

Lessons from demonetisation, according to Manmohan Singh

The 8 November 2016 decision by the Prime Minister to extinguish nearly nine-tenths of the value of currency in circulation and render Rs500 and Rs1,000 banknotes worthless overnight was a misguided act of coercion that shocked and had an impact on every single Indian. It was an ill-conceived economic policy decision. Even if one were to take the purported economic motives of eradication of black money or enabling a digital economy at face value, arbitrary demonetisation was not the means to achieve those objectives. Contrary to belief, demonetisation was not a case of a “good idea, bad execution”. It was a fundamentally flawed idea. One year later, it is well established that the reckless decision caused enormous damage. Not just economic but social, institutional and reputational damage.

The economic impact of demonetisation is quite evident in the slowing of GDP growth and deterioration of other economic indicators. The precise quantum of the negative impact of demonetisation on economic output is both inestimable and unimportant. What is important is that the current economic slowdown triggered by a liquidity shock due to demonetisation was needless and entirely self-inflicted. Such a shock may be temporary in nature but can have a lasting damage on the weaker sections of our society and industry. A liquidity crisis often turns into a solvency crisis for the weak, as is borne out in data and stories from poorer households and small businesses that are struggling to recover from the damage to their livelihoods caused by demonetisation.

It is said that money is an idea that inspires confidence. Similarly, a sudden withdrawal of money can dent confidence. Numerous surveys have shown that business confidence has plummeted. Stability and certainty are essential ingredients for a well functioning macroeconomy. Demonetisation has dented both. At a time when individual and regional economic inequalities in India are rapidly widening, measures such as demonetisation have only exacerbated such inequalities. Millions of our youth are being left out of economic development with limited access to jobs. Three-quarters of non-agricultural employment is in small and medium enterprises. Sectoral data from the Central Statistics Office has shown that sectors such as construction and small manufacturing have been hit the hardest post demonetisation.

The father of our nation, Mahatma Gandhi, exhorted us to “recall the face of the poorest and the weakest” while contemplating policy decisions. Advice that was evidently not heeded in the decision to demonetise India’s currency. That demonetisation inflicted tremendous suffering on the weaker sections of our society is now indisputable. That the demonetisation idea was whimsical is well established. It is then only appropriate that the Prime Minister now graciously accept this monumental blunder and seek support from all to rebuild our economy for the larger good of the nation and her youth.

It is also quite likely that economic growth measured in GDP numbers will now begin to recover from current lows but the nature of recovery is likely to be unequal and unhealthy. Any headline economic recovery may not adequately capture some of the permanent damage to the informal sector. Unequal and jobless economic growth are the twin challenges confronting our nation today. It is important we do not get distracted from these challenges. In a quest to construct a facade of justification for the demonetisation decision, there is a genuine risk of chasing wrong priorities for our nation. I am afraid that a pretentious pursuit of a ‘less cash economy’ to justify a fundamentally flawed act neither recognizes nor solves these twin economic challenges. It is imperative that we move beyond the rhetoric and politics of demonetisation and come together to find solutions to our challenges of employment and equality. But economic damage of demonetisation aside, I also worry deeply about a creeping culture of erosion of institutions and their credibility.

The India that awoke to freedom in 1947 was a geographical mass of impoverished humanity embarking on an audacious journey of self-governance and nation-building. Seven decades later, we are a proud, cohesive nation rapidly ascending the ladder of global power. This enormous rise of our nation has been built on the edifice of strong institutions, conceived, built and nurtured by our founding fathers and subsequent leaders. Legislative institutions such as the Lok Sabha and the Vidhan Sabhas, judicial institutions such as the high courts and the Supreme Court, the media, educational institutions such as our public universities, institutions of democracy such as the Election Commission, investigative institutions such as the Central Bureau of Investigation, economic institutions such as the Central Statistics Office, the Reserve Bank of India, the Securities and Exchange Board of India, cultural institutions and healthcare institutions have formed the bedrock of India's steep ascent in the global stage.

These institutions frame rules and ensure continuity, regardless of individuals in power. Institutions translate belief systems in a society into a set of procedures and processes that can stand the test of time and people. Independence, credibility and trust of these institutions is of utmost importance to India's sustained growth and development. It is these institutions that ensure the nation is accorded greater importance than individual leaders. Any attack on an institution's independence or credibility is a direct attack on the nation and her citizens. History is replete with lessons of the vitality of institutions for long term development of a society. Eminent economists and historians have documented in great detail, the pivotal role played by institutions that established and upheld justice and freedom, in the remarkable success of Western Europe and North America.

India's demonetisation saga is also a saga of institutions and their entrenched place in our society. The Reserve Bank of India (RBI) is an institution of utmost importance with carefully nourished independence and credibility. The demonetisation decision was an impingement on RBI's institutional authority. It is quite likely that RBI was not given a chance to exercise judgement or opine in the decision to demonetise currency. I am not insinuating complicity but am merely highlighting the importance of institutions to act as checks and balances to executive power. I have the utmost faith and confidence in the governor of RBI and sincerely believe that he will uphold the highest levels of integrity, trust and credibility of the institution in the remainder of his term. Recent incidents, such as the inexplicable delay by the Election Commission in its announcement of election dates for the state of Gujarat, further add to growing concerns about the solidity of the nation's institutions. Institutions such as the Election Commission are the very foundation of our republic with a rich and storied legacy. Any attempts to thwart the freedom of such institutions portend grave dangers for the nation.

The independence and integrity of the media, investigative institutions, educational institutions and cultural institutions are all being tested and subject to intense pressure. India today is experiencing a clash of the might of executive power against the resilience of its hallowed institutions. The leaders of India's pantheon of stellar institutions shoulder an enormous responsibility to defend their institutions with all their might for the sake of the nation's future. Every political leader is faced with a temptation to override institutional procedures in the garb of speed and efficiency. Leaders with a political majority even have the ability to fulfil those temptations. But succumbing to such temptations will be a betrayal of the sacrifices made by our freedom fighters and founding fathers in establishing the sovereign republic of India.

I sincerely hope demonetisation was just an economic blunder and not a harbinger of institutional erosion. Overriding institutions, circumventing consensus, and haste are what made the demonetisation decision possible. Therein lies the lessons of governance and nation-building. A truly liberal society is one that strives to ensure that not even a single innocent is punished unfairly. The role of institutions is vital in ensuring such order. It is indeed time to move on from demonetisation but not move away from institutions, procedures and processes. Jai Hind!

The author was prime minister of India from 2004 to 2014.

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