

# Demonetization: Decoding the Effects of Indian Currency Notes Ban

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## ABSTRACT

As the clock struck 8.15 pm on 8 November,2016,whole India came to standstill and our Prime Minister Narendra Modi announced the most ground breaking news for our Indian economy that seem to be a serious joke for every Indian at first . He announced the of banning Rs 500 and Rs 1000 currency notes and thus began India's struggle with demonetization. A year after the country was wiped out of old currency, the effects of Narendra Modi's demonetization can still be felt in our economy. Demonetization has been one of the most criticized moves by PM Modi and everyone from former Prime Minister Manmohan Singh to former RBI Governor Raghuram Rajan has condemned this move and its effects on the Indian economy. From slowing down the economic growth in various sectors to giving people nightmares of the long queues and the inability to spend liquid cash freely, the hullabaloo created by demonetization is remembered by one and all on its first anniversary. Demonetization began as a way to curb the black money from our economy was later addressed as a means of making India cashless and giving digital India a boost. So in this paper I would be discussing the impact and intensity of demonetisation on our various sectors of economy.

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## INTRODUCTION

With effect from 8th Nov. 2016 Tuesday Midnight PM Narendra Modi Banned the Currency notes of 500 and 1000. It is a strict decision of banning regular 500 and 1000 rupee notes from circulation which is a result of finding 1.25 lakh crore black money.

Within 3 days of that striking decision: - 35000 Crore Rs. Deposited in banks and approximate 1500 Crore Rs Black Money were destroyed.

According to the RBI's (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 pieces. Also, RBI data showed that as of March 2016, 632,926 currency notes were counterfeit—known as an FICN (Fake Indian Currency Note). As a proportion of NIC (Notes in Circulation), the 1,000 rupee and 500 rupee notes were the highest. Nullifying these FICNs was also part of the demonetization move.

Now we talk about the impact of Demonetization on Indian Economy Sector. First economy can be bifurcated in three broad segments Agriculture Sector, Manufacturing Sector and Service sector all these three sectors contributed in Indian GDP.

Agriculture Sector Contribute 17% in GDP  
Manufacturing Sector Contribute 30% in GDP  
Service Sector Contribute 53% in GDP

**After Demonetization all the three sectors faces negative impacts.**

### Objectives of the study:

1. To analyze the impact of Demonetization on different sectors of economy.
2. To analyze the impact of Demonetization on GDP
3. To analyze the future impact of Demonetization on Indian Economy.

## RESEARCH METHODOLOGY

The present study is quantitative in nature and secondary data will be used for the purpose of analysis. The sources of data include the facts released by Reserve Bank of India (RBI), Exchange, Central statistics office India and Different banks websites.

### **Conceptual Framework:**

#### **Reasons behind Demonetization:**

As per my study Following is the main reasons behind Demonetization.

#### **Black Money:-**

A recent study pegged India's black market economy at over Rs 30 lakh crore or about 20 % of total GDP. This is even bigger than the GDP of countries like Thailand and Argentina. So now after this Decision black money holders are left with just two options – either route this money through banks, declaring it to be their income or burn the stashed file.

#### **Fake Currency & Terrorism: -**

—Terrorism is a frightening thing. But have you ever thought about how these terrorists get their money? Enemies from across the border have run their operations using fake currency notes. This has been going on for years. So to stop the funding of these terrorists association the crucial step of demonetisation was taken.

#### **Election:**

We all know how much black money is used by political parties. It will be a very tough task to use trucks of money at least for the upcoming elections until others solutions can be found out by our political parties.

#### **Unorganized Trading:**

- 1.) Prices hike in Real estate sectors is mainly because of the involvement of black money, but after taking this decision the prices of property will surely come down to their real value to a very large extent .
- 2.) Unorganized dealing in share market will also be eliminated after this decision and this will gain positive result as well as more transparency in the economic dealings of the country.
- 3.) Banking system will also get strengthened as banks will be flooded with huge amount of money. This will also result in economic development in our country as the money will be channelized properly through banks.

#### **Cashless Economy:**

It is not possible to make India a 100% Cash-Less economy, but for the development and making transparency in the economy we will have to switch to Cashless economy. So for making people familiar with E-Payment and use of plastic currency , the move of demonetisation was made.

#### **Impact on different segments of economy:**

There is short-term and long-term impact of Demonetization on different sectors of economy.

**Agriculture:** The sector typically sees high cash transactions and therefore near-term impact could be seen till liquidity is infused in the rural areas.

As farmers face a temporary shortage of cash in hand, it could lead to a delay in payment which in turn would hurt the related companies in the short term. As liquidity eases and cashless transactions gain acceptance, the fundamentals would be driven by the longer term drivers of normal monsoons and positive traction in acreage.

#### **Manufacture:**

**Automobile- Two Wheelers:** Clampdown on cash transactions and temporary cash crunch could hurt purchases particularly in the economy segment of the two wheeler space where the percentage of cash transactions have been high. However, as companies learn to work around it, demand may pick up by overall growth in consumption on the rural as well as the urban side.

The seasonal slowdown seen during November and December months could get more pronounced as consumers delay purchases due to temporary liquidity crunch and expectations of rate cuts. However, as most passenger vehicles are financed through loans, the blip would be temporary and demand may recover on the back of growth in demand in rural and urban areas as well as trickle down benefit of the 7th Pay Commission Payouts. **Commercial Vehicles:** Slackness in the economy on account of demonetization could have a negative impact on the commercial vehicle volumes which have been under pressure in recent times. However, this slowdown may be short lived and demand may pick up, led by pre-buying in response to the changes in emission norms as well as a pickup in overall economic activity.

**Consumption-related** sectors like consumer durables, FMCG, etc: The outlook is near-term negative as cash sales account for a significant chunk of sales for companies in these sectors. As customers and companies migrate to the

cashless platforms, demand should come back making demonetization near term neutral. In the long term, demand may shift from the unorganized players to the organized players.

#### **GDP:**

According to the government's latest growth estimates, the pace of growth will be impacted by slowing growth in the manufacturing and mining sectors and also construction activity. This estimate is in line with the forecast of India's central bank, Reserve Bank of India, which in its last monetary policy had forecast GDP growth to be at 7.1 percent for the twelve months ending March. But this latest estimate does not consider the impact demonetization on the economy, "in the absence of sufficient information." While releasing the data, Chief Statistician T C A Anant said the figures for November were available and examined but "it was felt in view of the policy of demonetization of notes there is a high degree of volatility in these figures and conscious decision was taken not make projection using the November figure".

This latest government estimate has been released almost a month before the standard release date of February 7. According to the data released Friday January 6th: "the Gross Value Added (GVA) at basic prices for 2016-17 from the mining and quarrying sector is estimated to decline by 1.8 percent, as compared to growth of 7.4 percent in 2015-16," a statement from the Central Statistics Office of the government said Friday evening. The GVA at basic prices for 2016-17 from the manufacturing sector is estimated to grow by 7.4 percent, compared to growth of 9.3 percent in 2015-16, the data showed. The private corporate sector has a share of around 72 percent in the manufacturing sector.

#### **Facts and Findings:**

**Impact of Demonetization on Agriculture Sector:-** Agricultural growth in India contracted 0.2% in 2014-15 and grew no more than 1.2% in 2015-16, largely because of back-to-back droughts. It was expected to grow at 4% in this year as per CRISIL Report, but due to Demonetization this forecast is proven wrong because Farmers are running out of Cash to buy Seeds, Fertilizer, Equipments, and Wages payment to workers and Commission to Agents etc. Because of Cash shortage daily supply transport system has also suffered which was result in 25 to 50 % reduction in sales. Following is the main reasons;

I. Farmers are not educated and aware about how to work on E-Payment System, Recent study by RBI Says 78% of the population do not use internet in which almost 80 to 85 % are Farmers.

II. In most of the Villages Proper Banking system is not Developed yet and Villagers are need to go to the cities for the same because of that Farmer's most of the time is engaged in exchanging the old notes in Banks.

**Impact of Demonetization on Business sector:-** As per the study IPP says Growth in Business sector 0.7% in October 2016 but after 8th Nov.2016 Demonetization shows a different picture because of this decision labour turnover is also increased as lack of Production because of law demand of products people were purchase only if it necessarily required, for this I have studied on following business sector

I. Textile industry :-Most of the Brands and Retailers Report 40 to 60 % drop in sales after Demonetization in first few weeks but from December onwards this drop is slightly decrease, but still we can say the impact of this decision has affect the industry in 2017 also for at least 3 to 4 months.

II. Real Estate :

Demonetization smashed the real estate market and it will result in 50% drop down and it will remain for further 5 to 6 months. While the short-term impact is negative, Experts hoping that rate cuts in the coming months would boost home sales.

III. FMCG Products(Fast Moving consumer Goods):

Consumer expenditures also affected by that decision now only those products are purchased which was necessary for daily consumption and mostly the small traders like \_kirana store', \_small bodies', \_thela wala' etc. they all have done their daily transactions only in cash and because consumer has less cash in his pockets the daily sells of these traders drop down by 20 to 30 % . It is also a short term impact in future things get normal.

**Impact of Demonetization on Service Sector:** Service sector is hit very hard by Demonetization decision in November 2016.The worst Slump in nearly three year is noted.

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. 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.

On other hand if we talk about Banking Sector this is the only sector which was benefited by that decision in many aspects, this move will pull a large chunk of first time users to banks, who will have to use the system at least once to exchange their old notes for new ones. According to a study conducted by Moody's, people tend to continue using

banking services once they have crossed the 'first-time user' mark. This development will increase bank deposits by 1 to 2 percent compared to what they were before the demonetization schem

### **CONCLUSION**

The present study shows the impact of Demonetization on Indian economy's different sectors. GDP of Country slightly decreases as compare with the previous year but we cannot say it will be same in future also. —This intervention is a one-time draining of this current stock of black money but unless the root causes of corruption are removed, corruption will continue. It is sort of like a dialysis, more of a short term cleaning up than a solution of the problem. It needs to be repeated periodically. So at last I would like to say Demonetization cannot be said to be the perfect step for our economic development, it will take time and final decision can only be made by giving time ,taking important supportive steps for making it effective and then review its progress as well as its ultimate result on India

### **EXPERT REVIEW**

Finance Minister Arun Jaitley: —The goal of this is to clean transactions, to clean money.

Girish Vanvari, partner and head (tax), KPMG in India: —This announcement appears to be the most significant change made by the Modi government to date.

Crisil, a global S&P company: —Its impact could be even bigger than GST (the Goods and Services Tax which is still running the gauntlet of politicians)

Rajesh Chakrabarti, professor and executive vice dean of the Jindal Global Business School at Jindal Global University: Pointing out that only a small percentage (by some estimates as low as less than 6%) of the unaccounted wealth is held in cash.

Pronab Sen, country director of the India Central Programme of the International Growth Centre, a think tank: Demonetization has perhaps —penalized the entire informal sector and damaged it permanently, especially the informal financial sector, which could account for a fourth of bank lending, or 26% of GDP.

Sumeet Soni, Commercial Director, Benetton, says, —The impact is at both ends — production and consumers. In production, as large part of the industry is still unorganized and lot of activities is subcontracted which are getting impacted due to cash crunch. It has also compelled consumers to pull the plug on spending. The way of doing business, largely cash dependent, has impacted the inflow of products.

Shitanshu Jhunjunwala, Director, Turtle, Said:- —The Indian garment business relies on a lot of cash transactions and the demonetization has brought in a conservative spending sentiment, for which there might be a slight dip in the sales over the next one or two quarters. However, the impact should normalize in the long term and this move would be beneficial for the organized retail sector. The impact is felt more by the small traders and the unorganized retailing segment who rely more on cash trading and sales. Some sectors like jewellery and the luxury segment have been impacted more than mid-premium and mass segments and will no doubt take a longer period to revive. However, the use of plastic money and transactions through online payments will continue to increase consumer spend in the retail market.

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