

## India's Stride towards Demonetization

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**Abstract:** To become a cashless economy is the new agenda of BJP government. But has the effect been favourable, or it has just become a new source of pain, especially for the middle and lower-middle class public. The present article gives a detailed view on demonetization and its effect till date. It entails a brief view of demonetization, with a comparative analysis with other developing nations, and the condition after demonetization.

**Keywords:** Demonetization, cashless, digital, IMPS, banking system, e-payments.

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### I. Introduction

November 8, 2016 has been marked as PM Modi's bizarre war on cash. In his speech addressing the nation, he stated that in an effort to combat corruption, tax-evasion and counterfeiting all 500 and 1000 notes will no longer be recognized as legal tender. The announcement immediately triggered a haywire in the economy to get the burden of, from the expiring bank notes. Though people had until the year end to deposit the currency, but doing so has given them a chill of tax burden. Some hastened to petrol pumps, some to jewellery shops, and others to railway counters and authorised government bodies to disburse the currency. Long queues in-out-and around the banks, exchange counters and ATM's, including any place where people had the chance to exchange the non-functioning notes. India had gone through this phase before in 1946 when all 1000 and 10000 rupee notes were recalled, and again in 1978, 1000, 5000 and 10000 notes were demonetized. But, the present note-ban agonized more than other period.<sup>1</sup>

Though public, opposition parties, government authorities and others continuously commented that the recent stint of demonetization had been planned in secret by PM Modi. Conversely, Modi Sarkar defended it with the albeit statement of it as the launch of missile on the black marketers, hoarders and terrorists. And so it had come more as a surprise of flash flood so that it would not be an initiative of dismay or one can say a flop-show.<sup>2</sup> After the crossfire and jolts of the past one-month the question arises – “Will demonetization really make us FAST or FOOL?”

### II. Nigeria's Demonetization

Nigeria's effort towards cashless economy from January 3, 2012 proved beneficial till some extent. Especially transactions became faster with proven time as queuing up has reduced, cost of vending machines has declined, loyalty, hospitality charges and other clientele charges have become negligible. In addition, with the introduction of cashless system, the Nigerian government increased the size of online shopping by more than 20 per cent. The cashless economy has proved to be advantageous as it has overcome the vandalism and theft problems. In the realm of being a cashless economy, Nigeria did set-up a strong example for both the groups of developing and transition economies. However, barring these merits - demerits too have made a way through it. And, to some extent the same problem and challenges are to be faced by nearly all the economies of this group.<sup>3</sup> A cashless economy or system is a method of making purchases by using electronic mode of payment. One can say that it's an expedition towards creating electronic purses where the money can be stored for making payments through electronic mode. On the other hand it also converts the smart phones into mini-banks for the users. A cashless economy is an effort to make the economy free of currency notes and coins, and at the same time enjoying the benefits from paying utility bills to hotel bills to purchasing a Porsche. In Germany 20% of the economy is cashless, the USA is 68%, and best of all is Sweden who has created a benchmark in history, as its 98% of the economy is cashless. It has been possible only because of low corruption, reliable legal protection, social trust and advanced infrastructural facilities.<sup>4</sup>

### III. The Story Of Demonetization

Indian Finance Minister Arun Jaitley for the past two months has emerged actively towards making India a cashless economy. But will the economic havoc pave the way for cashless economy? Will the government be reliable, trustworthy and technologically advanced to attract the customers? Will ever the public believe the officials offering arbitrary power? Will they ever allow them to control the money? <sup>5</sup> Cashless economy has become more like a fantasy than a reality. In the last one month 85% of the Indian currency in circulation was no longer legal tender, even did not have the luck to be exchanged for new printed notes, which are in shortage. As the citizens are trying to cope with the snaky lines in banks and ATM's folding in their arms the new financial setup, officials again issuing contradictory directives in the next minute. People waiting for days opted for violent ways, only to find that banks even ran out of smaller bills, merchants lost their sales as customers could not pay. The hardest hit sectors are of services, fisheries, private doctors and FMCG companies. A few people reportedly died, elderly citizens waiting in cues busted into tears, pensioners are helpless, bank employees are in a depressive mode due to workload and marriages were called off.<sup>6</sup>

Amit Varma, Journalist of Times of India quoted "If you buy AIDS medication or a porn magazine, or book a hotel room for a romantic alliance, this information can be accessed by the government-or any hackers...." Mr. Varma also noted, "Cash is empowerment: Ask the young wife who saves spare cash from her alcoholic husband; of the old mother who stuffs spare notes under her ,mattress for years because it gives her a sense of autonomy."<sup>7</sup> Further, as quoted by Arpan Nangia, the Head of the Indian branch of HSBC's Commercial banking division "I personally think it's a chicken or egg situation because the more prepared you are the more people who are aware, the more opportunity you-re giving to people to find loopholes in the system. Whereas, the downside of making it a surprise was that the government and the central bank were severely unprepared to manage the whole situation."<sup>8</sup>

Despite the so called *Tu-Tu-Main-Main* on demonetization Indians have and are reacting with stoicism seemingly keen to heed the call to be patient for 50 days. His urge to his young friends to digitize the economy, to embrace e-banking, mobile-banking and more such technology. As quoted in an assiduous public media meme means asks –"If our soldiers can stand for hours every day guarding our borders – why can't we stand for a few hours in bank queues?"<sup>9</sup> Now, the question arises: What after 50 days? What if the tension does not ease? How will e-payment be a hit in an internet deprived economy like India? What will happen to patients who are returned from the hospitals because they do not have new currency? Who will feed families who cannot make e-payments? What if counterfeiting and terrorism still prevails? We also cannot overlook the point that the process has also brought out the crores and millions of cash and gold hoarded in the houses of corrupt people. As of Dec 10, 2016 public exchanged and deposited about Rs. 12.44 lakh crores worth of scrapped 500 and 1000 notes at different banks according to official RBI reports, and the countdown is still on.<sup>10</sup>

#### Sector-Wise Analysis of Effect of Demonetization

Demonetization is not a big disaster like global banking sector crisis of 2007, but at the same time, it acted as a liquidity shock that disturbed economic activities. The daily wage earners, small traders etc. who resides out of the formal economy uses cash frequently. These sections have nearly lost their income in the absence of liquid cash. Cash stringency has compelled firms to reduce labour cost, and thus reduced the income to the poor working class. India has nearly risked its position of being the fastest growing largest economy, with problems of reduced consumption; income, investment etc. thereby decreasing India's GDP growth, as the liquidity impact itself may last three -four months.

The major sectors affected shall be automobile sector, as the demand is likely to drop for a couple of months for two-wheelers. As the real estate business is majorly affected the cement industry is also been affected simultaneously. The capital goods sector won't be largely affected due to the passiveness of B2B nature of business, but payments to sub-vendors shall face some liquidity issues. Further, it shall be noted that the movement shall be fruitful for the organised industry, but in the short term, it may impact the working capital on FMCG companies. Anecdotally, there's always a huge panic among distributors that business shall be impacted in the short term with liquidity choking up, thereby impacting FMCG revenue growth. Further, a shift is also expected from unorganised to organised sector especially in the jewellery industry. Lastly, the asset finance companies may see short to medium term pain, as a large chunk of business is cash based. Housing finance companies will be affected majorly, due to affect on real estate as well impact on loan against property.<sup>11</sup>

#### Comparative Analysis of Cashless Economies in World

Since, PM Modi's demonetisation drive hit the economy, people have nudged into taking up the cashless lifestyle. From filling up Ola money and Paytm accounts, to paying rents via internet banking, all are making that effort of walking extra mile digitally to compensate for the lack of cash in their pockets. But here's the thing. There are a few countries out there where going cashless is the way of life. So much so, in some of these countries, policies have been made that encouraged the public to opt for cashless transactions.<sup>12</sup> A descriptive and comparative analysis of these nations world-wide has been provided below:

**1. SWEDEN**

Sweden is the world's first cashless society. The nation started its journey years back and the most fascinating part about the nation is the acceptance of digital currency all over - whether you buy a candy or a magazine, whether you ride a bus or cab, almost everywhere. Nearly 96% of their population have a debit card and the nation's payment system records 89% of transactions done digitally or electronically. Here the cash transactions have decreased to just 3% in the national economy. This actually put a dent on bank robberies in the country, which dropped from 110 (in count) in 2008 to 16 in 2011, as most Swedish banks didn't have cash anymore.

**2. NORWAY**

Norway is already leading the global race of going completely pro-electronic banking. Here, even street food and newspapers are bought via mobile banking. DNB, the largest bank in Norway, called for the public to stop using cash urging that it shall eliminate the black money and crimes like money laundering.

**3. DENMARK**

Almost one-third of the population in Denmark use mobile apps and e-wallets to do their monetary transactions. In fact, businesses such as clothing retailers, restaurants and petrol pumps are actually legally free to refuse cash payments from customers. This, however, doesn't apply to services like hospitals, post offices, etc. Reports have it that the Danish government has "set a 2030 deadline to completely do away with paper money."

**4. BELGIUM**

On an average of 93% of the population have opted for cashless transactions in Belgium, with 86 per cent making payments via debit card. Moreover, the Belgian government has imposed a limit of 3000 Euros on cash payments in the country, hence coaxing people to opt for digital transaction. People use mobile app Sixdots widely for transactions, an app supported by Belgian banks.

**Table 1: Ranking of Top-10 cashless economies**

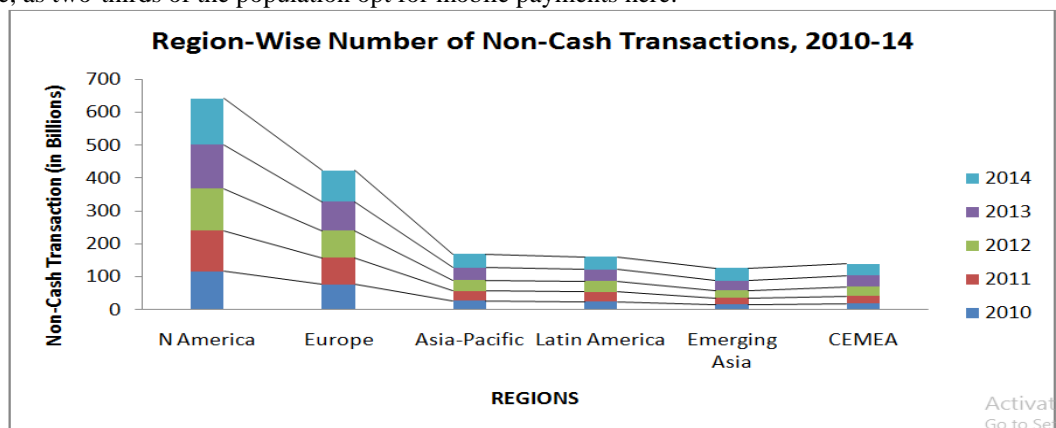
Rank	Country	Noncash Payments' Share Of Total Value Of Consumer Payments	% Of Population With A Debit Card
1	Belgium	93	86
2	France	92	69
3	Canada	90	88
4	United Kingdom	89	88
5	Sweden	89	96
6	Australia	86	79
7	The Netherlands	85	98
8	United States	80	72
9	Germany	76	88
10	South Korea	70	58

**5. FRANCE**

The French people use a variety of methods for making cashless payments, like mobile payments, contact-less cards and m-POS to carry out their daily transactions. In France, nearly 92 per cent of population have gone cashless with transactions.

**6. UNITED KINGDOM**

In UK an average of 89 per cent of the population uses digital banking for transportation and other transactions here. Paytm being UK's most popular mobile payment system has crossed 26 million pounds in transaction volume, as two-thirds of the population opt for mobile payments here.



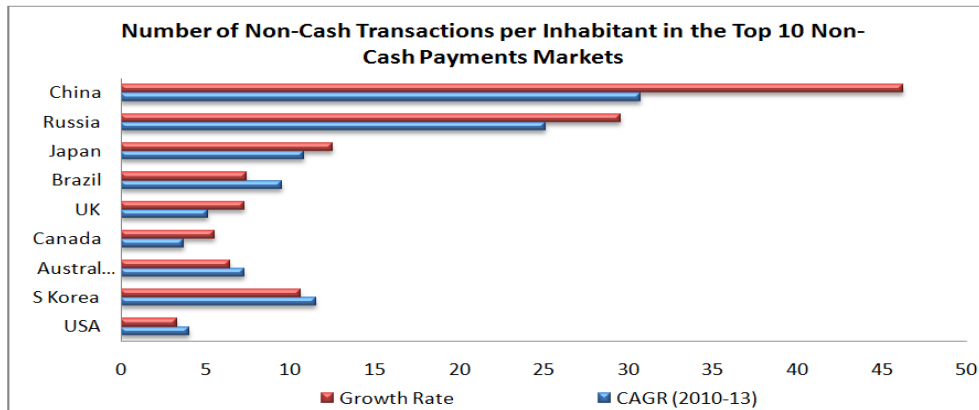
**Graph1: Region-Wise Non-Cash Transactions, 2010-14**

**7. SOMALILAND**

Despite being one of Africa's poorest countries, people in Somaliland opt for electronic banking than in most developed countries in the world. Liquid cash is rapidly decreasing in the market here, as even street vendors accept mobile payments. So much so that even the cards are becoming a rudimentary mode of payment. According to a survey on an average customers here makes at least 34 online transactions per month, which is higher than almost anywhere in the world.

**8. KENYA**

In Kenya, some 15 million users are subscribed to M-Pesa, a mobile-based money transfer app. All from sending money to rural areas, paying bills, to school fees is done through M-Pesa. People even receive their salaries via this app. The usage of cash is becoming more and more obsolete in Kenya.



**Graph 2:** Non-Cash transactions per inhabitant of Top Cashless Markets

**9. CANADA**

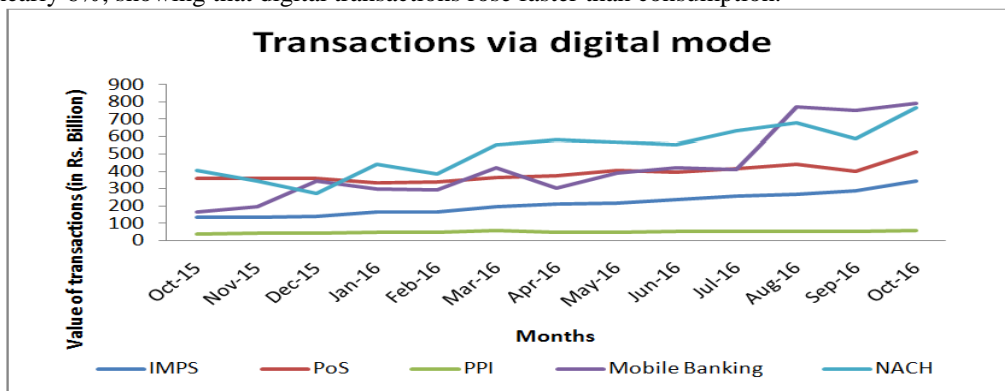
In Canada, 90 per cent of the population opt for cashless transactions, among which on an average 70 per cent of payments is done by cards. Reports state that new currencies have not been printed in Canada since January 1, 2013. A survey held by PayPal in Canada depicted that 56 % of the public preferred online wallet to carrying cash, for security reasons.

**10. SOUTH KOREA**

South Korea is one of the few Asian countries that is slipping towards a cashless economy. The government to promote the cashless mode has adopted preferential VAT treatment for consumers who pay with cards, as compared to those using cash.

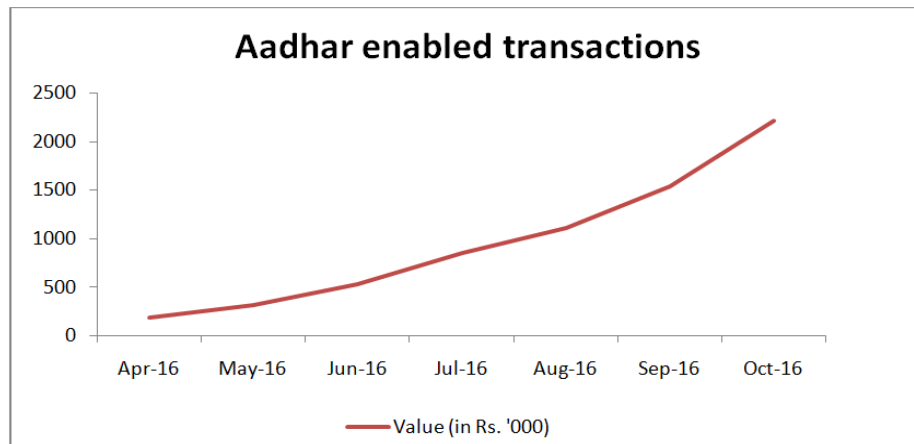
**Success of Cashless India – So Far**

A year, which shall be remembered for its notebandi, a conversational term for the withdrawal of almost 86% of India's currency in circulation making the Indians steadily accepting various digital payments modes. Consumers used the Unified Payments Interface, released in August 2016, for 300,000 transactions amounting to Rs 90 crore in November 2016. The number grew to 1.4 million transactions, worth Rs 480 crore, till December 25, 2016.<sup>13</sup> Money transfers using mobile banking and immediate payment system (IMPS), showed the highest increase in over 12 months (Oct. 2016 to Oct. 2017). Mobile banking transactions grew 175% while money transacted using mobile banking grew 369%.<sup>14</sup> Over the same period, non-cash payments–NEFT, PPI, mobile banking, Point of Sale (PoS) terminals and National Automated Clearing House (NACH), rose by nearly 6%, showing that digital transactions rose faster than consumption.<sup>15</sup>



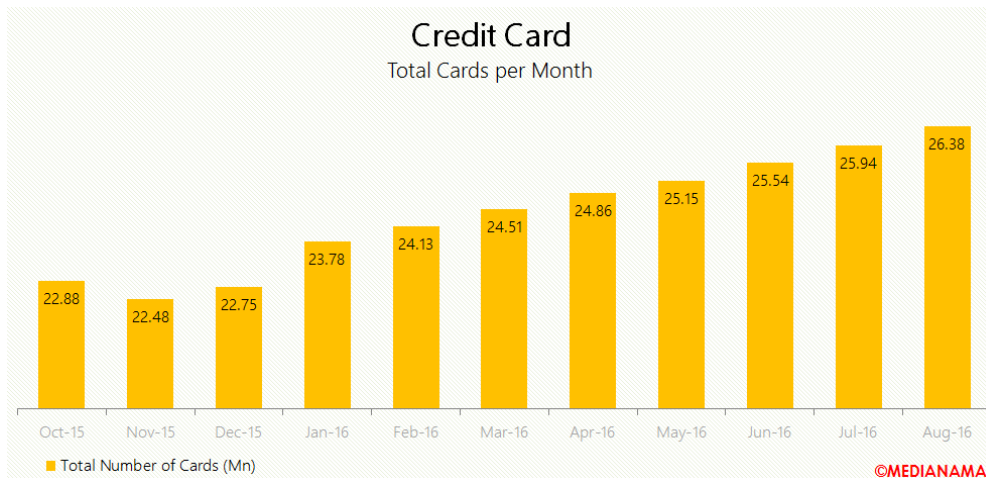
**Graph 3:** Transactions made through digital modes

The NACH has been used for making bulk transactions towards distribution of subsidies, dividends, interest, salaries, pensions, and for bulk transactions towards collection of payments pertaining to telephone, electricity and water bills, loans, investments in mutual funds and insurance premiums.<sup>16</sup> In addition, to these, in places where banks did not have sufficient branches, banking correspondents could not reach out to people directly, they used the Aadhaar Enabled Payment System (AEPS) to transfer money specially under government schemes, such as old age pensions, Mahatma Gandhi National Rural Employment Guarantee Scheme (NREGA) etc.<sup>17</sup>

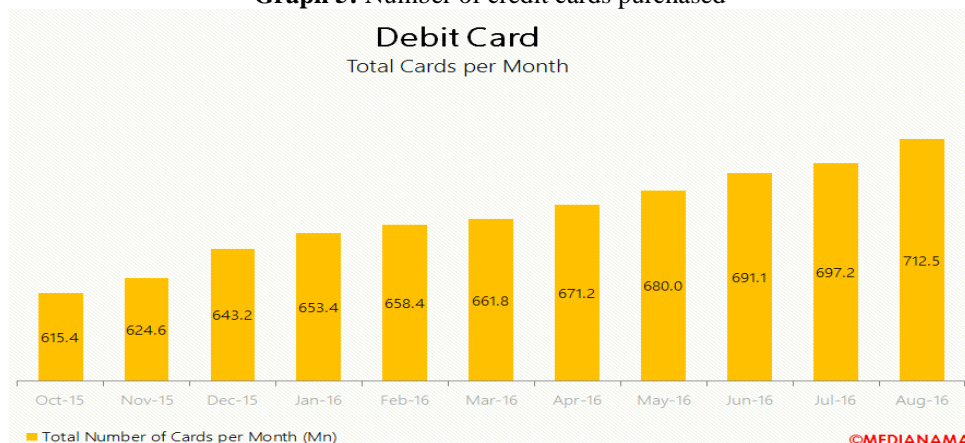


**Graph 4:** Aadhar enabled transactions

This mode showed one of the highest growths of more than 6-times, in a small period of six months. The number of purchase of debit and credit cards also increased vehemently, in a period of nearly a year. Simultaneously, the use these cards also increased rapidly within a year.



**Graph 5:** Number of credit cards purchased



**Graph 6:** Number of credit cards purchased

Thereafter, growth was also noted in transactions through unstructured mode of payment, where mobile networks and third parties were used for transfers and payments. There were 7,000 transactions amounting to Rs 73 lakhs in November 2016 through the Unstructured Supplementary Service Data (USSD), making it the least used digital payment platform by number and value of transactions. USSD volume of transactions rose to 60,000 in December 2016, amounting to Rs 6.6 crore until December 25, 2016.<sup>18</sup>

#### IV. Conclusion

With this mixed analysis it can be said compactly that the initiative is for a good purpose, but the implementation is shabby. Because the patience and time both are running out to fix the avalanches of the policy through amendments, roll backs and patches works, because if the undercuts are not mended it is surely going to hamper the reputation of Modi government. Demonetization as a cleanser may produce several good things in the economy. Since, it can be noted that with the advent of time the public is adjusting with the new trend. Simultaneously, it is also trying to get acquainted with the e-payments and digital modes of payment. Because, this process has proved to be a hurdle to the growth of black money and corruption in many leading economies of the world. At the same time, it shall also create unavoidable income and welfare losses to the poor sections of the society who gets income on daily basis, and those who don't have the digital transaction culture. Overall economic activities will be dampened in the short term. But, the immeasurable benefits of having more transparency and reduced volume of black money activities which will surely be revealed as long term benefits for our society.

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