Impact of Demonetization on Retail Sector

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Abstract: Demonetization refers to withdrawal of a particular form of currency from circulation. Demonetization is necessary whenever there is a change of national currency. The old unit of currency must be removed and substituted with a new currency unit. 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. In this paper we discuss the impact of demonetization on the Indian retail sector.

Keywords: Demonetization, Black Money, retail sector, retailers

I. INTRODUCTION

Demonetization is an economic term which is used to mean the ‘scrapping’ of old currency notes and stripping them off their status of legal tender, usually when a new currency note or currency is being introduced in the economy of the country. This is a standard practice followed by all major economies of the world for different reasons. For instance, when the ‘Euro’ was introduced as the common currency of the European Union, the participating countries had effectively followed a ‘demonetization’ drive of their respective currencies by fixing exchange rates for the old currency to the newly introduced Euro. Indian Rupee has been demonetized various times as well. The Rs. 10,000 notes were demonetized once in January 1946 and then again in January 1978. Recently, the Rs. 500 and Rs. 1000 notes were demonetized in a surprise move on November 8, 2016. The recent scrapping of Indian 500 and 1000 rupee currency notes has sent the entire country in a whirlpool of confusion. The country may be happy about the initiative or upset with the move, but the word ‘demonetization’ has recently become the trend. In this single move, the Government has attempted to tackle all the three issues affecting the economy i.e. a parallel economy, counterfeit currency in circulation and terror financing. This decision was considered as biggest cleanliness drive against the black money in the history of Indian economy. Demonetization is intended to combat untaxed black money, rampant corruption, encourage cashless transactions, and checkhawala transactions to counter terrorist activities and to bring more accountability in the informal sector of the economy. In a country where 90% transactions are carried out on cash basis it was a revolutionary move to transform from cash to cashless transactions.

Need of the study

The decision to demonetize Rs 500 and Rs 1,000 currency notes had a huge impact on the retail sector in India. Most retail stores placed a notice at their entrances, declaring their compliance with the government’s order and requesting customers to tender notes of Rs 100 denomination or use e-wallets, credit and debit cards for any purchase. This led to fall in sales in most of the retail outlets. In the short to medium-term, large denomination purchases will likely be made via electronic purchases rather than through brick and mortar outlets. This will impact the retail sector adversely. Hence the present study is taken up to understand the impact of demonetization on the retail sector.

Objectives of the study

The objectives of the study are:

- To study the impact of demonetization on retail sector
- To study the impact of demonetization on consumers

II. METHODOLOGY

This paper is based on secondary data. The secondary data was collected from various sources like reports, magazines, journals, newspapers etc.

History of Demonetization

This is not the first time the Indian governments has demonetized currency notes. RBI first demonetized Rs 1, 000 and Rs 10,000 banknotes in January 1946. Banknotes for Rs 1,000, Rs 5,000 and Rs 10,000 were reintroduced in 1954. However, Rs 1,000, Rs 5,000 and Rs 10,000 were once again demonetized in January 1978 once again. In 1978 the then Government said the move was aimed tackling the issue of the black money which had grown to large proportions at that time. The measure was enacted by passing the High Denomination Bank Note (Demonetization) Act, 1978. The law’s preamble said that this was an Act to provide in the public interest for the demonetization of certain high denomination bank notes and for matters connected therewith or incidental thereto.
However, Rs 1,000 was big money in those days, clerks earned Rs 200-300, most officers earned between Rs 500-1500 and even President of India earned a mere Rs 10,000, while Managing Directors of even the largest corporation earned just Rs 5,000. Most Indians in those days had never seen such a note in their lifetime.

The main objectives of demonetization are:

- To curb black money
- To discourage cash system
- To combat inflation
- To fight against terrorism
- To stop money laundering activities
- To mitigate corruption and so on

India remains to be a very cash reliant economy than any other country in the world. The cash centric informal sectors like agriculture, real estate, fishing etc. have been affected by demonetization. The retail market is unable to function, people are not able to buy vegetables or other commodities, weekly markets are non-functional, banks are witnessing long queues and trading has come to a halt.

However this might be a short term scenario and this move will give positive long term consequences. There will be clean and more transparent business transactions and money transfers as cashless transactions are track-able and more transparent. The move will also check fake note flows, a bane which has been dogging the Indian financial markets for years. As the physical usage of currency remains low, there will be lower chances of unaccountable transactions. It will also curb the parallel shadow economy (black economy) which runs majorly on cash basis. And also eliminate the role of intermediaries who usurp the share of welfare money spent on people.

**Need for Demonetization**

Demonetization is one of the Government’s bold steps towards transformation of Indian Economy. It is probably one of the biggest big-bang reforms undertaken by Government after a long time. In spite of many reasons quoted by Government, RBI in its FAQ on “Withdrawal of legal tender character of existing bank notes in the denomination of Rs. 500 and Rs. 1000” mentions reasons why this scheme is introduced. It reads as follows: “The incidence of fake Indian currency notes in higher denomination has increased. For ordinary persons, the fake notes look similar to genuine notes, even though no security feature has been copied. The fake notes are used for antinational and illegal activities. High denomination notes have been misused by terrorists and for hoarding black money. India remains a cash based economy hence the circulation of Fake Indian Currency Notes continues to be a menace. In order to contain the rising incidence of fake notes and black money, the scheme to withdraw has been introduced”.

Prime Minister Shri. Narendra Modi quoted the following reasons for demonetization during a television address to the nation on 08.11.2016: “In a historical move that will add record strength in the fight against corruption, black money, money laundering, terrorism and financing of terrorists as well as counterfeit notes, the Government of India has decided that the five hundred and one thousand rupee notes will no longer be legal tender from midnight, 8th November 2016. The Government has accepted the recommendations of the RBI to issue Two thousand rupee notes and new notes of Five hundred rupees will also be placed in circulation.”

One more reason for demonetization is to minimize Fiscal Deficit. It has subsidiary benefits as it will take out the counterfeit notes from circulation and the unaccounted money, if does not come out, will be of no use. It will stop Hawala trade too. Some of the facts and figures to describe the existing parallel economy can be viewed and analyzed as follows: First of all, if you look at our currency system, India is a cash-based society. 70% of values of transactions are in cash and even our gross domestic product (GDP), 45% of our GDP comes from informal sector. Informal sector accounts for 80% of our population. Let us look at the currency in circulation, both in quantity as well as in value.

| Table 1: showing the currency in circulation, both in quantity as well as in value |
|----------------|----------------|----------------|----------------|----------------|----------------|
| Denomination  | Volume in Crore pieces | % of all currency notes | Denomination | Value of currency notes | % of currency value |
| 2 and 5      | 1,162.6 | 12.88 % | 2 and 5 | 4,500 | 0.27 % |
| 10          | 3,201.5 | 35.47 % | 10 | 32,000 | 1.95 % |
| 20          | 492.4 | 5.45 % | 20 | 9,800 | 0.60 % |
| 50          | 389.0 | 4.31 % | 50 | 19,400 | 1.18 % |
| 100         | 1,577.8 | 17.48 % | 100 | 1,57,800 | 9.61 % |
| 500         | 1,570.7 | 17.40 % | 500 | 7,85,400 | 47.85 % |
| 1000        | 632.6 | 7.01 % | 1000 | 6,32,600 | 38.54 % |

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So, if you look at our currency in circulation from the above table, India probably has one of the highest currencies in circulation ratio. From the above table it is clear that Rs. 500 and Rs. 1,000 notes account for only 24% of the volume in circulation whereas the same notes account for about 86% of the value of currency in circulation. The amount of money that Government aims to withdraw from circulation is Rs. 14,18,000 Crores (86% of value) by demonetizing the 2,203.3 Crores (24% of Volume) currency notes of Rs. 500 and Rs. 1,000 denomination. But only time will decide how much money will be deposited into bank including that of black money.

III. REVIEW OF LITERATURE

Kanchan (2016) gives us the basic understanding of what the word means, when and how the demonetization of Indian currency was brought into effect and why it is good or bad. Ashish (2016) resolved that Indian financial system and its regulators were not ready for this change. Due to this the laymen or the common person including farmers are the sufferers. Anil and Basavaraja (2016) concluded that demonetization obliviously brings many inconveniences to common people but it is for only short term. However the long term benefits of demonetization overrides the short term challenges. Government initiatives like Income Declaration Scheme 2016, Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act 2015, Joint Declaration of AEOI between India and Switzerland to address black money etc. in redefining Indian economy are to be appreciate and these initiatives leaves their footsteps as part of history. Sandeep (2016) in his research article established that the move of demonetization would be positive for sectors like banking and infrastructure in the medium to long term. This could be negative for sectors like consumer durables, luxury articles, gems and jewelry, real estate and allied sectors. Most of the literature focuses on demonetization and its impact on the Indian economy in general, so the present study is taken up to understand the impact of demonetization on retail sector in particular.

IV. IMPACT OF DEMONETIZATION ON RETAIL SECTOR

Impact on small shops and vendors

A sudden demonetization will adversely impact this segment of the economy and it will witness immediate contraction. The nature, frequency and amounts of the commercial transactions involved within these sections of the economy necessitate cash transactions on a more frequent basis. Thus, these segments are expected to have the most significant impact. In spite of the initial hiccups and disruptions in the system, eventually this change will be well assimilated and will prove positive for the economy in the long run. Short term fall in real estate prices might benefit middle class citizens. This move by the Government along with the implementation of the GST will eventually make the system more accountable and efficient.

A survey was conducted by the local circles citizen engagement platform where 8,000 traders participated. 90 per cent of traders and small retailers across the country experienced a decline in the business post the demonetization of Rs 500 and Rs 1,000 notes. Approximately 16 per cent traders across the country are experiencing sales declines in the range of 60-90 per cent. These include jewelers and those dealing in furniture, and sanitary ware. 28 per cent traders experienced a decline of 30 per cent to 60 per cent. These included traders in automobile, computers, mobile phones and garments. 90 per cent of the small retailers across the country experienced a decline in their business ranging from 0 to 90 per cent. According to the poll, approximately 46 per cent traders are experiencing sales declines in the range of 0 to 30 per cent and these include general stores and prepaid recharge dealers.

Table2: showing the impact of demonetization on retail sector

<table>
<thead>
<tr>
<th>S.no</th>
<th>Respondent</th>
<th>%</th>
<th>Decline in sales (in %)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Traders in jewelry, furniture and sanitary ware</td>
<td>16</td>
<td>60-90</td>
</tr>
<tr>
<td>2</td>
<td>Traders in automobiles, computers, mobile phones and garments</td>
<td>28</td>
<td>30-60</td>
</tr>
<tr>
<td>3</td>
<td>Small retailers</td>
<td>90</td>
<td>0-90</td>
</tr>
<tr>
<td>4</td>
<td>General stores and prepaid recharge dealers</td>
<td>46</td>
<td>0-30</td>
</tr>
</tbody>
</table>

Source: A survey conducted by the Local Circles Citizen Engagement Platform.
The above chart gives us statistics about packaged food value sales in India, by channel in 2016. Traditional grocery retailers still account for more than 90% of packaged food value sales in India. Since a big part of these retailers are not well equipped with card payment machines, it is likely that sales during this period will have gone to modern/internet retailers, which offer consumers the convenience of paying by card or through net banking.

Impact on online retailers

The online payment and commerce segment stands to benefit the most as this move would provide a boost to digital payments and encourage people to shop online more. Cash on delivery (CoD) options will see a fall which in turn will lead customers to place more orders through cards and net-banking. Wallets like Paytm, Jio Money will see an increase of usability.

On the other hand, India's leading online retailers have been struggling to keep pace with the recent action taken by the government of scrapping Rs 500 and Rs 1,000 notes. Until the new 500 and 2000 Rupees notes get widely circulated in the market, money supply is expected to reduce in the short run. Order volumes for online retailers have reduced by 50-60 percent since the surprise announcement on demonetisation on November 8. It has marginally hit the Cash on Delivery (COD) payment business of major e-commerce business organisations.

V. IMPACT OF DEMONETIZATION ON CONSUMERS

It has been argued that demonetization has caused widespread chaos in the nation, with people (mostly lower strata) facing sudden cash shortage, long queues accumulating in front of Banks and ATMs.

It has also been argued that this demonetization strategy will have no significant effect on curbing black money, because of two reasons:

1. Most of the black money is deposited in foreign banks and is not in Indian currency.
2. Even in India, a bigger chunk of the black money is not kept in liquid form, but as Gold.

Both of these are true to much extent but to focus only upon these will not show a correct picture of the impact of demonetization. Earlier everyone appreciated the ban, then some started arguing and now everyone is struggling. Coupling this with the long term positive impacts of demonetization like checking cross border fake currency movement (According to the RBI data, fake currencies worth Rs 16.50 lakh Crore has been circulating in India with most of them of high-valued denominations), terrorist funding (both of these highly detrimental to the interests of common man), it is seen that the positives far outweigh the negatives.

Table 3: showing the impact of demonetization on consumers

<table>
<thead>
<tr>
<th>S.No</th>
<th>Reasons</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Support demonetization</td>
<td>90</td>
</tr>
<tr>
<td>2</td>
<td>Black money did exist</td>
<td>98</td>
</tr>
<tr>
<td>3</td>
<td>Brilliant/nice move</td>
<td>99</td>
</tr>
<tr>
<td>4</td>
<td>Curbing black money, corruption, etc</td>
<td>92</td>
</tr>
</tbody>
</table>

Source: Survey conducted by Prime Minister Narendra Modi app.

In a survey conducted by our Honorable Prime Minister Narendra Modi, over 5,00,000 consumers participated. 90% of the respondents supported the decision of our Prime Minister for his decision on demonetization. 98% of the respondents thought that black money did exist in India. 90% of the respondents opined that the government’s move to tackle black money through demonetization was good. 99% of the respondents felt that the evil of corruption and black money needed to be fought and eliminated. 92% of the respondents think that demonetization will have an impact on curbing black money, corruption and terrorism.
VI. MAJOR FINDINGS OF THE STUDY

- Approximately 16 per cent traders across the country are experiencing sales declines in the range of 60-90 per cent.
- Order volumes for online retailers have reduced by 50-60 per cent since the surprise announcement on demonetisation on November 8.
- 90% of the retail consumers supported the decision of our Prime Minister for his decision on demonetization.

Limitations of the study

The present study is based only on secondary data and is confined to the study of impact of demonetization on retail sector and retail consumers.

Sources of funding the study

The present study is a conceptual study based on secondary data which is self-financed by the authors.

Scope for further research

1. Impact of demonetization on real estate
2. Impact of demonetization on agricultural sector
3. Impact of demonetization on luxury goods

VII. CONCLUSION

Demonetization is a historical step to curb black money but it has to be taken into consideration that most of the black money is kept in the form of land, buildings or gold or kept abroad. What is in cash constitutes only 4% of the total amount of black money on which taxes are not being paid. Small farmers, sellers, merchants, daily wage laborers and traders are suffering because of lack of proper planning, intelligence and foresight such as recalibration of ATM machines. This is a terrible setback for the international standing of the Indian economy. At this time, the economy is struggling with slowdown. There is demand sluggishness in the economy leading to practically no private sector investment and stagnant industrial growth. Farmers generally deal in cash and India is also largely a cash economy. The cash transactions in this economy are far more than the total number of electronic transactions done on a daily basis. Even if more than 50% of money in circulation is black money, but most of it will find its way back to the banking system one way or another, and be recycled as new notes.

Demonetization may have had considerable negative effect in the first few days but in the long run it will have a positive impact on the economy. If substantially implemented, this will send a strong signal about India’s anti-corruption drive and is very likely to improve the country’s reformist stance. It also provides a boost to the government’s financial inclusion drive, pushing more households towards efficient banking and payment infrastructure. It helps the government to track people who are having large sums of unaccounted cash or cash on which no income tax has been paid.

Since black money is used for illegal activities like terrorism funding, gambling, and money laundering and also inflating the price of major assets classes like real estate, gold and due to demonetization all such activities will get reduced. Demonetization is a historical step and should be supported by all. One should look at the bigger picture which will definitely fetch results in the long term. The Indian economy has been provided a new lease of life with huge positive implications for liquidity, inflation, fiscal and external deficit in the short term. Over the next two-three years, improvement in India’s position on transparency and corruption in the global stage will further add to its investor appeal.

VIII. REFERENCES

[5] www.rbi.org.in