in circulation.

In the past, the Bharatiya Janata Party (BJP) had opposed demonetisation. BJP spokesperson MeenakshiLekhi had said in 2014 that "The *aamaurats* and the *aadmis* (general population), those who are illiterate and have no access to banking facilities, will be the ones to be hit by such diversionary measures."

However, the present Government of India has a strong faith in Demonetization. Mr.Modi said that the queues due to demonetisation were the last queues that would end all other queues.

SWOT ANALYSIS OF DEMONETISATION

It is the time that we do an in-depth analysis of the strengths and weaknesses that are integral to this hard-hitting measure. We must also analyse the broader opportunities and threats to identify the potential problems or say, the cost to the society that needs to be recognised and possibly addressed.

STRENGTHS

- Black Money and Counterfeits: Two primary reasons were touted for this drastic move – to hit at black money and to check counterfeits. This move left the parallel black economy choked and gasping. The elimination of fake currency is inevitable, and one also hopes that a check is well in place while these notes are routed through banking channels. It will be a tremendous achievement.
- Countering Terror & Crime, while the government has clearly pointed out the use of fake currencies by terror outfits, some have spoken about uses of cash by criminals. This move has already halted many terror operations and has the potential to force a significant shift in the terror infrastructure.
- As the large chunk of Hawala money is delivered to separatist leaders and local politicians to fuel protesters, the four-month-long unrest in the valley is also getting wiped out in the absence of cash inflow, security agencies believe. Besides, the lack of

Hawala money would also hit the Maoists activities and other insurgent groups across India, especially in the northeast region, intelligence officially said.

- Timing: No timing is perfect, but in hind-sight, the timing seems obvious. If we connect the dots, the very first decision of Modi Govt was to establish a SIT on Black Money. The Pradhan Mantri Jan-DhanYojana (PMJDY) nearly compelling all citizens' access to bank accounts. The next was crack down on hoarders /foreign accounts (approximately RS. 80,000 Cr was collected). After which came Declaration Scheme, with a deadline of 30th Sept 2016. Another window of opportunity was given to people to declare their amassed wealth. (Rs. 65,000 Cr collected) Now, if you still have the Black Money, the government will ensure that either you declare and become mainstream or else face the hammer. Commendable chronology!
- Reformist Stance: Demonetisation is not a foolproof measure, but it attacks the black money problem with unprecedented force and at multiple layers. If the objectives are achieved through sound implementation, this will show a strong signal about India's anti-corruption drive and also its reformist stance.

WEAKNESSES

- Preparedness: The entire banking and postal system were caught unaware. The government says that it will now take two more weeks to configure all ATMs. The situation is testing in small towns, most ATMs are still not dispensing cash, and some branches are easily running out of cash. It seems that the planning ahead of such massive event lacked matching preparedness. But the government could not have stashed large cash in banks and reconfigured ATMs. It would have led to the corrupt getting wind of the announcement and overnight getting much of their illicit wealth converted.
- Logistics: There is always the risk that the infusion of the new currency notes is not sufficient to satiate the demand for currency. The government has fixed certain limits, which for all practical purposes seem moderately small.
- Unaccounted Wealth: There are many means to store wealth; in cash, foreign currency, gold, real estate, and several other instruments. Out of which hard cash is relatively unattractive as it earns a negative rate of return, whereas, other modes of unaccounted

wealth are laundered, and becomes much harder to identify. So this strike is only on black-cash and not on the entire parallel economy per se.

- **Cutting Corruption:** Demonetisation does not promise that there will not be any future corruption. Crooks are always creative and will find ways to circumvent this demonetisation. At best, this is a reset button.
- **Sluggish Economy:** This process would increase bank deposits with an obligation to pay interest. Can the financial institutions mobilize these funds fast enough and be able to disburse as loans, especially in a sluggish economy?

OPPORTUNITIES

- **Windfall Profit:** The Chief Economic Advisor of the government has argued that this decision would lead to transfer from black money holders to the RBI and then to the government. For the cash that does not return, should the RBI simply decide to reduce its liabilities and create a profit? It won't be unwise in this exceptional case of the fight against black money but may send wrong messages. RBI may take some time and carry the liabilities on its balance sheet for the foreseeable future but should not announce this in advance.
- **High cost of Future Crimes:** Cash facilitates crime because it is anonymous and big bills are easy to carry. By inflicting a cost, demonetisation cripples the ability to engage in future corruption. It is far easier indulging in crime with substantial cash in hand. The costs of crime will become much higher and will have an indirect but powerful impact on future corrupt practices committed with the help of currency.
- **Checks on Loose Sectors:** Black money spawns in an economy in areas where the checks and balances are weak and have larger cash component in their transactions like commodity hoarding and trading, movie production, campaign finance, and of course real estate. Since liquidity dries up, hoarders' and black-marketers' holding power collapses leading to prices collapse. Demonetisation will result in a correction in these markets, either by a reduction in prices or a reduction in business. We will see the outcome in time to come. However, these corrections will move the market to equilibrium reflecting genuine demand and supply in the real economy.

- **Less-Cash Economy:** Cash greatly facilitates transactions and hence we should aim for a less-cash economy and not cash-less. A less-cash economy is an excellent balance between maintaining ease of financial operations and also curbing malpractices.
- **Financial Inclusion:** It also provides a boost to the government's financial inclusion drive, pushing more households towards efficient banking and payment infrastructure.

THREATS

- **The Cost of Harassment:** A massive logistics exercise was undertaken causing countrywide panic and confusion. If the government does not invest all its energies into replenishing and re-calibrating ATMs, fostering inconvenience will lead to backlash and has potential to undo the intended good work. Daily wage earners, truck drivers don't have much time to stand in line every day. People can only do this for a limited time. It will also give the opposition a stronger opportunity to carry sustained attacks.
- **Lower Economic Activity:** Overall the adoption of electronic payment instruments is slow, and the infrastructure is weak. During the transition period, the shortage of the lubricant of economic activity disrupts the smooth working of the economy. As a consequence, in coming weeks, business is likely to be sluggish. In informal labour markets, daily wage labourers are not able to get enough work. Many other markets that depend on full or partial cash payment are also affected. These costs will show up in the form of lower GDP (it counts all output, with tax evasion or not) during the affected period.
- **Panic and Confusion:** This is the biggest threat. The political discourse is at the lowest. The opposition parties have been quick to fuel and magnify public annoyance over the teething problems. Misinformation and confusion is being propagated on an hourly basis to see to it that somehow this move is unsuccessful. Even majority of the TV channels, instead of being helpful or providing tips to people, are indulging in fear-mongering. OpIndia.com has busted many such rumour mongering.

CONCLUSION

The biggest hurdle in India is the lack of State capacity. But the government and the RBI are taking steps to make life easier for people and should flood the Banks and ATMs with new notes without delay so that panic is removed. The next few months are going to be painful and disturbing and should be seen as an emerging economy trying hard to reform its corrupt self. Our generation has not seen revolutions. Fortunately, they are witnessing as well as indulging in it. Watchmen, carpenters, maids, shopkeepers, cooks, sweepers, almost all are showing relatively calm, positive and mature understanding of the after effect.

No defining change comes without some pain. Behind the joy and hope of unification of two Germany's, lurked the pain of actually merging the two. It took the deep reserves of the famous German grit and many painful years to not just recover, but emerge as the one of the world's chief economic engine.

When an economy is suffering from cancer, the only way to deal with it is painful doses of chemotherapy. With intense follow-up and awareness campaigns, the government can have people on its side even during their continuing hardship. Hope the story of demonetization in India has a happy ending.

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