



Evaluating Demonetisation Today

Demonetisation, one of the most significant economic experiments in Indian history, marked its eighth anniversary in November 2024. Announced on November 8, 2016, by Prime Minister Narendra Modi, it aimed to eradicate black money, curb counterfeit currency, promote digital payments, and counter terrorism.

This bold move rendered the Rs 500 and Rs 1,000 currency notes invalid, effectively wiping out nearly 86% of the cash supply overnight. Eight years later, it is worth revisiting its implications, outcomes, and the long-term impact it has had on India.

The Announcement and Its Nature

The demonetisation announcement took the nation by surprise. PM Modi, in his televised address, underscored the necessity of withdrawing high-value currency notes. He argued that cash was the lifeblood of corruption, black money, counterfeit operations, and illegal trade, including terrorism financing. The move was expected to disrupt the informal economy, prompt a transition toward digital payments, and significantly dent the black money reserves.

The nature of demonetisation was abrupt and sweeping. It required citizens to exchange or deposit the invalid notes within a stipulated time, leading to long queues outside banks and ATMs. The Reserve Bank of India (RBI) introduced new Rs 500 and Rs 2,000 notes to replace the invalidated currency.

The Immediate Impact

The immediate aftermath of demonetisation was marked by chaos and economic disruption. People struggled to access sufficient cash, and businesses—especially small, cash-dependent enterprises—faced severe challenges. However, proponents of the move argued that short-term inconvenience was a necessary price to pay for long-term gains.

In FY17, the cash supply plummeted from Rs 16.63 trillion in FY16 to Rs 13.35 trillion. The cash-to-GDP ratio also dropped significantly from 11.9% to 8.5%. Yet, contrary to expectations of a cashless society, the cash supply gradually rebounded in subsequent years, reaching approximately Rs 35 trillion in FY24. This highlights that cash remains integral to the economy, as noted by economists like Arun Kumar, who argue that hoarding cash is common during uncertainty and does not necessarily indicate black money generation.

Black Money and Corruption

One of the key objectives of demonetisation was to tackle black money. However, the results in this area have been mixed. While large sums of unaccounted cash were deposited into banks, the share of black money in cash form has always been small. Most black money, as experts pointed out, is parked in real estate, gold, and offshore accounts.

A recent report suggests that 90% of Indians still believe black money thrives in the real estate sector. Efforts to digitize and centralize property records are ongoing but remain incomplete. Consequently, demonetisation appears to have had limited success in addressing black money and corruption comprehensively.

Digital Payments Revolution

One of the undeniable successes of demonetisation is the exponential growth of digital payments. Before demonetisation, digital transactions were on the rise but received a substantial push after the currency ban. Unified Payments Interface (UPI), a flagship digital payment system, grew from Rs 1 trillion in FY18 to an astounding Rs 200 trillion in FY24, with a compound annual growth rate (CAGR) of 138%.



Digital payment systems such as Google Pay and Paytm have gained widespread acceptance, even in rural areas. This growth aligns with the government's aim of promoting financial inclusion. Ease of use, convenience, and robust digital infrastructure have sustained this upward trend, making India a global leader in digital payments.

Despite this success, critics like Pronab Sen argue that digital payments were already growing before demonetisation. The sudden spike post-demonetisation was largely due to the unavailability of cash and has since normalized, with annual growth rates tapering to around 9% in FY24.

Counterfeit Currency

Counterfeit currency, another major target of demonetisation, witnessed an initial spike post-2016, as new Rs 500 and Rs 2,000 notes became the focus of counterfeiters. The number of counterfeit notes rose from 630,000 units in FY16 to 760,000 in FY17. However, this number has since declined significantly, dropping to 220,000 units in FY24.

While the value of counterfeit currency has decreased, experts argue that demonetisation was a disproportionate response to a problem that constituted a minuscule fraction of the total currency in circulation. Counterfeit notes made up just 0.00015% of the currency supply in FY24, highlighting the limited impact of demonetisation on this front.

Impact on Terrorism and Corruption

Another objective of demonetisation was to curtail terrorism by choking off its financial channels. Data from the South Asia Terrorism Portal indicates a decline in terrorist activities, from 2,394 incidents in 2016 to 1,323 in 2024. Proponents argue that reduced cash flow and enhanced audit trails in financial transactions have restricted terrorist funding. However, critics attribute the decline to geopolitical factors, including Pakistan's internal challenges, rather than demonetisation.

Similarly, while digital transactions have improved financial transparency, demonetisation alone cannot be credited for reducing corruption. Much of India's corruption resides outside the cash economy, in systemic inefficiencies and opaque institutional practices.

Assessment of Long-Term Impact

In assessing demonetisation's long-term impact, the outcomes are varied:

- Economic Growth and Cash Resurgence:** Despite initial disruptions, the Indian economy rebounded, and cash circulation surpassed pre-demonetisation levels. This underscores the enduring reliance on cash in India's economy.
- Behavioral Shift:** While cash usage remains significant, demonetisation nudged many toward digital payments, creating a shift in financial habits. UPI and similar platforms have enabled seamless, secure transactions across all sections of society.
- Institutional Reforms:** Demonetisation spurred discussions on tax compliance and financial accountability. Measures like the GST rollout and property digitization aim to address black money issues more systematically.
- Missed Opportunities:** The move fell short of achieving its stated goals of eradicating black money and counterfeit currency. Experts emphasize that tackling black money requires addressing deeper systemic issues, including reforms in real estate, gold trade, and offshore banking regulations.



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Conclusion

Demonetisation remains a polarizing chapter in India's economic history. While it accelerated the adoption of digital payments and raised awareness about black money, its success in addressing core issues such as corruption, counterfeit currency, and terrorism is debatable. Critics argue that the disruption to lives and livelihoods was disproportionate to the gains, while supporters view it as a necessary step toward modernizing the economy.

Ultimately, demonetisation serves as a case study in the complexities of economic policymaking. Its legacy underscores the importance of balancing bold initiatives with meticulous planning, transparent communication, and long-term strategies to achieve sustainable development.

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