

THE GOVERNMENT CONTINUES TO CLAIM THAT IT HAS SCORED A GOAL WITHOUT ADMITTING THAT IT IS A SELF-GOAL—DEMO CAUSED SIGNIFICANT DISRUPTION

Growth numbers tell the truth

THE TWO REPORTS released in the last week—RBI's Annual Report and the Quarterly Estimate of the GDP—have once again drawn focus to the issue of economic slowdown and the impact of demonetisation in decelerating growth. While the opposition parties have called it a disaster, a monumental blunder and a measure that inflicted enormous pain without gain, the ruling party mandarins have termed it as the most innovative move to curb the black money, advancing the process of formalisation of the economy and ending anonymity. In this din and buzz, where positions are taken on party lines, the common man is left confused.

That RBI got back ₹15.28 lakh crore of demonetised notes as against the total of ₹15.44 lakh crore has not come as a surprise. I had pointed out in an earlier column in this paper (December 6, 2016) that the black wealth held in cash was estimated to be just about 5-6%. Furthermore, it was not difficult for those with black wealth held in cash to find ways and means to bring it back to the system. Similarly, the small proportion of counterfeit notes discovered by RBI is also not a surprise as the study by ISI had estimated counterfeit currency to be a minuscule proportion of the total currency in circulation. I had argued that demonetisation would not discourage future accumulation of black money as it does not alter either the probability of detection or the penalty rate.

RBI's numbers simply confirm the fact that cancellation of selected bank notes has been a costly exercise without much tangible benefits. The prime minister, in his speech on November 8, had set three objectives namely, removing black economy, abolishing fake notes and putting an end to terror financing. The decision was kept secret until it was announced on November 8, precisely to catch the black money hoarders off-guard and nullify these notes as the hoarders were not expected to put them in the banks. The attorney general made a clear statement to the Supreme Court that the government expected ₹10-11

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lakh crore to be deposited in the banks, and the remaining ₹4-5 lakh crore which was used to fund terrorist activity would be neutralised. This has come completely unstuck. Despite the surprise element, those who held black money found ways to deposit them. The statement by the finance minister that the money has now been identified with the owner is nothing more than a truism.

One outcome from the exercise is stated to be a closer scrutiny of suspect accounts. The government hopes to scrutinise 1.3 million suspect accounts of 9,72,000 persons involving ₹2.99 lakh crore. This however, is going to be a long and drawn out affair. First, does the tax department have the capacity to scrutinise these many accounts? Second, how many of the big cases will end up in courts and pushed to the back-burner? How long do we have to wait to know how much of the black money has been caught after bearing all the pains? As a matter of fact, the narrative on the objective of demonetisation has continuously changed and the poor have been dished out the dream of better days while promises were made to punish the rich man who cheated the system!

On the positive side, the Economic Survey has reported the sharp increase in the number of taxpayers during 2016-17 over the previous year. The Survey states that the number of income tax returns filed increased from 63.5 lakh in 2015-16 to 80.7 lakh in 2017-18 and estimates the increase on account of demonetisation at 5.4 lakh taxpayers and the reported additional income by these taxpayers was about ₹10,600 crore and at about 20% average tax rate, additional tax is estimated at a little over ₹2,000 crore. The Survey estimates the gains

from digitisation in terms of the reduction in the level of cash in transactions at ₹3.5 lakh crore. A part of this might have been forced on account of lower cash available and, therefore, the Survey states that the extent of the gain will be known only when the reduced ratio of cash-to-GDP persists over time. Another gain is stated to be the increase in financial sector savings. The net financial sector savings relative to GDP increased from 7.8% in FY16 to an estimated 8.1% in FY17.

On the flip-side, the Annual Report shows the sharp reduction in the profitability and dividends from RBI and additional cost of remonetisation. Of course, there have been tales of hardships, losing daily wages, loss of unorganised businesses, lower banking sector activity with the preoccupation of the banks with taking deposits of old notes and dispensing new notes. Some enterprises went out of business temporarily while some others became unviable altogether. The horror stories of places like Mandasaur and Bhiwandi are yet to be captured by any statistics.

The second quarter estimate of GDP released by the chief statistical adviser confirms the adverse impact of monetisation on economic activity. The GDP growth during the quarter, at 5.7%, was much lower than 7.9% during the first quarter of last year. In the previous quar-

ter it was 6.1%. The growth in Gross Value Added, which is the real measure of economic activity, at 5.6%, was the same as the previous quarter, but much lower than 7.6% recorded in the first quarter of last year. Indeed, the growth rate of the economy has been decelerating right from the second quarter of last year on the back of decelerating investments largely due to the twin balance-sheet crisis. But, during the last quarter of the previous year, when demonetisation was effected, virtually every sector of the economy decelerated except agriculture and public administration—the latter actually grew at 1.7%. The deceleration in agricultural incomes is stated to be due mainly to animal husbandry. Perhaps, we

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have been scoring self-goals by putting curbs on the buffalo meat industry. The sharp deceleration in the manufacturing-sector growth during the last quarter has been ascribed to wholesale price index moving from the negative to positive territory and destocking by businesses due to GST. This, however, cannot entirely explain the sharp reduction in the growth rate, to just 1.2% from 5.3% in the last quarter. Even this is an underestimate as the estimates are based on the formal sector data, and the effect of demonetisation will be clearer only when the revised estimates come in when the informal sector's impact is captured better.

The only thing that can be said at present is that there has been substantial disruption on account of demonetisation. Indeed, the government continues to claim that it has scored a goal without admitting that it is a self-goal. After all, it is the player, judge and the jury and neither the ruling party nor the opposition, but the people are the sufferers in these games.

