

Impact of Demonetization on the Value of Indian Rupee



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Abstract

India is a developing country. In India there is a problem of black money. The reason behind is that there was no control over the outflow of Indian currency. Many steps were taken to control the outflow of Indian Rupee by the Indian Government. The problem of black money also had adverse impact on the value of Indian Rupee. Continuous increase in corruption and black money was responsible for depreciating the value of Indian currency. Thus on 8 November 2016 Prime Minister Narendra Singh Modi decides to ban the 500 Rupee and 1000 Rupee note. As it has been appreciated for removing the black money from the India, at the same time demonetization has been criticized due to sudden appearance without any legal information the paper aim is to see the impact of demonetization on the value of Indian currency. The paper will also see the value of Indian currency against the United States Dollar, Chinese Yuan, European the short term and long term due to demonetization. The secondary data will be collected to see the impact of demonetization on exchange rate of India against other country currencies. Data will be collected from the Reserve Bank of India and World Bank report. The data will be collected for the time period of 2015 to 2018. The paper will also see for which currencies its value has been increased or decreased. Short term and long term impact of demonetization will also be checked.

Keywords: Indian Currency, Demonetization, Appreciation, Depreciation, Black Money.

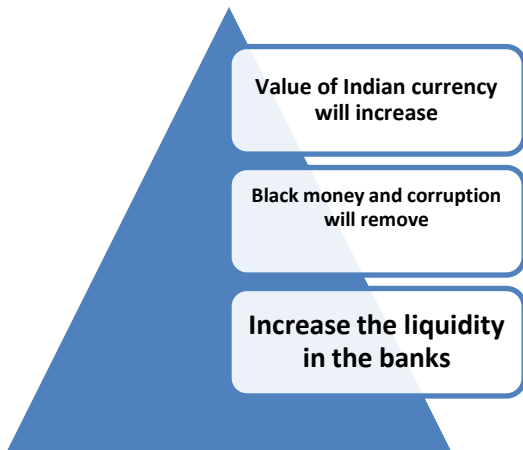
Introduction

India was a prosperous country at the time when the needs of the people were limited. People required less amount of money to fulfill the needs. But as the needs increased, greed for money increases and various problems arise in India like black money, corruption, terrorist activities and smuggling. India is a country where the problem of black money exists. The black money has adverse affect on the value of currency against other currencies. So, to be out of the problem of black money, one major step had been taken by the Prime Minister Narendra Singh Modi. The step was demonetization. This step was taken by the Prime Minister in order to stop the illegal activities and black money from the Indian economy. 500 and 1000 Rupees notes had been made out of circulation on the midnight of the 8 November 2016 as they consist the 86 % of the total money and new currency of denomination 500 Rs and 2000 Rs were introduced. It was not the first effort taken by the government .Before the demonetization; two times efforts were done by the government in 1946 and 1978 respectively. Government of India decision regarding the demonetization of 500 and 1000 Rs notes was a surprising act for both Indians and International observers. To understand the meaning of demonetization and to see its impact on Indian rupee value present paper has been discussed.

Demonetization

It is a one of the way adopted by the government to snatch the status of legal tender for decided currency units. In this process, some of the currency units are banned and new notes of other denominations are introduced against the banned currency. It means to keep the money out of circulation. The money does not remain legal after the declaration of the demonetization. In India, on 8 November 2016 demonetization was introduced by the Prime Minister Narendra Singh Modi. Due to demonetization 500 Rupee and 1000 Rupee notes were declared out of circulation. But Indian Prime Minister Narendra Singh Modi announced that new currency notes of dominations of 500 and 2000 Rupees will introduce against the 500 Rupee and 1000 Rupee notes.

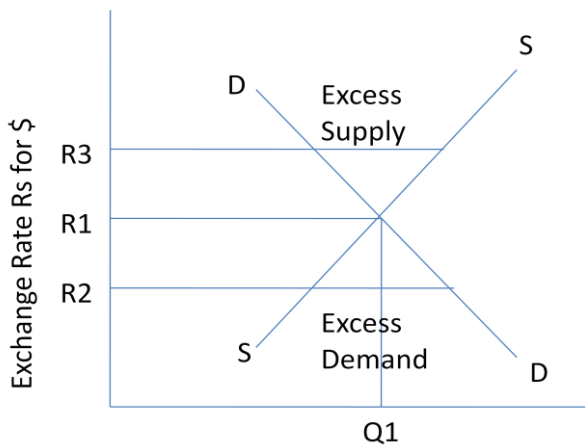
Expectation from the Demonetization



How the Demonetization is Related with Indian Currency

Value of Indian Rupee Is Determined as per Market Forces (Demand and Supply)

Any change in demand and supply bring fluctuation in the value of Indian Rupee. If Indian currency has excess of supply than the demand then value of Indian currency will decreased or depreciated against the other currencies. On the other hand, if Indian currency has excess of demand than the supply then value of Indian currency will appreciated against the other currencies.



Demand and Supply of Foreign Exchange

The above mentioned diagram reveals that value of Indian currency in foreign market depends upon the demand and supply.

Demonetization is a process through which some currency notes are made out of circulation. So it helps in reducing the supply of currency and it is beneficial for increasing the value of Indian currency.

Thus demonetization is interlinked with the value of Indian currency.

Short term impact of demonetization on the value of Indian Rupee

As the demonetization of 500 Rupee and 1000 Rupee notes were announced, there was shortage of the supply of Indian currency as they were near about the 87 % of the total money. Value of

Indian currency was appreciated due to the demonetization and shortage of money supply from India. As the India exchange rate was 68.8 at time before the demonetization. But after soon the announcement of Value of Indian currency was improved and reached to 67.73 against United States Dollar.

The 500 Rupee and 1000 Rupee notes were banned so, supply in India and rest of the world has been decreased but there is less decrease in the demand of the currency. For these reasons, in the short time period value of Indian currency has been appreciated against many other currencies.

Impact of Demonetization on the Value of Indian Rupee from Economic Point of View

Demonetization helps in reducing the black money, tax evasion, terrorism and smuggling of currency by banned the units of currency which can be easily carried for uneconomic activities by stopping the flow of the currency. Demonetization increases the liquidity in the banks. In these ways, value of Indian currency is affected by the demonetization. Demonetization is going to be one of the economic events of our time. Impact of demonetization is felt by every citizen of India. Demonetization affects the economy through the liquidity side. Effect of demonetization will be telling one because nearly 86 per cent of currency value in circulation was withdrawn without replacing bulk of it.

Impact of Demonetization on the Value of Indian Rupee from Prices Point of View

It helps in reducing the prices, as it can reduce the demand due to less money supply in circulation. It reduces the demand from the economy. Less demand leads to reduction in prices. Decrease in prices increases the value of the Indian currency.

Long term impact of demonetization on the value of Indian Rupee

In the long term impact of demonetization on Indian currency value is different from the short term impact. As it clear those 500 Rs and 1000 Rs notes are banned but at the same time Indian government has introduced the new notes of denominations 2000 Rs and 500 Rs. In such a way value of Indian currency becomes weak against many countries currency such as against United States Dollar. The reasons for depreciating the value in the longtime period are:

1. The introduction of 2000 Rs notes make the process of illegal activities like black money and in economic activities like smuggling a easy task as it is very easy to increase the outflow of Indian currency. These activities help in reducing the value of Indian currency in the long time period.
2. 2 People cannot decrease their consumption so as in the long time period when liquidity will increase in the hand of the people of new denominations then prices will increase which results in depreciating the value of Indian currency.

Reasons behind the decreasing value of Indian currency after the demonetization

Less liquidity

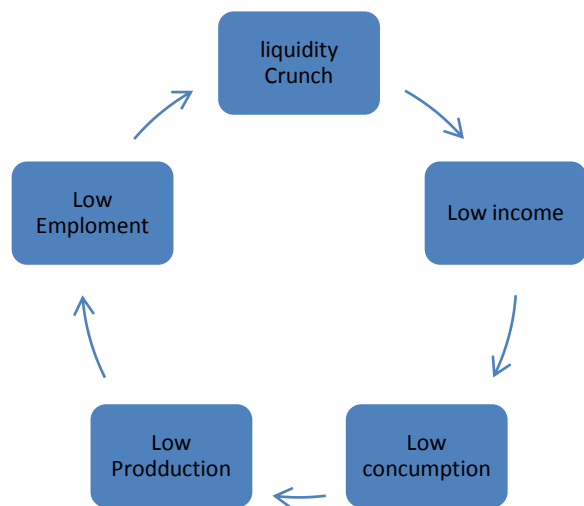
The main reason behind decreasing the value of Indian currency after the demonetization is the shortage of liquidity in the hands of the people. Liquidity crunch is responsible for depreciation as due to less cash in the hand, salary of the middle class will be reduced. It will lead to decrease in the National income. Foreigners will not invest in India. So, the Indian Rupee value will depreciate against United States Dollar.

Arrival of higher denomination notes

After the ban on the 500 Rs and 1000 Rs notes new notes of denomination 2000 were introduced. These notes were not used for daily consumption. The motive behind to print the notes of 2000 Rs to increase in saving. Due to 2000 Rs notes arrival and ban on 500 Rs notes consumption has been reduced and there is a situation of depression in India .In such a situation investor's do not want to invest in India. The entire situation is responsible for reducing the value of Indian currency.

Depression

Due to the demonetization, situation of depression in India will generate. Depression is a situation of less of income, employment and output. Due to liquidity shortage , people will be paid less, There income is reduced. No one is hired on the job. It reduces the employment and output from the economy. In the depression situation there is decrease in the foreign reserves and value of Indian currency depreciates against Unites States Dollar.



Process of Depression

These process leads to decrease in the value of Indian currency. This situation occurs due to the demonetization as due to demonetization people will have less liquidity in the hand and they will consume less. These will leads to less of the production. Less production will reduce the employment so situation of depression will arise .In the depression no investor want to invest which results in less of the foreign reserves. All these

reasons are responsible for depreciating the value of the Indian currency.

Less Foreign Direct Investment

Foreign Investors invest in a country where they can high rate of return. But due to demonetization rate of return decrease so foreigners do not want to invest And there is shortage of foreign reserves in India .For these reasons value of Indian currency fall against the other currencies.

Wrong assumptions

Government have wrong assumption that demonetization will improve the banking system. Improved banking system will share its profits in the investment process which will leads to capital formation. But all the activities will remain for the short time period. In the long time period Indian people will keep the money out of the bank. They kept the money in the bank to convert their old currency into new currency. These will reduce in investment which is responsible for depreciating the value of Indian currency.

Reasons for opposition of demonetization

The main reason that the demonetization was not accepted was that it came in existence with all sudden. People have to stand in long queues for long time to get the payment. It was very difficult process as liquidity fall very sharply. To fulfill the basic needs people have to wait in lines to convert their money in to other denomination based notes.

Ways to convert black money into white money at the time of demonetization

People adopted various ways to get rid of the problem and to save their previous money.

1. Deposit the money in the accounts of poor relatives.
2. Convert their black money in to gold.
3. Paying back the loans.
4. Payment of salary to the employees in advance.

Objectives of the study

The each and every study is coined for finding out the results by keeping in mind the certain objectives. For attaining the results some of the objectives are essential. Without the objectives study moves in wrong direction. The objectives of the study are:

1. 1 To see the impact of demonetization on the value of Indian currency.
2. 2 To see the value of Indian currency against the United States Dollar, Chinese Yuan, European Euro, Australian Dollar and Canadian Dollar due to demonetization.
3. 3 To see how the demonetization will remove the black money.

Review of literature

A different type of research has been done within two years to see the impact of demonetization on the value of Indian currency.

Gupta (2016) says that the main aim of demonetization to curb the black money from root. The paper reveals that citizens of India has given green flag to the decision of demonetization taken by the government The new currency which replaced the old one is of denomination of 500 and 2000 notes. Though the people faced a lot of inconvenience owing

to shortage of funds they did not criticize the government for the move. Even they lauded the currently (2016) Prime Minister of India for this big move. Prime Minister also addressed the people many times telling the people that it was a Mahayana and they must offer their own ahuti in it. Moreover, further said Modi was aware the hardships, people would suffer from but he sought only 50 days for setting the things right. He jibed at the chief political leaders who have stashed big amount of money and now joined hand to force government to take the decision back.

J. (2016) reveals that demonetization is like an effort to remove the corruption and black money from India. The aim of the study is to make people aware regarding the decision taken by the government that demonetization is an brave and courageous effort performed by the government. There is less development and investment in India due to the high rate of Inflation which is due to the existence of high money supply.

Patnaik (2016) reveals the reason behind the black money. The paper reveals that the main reason behind the black money is that people of India do not pay the taxes. And collect the money from illegal activities. To remove the black money, demonetization is a great step. If demonetization has good impact at the similar time demonetization was riot by the people. The paper gives the solution that liquidity should be kept with the citizen so they can fulfill their basic needs.

Vijay (2016) reveals that demonetization is not new for India. Prior to the effort, two times demonetization had been attempted but not successful. According to Reserve Bank of India statement demonetization was done in 1938 and 1978. The paper reveals that Reserve Bank of India is the manager and reservoir of Indian currency as well as print the currency. The effort was performed to stop the illegal use of currency.

Mittal (2017) Reveals that demonetization has primarily adverse impact upon the people of poor

class, agriculturists and small trader's .Moreover demonetization has adverse impact upon the Gross Domestic product of India. The reason for adverse GDP is that people were not able to reduce the consumption. But due to less money, prices were increased It also has bad impact upon the Gross Domestic Product.

Sachin (2017) reveals that in the last two years demonetization impact on small traders, Micro small and medium enterprises has been checked and find out that negative is the impact of demonetization on the on small traders, Micro small and medium enterprises.

Sharma and Gupta(2017) reveals that that in the last two years demonetization impact on small traders, Micro small and medium enterprises has been checked and find out that little and positive is the impact of demonetization.

Research Methodology

This will be all India study based on secondary sources of data to be collected from published and non - published sources.

Sources of Data

As mentioned above, the study will be based on the secondary sources of data.

The study undertaken under

Impact of Demonetization on value of Indian Rupee is completely based on the secondary sources of data. The secondary data will be collected from the World Bank Database, Reserve Bank of India site. Newspapers, clippings and research paper of other researchers.

Dependent Variables

Exchange Rate of India

Independent Variables

Inflation, interest rate, Gross Domestic Product, External debt and Foreign Direct Investment.























Data Collection

Data has been collected to see the impact of demonetization on the value of Indian currency against other currencies has been collected.

Shrinkhla Ek Shodhparak Vaicharik Patrika

Table 1

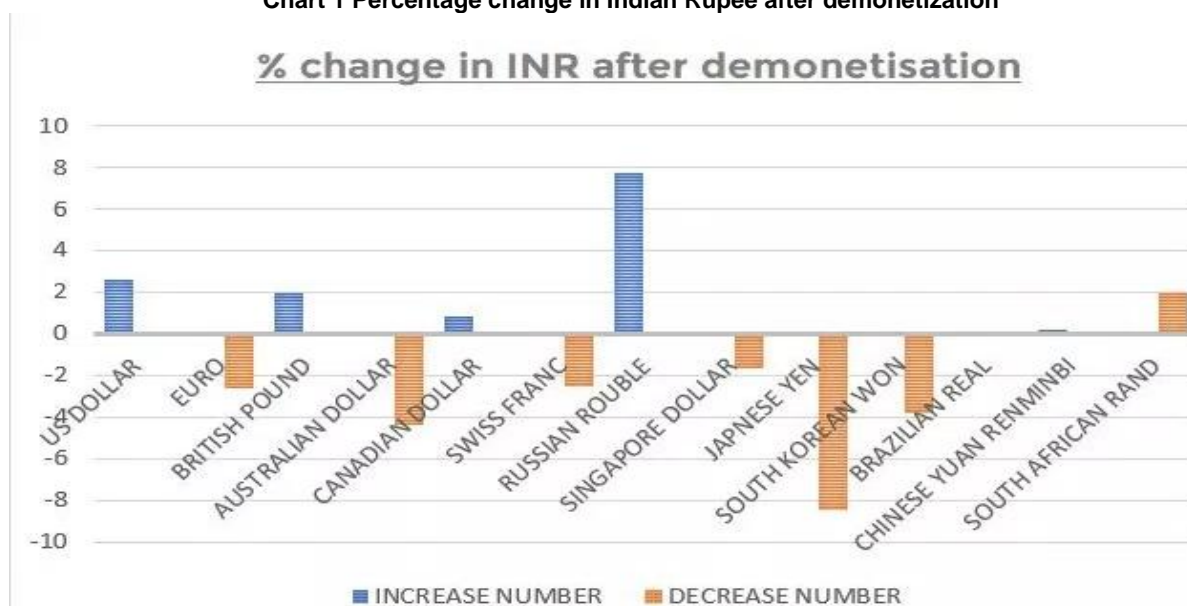
Indian currency value against other countries currency after demonetization

Country	currency Code	Currency Name	08 Nov 2016	28 Dec 2016	Change (%)	
ASIA						
	China	CNY	Chinese Yuan Renminbi	9.7838	9.8028	0.1942
	Indonesia	IDR	Indonesian Rupiah	0.0051	0.0051	0.0000
	Japan	JPY	Japanese Yen	0.6326	0.5793	-8.4255
	South Korea	KRW	South Korean Won	0.0586	0.0564	-3.7543
AFRICA						
	Algeria	DZD	Algerian Dinar	0.6004	0.6144	2.3318
	Egypt	EGP	Egyptian Pound	3.6755	3.5738	-2.7670
	Morocco	MAD	Moroccan Dirham	6.7510	6.7064	-0.6606
	Nigeria	NGN	Nigerian Naira	0.2098	0.2169	3.3842
	South Africa	ZAR	South African Rand	4.9977	4.8978	-1.9989
NORTH AMERICA						
	Canada	CAD	Canadian Dollar	49.7921	50.2238	0.8670
	Mexico	MXN	Mexican Peso	3.6000	3.2837	-8.7861
	Panama	PAB	Panamanian Balboa	66.4044	68.1720	2.6619
	United States	USD	US Dollar	66.4044	68.1720	2.6619
SOUTH AMERICA						
	Argentina	ARS	Argentine Peso	4.4168	4.3855	-0.7087
	Brazil	BRL	Brazilian Real	20.8618	20.8413	-0.0983
	Colombia	COP	Colombian Peso	0.0221	0.0228	3.1674
	Peru	PEN	Peruvian Sol	19.6916	20.1961	2.5620
	Venezuela	VEF	Venezuelan Bolivar	6.6536	6.8206	2.5099
EUROPE						
	France	CHF	Swiss Franc	68.0623	66.3407	-2.5294
	Germany	EUR	Euro	73.2762	71.3660	-2.6068
	United Kingdom	GBP	British Pound	82.1321	83.7567	1.9780
AUSTRALIA						
	Australia	AUD	Australian Dollar	51.3344	49.0953	-4.3618

The above mentioned data reveals the Indian currency value against other currencies at the time of demonetization and immediate after the demonetization. The data reveals that Indian currency

value was depreciating against the United States Dollar, Canada, Panama, Peru, Venezuela, and United Kingdom. Indian currency value was appreciating against Germany, France and Australia.

Chart 1 Percentage change in Indian Rupee after demonetization



The above mentioned chart clearly depict that Indian Currency was depreciating against many currencies and appreciating against only three

currencies. So, data reveals that Indian currency value was mainly depreciating against other currencies.

Table 2 depicts the impact of inflation, interest rate, external debt, GDP and Foreign Direct Investment on the exchange rate of India

Years	Exchange Rate against \$	Inflation (CPI)	Interest Rate (Lending rate)	External Debt (Current US\$)	GDP (Current US\$)	Foreign Direct Investment (Current US\$ Billion)
2015	66.13	5.3	6.75	475.0	2073	26.386
2016	67.8	4.8	6.50	479.7	2250.99	73.456
2017	64.4	2.36	6.69	485	2457.75	31.891

The data reveal the impact of all variables on the exchange rate. The data reveals that value of Indian currency will increase due to demonetization in the long time.

Conclusions

Some of the conclusions are followed after the complete study.

1. Demonetization is an effort of the government to reduce the black money and illegal activities like corruption, smuggling and terrorism from India.
2. In the short time, Demonetization will reduce the value of Indian currency. Decrease in value is due to the low consumption, income and employment.
3. In the long time period, value of Indian currency will increase as inflation will reduce. Inflation will decrease as demand will increase as compare to supply of Indian currency,
4. Higher interest rate arise expectations in the mind of the investors that they can get highest rate of return in India due to demonetization. It appreciates the value of Indian Rupee.
5. Gross Domestic Product of India will improve due o demonetization process as the banking habits will generate among the citizens.
6. Foreign Direct Investment will increase in India due to the highest rate of return. These appreciate the value of Indian currency.
7. In the short time period time Indian currency value will depreciate due to depression like situation generates in an economy..
8. Overall Demonetization has positive impact on the value of Indian currency as it decreases the illegal activities like black money, smuggling and terrorism.

Suggestions

To improve the situation of the economy, demonetization is a good step. But it will be accepted by all if the benefits of it will be disclosed to the citizens. The information about benefits will be informed to the citizens. People of India are illiterate so they are not familiar with the banking process. Government should organize awareness and training programmes to provide training how to deal with the banks. If Government will spread information about it than people will show their interest in the demonetization.

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