The publication discusses the economic impact of two major measures taken by India: a) Goods and Services Tax and b) Demonetization. It deals with GST and its impact on various relevant sectors as well as demonetization and its economic impact on the economy as whole.

Economic Revolution

India: GST & Demonetization

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ECONOMIC REVOLUTION: GST & DEMONETIZATION

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SECTION I

INTRODUCTION:

India, being the largest democracy in the world with a population of over 1.25 crores must cater to the need of a greatly diverse society. Since independence, multiple measures have been taken by different governments to further the economic growth. The efforts taken in this direction have been subdued by social problems such as rising population and deep-rooted corruption in the society.

The paper discusses the economic impact of two such major measures taken by the government: a) Goods and Services Tax (hereinafter refers to as "**GST**") and b) Demonetization. This paper is divided into two sections. Section I deals with GST and its impact on various relevant sectors whereas Section II deals with demonetization and its economic impact on the economy as whole.

In order to study the impact of GST on economy as a whole, the author of this Paper has taken some relevant sectors which are majorly affected by this uniform taxation. The author has also tried to explain the GST model in brief and its advantages over the old taxation system so as to have a comparative viewpoint. Interestingly, this idea of GST, a uniform tax, was originally introduced by the previous government. This feat was achieved by the current government that successfully got the bill passed in the parliament.

Similarly, demonetization was also attempted before to revamp the economy in 1954 and 1978. However, in contrast to the recent demonetization, the currency that was demonetized during 50s and 70s did not form the majority of the circulation. The measure created a massive cash crunch and lives were affected adversely. Hence, to study the impact of demonetization, the author has divided the economy into three major economic sector and has discussed the impact of demonetization on each of these sector.

GOODS &SERVICES TAX: BASICS AND ESSENTIALS

After the introduction of VAT, Goods and Services Tax was the logical step towards a comprehensive indirect tax reform.[1]Introduction of GST aims in a way to reduce the complexities prevailing in the indirect tax structure in India. The Central government passed four sets of GST Acts in the Budget session of 2017. These were:

i. Central GST Act, 2017;
ii. Integrated GST Act, 2017;
iii. Union Territory GST Act, 2017; and
iv. GST (Compensation to States) Act, 2017.

Legal Justification of GST:

Despite the success of VAT, there existed some shortcomings in the structure of VAT with respect to availing of CENVAT credits by manufacturers and dealers. The reason for such shortcoming was non-inclusion of several Central taxes in the framework CENVAT. Moreover, no step was taken to capture the value-added chain in the distribution trade below the manufacturing level in the existing scheme of CENVAT.

At state level, there existed taxes of indirect nature such as luxury tax, entertainment tax that was not included in the ambit of VAT. Furthermore, any commodity, in general, is produced on the basis of physical inputs as well as services, and there should be integration of VAT on goods with tax on services at the State level as well, and at the same time there should also be removal of cascading effect of service tax. In the GST, both the cascading effects of CENVAT and service tax are removed with set-off, and a continuous chain of set-off from the original producer’s point and service provider’s point upto the retailer’s level is established which reduces the burden of all cascading effects. This is the essence of GST, and this is why GST is not simply VAT plus service tax but an improvement over the previous system of VAT and disjointed service tax.

[1]The Empowered Committee Of State Finance Ministers, *First Discussion Paper On Goods and Services Tax In India,* Nov 2009, http://empcom.gov.in/WriteReadData/UserFiles/file/Discussion%20Paper/first_dis.pdf

GST Model:

GST being a multi-tier tax, the ultimate burden of tax falls on the consumer of goods/ services. It is referred to as value added tax because at every stage, tax is being paid on the value addition. Under the GST scheme, a person who was liable to pay tax on his output, whether for provision of service or sale of goods, is entitled to get input tax credit on the tax paid on its inputs.[2]

Prior to GST, before any commodity was produced, inputs were first taxed, and then after the commodity got produced with input tax load, output was taxed again. This was causing a burden of multiple taxation with a cascading effect. Moreover, in the sales tax structure, when there was also a system of multi-point sales taxation at subsequent levels of distributive trade, then along with input tax load, burden of sales tax paid on purchase at each level was also added, thus aggravating the cascading effect further.

Salient features of the proposed model are as follows:[3]

- (I) GST shall have two components: one levied by the Centre (referred to as CGST), and the other levied by the States (referred to as SGST).
- (II) The CGST and the SGST would be applicable to all transactions of goods and services made for a consideration except the exempted goods and services.
- (III) Since the CGST and SGST are to be treated individually, taxes paid against the CGST shall be allowed to be taken as input tax credit (ITC) for the CGST and could be utilized only against the payment of CGST.
- (IV) Cross utilization of ITC between the CGST and the SGST would not be permitted except in the case of inter-State supply of goods and services.
- (V) Ideally, the problem related to credit accumulation on account of refund of GST should be avoided by both the Centre and the States except in the cases such as exports, purchase of capital goods, input tax at higher rate than output tax etc
- (VI) The taxpayer would need to submit periodical returns, in common format as far as possible, to both the Central GST authority and to the concerned State GST authorities.

[2]Ibid at 1.
[3]Ibid at 1.

(VII) Each taxpayer would be allotted a PAN-linked taxpayer identification number with a total of 14/15 digits. This would bring the GST PAN-linked system in line with the prevailing PAN-based system for Income tax, facilitating data exchange and taxpayer compliance.

Dual GST: Both Centre and States will simultaneously levy GST across the value chain. Tax will be levied on every supply of goods and services. Centre would levy and collect Central Goods and Services Tax (CGST), and States would levy and collect the State Goods and Services Tax (SGST) on all transactions within a State. The input tax credit of CGST would be available for discharging the CGST liability on the output at each stage. Similarly, the credit of SGST paid on inputs would be allowed for paying the SGST on output. No cross utilization of credit would be permitted.

Inter-State Transactions and the **IGST Mechanism**: The Centre would levy and collect the Integrated Goods and Services Tax (IGST) on all inter-State supply of goods and services. The IGST mechanism has been designed to ensure seamless flow of incput tax credit from one State to another. The inter-State seller would pay IGST on the sale of his goods to the Central Government after adjusting credit of IGST, CGST and SGST on his purchases (in that order). The exporting State will transfer to the Centre the credit of SGST used in payment of IGST. The importing dealer will claim credit of IGST while discharging his output tax liability (both CGST and SGST) in his own State. The Centre will transfer to the importing State the credit of IGST used in payment of SGST.

Destination-Based Consumption Tax: GST will be a destination-based tax. This implies that all SGST collected will ordinarily accrue to the State where the consumer of the goods or services sold resides.

Benefits of GST

Benefits of GST over current indirect tax system in India[4]:-

1. *GST ensures a competitive pricing mechanism*: The implementation of GST will reduce net tax payment by final consumers which will reduce the prices of commodities. The process

[4] Adukia S Rajkumar, *A study on proposed goods and services tax framework in India*, p.34

will boost up the consumption and increase in production. When the cost of Production falls in the domestic market, Indian Goods and services will be more prices competitive in foreign markets which will improves export.

2. *Revenue Neutral Rate* (RNR) is considered to be the prominent factor for the success of GST. The government revenue would be less compared to the current system for the initial two years. By RNR Government ensures that its revenue remains the same despite of giving tax credits. So there is no question of loss for the states.
3. The online backup is one of the magnificent benefits of GST. The Government has already incorporated Goods and service tax network (GSTN). It will develop GST portal ensures the technology support for registration, return filing, tax payments, IGST settlements etc. An effective database system will always surpass all the hurdles.
4. As per Integrated Goods and Services Tax (IGST) central government will levy GST on inter-State trade and such tax shall be apportioned between the Union and the States in the manner as may be provided by Parliament by law. Import of goods or services would be treated as inter-state supplies and thus it would be subject to IGST in addition to applicable custom duties. Exports would be zero rated. The problem of different rate for different states on different products will be eliminated through the process. The confusion among dealers will reduce die to this process.
5. There will be only one law because GST shall subsume various taxes as specified above.
6. The will be one CGST rate and a uniform rate of SGST across all states. The current scenario of differential tax rates will be abolished, which will accelerate the interstate transfers which will ultimately increase the production.
7. The problem of Cascading effect arises because credit of Central Sales Tax and many other taxes not allowed. This situation will not arise as CST concept is being eliminated with introduction of IGST. Elimination of cascading effect will of course increase the production capacity of manufacturers and this will leads to improved production and export opportunities.
8. Tax burden is expected to reduce since all taxes are integrated and possible the burden to be split equitably between manufacturing and services. Over pricing of a particular product or service can avoid through this mechanism.

9. As GST mechanism removes cascading effect by providing credit, cost burden is also reduced. Reduction in production cost will lead to increased production.
10. GST is to be levied only at final destination of consumption and not at various points. This brings more transparency and corruption free tax administration.
11. A single taxation system could eliminate the roadblock for products in check posts and toll plazas lead to a lot of wastage for perishable items being transported. Additionally, GST would add to government revenues by widening the tax base.
12. There will be no entry tax as per GST, additional 1% of Tax to be levied on inter-state supply of selected goods. But currently being charged by selected states for interstate transfers.

A uniform tax system for a nation is the slogan of GST and this proposed mechanism will remove the effect of tax cascading in the nation. Goods and Service Tax will effectively surpass the various tax barriers persisted and the present indirect tax system.[5]

Economic Impact of GST

It was anticipated that impact of GST would be on the positive as far as economy was concerned. The primary reason that can be attributed to such anticipation was that of uniformity, i.e., GST will be levied on goods and services equally and no distinction will be made between the two unlike the erstwhile system.[6]

This new tax regime is to simplify life by bringing down the cost of logistics and inventory down significantly by replacing a number of other taxes like VAT, Service tax, CST, CAD, etc. Following is the impact of GST on certain important sectors:

Food Industry: The application of GST to food items will have a significant impact on those who are living under subsistence level.[7] But at the same time, a complete exemption for food items would drastically shrink the tax base.[8]

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[5]https://gst.caknowledge.in/role-chartered-accountants-gst/

[6]Dr. P.Paramashivaiah, *Introducing GST and its Impact on Indian Economy*, http://www.socialworkfootprints.org/uploads/5/6/5/4/56541763/introducing_gst_and_its_impact_on_indian_economy.pdf

[7]Ibid at 5.

[8]Ibid at 5.

Food includes grains and cereals, meat, fish and poultry, milk and dairy products, fruits and vegetables, candy and confectionary, snacks, prepared meals for home consumption, restaurant meals and beverages. Even if the food is within the scope of GST, such sales would largely remain exempt due to small business registration threshold.[9] Given the exemption of food from CENVAT and 4% VAT on food item, the GST under a single rate would lead to a doubling of tax burden on food.[10]

Housing and Construction Industry: In India, construction and Housing sector was needed to be included in the GST tax base because construction sector is a significant contributor to the national economy.[11] As far as GST's impact on the commercial office real estate market - with the existing service tax for commercial leases at 15%, GST would be likely neutral.[12]Landlords, too, have nothing to worry about GST on rent. Those who are earning a rental income by letting out their properties for residential use will not be taxed under the GST.[13]GST itself is expected to add about two per cent to India's gross domestic product (GDP). That is a substantial boost to the economy. If the economy does well, obviously, there will be more demand for real estate, and it will be a boost for the sector.[14] However, for people who wish to buy houses or invest in real estate should wait.

FMCG Sector: Despite of the economic slowdown, India's Fast Moving Consumer Goods (FMCG) has grown consistently during the past three – four years reaching to $25 billion at retail sales in 2008. Implementation of proposed GST and opening of Foreign Direct Investment (F.D.I.) are expected to fuel the growth and raise industry's size to $95 Billion by 201835.[15]

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[9]Ibid at 5.

[10] Kautilaya's Arthashastra (First book on Economics) http://www.igovernment.in/site/GSTfor-GDP-gains/ as accessed on 28 January, 2009

[10] http://gstindia.com/yahoo_site_admin/assets/docs/GST_rakesh_singh_2.347141245.pdf as accessed on 20 January 2009

[11]Ibid at 9.

[12]Anuj Puri, *How Will GST Impact the Real State*, ECONOMIC TIMES, (May 16, 2017, 8:10 P.M) http://economictimes.indiatimes.com/wealth/real-estate/how-will-gst-impact-the-indian-real-estatesector/articleshow/58588312.cms.

[13]Sunita Mishra, *No Additional Burden on Homebuyers Under GST*, PROP TIGER https://www.proptiger.com/guide/post/gst-the-real-estate-sector-all-you-need-to-know.

[14] Ibid at 12.

[15]According to a FICCI – Technopak Report, *Implemtation of GST will also help in uniform, simplified and single point Taxation and thereby reduced prices.*

Rail Sector: There were suggestions for including the rail sector under the GST umbrella to bring about significant tax gains and widen the tax net so as to keep overall GST rate low. This will have the added benefit of ensuring that all inter – state transportation of goods can be tracked through the proposed Information technology (IT) network.[16] The railways enjoy a 70% abatement which means only 30% of the value is taxable under service tax. Thus, the effective rate is =30% of 15% = 4.5% of the total fare.[17]

Financial Services: In most of the countries GST is not charged on the financial services. Example, In New Zealand most of the services covered except financial services as GST. Under the service tax, India has followed the approach of bringing virtually all financial services within the ambit of tax where consideration for them is in the form of an explicit fee. GST also include financial services on the above grounds only.[18]Service tax is currently levied at the rate of 15 per cent (including 0.5 per cent Krishi Kalyan cess and 0.5 per cent Swachh Bharat Cess) on most financial services.[19]

A bank charges service tax on most transactions - online money transfers or withdrawals from ATMs beyond specified limits. With GST, these services will now attract a tax of 18 per cent instead of 15 per cent service tax, charged currently.[20] However, experts are hopeful that the increase in cost may not last in the long run as banks will pass on the benefit of input tax credit, under GST, to their customers.

Information Technology enabled services: To be in sync with the best International practices, domestic supply of software should also attract GST. On the basis of mode of transaction. Hence if the software is transferred through electronic form, it should be considered as Intellectual Property and regarded as a service. And f the software is transmitted on media or any other tangible property, then it should be treated as goods and subject to GST[21]. GST on IT sector will attract 18% on software services provided by software companies. For purely software services,

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[16]https://www.gst.gov.in/.
[17]*Impact of GST Rates on Rail Transport*, https://cleartax.in/s/impact-of-gst-rates-on-rail-transport
[18]The Institute Of Chartered Accountants Of India New Delhi (www.icai.org/resource_file/17848icairecomgst.pdf).
[19]Renu Yadav, *How GST Rollout will Affect the Financial Service*, (July 2017) http://www.businesstoday.in/current/economy-politics/gst-rollout-will-affect-financial-services/story/255655.html.
[20] Ibid at 18.

the cost of such services will increase under GST.[22]Freelancers offering software services such as designing, app development, website designing etc., earlier paid a service tax of 15%. This has now increased to 18% under GST.[23]

Impact on Small Enterprises: There is three categories of Small Enterprises in the GST regime. Those below threshold need not register for the GST. Those between the threshold and composition turnovers will have the option to pay a turnover based tax or opt to join the GST regime. Those above threshold limit will need to be within framework of GST. There is possible downward changes in the threshold in some States consequent to the introduction of GST may result in obligation being created for some dealers. In this case considerable assistance is desired.[24]

In respect of Central GST, the position is slightly more complex. Small scale units manufacturing specified goods are allowed exemptions of excise upto Rs1.5 Crores. These units may be required to register for payment of GST, may see this as an additional cost.[25]GST will enhance the taxpayer base by bringing more SMEs under its ambit, and will definitely pass on the burden of compliance and associated costs to them. The fact GST will remove multiple taxation which in turn will ease the transfer of goods across states, small enterprises will have positive impact on this sector.

[22] https://cleartax.in/s/impact-of-gst-on-it-sector
[23] Ibid at 19.

[25]Alok Patnia, *Waking Up to a new GST Era and its Impact on Small Business*, https://yourstory.com/2017/07/impact-gst-small-businesses-india-tax-finance-arun-jaitley/.

DEMONETIZATION:

The government on 8th November announced that INR 500 and INR 1000 notes of Mahatma Gandhi series will cease to be legal tender effective immediately.[26]The term that describes this abovementioned process is called demonetization. Demonetization is the process of withdrawal of a particular form of currency from circulation or stripping a currency unit of its status as a legal tender.[27]

The reasons provided by the government for demonetization were twofold: a) first it aimed to curb the circulation of "black money" and counterfeit notes and b) second, the government aimed to promote a cashless, and more digitalized economy.

Legal Procedure:

The demonetization of 2016 was brought into effect through three legal instruments:[28]

a. The first was the Gazette Notification issued by the Ministry of Finance stating that in the exercise of its powers conferred under section 26(2) of the Reserve Bank of India Act the central government, on the recommendation of the Central Board of Directors of the Reserve Bank of India, had declared that banknotes of the existing series with the denomination of Rs. 500 and Rs. 1,000 shall cease to be legal tender from November 9, 2016.
b. Second, the Ministry of Finance issued a Gazette Notification specifying the new denomination of Rs. 2,000 notes.
c. The third Notification was issued by the Reserve Bank of India (RBI) to the banks specifying the actions to be taken by the banks for people to exchange old denomination notes for the new series of bank notes, called the Mahatma Gandhi (New) Series.

[26] Vishwanath Nair, *RBI notifications on Demonetization since November 8*, LIVEMINT (Dec 6, 2016, 8 P.M), http://www.livemint.com/Industry/WWhlfsa3RUvtFmOTvAAAHJ/RBI-notifications-on-demonetisation-since-8-November.html
[27] Syamsundar Palanisamy, *Demonetization-A Comparative Study With Special Reference to India, (*January 2017), https://www.researchgate.net/publication/312128645_DEMONETIZATION_A_COMPARATIVE_STUDY_WITH_SPECIAL_REFERENCE_TO_INDIA
[28] Yogesh Pratap Singh, *Legitimacy of Demonetization*, LIVELAW (Nov 21, 2016, 8:10 P.M) http://www.livelaw.in/legitimacy-of-demonetization/

The above mentioned notifications issued by government prohibit the transfer or receipt of banknotes that have been ceased to be legal tender after a certain deadline which violates section 39 of Reserve Bank of India. Hence, to formalize the notification and impose the deadlines for exchanging old notes with new ones, it was essential to pass or promulgate laws to that effect. Under lawmaking power of President, Mr. Pranab Mukherjee promulgated the Specified Bank Notes (Cessation of Liabilities) Ordinance, 2016 on December 30, 2016 making it illegal to hold Rs. 500 and Rs. 1000 notes after March 31, 2017. This legislation was passed on February 27, 2017 by the Parliament of India to give validity to the abovementioned Ordinance.[29]

Economic Impact:

According to the Reserve Bank of India Annual Report for April 2015 to March 2016, the value of the currency notes at the end of March 2016 was 16.42 trillion Indian rupees. The 500 rupee and 1,000 rupee currency notes formed 86.4% of the value. In one stroke, the government removed 86.4% of the currency in circulation by value. In terms of volume, the currency notes of these two denominations formed 24.4% of a total 90.27 billion piece.[30]

This section assesses the economic impact of this abovementioned massive withdrawal of money from the economy, on growth and inflation and their outlook in the context of subsequent re-monetization. To understand this, the economy could be bifurcated in three broad segments as following:

1. Agriculture sector;
2. Manufacturing sector, and;
3. Service sector;

Agricultural sector:

Agriculture contributes to seventeen per cent of the GDP.[31]Cash being the primary mode of transaction in agriculture sector, stress in agriculture was bound to appear because of demonetization.

[29] PRS Legislative Research, http://www.prsindia.org/billtrack/specified-bank-notes-cessation-of-liabilities-bill-2017-4601/

[30] Jai Bansal, *Impact of Demonetization on Indian Economy*, INTERNATIONAL CONFERENCE ON INNOVATIVE RESERCH IN SCIENCE, TECHNOLOGY AND MANAGEMENT, Jan. 2017 at 2.

[31] Ibid at 16.

Short-Term Impact: The short-term impact was mostly negative because of co-operative banks were barred from exchange-deposit of demonetized currency which formed the major portion of formal financing in parts like Punjab, Uttar-Pradesh, Odisha and Gujarat.[32]Sale, transport, marketing and distribution of ready produce to wholesale centers or mandis, is dominantly cash-dependent.[33]

Essentially, the farmers can be classified into following two categories on the aspect of demonetization:[34]

1. Farmers with KCC/Agri Loan account
2. Farmers with no KCC/Agri Loan account.

Farmers with KCC/Agricultural Loan Account: The government allowed farmers to withdraw up to Rs.25,000 per week against their crop loans to ensure sowing of winter crops is done properly. These farmers have at least a basic knowledge on how banking works and they could be able to sustain the impact of demonetization. Unless they have huge amount of money hoarded, they shall feel relaxed about the current situation. Since it is a winter crop harvesting period, they shall feel relaxed. The problem would be with the cash realized from previous sales which were not deposited into KCC account and not with buying the new seeds. If they do have large hectares of land, they can pay easily making a simple bank transfer. Further as of now, farmers can use old Rs.500 notes to buy seeds.

Farmers with no KCC/Agricultural Loan account: They will be largely affected as they do not have the facilities of withdrawing 25000 in cash. As it is generally seen that such farmers do not keep lump sum in bank accounts largely due to fact of low income or sometimes, lack of awareness. Credit transactions may increase in agricultural sector due to these farmers.

Further as of now, farmers can use old Rs.500 notes to buy seeds. Now coming to the different perspective, the farmers based in rural areas with no banks would be largely affected. They will face too much difficulty because of the demonetization. The cash crunch will hit them hard. Unless they have good connection with the suppliers, they are bound to suffer most.

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[32] Renu Kohli, *Demonetization: The Impact on Agriculture*, LIVEMINT, (Nov. 22, 2016, 8:30 P.M), http://www.livemint.com/Opinion/B1vFTOgwqHjdM5nkmg2CxJ/Demonetization-The-impact-on-agriculture.html.
[33] Ibid at 18.
[34] Dr.V.G.Sumathy & T.Savitha, *Impact of Demonetization on Agricultural Sector*, IOSR JOURNAL OF HUMANITIES AND SOCIAL SCIENCE, at 35.

In the scenario of lack of cash, most of the transaction going on credit basis. The input dealers (seed, fertilizer and pesticide dealers) are increasing prices by 20-30% of the normal price as the transactions are on credit basis. In product market also big traders and commission agents are offering credit to farmers at much higher interest (reaching 36% for just a month) than in normal conditions. The cash crunch caused by demonetization affected farmers badly who are not acquainted with cashless transactions. Prices in consumer markets (Delhi and Mumbai) are higher, but in villages there were no buyers for farmer's harvested crop.

Long-term Impact: Agricultural sector is still lacking behind in terms of innovation and irrigation. It is often seen that innocent farmers are exploited by the intermediaries. It is to be seen in future what Modi's government has in place for farmers in the future. Some of the impacts on presumptions would be: a) with recovery of black money likely to be in billions, the government can invest in the agricultural infrastructure. b) The rates of interest on loans are likely to fall. It will depend on how much the government does make recovery. c) Out of the money, the irrigation project can be financed. The government should try to reach out to the farmers of rural areas also. Otherwise, we might see rise in prices of the commodities.

So, in a nutshell, the farmers in rural areas being distantly linked with banking channels will be hit hard. This will adversely affect the demand and supply of grains, fruits and vegetables and hence their prices.

Manufacturing Sector:

Cash is the preferred mode of transaction globally, accounting on average for 85% of them. Easy accessibility, its certainty of acceptance and efficiency as the settlement is not dependent on any additional infrastructure, and no additional charges make it universally the most preferred mode. The only problem of cash transactions is the anonymity and difficulty of establishing an expenditure trail which make it an ideal mode for unreported transactions as well.

Demonetization of high-value currency notes in November has begun to hit the manufacturing sector, according to a private sector survey.[35]The Nikkei India Manufacturing Purchasing Managers' Index (PMI) fell to 49.6 in December, the first time it hit below the 50-mark in 2016, from 52.3 in November. Having held its ground in November following the unexpected

[35]The Hindu, *Demonetization Hits Manufacturing Sector*, THE HINDU, (Jan 2, 2017, 10:30 P.M), http://www.thehindu.com/business/Economy/Demonetisation-hits-manufacturing-sector/article16979062.ece.

withdrawal of ₹500 and ₹1,000 bank notes from circulation, India's manufacturing industry slid into contraction at the end of 2016.[36] Moreover, cash crunch has resulted in lower purchasing activity in turn leading to lower manufacturing output.[37]

In India's manufacturing and distribution value chain, there exists various components like suppliers, raw material, inventory, contract labor, dealers, customers etc. All the mentioned components are affected individually as well as a whole manufacturing sector. The key variables such as the logistics and contract labor that are used for loading and unloading is highly unorganized and was usually paid on a daily basis through hard cash. The dearth of cash effects these workers adversely and immediately. This in turn led to lower labor availability.
Make-to-stock sector also had challenges related to consumption of existing goods and material which in turn created 'bull-whip' effect across the supply chain.[38]

The major decline was seen in the demand of two wheelers than luxury cars/four wheelers since cash is the primary mode of transaction in the purchase of two wheeler vehicles. Another segment of automobile industry which is facing effects of demonetization is the used car industry wherein numerous car dealers have reported sudden decrease in sales. It is an unorganized industry and therefore, the modes of payments are not exactly regulated.[39]Business houses are an integral constituent of the country's economy. While medium and large scale business is unaffected to such ban, many small-size commercial establishments are deeply affected by such sudden move by the government.[40]A study by the All India Manufacturers' Organization (AIMO), which represents over three lakh small and medium scale industries, estimated a loss of 35% of temporary jobs in MSMEs across the country sector and a 50% drop in revenue during the first 34 days of demonetization.[41]

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[36] Ibid at 21.
[37] Sampath Venkataswamy, *Demonetization and its effect on Indian Manufacturing Sector*, Jan. 10, 2017 at 1, https://www.linkedin.com/pulse/demonetization-its-effect-indian-manufacturing-sector-venkataswamy.
[38] Supra.
[39]PHD Research Bureau, Impact of Demonetization on Economy, Business and People, at 9, http://phdcci.in/image/data/Research%20Bureau2014/Economic%20Developments/paper/Study%20on%20Impact.pdf.
[40] Ibid at 20.
[41] Kaustav Das, *Analysing Demonetization: The Economic 'Masterstroke' of Unending Narratives*, TIMES NOW, (Sep. 2, 2017, 2:52 P.M), http://www.timesnownews.com/business-economy/article/demonetisation-analysis-note-ban-hits-indian-economy-government-rbi-under-pressure/83902.

Service Sector:

Service sector is also referred to as tertiary sector of the economy, primary and secondary sector being farming and manufacturing respectively. The service sector produces intangible goods, more precisely services instead of goods, and according to the U.S. Census Bureau, it is comprised of various service industries including warehousing and truck transportation services; information sector services; commodities, securities and other investment services; professional, technical and scientific services.[42] Hence, any economic imbalance in the above mentioned area will affect the economy as a whole.

The Nikkei India Services Purchasing Managers' Index (PMI), which tracks services sector companies on a monthly basis, stood at 46.7 in November, down from 54.5 in October.[43] The Index slipped into contraction territory for the first time since June 2015 and pointed to the sharpest reduction in output for almost three years. A reading above 50 means the sector is expanding, while a score below this mark signals contraction. Due to cash crunch in the economy post demonetization, businesses declined in financial intermediation, hotels & restaurants and renting activities. The cash shortage resulted in fewer new business operations, which in turn caused a fall in activity and ended planned expansion in many cases. The drop in services activity is not surprising since the share of the unorganized sector in services (around 45% of total, as per 2004-05 data) is much higher than in manufacturing (around 23%), suggesting larger dependence on cash transactions.[44]

Long-Term Impact: The disruption in business activity was however to be "short-lived", with many economists anticipating a pick-up in activity as these high-value banknotes are replaced and black-market firms end their operations. Expectations of replacement of high-value rupee notes, improved advertising campaigns, favorable government policies and the withdrawal of unregulated companies from the market have boosted sentiment for the coming 12 months, the survey noted.[45]

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[42] Investopedia, http://www.investopedia.com/terms/s/service-sector.asp

[43] *Demonetization Effect: Service Sector Takes Hit,* DNA INDIA, (Dec. 5, 2016, 8:10 P.M), http://www.dnaindia.com/money/report-demonetization-effect-pmi-hits-worst-slump-in-3-years-at-467-innovember-2279902.

[44] Ibid at 29.

[45] Ibid at 29.

Recent data actually contributes to the expectation of the economists that service sector recovered that “short-term” of cash crunch by shifting to cashless way of payment which was the secondary agenda of government for demonetization.

Agendas of Demonetization: How far is it achieved?

As mentioned earlier, government had two essential agenda for demonetization:

a) First, it aimed to curb the circulation of “black money” and counterfeit notes, and;
b) Second, the government also aimed to promote a cashless, and more digitalized economy.

Circulation of “Black Money” and Counterfeit Notes: The reason given to the citizens at the night of November 8, 2016, was that demonetization will serve as a tonic for curbing the menace of black money in the country. It was further stated that a large amount of fake currency which is in circulation is in the form of 500 and 1000 currency notes and making these currency illegal tender will also affect their circulation making them obsolete and along with this a major problem of terrorism which the country is facing in the form of Inter-Services Intelligence of Pakistan and the Naxalites movement will also be effected due to the demonetization of the major currencies.[46]

The initial debate around demonetization was about the economics of whether black money should be discovered or destroyed. As it was a common perception that black money being destroyed will not help the economy because the first step of the owners of illegal money will be to destroy it rather than depositing it. However, government had provided an option that if the owners deposited the non-taxed/illicit money in the bank account within the provided time period, they will be given exemptions. The drawback of this step was that once an individual deposits huge amount of accounted money, he/she will be on the radar of tax department forever, which is enough to induce fear.

Essentially, forward and backward effects are two important ingredients of any policy to curb the flow of Black Money.[47] The entire demonetization process only provided a backward effect by destroying the black money already accumulated in the country. It affected only the hard cash

[46] Tandon And Kulkarni, *Demonetization In India : Good, Bad And Ugly Facets*, ASIAN JOURNAL OF RESEARCH IN BUSINESS ECONOMICS AND MANAGEMENT Vol. 7, Jan 2017, at 41-47
[47]Patnaik, Prabhat, *Black Money” And India’s Demonetization Project*, (2016, Nov 19), http://www. Globalresearch.Ca/Black-Money-And-Indias-Demonetization-Project/5557384.

that was accumulated in the currency denomination of Rs.500 and Rs.1000. It never defined a process to stop the creation of black money in the economy.

At 12% of GDP, India's cash economy is nearly four times the size of that of Brazil and South Africa. By demonetizing the Rs 500 and Rs 1000 notes, India could get rid of counterfeit currency and fake notes that allegedly entered the country through the Chinese and the Pakistani border. Some tax evaders will surely bring out their cash stashed away in mattresses and false ceilings. But this will be a trickle – a minuscule *percentage* of the total.[48]

Even after spending so much money and causing a panic in the country the ultimate gain of the demonetization process is just a back ward effect that is it has no restriction on the fresh accumulation of black money in the country.[49]

The major outcome of the entire demonetization process has been that it has created a sense of awareness amongst the people regarding black money and have also created a sense of fear in keeping with them money in the form of hard cash.[50] In urban areas steps are still on to create awareness regarding cashless modes of payments but in the rural areas people are still reluctant to go cashless. As far as effecting black money is concerned this process has certainly destroyed the black money accumulated by the people but not to the much benefit of the economy as the money was not discovered but destroyed.[51] What the future of black money in the country will still depend upon the legal and legislative measures to be taken by the government from time to time.

Cashless and Digitalized Economy: In order to deal with the shortage of cash in the economy and to prevent the accumulation of Black Money in future the government went forward to convert the economy from cash economy to cashless economy promoting digital payments.

The government wanted India to go cashless, but doing so was not easy. Cashless transactions had their downsides for consumers. But, for those with access to digital payments, rejecting cashless options or hesitating to embrace technology was also not an option in the wake of the

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[48]Abusaleh Sariff, *Why Will Demonetization Not Eliminate Black Money And Corruption*, (Nov. 16, 2016) https://thewire.in/80319/demonetisation-will-not-eliminate-black-money-or-corruption.

[49] Dr. Neeraj Emmanuel Eusebius, *An Analysis of Impact of Demonetization on Black Money in India*, IOSR JOURNAL OF HUMANITIES AND SOCIAL SCIENCE, Vol. 22, May 8, 2017, at 75.

[50] Ibid at 34.

[51] Ibid at 34.

cash crunch brought on by the demonetization move. Questions of access aside, a cashless world has its benefits.

National Payments Corporation of India announced that there has been an impressive surge in the usage of cards at Point of Sale terminals at shops and other retail outlets.[52] The value of transactions almost doubled after the announcement of demonetization.

Further 67% jump was noticed in number of transactions using immediate payment service to 2 million.[53] 3 times jump in Rupay transactions on point of sale to 10 lakh a day, three times the norms.[54] 7 million transactions Paytm has been witnessing daily with transactions worth Rs.120 crores and 15.00 lakh people are starting usage of cards. Debit cards transactions have doubled since demonetization.[55]

However, there exists structural problems as opposed to logistical problem for converting India to a cashless economy. Card acceptance infrastructure struggles to keep pace with India's growing population.[56]Only 18% of all ATMs are deployed in rural India.[57]The RBI's own research finds that states with a higher female population and a more rural populace show lower levels of financial inclusion.[58]The World Bank's Global Findex shows that Indians are significantly less familiar with digital banking – the use of credit or debit cards, making transactions using mobile phones, and using the internet to pay bills – than their peers in middle-income nations.[59]

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[52] B.M Saini, *Demonetization-Metamorphosis for Cashless India*, INTERNATIONAL JOURNAL OF SCIENCE AND RESEARCH, Vol 2, Dec. 2016.
[53] Manpreet Kaur, *Demonetization: Impact on Cashless payment System*, ICRTESM, Jan. 8th, 2017 at 684.
[54]PIYUSH KUMAR "AN ANALYSIS OF GROWTH PATTERN OF CASHLESS TRANSACTION SYSTEM" Vol. 3, Issue 9, Sep 2015, 37-44 © Impact Journals.
[55] Ibid at 39.
[56] Ibid at 38.
[57] Ibid at 38.
[58] Ibid at 39.
[59] Ibid at 39.

ANALYSIS AND RECOMMENDATION:

The paper extensively dealt with the two essential regulatory steps taken by the government in past one year. After the Economic Liberalization of 1991, GST and Demonetization would be referred to as economically revolutionary periods. The abovementioned steps were taken to make the Indian economy healthy again as this is what was propagated to the common man. There is no denial in the fact that both the measures shook the economy to its core. However, success for the measures are yet to be seen.

Demonetization created economic chaos and a vast portion of population was adversely effected, especially the middle class which is mostly dependent on cash for daily transaction. The GDP came down to a three year low as the data suggests. The reasons provided by the government for demonetization revolved around removal of Black money from the economy. However, in the recent reports as provided by RBI, it got just Rs 16,050 crore whereas it was said that the government had expected dividend of close to Rs 4-5 lakh crore. Senior politicians like P Chidambaram and Mamata Banerjee called the demonetization a big scam which facilitated the conversion of black money. So, was it wise decision to lose one per cent GDP for just Rs 16,000 crore? However, Demonetization has its other benefits as well, that should not be sidelined. The entire process formalized banking and increased the reach of financial inclusion. The use of digital payment gateways increased which fulfilled the other agenda of demonetization. Hence, it will be unfair to call demonetization a failure only because of its failure to discover huge amount of black money.

Goods and Services Tax, is comparatively a new step taken and its actual impact is yet to be seen. The rates of GST starts to apply from 1 July, 2017. There exists lots of confusion around the application of various rates and the procedure for the same. However, it is anticipated that GST will simplify the levy of tax and widen the tax base for the government. The generation of huge amount of revenue is expected form the widening of the tax base. Though it would be recommended that government should take some steps to educate people about the new tax and its applicability through seminars or courses. The Law also needs to be free from major loopholes and confusion as it will directly affect the economy, which in turns effects the common man. As of now, we can wait for the actual impact of GST on our economy.

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