

DEMONETIZATION IN INDIA: PRE AND POST EFFECT ON INDIAN INDUSTRY

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ABSTRACT: The present government took an enormous step to terminate Rs 500 and Rs 1000 notes with prompt effect on 8th November 2016. Proceed was aimed to control the fake currency circulation, black money and terror financing movements in the country. India has the highest level of currency in circulation at nearly 13% of GDP. The act of demonetization is expected to have a marked impact on various sectors. The sectors which are based on cash transactions will witness more disturbances. Therefore an attempt has been made to analyse the impact of demonetization on various prominent sectors of Indian economy that are automobile, pharmaceutical, agriculture and consumer market sector etc. Also compare performance of the sectors for pre and post period of demonetization.

KEY WORDS: Demonetization, Fake Currency, liquidity crunch.



INTRODUCTION:

India is a cash based economy, hence the circulation of fake notes is likely to cause harm to the society. Fake notes are used for various inflammatory activities such as spying, smuggling of arms, drugs and other illegal traffic in India. The high denomination notes contribute 86% to the total supply of money in the economy. The value of these notes is more than 13% of GDP in 2016, which is much more than in any other developing country like Brazil and China. As per the reports number of fake notes in the banking system in 2006 was 1.24 lakh and it went to 6.33 lakh in 2016 and also the share of high value notes increased from 10.4% to 64% from 2006 to 2016. To track the same issue of fake currency notes and to invalidate black money, the government of India announced that Rs 500 and Rs 1000 notes will be no longer legal tender from midnight, November 8 2016.

This is not a new step in the history to demonetise the currency. In 1946 first time the currency of Rs 1000, Rs 5000 and Rs 10,000 was demonetised and phase out these notes. In 1938 RBI printed the highest value notes of Rs 10,000 which was demonetised in 1946. Rs 1000, Rs 5000, Rs 10,000 were in circulation in 1946 which was reintroduced in 1954 and further all these notes were demonetised in January 1978. Rs 1000 note was again introduced in November 2000. Rs 500 were circulated in 1987 as an attempt to control the volume of bank notes due to inflation. Hence Rs 2000 note was introduced for the first time. In 1967 the bank notes with Ashoka pillar watermark were introduced. In October 1987 the notes were imprinted with the portrait of Mahatma Gandhi. The Rs 50, Rs 100 banknotes were issued in August 2005, followed by Rs 500 and Rs 1000 in October 2005, which continued till November 2016.

The liquidity crisis and clampdown on black money on account of demonetization headway is expected to impact the sectors that are based on cash transactions to a great extent.

REVIEW OF LITERATURE:

Dr. Manmohan Singh(2016): confronted that this step of present government to demonetise the currency will create disorder in lives of millions of poor people as cash is the base of their livelihood.

Charon Singh(2016), RBI chair professor said that this step will result in positive and negative impacts on the society. He concluded that this will also bring up India's rank as it reflects that our country is against corruption and wants to eradicate it. Moreover the output in agriculture and many more industries was reduced due to scarcity of cash.

Patil(2016): Due to demonetization the credit cost dropped quickly which led to increase in raising money for investment purpose. As Rs 500 and Rs1000 notes were declared invalid people were forced to deposit their currency in banks to get it changed with new currency notes. Thus they were able to raise loan to be used for investment in business.

Kumar(2016): Demonetization is an act of declaring currency as not valid wherein old notes are withdrawn and replaced by new currency notes. The act of demonetization is not new in the history as it is being adopted by various countries. Ghanna demonetised its 50 cedi currency notes to check corruption. Myanmar demonetised 80% of its currency to track black money.

RESEARCH METHODOLOGY

Research is a process of systematically obtaining accurate answers to significant and pertinent questions by the use of scientific method of gathering and interpreting information. This study is based on the secondary data i.e. financial information and data about the impact of demonetization taken from the news papers, magazines etc. The study is focus on determining the impact of demonetization on the industrial growth of the country and analyse the change in trend of progress of the Indian industries after and before the demonetization of currency note in 2016. To achieve the set objectives of the study the analytical technique is applied with the view to observe the impact of demonetization on the different Industries of India i.e Automobile, Pharmaceutical, Agriculture etc. Similarly the Objectives of the Study are

1. To study the growth of different industries during the post and pre demonetization era.
2. To determine the future aspects of demonetization with regard to the economic growth of the country.

ANALYSIS OF STUDY

Various sectors are being analysed in this study in detail to observe pre and post effects of demonetization.

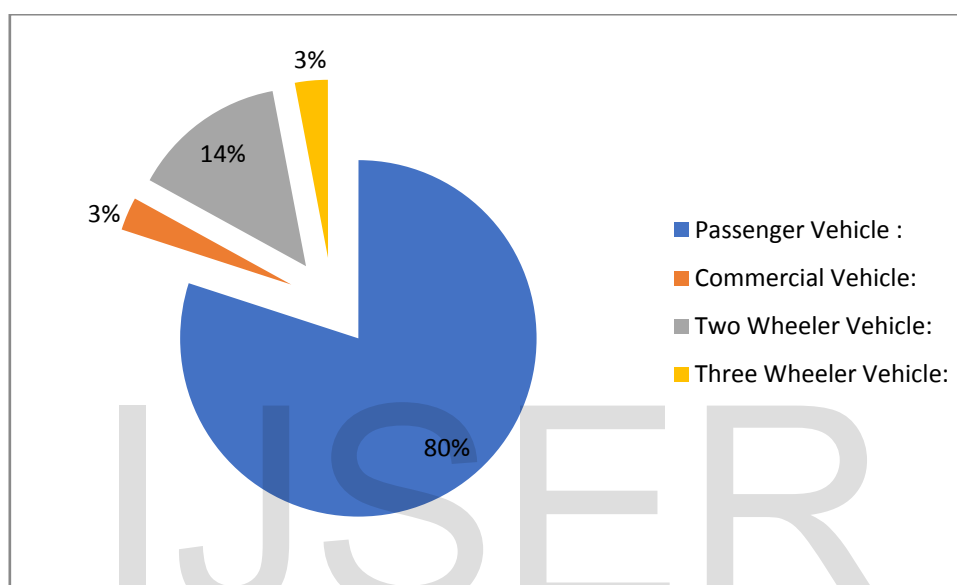
AUTOMOBILE INDUSTRY

Indian automobile Industry stands as one of the booming industry in the world with annual production of 23.37 million vehicles in 2014-15 touching the growth of 8.68% since last year. Indian automotive aftermarket stood around US\$ 7 billion by 2021 with the growth rate of 10-15%. The industry was able to allure FDI worth US\$ 15.79 billion during April 2006 – September 2016. (Source: Department of industrial policy & promotion)

Pre Demonetization: The industry accounts for 7.1% of country's GDP. The total production of the industry is 23960940 vehicles (including passenger vehicles, commercial vehicles,

three wheelers & two wheelers) during April – March 2015 the number stood to 23,358,047, which recorded a growth of 2.58%. As per the graph shown below two wheelers segment with 80% market share is the leader in the domestic market, the reason behind the growth is due to growing middle class and young population in India. The growing interest of companies to hunt the rural market also promoted the growth of the sector. Passenger vehicle segment with 14% market share is follower of two wheeler segment and others are commercial vehicle and three wheeler market shares of 3% each.

Domestic Market Share for 2015-2016



Source: <http://www.siamindia.com/statistics.aspx>

Similarly passenger vehicles, commercial vehicles, three-wheeler and two-wheeler showed a growth of 6.89%, 13.77%, 18.69% and 16.60% respectively during 2010 to 2015. Two wheelers made a remarkable share of export at 69.4% in 2015, followed by 16.7% for passenger vehicles and three-wheeler accounted for 11.1% exports in 2015. Luxury cars market is expected to reach 150000 units by 2020. Various steps are being initiated by the Indian government and automobile companies to make India a leader in the market by 2020.

Post demonetization: Certain precautionary steps are required to bear the heat of capricious event of demonetization; the downfall is clearly portrayed in the detailed figures below in the table. Till October 2016 the automobile sales were in growing percentage at the rate of 4.5%, but sales started to decline after the announcement was made by Prime Minister Narendra Modi, despite aggressive sales push to thrash the year end indolence. The domestic sales declined by 5.5% and maximum decline was observed in case of three wheelers which dropped by 25.9%.

Domestic volume growth trends across segments in December 2016

Segment wise sales	Dec-15	Dec-16	Change (%)
Passenger vehicles	230959	227824	1.40%
Commercial vehicles	56840	53966	5.10%
Two wheelers	1167621	910235	22.00%
Three wheelers	46894	29904	36.20%

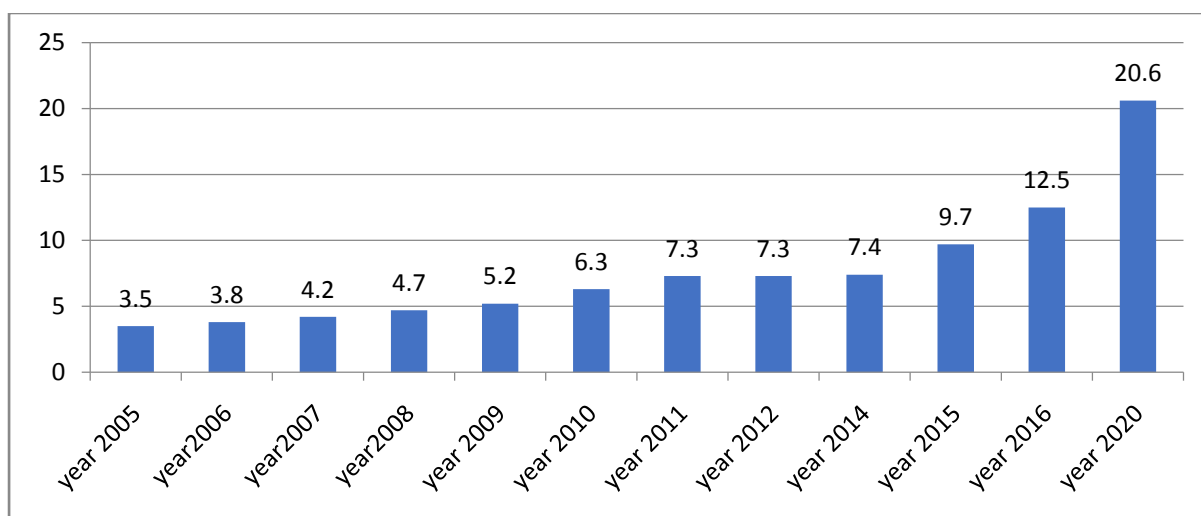
The above table clearly shows the overall decline in sales of all the segments of the industry due to demonetization as compared to previous year 2015. The sales of passenger vehicle went down by 1.4%. Two wheeler volumes declined sharply during December 2016, a second consecutive month of decline. With consecutive 10 months of increased sales December 2016 observed the maximum downfall. The sharpest downfall was seen in scooters lowering by 26.4% followed by motorcycles that slumped by 22.5% even as mopeds continued to return upbeat volume growth. Domestic sales of commercial vehicle went down by 5.1% during December. The sales of trucks and buses observed positive sales. The export market in the automobile reduced 35% in 2016. In the coming months ICRA expects the growth of 3 wheelers industry around 0-2% in 2017. From low priced two wheelers to the luxury cars the whole line has been affected. Though discomfort is caused but it will be a dominant spring in cashless economy and will bring transparency into the system.

CONSUMER MARKETS

Indian consumer segment includes market for the consumer durables and fast moving consumer goods. This sector is composed of huge middle class, relatively large wealthy class and small economically low class, for which it is foreseen to double the spending class by 2025. As per the reports India's share of worldwide consumption is anticipated to increase twice at the rate of 5.8% by 2020.

Pre-demonetization: India scored second position in global consumer confidence index with the score of 128 points till June 2016, and Philippines scored 132 points. The Indian consumer market showed a positive growth at annual rate of 5.7% from 2005-2015, and it's expected to grow at 6.7% for the year 2015-2020 and 7.1% for the year 2021-2020. Whereas FMCG sector is growing on an average of 11% for last 10 years, and is expected to increase at 14.7% and reach US\$ 110.4 billion from 2012 to 2020. The rural market share is increasing at the rate of 17.7% and has reached US\$ 100 billion. Food products is leading with the share of 43% of overall market share followed by personal care 22% and fabric care 12%.

Size of consumer durables market (US\$ billions)



Source: Electronic industries association of India

The above graph depicts the growing sales of consumer durables from 7.3 US \$ billion in year 2012 to 12.5 US \$ billion in 2016. The expectations are to touch 20.6 US \$ billion in 2020.

Post Demonetization: Due to the act of demonetization of the high currency notes overall sales went down by 20-25% for November and 10-12 % for December. Rural growth was expected to revive backed by a good monsoon season, consumers actually landed up curtailing their purchases due to reduction in currency notes in circulation after demonetization, with consequent adverse impact on business revenues. FMCG and consumer durables saw significant decline in sales and its impact can be studied under three sectors consumers, channels and trade partners.

Consumers: As the cash in hand was impacted this further lowered the purchasing power of consumer. Therefore the sales of FMCG were reduced and impulse buying was also restricted. 70-80% decline was seen in consumer durables in up-country markets and 40% in larger cities. The positive impact was that 1.2 cr. Indians registered for digital wallets during Nov 2016.

Channels: Nearly 62% traditional retailers suffered severely with the impact of demonetization because less than 1% of these retailers had the infrastructure for electronic payments. But modern retailers with the facility of electronic payment witnessed increase in sales by 21% as compared to previous year.

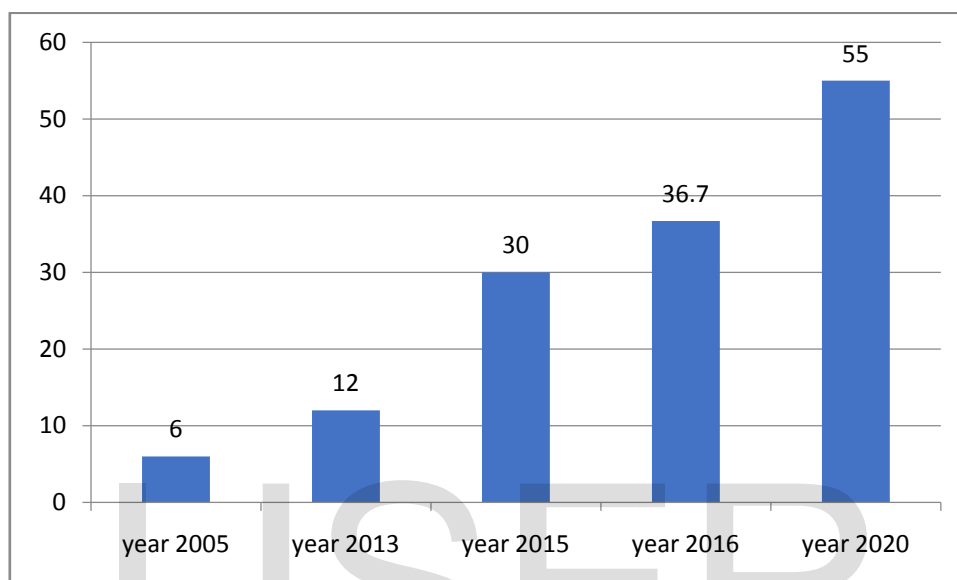
Trade partners: Distributors had to extend credit to the retailers as they had surplus stock inventory. As this market is based on cash and carry the sales went down as compared to previous year due to scarcity of cash.

To reduce the impact and boost the sales various companies have introduced incentive schemes also the companies are considering production cuts for a shorter time till the economy is back to normal.

PHARMACEUTICAL SECTOR

Indian pharmaceuticals market is the third largest in size and thirteenth largest in terms of its financial worth (as per the report by equity master). India's share for generic drugs in global markets is 20% in terms of volume. Recently fortification has become an important characteristic of Indian pharmaceutical market as industry is highly disintegrated. India has a remarkable position worldwide in pharmaceutical sector.

Revenue of Indian pharmaceutical sector (US\$ billion)



Source: Department of pharmaceutical, PWC, McKinsey, TechSci Research.

Pre-Demonetization: The Indian scientists and engineers have the promising potential to direct the pharmaceutical industry to higher level. The industry is anticipated to grow over 15% per year 2015-2020 and will outplay the global market with growing rate of 5%. The market is expected to reach US\$ 55 billion by 2020 and will be declared sixth largest pharmaceutical industry globally.

Indian exports exceeds than China's exports with growth of 11.44% to US\$ 12.91 billion in 2015-2016(data from ministry of commerce and industry) and are growing at a rate between 8-10% in 2016-2107. Imports of pharmaceuticals reached US\$ 1641.15 million in 2016-2017. The USFDA (US food and drug administration) has given 201 endorsements in 2015-16 compared to 109 in 2014-15. The country fix upon for around 30% volume and 10% value in US\$ 70-80 billion in US generic market.

Post-Demonetization: With the act of demonetization, the pharmaceutical sector sales slumped down by 8-10% in November 2016 and maximum effect was seen on sales for acute diseases because of lower patient turnout. The sales of continuing diseases increased in first 2 weeks as patients equipped medicines by using old notes at pharmacies, as it was allowed by government to buy medicines using old notes for specific days. The sales at the level of wholesaler and stockist went slow therefore the companies had to extend its credit period. The advanced buying of medicines for chronic diseases made the sales drop in month of December-March. The impact of subdued sales was observed in few next months. The slump

is observed to be temporary and the impact will not be seen in long run as the demand for medicines is inelastic. The 78% of stockists reported the decreased sales in November due to demonetization. All the remedial treatment felt the heat, however chronic is somewhat better than acute. As cash flow is going to be dwindled all transactions will be done through bank and online, proper invoicing will be done at all steps. No one can earn more profits as it has to be shown in ITR. It will increase legal billing which will result in more facilities in banking transaction; therefore government will be able to frame better regulations over the market. At the same time prices of expensive medicines will fall down and benefit the public. So there are benefits associated with demonetization of Indian pharmaceutical sector. The loss faced will not prolong and system will get smoother in long-run.

AGRICULTURE SECTOR

Agriculture plays an important role in the Indian economy. 58% of rural people depend on agriculture as a source of income. Agriculture sector also includes fishery and forestry which altogether has maximum contribution to India's GDP. As per the estimates of CSO (central statistics office) agriculture and its allied sectors has 17% of gross value added during 2016-2017.

Pre-Demonetization: India is the largest producer, consumer and exporter of spices. India is the second largest fruit producer in the world. India's horticultural output is 287.3 million approximately in 2016-2017. India grabs third position in farm and agriculture products. Agricultural exports accounts for 10% of country's exports and is fourth largest in the world. The Agro industry in India includes various sub segments mainly as canned, dairy, processed, frozen food to fisheries, meat, poultry and food grains. The agriculture GDP is to grow at 4.1% to reach US\$ 1640 billion as per CSO. Indian agrochemicals industry is expected to grow at 7.5% and reach US\$ 63 billion by 2020. Its demand in Indian markets is growing at 6.5% per annum and worldwide demand at 9% per annum.

Post-Demonetization: Demonetization has severely hit this sector which employs 93% of India's workers. Indian farmers use cash for buying seeds and fertilisers. This sector employs labour on daily wage basis, paid in cash. Cash is used by them for buying daily utility items and grocery. Around 80% of farmers suffered as India holds 25 crores account for rural and semi urban people which needs cash for daily transactions but they received only Rs 8000 crore from November 2016, which is negligible to meet the expense as it only claims Rs 350 per account. In such a clamp Indian agriculture sector may go 10 years behind from where it stands now. The cash crunch also led to less sowing areas. The sown area under Rabi crop that is 554.91 lakh in December 2016 compared to 523.40 lakh Hectare in 2015 but there will be 12% less sowing as farmers feel the deficit of cash to buy seeds and fertilisers. The act of demonetization severely impacted the pulses, onion and wheat as it showed increase in prices. Fishery and Jiggery business are totally money based and involves cash transactions felt the heat of demonetization. Moreover, dairy, textile and handicrafts will be severely affected because of reduced supply and increased prices. The slowdown in this sector is going to affect the whole country's economy, as it is the main contributor to the country's GDP.

FINDINGS

The big bang initiative taken by government was necessitated to tackle the issue of counterfeit Indian bank notes, effectively nullify black money boarded in cash & curb terrorism with fake notes. The sudden announcement created a crash crunch in the economy where in every sector was effected. The impact of the measures brought a disruption and ambiguity in short term and will show positive implication in long run. Impact of demonetization was analyzed on four sectors in this study which brought out following findings:

- Demonetization completely stalled the market for a couple of weeks .which led to increase inventory, production cuts & plants shutdown
- The consumer sector has grown at an annual rate of 5.7% from 2005 to 2015 but due to cash crunch in the consumer pockets they were forced to cut down their spending and purchase in small amounts.
- The disruption for a short term was a difficult phase .But in long run proper invoicing for each purchase will be a great achievement for economy in tracking the black money
- Demonetization has severely hit agriculture sector which includes farmers & daily wage laborers. As it employs 93% of Indian work force which use cash transactions for buying seeds fertilizers for trading products & commodities and because of scarcity of funds farmers had to face major problems which also led to less sown area.
- Demonetization did not have any major impact on Indian pharmacy market and demand for the medicines was inelastic. However, luxury hospitals saw some impact on the OPD patients.
- Demand was likely to dip for a couple of months for two wheelers where purchases were made via financing, while rests were through banked cash. No cash deals were processed during this period. But expected to revive in few months from now.
- Lack of liquidity would result in pain to primary producer who don't have much money, so that they can hold their produce for longer time and on the other hand due to lack of cash they were offered less by the buyer.

CONCLUSION

As the demonetization initiative encourages the use of plastic and electronic money, cash transactions will become less common. The transition to a cashless economy will also improve savings in financial assets which will benefit the banks and the Government. The move was also initiated to curb or eliminate the black money which impacted various sectors of the economy. There are short term implications for cash intensive sectors like consumer market and agriculture sector. In the agriculture sector, farmers faced shortage of cash in hand which led to delay in payment and affected the related companies for a short term. As cash sales account for significant amount of sales in consumer market where it was observed the customers started small purchases and negligible impulse buying. As customers and companies are shifting to cashless platform, demand will come back from unorganized players to organized ones. The automobile sector saw a short term impact where the purchases were delayed due to scarcity of funds, but was neutral for purchases through financing or banked cash. Negligible impact was seen on pharmaceutical sector as demand for the medicines is inelastic. However, in medium term, benefits through higher Government spending, better transmission, greater financial inclusion and movement of household savings from physical to financial would lead to potential growth of economy. It would also help to reduce poverty and corruption in the country.

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