

## IMPACT OF DEMONETIZATION ON INDIAN BANKING SECTOR

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### ABSTRACT:

*Demonetization is the act of stripping a currency unit of its status as legal tender. It is a process of removing a currency from general usage or circulation of money in a country. Demonetization is an act where the old unit of currency gets retired and replaced with a new currency unit. It can also be considered as withdrawal of a specific currency from market. To check undisclosed black money, corruption and fake currency the Government of India on the 8 November 2016 announced demonetization of high denomination currency notes Rs 500 and Rs1000. A new redesigned series of Rs 500 and Rs 2000 banknote is in circulation since 10 November 2016. Banking can be defined as the business activity of accepting and safeguarding money owned by other individuals and entities, and then lending out this money in order to earn a profit.*

*As of December 28, official sources said that the Income Tax department detected over 4,172 crore of un-disclosed income and seized new notes worth 105 crore as part of its country-wide operations. The department carried out a total of 983 search, survey and enquiry operations under the provisions of the Income Tax Act and has issued 5,027 notices to various entities on charges of tax evasion and hawala-like dealings. The department also seized cash and jeweler worth over 549 crore out of which the new currency seized (majority of them 2000 notes) is valued at about 105 crore. The department also referred a total of 477 cases to other agencies like the CBI and the Enforcement Directorate (ED) to probe other financial crimes like money laundering, disproportionate assets and corruption.*

*It is a radical financial step in which a currency unit's status as a legal tender is declared invalid. This move is usually executed when old currencies have to be replaced by new ones or whenever there is a change of national currency. However, given the extent to which the project has to be executed, the move has to be well planned in advance.*

***In this paper I want to discuss the impact of demonetization on Indian banking sector.***

**Keywords:** *Demonetization, Financial Environment, Currency Scarcity and Political Situation Etc.*

### INTRODUCTION:

Banks are core part of any economy. They channelized the money to the smooth functioning of different sectors. Initiatives of Green Banking, made the banks to transform conventional banking services into modern banking services. The products and services are offered through electronic devices with the help of internet. Now a day, bank services are catered at the finger tip of customers. Surgical Strike on Black Money called 'Demonetization' brought enormous changes in all the sectors of the country. Banks are not exceptional from the influence of Demonetization and it made vibrations in the operations as well as products and services of Banks. It created greater demand to digital banking services where cashless transactions are prioritized. Day to day operations of Banks are affected and found tough in Management of liquidity and Employees. It made greater influence on Management of liquidity and its demand raised by customers in exchanging of their banned currency notes while minimizing risk and maximizing quality of service. At the same time meeting the guidance of Reserve Bank of India was challenging. Demonetization has disturbed the bank operations and made the employees to work under unconditional stress in extended working hours of a day. Most of the banks were not able to discharge other banking services while exchanging the banned currency notes. Hence, the present study is made to figure out the influence of demonetization on banking sector. It showcases post demonetization effect on banks and its operations.

## DEMONETIZATION

Demonetization is the act of stripping a currency unit of its status as legal tender. It occurs whenever there is a change of national currency. Sometimes, a country completely replaces the old currency with new currency. The opposite of demonetization is demonetization, in which a form of payment is restored as legal tender.

The currency was demonetized first time in 1946 and second time in 1978. On Nov. 2016 the currency is demonetized third time by the present Modi government. This is the bold step taken by the govt. for the betterment of the economy and country. For example, gold was demonetized in this way when it ceased to be used as an everyday currency. The Indian rupee

(INR) is the official currency of India. The recent sudden move to demonetize Rs 500 and Rs 1,000 currency notes is not new. Rs 1,000 and higher denomination notes were first demonetized in January 1946 and again in 1978. The highest denomination note ever printed by the Reserve Bank of India was the Rs 10,000 note in 1938 and again in 1954. But these notes were demonetized in January 1946 and again in January 1978, according to RBI data.

In 2016, the Indian government decided to demonetize the 500- and 1000- rupee notes, the two biggest denominations in its currency system; these notes accounted for 86% of the country's circulating cash. With little warning, India's Prime Minister Narendra Modi announced to the citizenry on Nov. 8 that those notes were worthless, effective immediately – and they had until the end of the year to deposit or exchange them for newly introduced 2000 rupee and 500 rupee bills.

## ORIGIN OF DEMONETIZATION:

Historically, previous Indian governments had demonetized bank notes. In January 1946, banknotes of 100 and 1,000 rupees were withdrawn and new notes of 100, 500 and 1000 rupees were introduced in 1954. The Janata Party coalition government had again demonetized banknotes of 1,000, 5,000 and 10,000 rupees on 16 January 1978 as a means of curbing counterfeit money and black money.

On 28 October 2016 the total banknotes in circulation in India was 17.77 trillion. In terms of value, the annual report of Reserve Bank of India (RBI) of 31 March 2016 stated that total bank notes in circulation valued to 16.42 trillion of which nearly 86% (around 14.18 trillion) were 500 and 1,000 banknotes. In terms of volume, the report stated that 24% (around 22.03 billion) of the total 90266 million banknotes were in circulation.

The Government of India devised an Income Declaration Scheme (IDS), which opened on 1 June and ended on 30 September 2016. Under the scheme, the black money holders could come clean by declaring the assets, paying the tax and penalty of 45% thereafter.

## REASONS FOR DEMONETIZATION IN INDIA

In a single master stroke, the government has attempted to tackle all three malaises plaguing the economy, a parallel economy, counterfeit currency and terror financing. The main reasons for demonetization are:

1. To tackle black money in the economy.
2. To lower the cash circulation in the country this “is directly related to corruption in our country,
3. To eliminate fake currency and dodgy funds which have been used by terror groups to fund terrorism.

## Review of Literature

- **Nithin and Sharmila (2016)** studied demonetization and its impact on Indian Economy. They opined that demonetization has short term negative impact on different sectors of the economy and such impacts are solved when the new currency notes are widely circulated in the economy. They also argued that the government should clear all the problems created due to demonetization and help the economy to work smoothly.

- **Nikita Gajjar (2016)** deliberated a study on Black Money in India: Present Status and Future Challenges and Demonetization. She described the framework, policy options and strategies that Indian Government should adapt to tackle with this issue and the future challenges to be faced by the Government.
- **Vijay and Shiva (2016)** examined demonetization and its complete financial inclusion. They felt that the rewards of demonetization are much encouraging and the demonetization is in the long-term interest of the country. They expressed that it had given temporary pain but it taught financial lessons. It influenced banking industries to do considerably investment on digitalization of banking services.
- **Manpreet Kaur (2017)** conducted a study on demonetization and impact on Cashless Payment System. He said that the cashless system in the economy has many fruitful benefits less time-consuming, less cost, paper less transaction etc. and he expected that the future transaction system in all the sectors is cashless transaction system.
- **Lokesh Uke (2017)** researched on demonetization and its effects in India. He studied positive and negative impact of demonization in India. The study was based on secondary data available in newspaper, magazines etc. The main purpose of demonetization is to eradicate the black money and diminish the corruption. He expressed that Government of India has become success to some extent. Demonetization had negative impact for a short duration on Indian financial markets. But he said that the real impact will be shown in future.
- **Sweta Singhal (2017)** carried out research on Demonetization and E Banking in India. It was a case study to check the awareness level of people of rural areas in India about e-banking facilities and how much it has increased after demonetization. A sample size of 100 was used with ANNOVA test to show that rural people differ much with urban people in their awareness level as well as usage level of e-banking. It was found that urban male youth have higher awareness and usage of e-banking. She felt that the study shall also helpful for banks to improve their e-banking facilities.

### Objectives of the Study

1. To study the impact of demonetization of currency in Indian banking scenario.
2. To find out positive and negative results of post demonetization on Bank operations.

### Methodology of the Study

The study is based on Secondary Sources of data. It includes available published literatures such as books, journals, newspapers and relevant government websites. The study tries to look at the extent of demonetization influence on normal banking operations.

### Reasons behind Demonetization:

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

- **Black Money:** A recent study had 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.
- **Economy:** The Major impact of this decision is on the economy because it gives highly positive impact on the economic Stability in near future. The coming six to seven months are expected to witness a considerable level of deflation. Sectors like real estate, construction material, Gold, unorganized trade and services will see significant pain in the near time.

- **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 five state elections. Now in upcoming UP election which was held in January neither of the parties can purchase the vote of poor people and Some drastic change in the elections going to be seen by everyone.
- **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. 2.) Unorganized dealing in share market will also be eliminated after this decision and this will gain positive result in the economic condition of the country. 3.) The problem of inflation will get solved with this step as the government will get more money in its pocket in form of taxes and undisclosed income. 4.) Banking system will also get strengthened as banks will be flooded with huge amount of money. This will also result in more economic development in the nation as the money will be channelized properly through banks.
- **Less Cash Economy:** It is not possible to make India Cash-Less economy, but for the development and making transparency in the economy we can say use of less Cash is possible. So for making people familiar with E-Payment and use of plastic currency.

#### **Impact on Different segments of economy (Fact 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, Equipment's, 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.
- **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.
- **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.
- **FMCG Products:** 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 1. Kiranastore , 2. Small bodies , 3. Thelawala 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 heard by Demonetization decision in November 2016 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 scheme.

### **FINDINGS:**

This research was conducted to find the “*Impact of Demonetization of Currency in Indian Banking Scenario*” at the end of this research we can say that Demonetization does have an impact on the banking sector. Through this study we got an Idea about the views of bank employees towards Demonetization. After completing this study we can say that:

- Demonetization helped reduce black money, corruption and terrorism in India because there are equal responses for the two options i.e. somewhat and yes.
- People mind the inconvenience faced through demonetization as maximum number of people have opted for the option yes.
- Demonetization has not at all helped the bank employees.
- There was an impact of demonetization on the workload of Bank Employees. We all know that the workload of the bank employees increased a lot. They had to work overtime.
- The cash flow in banks decreased after demonetization. There was not much currency in circulation after demonetization thus the government had restricted the withdrawal amount.
- Interest rates decreased after demonetization. The interest rates were decreased to increase lending of money.
- Money lending decreased after demonetization thus the interest rates were decreased to increase the money lending.
- The use of online banking increased after demonetization due to decrease in the circulation of currency and long queues outside ATM and bank branches people started using online banking.
- The use of Plastic cards has increased due to less circulation of money in market.
- The number of new accounts has increased because people have to deposit their money in the bank account to have new currency.
- The functioning of ATM has increased because more and more people are using the ATM to withdraw their cash and they are using it number of times to fulfill their cash requirement because of the withdrawal limit.
- The numbers of customers in the branches have increased. We have seen long queues of people outside bank branches and ATM after this announcement.
- 70% of the people believe that there was an impact of demonetization on the banking sector.

### **SUGGESTIONS:**

- ❖ The new 500 and 2000 banknotes should have been printed and kept ready for distribution.
- ❖ Rs 100 banknotes should have been increased in circulation.
- ❖ The new notes should have been of the same weight, thickness and size as the old ones.
- ❖ Permission should have been granted to cooperative banks to accept deposits and to exchange notes.
- ❖ To solve the problem of black money strong administrative and tax reforms should have been implemented.
- ❖ For eliminating fake currency, the government should have announced a time period to exchange the currency (say 3 months).
- ❖ Promote the use of cashless transactions.

## CONCLUSION

At the end of this research, we can conclude that Demonetization has helped reduce black money, bribery and terrorism in India. People have faced inconvenience because of demonetization and they are not happy with it. It has not helped the bank employees as their workload has also increased because of it. The cash flow in bank has decreased followed by the decrease in Interest Rate and money lending. Demonetization has led to the increase in the use of plastic cards, online Banking, opening of new accounts, number of customers in the branches and the use of ATM.

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