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IMPACT OF DEMONETIZATION ON GROSS DOMESTIC PRODUCT (GDP) – AN ANALYTICAL APPROACH

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ABSTRACT

With a view to curb financing of terrorism and activities such as espionage, smuggling of arms, drugs and other contrabands to India and also for eliminating black money, it has been decided to cancel the legal tender character of high denomination bank notes of Rs.500 and Rs. 1000 denominations issued by RBI. At the beginning there was a negative impact on the various sectors of the economy which resulted in to lower growth. Reports from various sources across the country suggest that every sector and regions has adversely affected. Apart from all this reports later at the end of this financial year the country showed a growth of 7.1%. This paper elucidates the impact of such a move on the GDP and analysis of some data's in an analytical approach.

Keywords: Black Money, Demonetization, GDP, National Income

I. INTRODUCTION

In the history of Independent India, the government at various times in order to curb black money in the country announced some voluntary disclosure schemes but it went unnoticed. Suddenly on 08thof November 2016 Prime Minister of our country announced a decision on India's first major "Currency vasectomy" and amid the result in cash squeeze coming as a disruptive step to fast forward the country into a breakaway economy. Major aim of demonetization is making India "Cashless society and to weed out the stocks of black money out of the economy.

Demonetization is a process by which a series of currency will not be a legal tender. The series of currency will not be acceptable as a valid currency. In the same way Rs. 500 Rs 1000 will not be acceptable as a valid currency. The sudden move to demonetize these currencies has paralyzed the economy to a certain extend. It has caused many difficulties for the common people because of insufficient availability of new currency notes. People have to make long queues in front of banks as well as ATM counters which are yet to be upgraded.

Apart from all these problems it has affected the country economically. Most of the sectors have also been affected which ultimately affected the economic growth of the country. The disruption to the economy will be such that there will be, possibly not just no growth in the last quarter of the year but actually a shrinking of the economy. During the month of October to December 2016 the GDP growth contracted thus showing negative growth.

After demonetization, the data of first two weeks shows that production and normal consumption is disrupted continuously. Apart from this many of the statician has predicted severe crisis in the economy for at least few months and its aftermaths will be there for few years. Leaving all this predictions behind, as per the data released by The Central Statistical Office declared that the growth in gross GDP of the country is 7.1%, signaling that independent economic forecasters may have overstated the drag on the economy from the November withdrawal of high value currency notes.

This paper makes an attempt to present the impact of demonetization on different sectors and also on GDP and tried to analyze the data available.

II. GDP AND ITS HISTORY

Gross domestic product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period. Though GDP is usually calculated on an annual basis, it can be calculated on a quarterly basis as well. GDP includes all private and public consumption, government outlays, investments and exports minus imports that occur within a defined territory. Put simply, GDP is a broad measurement of a nation's overall economic activity.

Gross domestic product can be calculated using the following formula: GDP = C + G + I + NX

Where, C is equal to all private consumption, or consumer spending, in a nation's economy, G is the sum of government spending, I is the sum of all the country's investment, including businesses capital expenditures and NX is the nation's total net exports, calculated as total exports minus total imports (NX = Exports - Imports).

III. HISTORY

GDP first came into use in 1937 in a report to the US Congress in response to the Great Depression after Russian economist Simon Kuznets conceived the system of measurement. At the time, the preeminent system of measurement was the Gross National Product (GNP). GNP differs from GDP in that GNP measures the productivity of a nation's citizens regardless of their locales, as opposed to the GDP's measurement of production by geographic location. After the Bretton Woods conference in 1944, GDP was widely adopted as the standard means for measuring national economies.

Beginning in the 1950s, however, some began to question the faith of economists and policy makers in GDP internationally as a gauge of progress. Some observed, for example, a tendency to accept GDP as an absolute indicator of a nation's failure or success, despite GDP's failure to account for health, happiness, and other constituent factors of general welfare. In other words, these critics drew attention to a distinction between economic progress and social progress. Others, like Arthur Okun, an economist for President Kennedy's Council of Economic Advisers, held firm to the belief that GDP is as an absolute indicator of economic success, claiming that for every increase in GDP there would be a corresponding drop in unemployment.

In recent decades, governments have created various nuanced modifications in attempts to increase GDP accuracy and specificity. Means of calculating GDP have also evolved continually since its conception so as to keep up with evolving measurements of industry activity and the generation and consumption of new, emerging forms of intangible assets.

IV. OBJECTIVES OF THE STUDY

To know the impact of demonetization on different sectors of the economy and how it affected the GDP of the country.

V. REVIEW OF LITERATURE

According to Ambit Capital, a respected Mumbai based equity research firm is hopeful that a strong formalization of the informal economy will ensue through 2017 until 2019 and this disruption could also crimp GDP growth in 2017-2018 to 5.8% from their earlier estimate of 7.3%.

1. According to Tim Worstall, Forbes contributor, in the article "Effects of demonetization on India's GDP-Difficult to calculate, we don't even know the sign", Nov 19, 2016, that the flow of money in to bank accounts will reduce interest rates and that has a stimulatory effect upon economic growth.
2. According to a press release made by Ministry of finance, Department of economic affairs, government of India, in Chronicle journal, vol.XXVIII, January 2017, stated that estimates for gross GDP growth in financial year 2017from financial analyst vary from a low of 3.5% to a range of 5.5-6.5%.
3. According to Care Ratings, November 18, 2016, the transition from GVA to GDP would remain unchanged at 0.2% as per initial estimate, overall GDP growth would be affected by 0.3-0.5%.
4. According to CMA Jai Bansal in his paper "Impact of demonetization on Indian Economy", January 2017 Governments intervention is a onetime draining of this current stock of black money but unless the root cause of corruption are removed, corruption will continue .it is a sort of like a dialysis, more of a short term cleaning up than a solution of the problem. It needs to be repeated periodically.

VI. SOURCES OF DATA

All the data used for this paper is from secondary sources. As an analytical study is done the data's are collected from various sources like journals, magazines, news papers and websites.

VII. LIMITATIONS OF THE STUDY

1. Inspite of best of efforts to minimize all limitations that might creep in course of research there were time constrains for the research.
2. The study is limited to secondary data only.

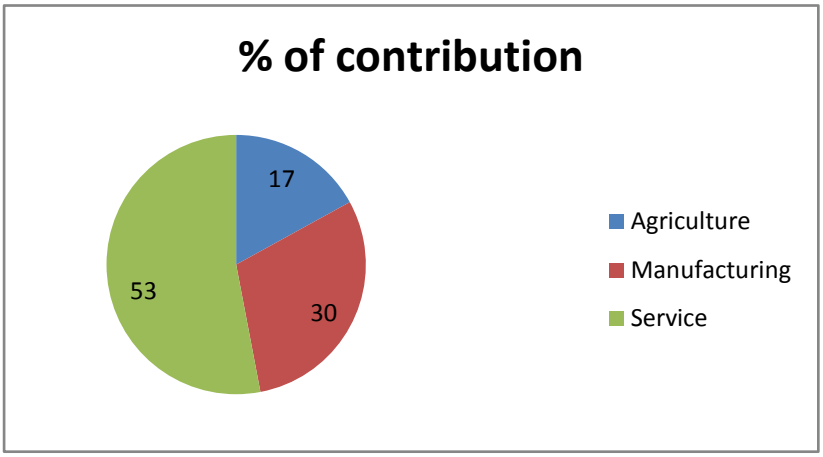
VIII. DATA INTERPRETATION

For analysis purpose of the study certain data have been collected through secondary sources. The data related to GDP and the data analyses of the sectors that affect the GDP have been considered for the study.

1. TABLE SHOWING THE CONTRIBUTION OF DIFFERENT SECTORS IN GDP AFTER DEMONETIZATION

Sr. No	Name of the Sectors	% of contribution
1	Agricultural Sector	17
2	Manufacturing Sector	30
3	Service Sector	53

2.CHART SHOWING THE CONTRIBUTION OF DIFFERENT SECTORS IN GDP AFTER DEMONETIZATION



IX. OBSERVATION

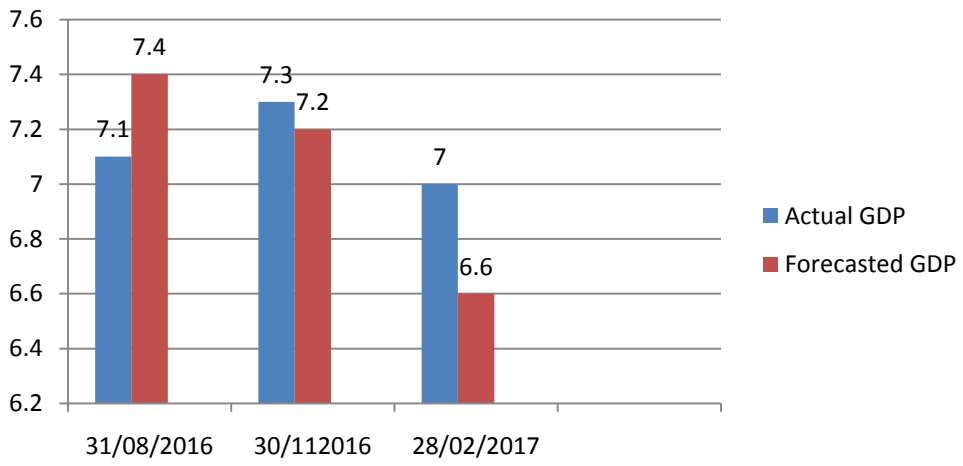
Economy of the country is divided in to three sectors called agriculture, manufacturing and service sectors which contribute in GDP. From the above table it is observed that after demonetization there is a negative impact in all the three sectors and there is less contribution by all the three sectors in GDP compared to previous years which is because of the cash crunch faced in the economy. The following are the reasons for less contribution.

1. As agriculture sector are dealt by the farmers which is mostly situated in the rural part of the country, most of the transactions are carried on cash. Since, the farmers face complete shortage of cash it could result in delay in payments.
2. As far as manufacturing sectors are concerned there was a drastic decrease in cash transaction and high cash crunch.
3. Service sectors hit worse during demonetization. It has been noted worst slump in three years. But banking sector is the only sector which was not affected by demonetization where bank deposits were increased from 1-2% compared to what it was prior.

3. TABLE SHOWING INDIA'S GDP GROWTH RATE

DATE	Actual GDP	FORECASTED GDP
31/08/2016	7.1%	7.4%
30/11/2016	7.3%	7.2%
28/02/2017	7%	6.6%

4. CHART SHOWING INDIA'S GDP GROWTH RATE



OBSERVATION

From the above figure it is observed that during the second quarter of 2016 i.e. 31st august 2016 the forecasted GDP was 7.4 wherein the country achieved 7.1% of it. In the third quarter i.e. on 30th November 2016 the forecasted GDP was 7.2% where it has achieved 7.3% which is 0.2% of targeted one and the latest GDP rate is 7% which is 0.4% greater than the forecasted GDP.

FINDINGS

1. The Indian economy advanced 7 percent year-on-year in the last three months of 2016, slowing from an upwardly revised 7.4 percent rise in the previous quarter but beating expectations of a 6.4 percent growth. The expansion was mainly driven by a surge public spending and agriculture. The GDP is expected to grow 7.1 percent in the fiscal year ending in March 2017.
2. This increase in GDP is because of the private spending rose 10.1 percent, Government spending went up 19.9 percent and Imports rose to 4.5 percent.
3. In the month of November 2016 India's gross domestic product advanced 7.3 percent year-on-year in the third quarter of 2016, following 7.1 percent expansion in the previous period and missing market expectations of 7.5 percent growth. Private consumption expanded at a faster pace while government spending slowed down and fixed investment dropped further.
4. In the month of august 2016 India's gross domestic product advanced 7.1 percent year-on-year in the second quarter of 2016, slowing from a 7.9 percent expansion in the previous period and missing market expectations of 7.6 percent growth. It was the lowest reading since the fourth quarter of 2014, as private consumption expanded at a slower pace while fixed investment dropped further.

5. Highest contribution to GDP has been made by the service sector i.e. by the banking sector as banks had a highest income in the form of deposits.

CONCLUSION

The present study has highlighted the impact of demonetization on GDP and the contribution of different sectors in GDP. Demonetization is represented as a surgical strike on black money, terrorism, counterfeit currencies etc. but at the same time it has affected the economy as a whole. Many sectors which play an important role in generating income to the country has crash down due to cash crunch as more than 60% of transactions are made in cash only. At the beginning after the declaration of demonetization country faced number of problems where it affected the GDP rate in November 2016. Slowly and gradually it is overcoming the situation and it raised the GDP to 7% from the forecasted GDP of 6.6%. The use of plastic money and transaction through online payments has increased and this resulted in the sustainability of different sectors. Once the currency circulation is normal the economy will be stable. The International Monetary Fund (IMF) in a report released last week said India's economic growth is expected to show the growth of7.2% in the first half of FY2017.

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