



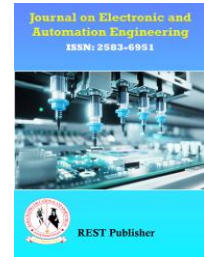
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Demonetization and Its Effects: A Socio-Economic Analysis

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Abstract: Demonetization refers to the withdrawal of a particular form of currency from circulation. On November 8, 2016, the Government of India announced the demonetization of ₹500 and ₹1,000 notes, aiming to curb black money, counterfeit currency, and corruption. This research paper analyses the short-term and long-term economic and social effects of this policy decision. The paper will explore its impact on various sectors such as banking, trade, informal employment, and digital transactions.

Keywords: Demonetization, Black Money, Cashless Economy, Informal Sector, Indian Economy, Financial Inclusion

1. INTRODUCTION

Demonetization is a drastic monetary policy measure, involving the withdrawal of specific currency denominations from circulation. Governments employ it to combat illicit economic activities such as corruption, tax evasion, and counterfeit currency circulation. On November 8, 2016, Prime Minister Narendra Modi announced the demonetization of ₹500 and ₹1,000 currency notes. The move intended to unearth black money, reduce the use of counterfeit currency and promote a cashless economy.

The unprecedented nature of the policy and its sudden implementation caused widespread disruption across various sectors. This paper seeks to delve into both the immediate and long-term consequences of demonetization on the Indian economy and society.

2. OBJECTIVES OF THE STUDY

- To examine the rationale behind the demonetization policy.
- To analyze the immediate and long-term economic impacts.
- To assess the social consequences on different demographics.
- To study the effects on financial inclusion and digital payments.

3. RESEARCH METHODOLOGY

This research follows a descriptive and analytical methodology. It primarily uses secondary data gathered from official government reports, RBI publications, academic articles, newspaper editorials, and economic surveys.

4. DEMONETIZATION IN INDIA: THE 2016 EVENT

The announcement on the night of November 8, 2016, rendered all existing ₹500 and ₹1,000 notes invalid. Citizens were given a limited window to exchange old currency for new ones or deposit them into banks. The stated goals included:

- Eliminating black money.

- Reducing counterfeit currency.
- Curbing terror financing.
- Promoting digital transactions and transparency.

The event saw long queues outside banks and ATMs, shortages of cash, and a significant shock to the informal economy.

5. ECONOMIC IMPACT

5.1 GDP and Economic Growth: The Ministry of Statistics and Programme Implementation (MOSPI) reported a slowdown in GDP growth to 7.17% in 2017-18, compared to 8.17% in 2016-17. This decline was partly attributed to the 2016 demonetization, which disrupted economic activity, particularly in the informal sector.

5.2 Employment and Informal Sector: The informal sector, which contributes nearly 45% of India's GDP and employs over 80% of the workforce (ILO, 2018), was hit hardest. Daily wage laborers and small vendors experienced job losses and income disruptions due to the cash crunch.

5.3 Banking Sector and Liquidity: A significant increase in bank deposits occurred, with over ₹1.5 lakh crore deposited within weeks (RBI, 2017). Liquidity in banks surged, which temporarily reduced interest rates. However, the operational stress on banks, long queues, and security concerns dominated the headlines.

5.4 Digital Payments and Financial Inclusion: One of the intended goals of demonetization was to foster a digital economy. Digital payment platforms like Paytm and UPI saw exponential growth. According to the National Payments Corporation of India (NPCI), UPI transactions increased from 0.1 million in October 2016 to 199 million by October 2018. However, digital literacy and internet access remained obstacles, especially in rural areas.

6. SOCIAL IMPACT

6.1 Impact on Rural and Marginalized Communities: Rural India faced significant challenges due to limited access to banking infrastructure and digital tools. Farmers, relying heavily on cash transactions for seeds, fertilizers, and labor, struggled during peak agricultural seasons.

6.2 Public Sentiment and Behavioral Changes: Initially, a large portion of the population supported the move, viewing it as a necessary step against corruption. Over time, as economic hardships increased and benefits remained unclear, public opinion became more divided. Consumer behavior shifted temporarily towards online and card-based purchases.

7. LONG-TERM EFFECTS AND REFORMS

7.1 Increase in Tax Compliance: Following demonetization, there was a noticeable increase in income tax filings and collections. The number of tax returns filed rose by 25% in the year following the policy (Income Tax Department, 2018).

7.2 Formalization of the Economy: More businesses and workers moved toward formal channels, including registration and banking. Initiatives like the Goods and Services Tax (GST), introduced soon after demonetization, further supported this shift.

7.3 Rise in Digital Infrastructure: There was a considerable push towards building digital infrastructure. Initiatives like BharatNet aimed to expand rural internet connectivity, while banks and fintech companies launched user-friendly digital tools.

8. CRITICISM AND LIMITATIONS

- The suddenness of the announcement, inadequate supply of new notes, and lack of preparedness in banking systems led to confusion and economic disruption.
- The cash-intensive sectors took significant time to recover. Small enterprises, especially those not integrated with formal banking, faced liquidity issues.

9. CONCLUSION

Demonetization was a bold policy initiative with ambitious objectives. While it did lead to a short-term increase in digital payments and a push toward formalization, its broader economic and social consequences were mixed. The policy's success remains a topic of debate, with lessons to be drawn regarding preparedness, implementation, and impact assessment. Going forward, structural reforms, financial literacy, and infrastructural development will be key to realizing the vision that underpinned demonetization.

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