



## IMPACT OF DEMONETIZATION ON BANKING SECTOR

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### ABSTRACT:

*Demonetization is a tool to battle Inflation, Black Money, Corruption and Crime, discourage a cash dependent economy and help trade. Its policy of the government by banning Rs. 500 and Rs.1000 currency notes has influenced all almost all the corners of the economy. Its effect on Banking Sector is significant as Bank is a center for channeling the legal tender money to all needs of the society. The biggest beneficiaries of demonetization are Banks. It made the banks to accept the deposits without any cost of promotion and drastically increased liquidity position of the banks. Opinion of many Banks' higher officials has been included to understand whether this move yields positive responses and its impact on economic growth. The present study is made out of available literature on post demonetization. It portrayed the effect of demonetization on Banking Sector. It encompassed the recent decision of the central government on Demonetization and its gradual effect on Indian banking sector. 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 operation.*



**KEYWORDS:** Demonetization, Banks, Liquidity, digitization, Economic Growth.

### INTRODUCTION :

Demonetization is a process by which a series of currency will not be legal tender. Then the series of Currency will not acceptable as a valid currency. The announcement done by our Prime Minister Sri Narendra Damodardas Modi on 8th November 2016 regarding the demonetization of Rs. 500 & Rs. 1000 notes is a bold decision relating to economic policy of the nation. The basic reason behind the decision is curbing all black money in India. 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. Nowadays, 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.

#### GOVERNMENT POINT OF VIEW:

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

#### OPINION OF FEW EXPERTS FROM BANKING AND OTHER SECTORS ON DEMONITIZATION:

Almost all the stalwarts of the banking sector including Deepak Parekh, Chanda Kocchar think that the move will help curb black money in the economy.

1. **Chidambaram**, Former Union finance minister "It will take at least 2 years for the economy to recover from the ill-conceived decision of the Prime Minister, —The decision with horrendous consequences is likely to limit the GDP growth rate to 6% to 6.5% during 2017-18 and 2018-19,|| he estimated."
2. According to **Chanda Kocchar**, MD & CEO, ICICI Bank,"this move will definitely bring about a whole amount of transition to no cash or low cash kind of transactions."
3. **Harish Salve**, one of the leading lawyers in taxation laws "A parallel black economy will collapse."
4. **Deepak Parekh**, HDFC Chairman anticipated that the Land will become cheaper and "one expects that retail prices will come down in medium term."

Prior to announcement by Prime Minister Narendra Modi that high denomination notes would stop being legal tender from 9th November, 2016, there were two similar instances in India. The first instance was in 1946 and the second in 1978 when an ordinance was promulgated to phase out notes with denomination of Rs 1,000, Rs 5,000 and Rs 10,000. The government's move to demonetize, even then, was to tackle the issue of black money economy, which was quite substantial at that point of time.

In January 1978, the Indian government demonetized Rs 1,000, Rs 5,000 and Rs 10,000 notes which was quite substantial at that point of time. The move was enacted under the High Denomination Bank Note (Demonetization) Act, 1978. Under the law all high denomination bank notes ceased to be legal tender after January 16, 1978. People who possessed these notes were given till January 24 the same year — a week's time — to exchange any high denomination bank notes. The main difference between then and now is that currency of higher denomination was barely in circulation, unlike the Rs 500 and Rs 1000 note today.

#### DEMONETIZATION AFFECT ON BANKS IN TODAY'S INDIA:

The negative impacts are because of regulation, costs of demonetisation, loss of opportunity and short-term damage to economy.

1. The 100% cash reserve requirement (CRR) on incremental deposits meant that banks did not earn any interest on Rs 3 lakhs crores of deposits for nearly a fortnight.
2. The waiver of ATM charges would result in banks losing Rs 20 in every transaction.
3. The waiver of merchant discount rate on cards would result in banks losing 1% in every card transaction.

4. Banks use third parties like cash logistics companies for cash transportation. Moving out Rs 15 lakh crore of currency notes and moving in Rs 7 lakh crore plus from currency chests would have cost several thousand crores of expenditure.
5. As banks have been focused on exchanging currency notes, they have not been able to sell any loan products.
6. Some SME businesses have seen their sales drop 50–80% and could default in their instalments. They won't immediately be classified as NPAs because of some relaxations, but if the delay persists bank NPAs might worsen.
7. Uncertainty has resulted in drop in spending on high value items from credit cards. These are the transactions which are converted into EMIs and banks earn from them.

### THE POSITIVE IMPACT ON TOP TEN BANKS:

State Bank of India and HDFC Bank were the most successful in attracting and retaining deposits in the wake of demonetization of currency, according to an analysis of their deposits growth so far this financial year. The highest growth was reported by State Bank of India, which added a massive Rs 3.15 lakh crore of deposits as of Dec 31 when compared to Apr 1, the first day of the financial year. The growth in deposits at SBI was a massive 19.3% in the nine months. As of December 31, the total deposits at the bank had risen to 19.52 lakh crore, which was about 26% of the total money held by all public sector banks in India at the time. The number does not include the share of associates such as State Bank of Travancore, which are in the process of being merged with SBI. The second biggest beneficiary of demonetization was HDFC Bank, which saw its deposits jump 16.6% as of Dec 31, when compared with the corresponding number of April 1. Against the Rs 3.15 lakh crore added by SBI, HDFC Bank added a more modest Rs 89,402 crore. Its total deposits at the end of 2016 stood at Rs 6.29 lakh crore, or about a third of SBI's. HDFC Bank too accounted for 26% of the total deposits in all private sector banks in India at the time.

### DEMONETIZATION- KEY DEVELOPMENTS :

- New currency notes
- Limits on ATM cash withdrawals to cease 1st February onwards
- No cash withdrawal limits from March 13: RBI
- IT Dept expands list of transactions under scanner
- Benami property holders under scanner

Demonetization has brought plethora of challenges in additions to the challenges which are already facing by Banks. The influences were short-term and long-term views. In short-term, it disrupted the banks and stressed strongly to carry out bank operations and in long run it helped the banks to pool the deposits without incurring of any cost. Here are four influences of demonetization on Banks.

**1. Increase in Deposits:** demonetization has increased the deposits in Banks. Unaccounted money in the form of Rs.500 and Rs.1000 were flowing to the Banks and the sizes of deposits have been increased. It helped the banks to grab the deposits and increase their deposits.

**2. Fall in cost of Funds:** Over the past few months, the deposits are increased. It led the banks to keep a major part of deposits in the form of cash deposits. PSU Banks have a lion share (over 70%) of the deposits and biggest gainers of the rise in deposits, leading to lower cost of funds.

**3. Demand for Government Bonds:** After sharp rise in deposits on post demonetization, banks started lending such surplus deposits to the RBI under the reverse repo options. PSU Banks, particularly, deployed excess funds in government bonds. The return on bond investment is likely to add 15 to 20 per cent increase in the earnings of banks.

4. **Sagginess in Lending:** lending growth of the banks is considerably less even after demonetization and its impact of growth in the amount of public deposit. Banks have tried to lend the money to the needy group by reducing their interest rates, but it shrunk over the last few months.

### CONCLUSION:

Demonetization is a tool used by central government to fight against corruption and black money. In the same path, it influenced and brought changes in all the corner of the economy. Banks are major institutions affected by demonetization. Banned denominations were ploughed back and allowed the citizens to exchange with the banks. While exchanging, it disturbed temporarily and influenced its regular operations. Though it affected badly to major extent of bank operations, it helped the economy to find growth and development of the country through financial institutions like Banks. Demonetisation would be positive for sectors like banking and infrastructure in the medium to long term and could be negative for sectors like consumer durables, luxury items, jewellery, real estate and allied sectors, in the near to medium term. It can also lead to improved tax compliance, fiscal balance, lower inflation, lower corruption, complete elimination of fake currency, a step for sustained economic growth in the longer term. As people are not very much versatile with digital operations, they may face various operational risks like cyber fraud. Thus, demonetization is not an unmixed blessing but merits are more than demerits and the economy will move forward with less cash holdings by banks.

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