

DEMONETISATION IN INDIA AND POLITICS REVIEWS

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ABSTRACT

On 8 November 2016, India's Prime Minister Narendra Modi announced that, from midnight onwards, the country's two largest-denomination notes would be “demonetised”, or withdrawn from use. According to Modi, the policy would tackle corruption, undermine counterfeiters and punish hoarders of undeclared income. This paper discusses the way the Modi administration positioned demonetisation as an anti-corruption initiative, addresses civil society challenges regarding the policy’s impact on the rural poor and, in turn, the government’s responses to such criticism. Ultimately, we argue, demonetisation re-invigorated the Indian public debate on the need for integrity and accountability. However, by positioning corruption primarily as a cash-based issue, the policy may divert attention from future strategies that take a more holistic approach, such as strengthening legislation and capacity-building of regulators and anti-corruption watchdogs.

Keywords: Denomination, Corruption, Black money.

INTRODUCTION

Many political parties are surely tripped and left with a huge cache of cash turned into paper which they do not know what to do with. The swelling of the Jan Dhan accounts and instances of cash moved to tax – free states like Nagaland is a manifestation of the trouble that has hit political outfits, many of whom are forced to keep quiet and swallow the destruction of their cash dump. The net result of the whole exercise will be a political playing field that will be loaded in favor of Modi and against the Mulayams and Mayawatis of the world (so to say). Thus it is a win- win situation for Modi and only a full time political being like him who thinks, lives and sleeps politics, could envisage and play out such a master stroke. But what about the contraction of the economy, that will hit everyone – including the poorest of poor and those without black money-below the belt? When 86 per cent of the cash in the economy (Rs 500 and Rs 1000 constituted that much of the cash in circulation) is suddenly withdrawn, there is a sudden mismatch between demand and supply. Goods are in demand and sellers are also willing to sell, but with demonetization, buyers don't have cash to buy and thus demand is going unfulfilled. Finding this, sellers are not replenishing their stocks and reducing their demand for goods supplied by manufacturers. So manufacturers are being forced to cut back on their production. This leads to cut in employment and work.

On the evening of 8 November 2016 India's Prime Minister Narendra Modi made an announcement that surprised the nation: From midnight onwards, the country's two largest-denomination notes, worth 500 and 1000 rupees, would be “demonetised”, or withdrawn from use. In their place, a re-designed 500 rupee note and a new 2000 rupee note would be introduced. According to Modi, the policy had three goals: Tackling corruption, undermining counterfeiters and

punishing hoarders of undeclared income, popularly referred to as “black money”. While communications regarding the rationale behind the policy were limited – a key issue this paper seeks to address – Modi highlighted that “the magnitude of cash in circulation is directly linked to the level of corruption.” Thus, reducing the cash in circulation would reduce corruption (Modi 2016).

The notes withdrawn made up 86%, by value, of cash in circulation). Compounding the sheer logistical challenge required to replace such a large amount of cash was the fact that a significant proportion of the new notes had yet to be printed at the time of the announcement, causing weeks-long cash shortages, which in turn led to significant, government-mandated restrictions on cash withdrawals. 90% of all transactions in India are conducted in cash (D'Monte 2016); in spite of these challenges, public reactions to demonetisation were initially broadly positive. The policy's perceived decisiveness struck a chord with the electorate. It appeared there was a consensus that innovative, perhaps radical anti-corruption policies were needed, and that this consensus was so strong, it outweighed even personal inconvenience and potential economic losses.

Gradually, however, the public mood began to change. Agricultural associations complained that farmers across India were unable to sell recently-harvested summer crops or purchase seeds for the upcoming winter sowing season. Opposition parties claimed that some members of Modi's Bharatiya Janata Party (BJP) had received advance warning of the decision, allowing them to save at least parts of illicitly accumulated cash. Such criticism led to a number of modifications to the policy mechanics of demonetisation which, in turn, led to accusations that the government had failed to think through the policy properly.

This paper uses publicly-available sources such as policy directives, government communications, opinion pieces and statements by industry- and regional advocacy groups to analyse how the government of the world's largest democracy communicated to its citizens one of the most radical anti-corruption initiatives implemented in recent years, and how it has responded to challenges about the effectiveness and appropriateness of the overall policy. Ultimately, we seek to provide a case study about the relationship between government-instituted anti-corruption policies and grass-roots concerns about political integrity, ethics and compliance.

including legal debates surrounding the making and implementation of demonetisation, the role of anti-corruption policies in Indian electoral politics or the relationship between cash and corruption in India and elsewhere.

Following a discussion on the evolution of the policy mechanism in section two, we argue that the Modi administration has successfully portrayed support for demonetisation as a civic and patriotic duty, using paternalistic messaging and repeated assurances that the end justifies the means (section three). Section four discusses some of the criticism of demonetisation and the respective government responses, focusing on the rural economy, allegations of political nepotism and accusations that demonetisation had been developed in a way that failed to take into account other key stakeholders, including most noticeably the Reserve Bank of India (RBI), India's custodian of monetary policy.

Ultimately, we argue that demonetisation has re-invigorated the Indian public debate about anti-corruption, however, at the cost of establishing a narrative that portrays corruption as a largely cash-based issue, potentially damaging the credentials of future innovation in anti-corruption policy-making in India.

POLITICAL PARTIES REVIEW

Demonetisation the biggest disaster, GST a great stunt: Mamata

West Bengal Chief Minister Mamata Banerjee today raked up the issues of demonetisation and the Goods and Services Tax, dubbing the note ban as the "biggest disaster" and the new tax regime a "great stunt". "As I had said earlier, demonetisation is the biggest disaster. It has completely ruined the country's economy. Also, the GST is a great stunt," she wrote on her Twitter handle.

Banerjee had earlier called the GST roll-out as another "epic blunder" of the Centre after the demonetisation. Claiming that the government had "hurriedly" introduced the GST, the chief minister demanded an investigation into the new tax regime. "Why Govt started it hurriedly without making proper plans? The commoners & all traders are the worst sufferers.

Thorough investigation is needed," she said.

Demonetisation, hastily implemented GST damaged economy: Rahul

Congress Vice President Rahul Gandhi on Tuesday criticised Prime Minister Narendra Modi for demonetisation and the hastily implemented Goods and Services Tax (GST) regime. Both he said caused "tremendous damage to the Indian economy". Gandhi, who is on a two-week visit to the US to interact with political leaders, global thinkers and overseas Indians, spoke on the political environment in the country, the Congress party, the effects of demonetisation among other issue

Demonetisation a foolish step, GST faulty, says P. Chidambaram

It's work in progress. Three events dominated India's economic landscape last year, but whether they can be described as "progress" is debatable. One definitely isn't: the unseemly brawl that broke out over control of the Tata group with Ratan Tata returning as interim chairman after ousting incumbent Cyrus Mistry. A lot of dirty linen is being washed in public, putting partly in the shade the political charges being traded elsewhere.

The second is the goods and services tax (GST), whose objective is to replace all taxes levied by the federal government and the states with one central tax. The GST is scheduled to come into effect by April or — at the latest — by September. Although both houses of Parliament have approved the bill and the President has signed off on it, a GST Council is now squabbling over the details, which could delay implementation.

"The timing is not right for implementation," says West Bengal finance minister Amit Mitra, who is also chairman of the empowered committee of state finance ministers. He lays the blame squarely on the center's move to demonetize Rs500 (\$7.4) and Rs1,000 notes. "We all supported the GST under the premise that this would be the only destabilization factor," Mitra told a TV channel. "We did not know that there would be a much bigger destabilization in the form of demonetization that would be let loose on the country."

Demonetisation Not A Political Decision: Ram Madhav

Demonetisation was never a political decision, BJP general secretary Ram Madhav said today and insisted that the move had increased the tax payers base and black money had been disclosed. Mr Madhav said that cracking the whip on corruption and black money was one of major promises made by the BJP during the 2014 Lok Sabha polls, and the Centre has taken a series of steps in this regard like the Voluntary Disclosure Scheme. "The government undertook a series of measures (to counter the menace of black money and corruption). Demonetisation was one of the four or five steps he (Prime Minister Narendra Modi) took," Mr Madhav said. The senior BJP leader, who is also one of the directors of India Foundation, an influential think tank known for its proximity to the Modi dispensation, was speaking at a book release event. "It was never thought of as a political decision in the first place," Mr Madhav said,

dismmissing claims by the opposition that the note-ban was announced keeping in mind assembly polls in Uttar Pradesh and other states held early this year.

"Many thought it (the demonetisation decision) would harm us politically and (BJP) would lose all elections after demonetisation," he said. Just after the demonetisation move, the BJP secured a landslide victory in Uttar Pradesh and Uttarakhand.

Speaking about RBI report which stated that 99 per cent of demonetised value notes are back in system, Mr Madhav said it is wrong to think that all the black money had become white now just because it had been deposited in banks. "So if anybody is thinking that we have deposited that money in banks and now (if) he is thinking that my money has become white, then he should be prepared for the consequences. It has not become white, (but) the black (money) has been disclosed," he said.

The BJP leader asserted that his reading on demonetisation and the interactions he had with the government suggest that the results of this decision are "good" for the economy. The GDP has slumped post demonetisation and note ban is being dubbed as the main reason by the critics. Mr Madhav said it is difficult to comprehend that India with a population 1.3 billion people has only 3.7 crore people who pay income tax. "Close to a crore people said their income is less than 2.5 lakh. Remaining said their income is between 5-10 lakh, which is just not the reality of our country," Mr Madhav added. Citing the low tax payers base, Mr Madhav said this kind of anomalies cannot make one a strong, progressive economy. "The good thing about it (demonetisation) is the currency part of our economy is clear. It is black and white before us now. Tax base has increased," he said.

Lauding the prime minister, Mr Madhav termed him a "leader with a long term vision who has before him the objective of setting India's economic basics right".

CONCLUSION

The decision to demonetise 86% of India's currency has been widely and substantially debated by notable scholars of political science and economics. This article wishes to add to that debate, by focusing on macroeconomic theory and how the policy decision affects the organised and unorganised sectors of the Indian economy—provided certain assumptions remain in place. The following analysis is based on the money-multiplier theory and the segmented markets model of economic and monetary policy analysis. Thus, despite the mitigating factors contributed by the connected or formal economy, the above analysis suggests that the Indian economy will be depressed for at least a few quarters. As the money supply is restored, the economy will not bounce back until all the adjustments, post the surprise demonetisation decision forced onto consumers and firms, pans out. I doubt anything would change in terms of future flows to the black economy as they depend on factors like the complexity of the tax system, labour market regulations and trust in the ability of the government to provide public goods among others.

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