No Proof Required: Demonetisation and its contents

Today is the first anniversary of an unprecedented and bold political and economic experiment — demonetisation (DM). Nobel laureates are cited to suggest that this was an uncalled for, unneeded, and unnecessary experiment — one with magnificent costs and precious little benefits. Most economists, left and right, have argued that DM was a costly and ineffective exercise. Given this convergence, some have declared that there is no debate on the efficacy of DM — an economic version of “Jab miya bibi raazi to kya karega kazi”. Impeccable logic, which can only be proved wrong by empirics.

As far back as November 19, 11 days after D-day, in an article in this paper, ‘Demonetisation — Big Bang or Big Thud’, I argued that increased tax compliance was the most important metric to judge the success or failure of DM. Curiously, but not at all surprisingly, political anchors who want to berate DM will mention everything in their fertile imagination to pronounce DM as demonic, but will not utter a single word about tax compliance. Fake news and flaky analysis was discovered in India considerably earlier than that in the US on D-day 2016.

Let us now talk evidence. The table documents various aspects of the Indian economy pre- and post DM. The post-DM period is April to September 2017; the pre-DM period is the same period last year. Some data (for example, CMIE data on employment) are only available till August, and for such data the comparison is with January-August last year.

As many have noted, the GDP growth slowdown happened well before November 2016. After hitting a high of 10.3 per cent for two consecutive quarters, 2015Q4 and 2016Q1, industrial growth, as measured by GDP accounts, was reduced to nearly half the rate (5.9 per cent) by September 2016. If one looks at the industrial growth and credit growth numbers in the accompanying table, they paint a very sorry, and sad, picture of the economy. Industry, which accounts for nearly 30 per cent of GDP, has been crawling for quite some time now. This crawl has been accelerated, and encouraged, by the RBI/MPC which has allowed real policy rates to rise from 1.1 per cent in December 2016 to 3 per cent in September 2017, and headed higher. Unless you are living in a pre-historic cave (like several members of the political Opposition who are the only ones cheering this inexplicable RBI policy), most people agree that interest rates affect demand, and hence, production. My plea to all those commenting on the growth slowdown caused by DM: Spare a tear for the countless poor and rich who have been made considerably poorer by a high interest rate policy. And note that during the year the MPC has been in operation, CPI inflation has averaged 3.1 per cent.