

Demonetization-Its Impacts on Business and Way Forward

SUBHASH C. AGRAWAL
FCMA, FCS, FICA, LL.B.
Co-Founder, CFO4SME
FORMER:
CHAIRMAN, NIRC of ICAI
DIRECTOR-FINANCE, CCI Ltd.
C.M.D., Triveni Structurals Ltd.

ISMA CFO4SME Joint Program on 24.12.16 at Noida



**Saala 2 din se
aisa lag raha hai
jaise Indian Currency
leke Mai Foreign
me ghum raha hu**

What is the expected size of black economy in India???

In the form of :

-CASH

-GOLD

-Benami Properties

-Foreign Countries

**On 8th Nov., demonetisation of Rs.500 and 1000 notes
Announced by PM**

Objects:

- **Fake Currency**
- **Terror funding**
- **Black money**

17.5 L crs currency

86% in 500 and 1000 notes, i.e. about 15 L crs

**Expected about 25-30% will be extinguished having
a windfall to Govt of 3-4 L crs**

*12.5 L crs already back in banks till 8th Dec.,
2016 in one month of demonetisation,*

Still 21 days left

Enough anecdotal evidence of people exploiting the Rs 2.5 lakh limit of near and dears as well as Jan Dhan Accounts.

Unaccounted money "taken care of" as "legit" money and back in the banking system.

Now expecting near to whole will come back, after Pradhan Mantri Garib Kalyan Yojana (called as new IDS), announced by Govt. by amending the Income Tax Act, 1961, in Sec. 115BBE, incorporating Sec199A to 199R,etc.

As per reports, it is estimated that about Rs 2.5 lakh crore will be declared under this new income disclosure scheme (IDS)

At 49.9 % tax on the amount declared under the Pradhan Mantri Garib Kalyan Yojana (PMGKY), the immediate benefit would be less than Rs 1.25 Lakh crore to Govt.

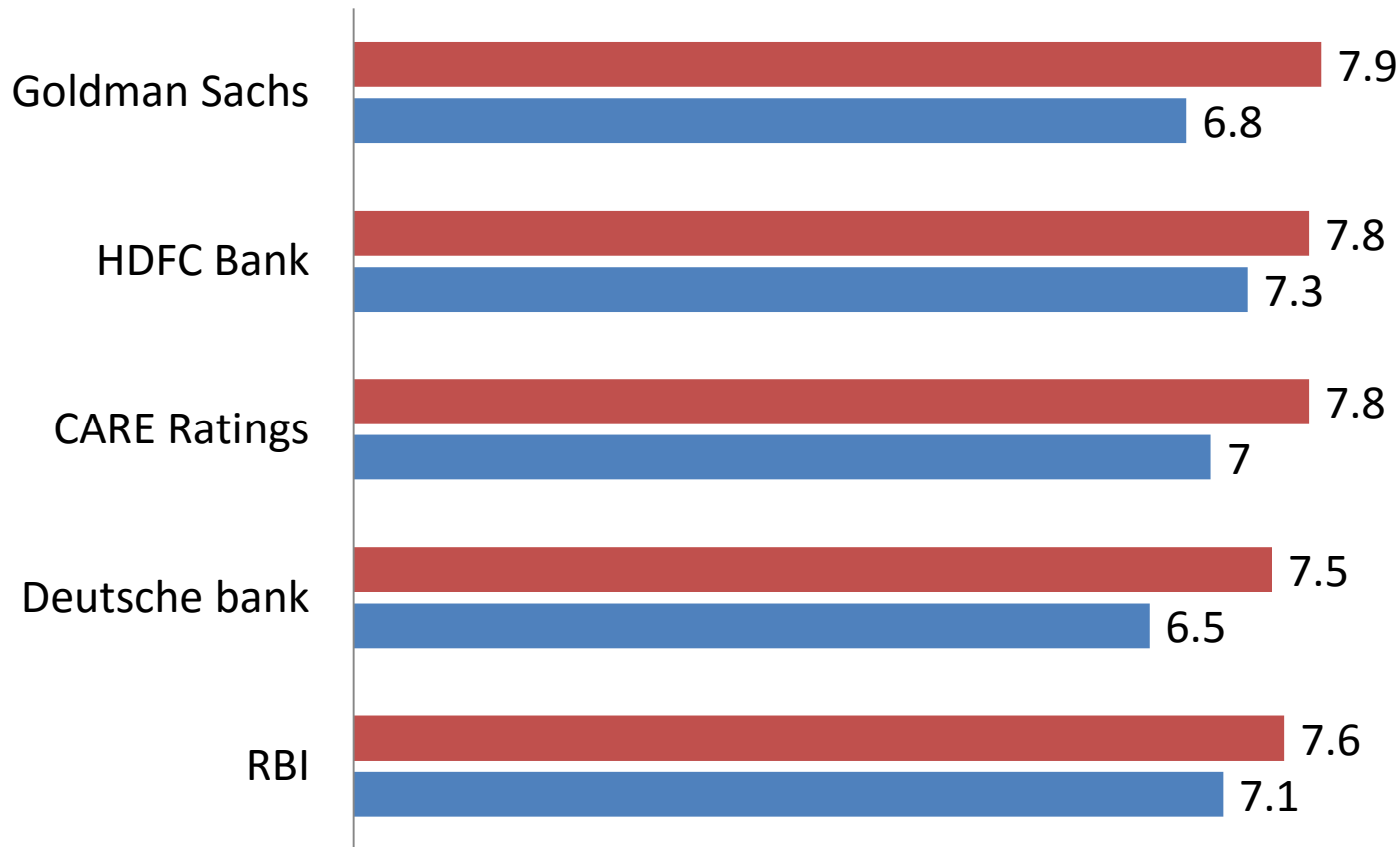
Plus about Rs 5,000 Crs savings as interest, on the 25 per cent that has to be deposited under the PMGKY.

Income Tax Raids detected 3185 Crs undisclosed income & 428 Crs cash & jewelries.

Total gain to Govt. will be around Rs 1.3 Lakh crores.

India's GDP revision one month after Demonetisation

Original Revised



It is estimated that the nation's GDP will take a hit of about Rs 1.2 lakh crore during the year 2016-17.

The actual cost of executing the demonetisation drive

- Printing the new notes,**
- Logistics**
- Destroying old notes**
- Advertisements**
- Discounts & Reliefs (Tax, NHAI, etc.)**

estimated at more than Rs 20,000 crore.

There will be cost of about Rs 1.4 lakh crores to economy.

Against a gain of Rs 1.3 Lakh crore.

Of course, there will be "long-term benefits" such as

- move to a cash-less economy
- widening the tax base,
- Probable reduction in tax rates

India's Purchasing Managers Index (PMI):

-An Economic indicator of the Manufacturing Sector that tracks new orders, inventory levels, production, supplier deliveries and the employment environment was **52.3**, i.e. 2 points lower than the 36 months high of **54.4**.

A PMI of less than 50 indicates a contraction in the economy.

5 yrs PMI



Cash shortage has hampered :
-growth of new work/projects
-buying activity, and
-production"

the impact of demonetisation on the manufacturing sector will be more through December.

"Sales have been hit hard, which will result in higher inventory and sharper production cuts in the months ahead.

But despite the disruption, it is believed that Indian manufacturing will be able to survive.

Services perhaps the worst hit by demonetisation move

It comprises areas such as trade, hotels and Restaurants, transport, communication, finance, insurance, real estate, among others, and accounts for 60% of India's GDP.

The number of rural households getting work under MNREGA in Nov., 2016 dropped by 23% compared to previous month.

The work given in Nov., 2016 is down by about 55% compared to the same month last year.

The **Services Purchasing Managers' Index**—
which measures sales, employment, inventories, and prices at service sector companies - sank to **46.7** in
November, from **54.5** in October.

This is the first time since June 2015 that the index has slipped below the 50 mark.

The decline of 7.8 points was also the biggest one-month drop since November 2008.

Yet, it is believed that the sector will rebound quickly.
“The disruption is expected to be short-lived”

Consumer spending

Indian economy has also been hit by poor consumer spending since demonetisation. Private consumption expenditure accounts for around 60% of India's GDP.

“the consumer goods sector, which has reported solid growth so far, was the weakest performer in Nov.”

“Rural consumption also looking dip due to their higher dependency on cash transactions, leading to further problems for farmers and having a domino effect on their ability to purchase.”

Agriculture Sector

It constitutes about 15% of India's GDP but in 2014 and 2015, grew by a paltry 0.2% and 1.2% respectively

India's agriculture sector was widely expected to have a robust year.

- Good rainfall after two years of drought
- Sector was expected to grow by about 4% in the current fiscal.

Agriculture - a cash-rich sector,
Most of the payments for the purchase of seeds, fertilizers, tools and labourers' wages, are carried out in cash.

Harvested Kharif crops and preparing land for the Rabi crops which are harvested during spring.

Sale, transport and distribution of agricultural products in Mandis, buying seeds, payment to labourers, fertiliser, almost entirely dependent on cash.

In addition, RBI has also banned the exchange of old notes at co-op. banks, which farmers visit more often.

"Farmers finding tough to sell their produce in the markets.

"Despite a good harvest, it is unlikely to commensurate with improvement in rural demand."

The agriculture sector will bear the brunt of demonetisation,"

Sensex and foreign inflows

Meanwhile, investors have also been jittery since the news of demonetisation.

Since 8th Nov., the **Sensex** has fallen by around **5%** while foreign portfolio investors (FPIs) withdrew some **Rs37,300 crore** in November, the highest since June 2013.

Recovery in sight

But not all is lost for the Economy.

Despite the imminent slowdown across sectors and the hit on the Indian economy, experts also see an eventual recovery over the next year.

<https://in.finance.yahoo.com>

S&P BSE SENSEX

■ ^BSESN

9 Dec, 2016

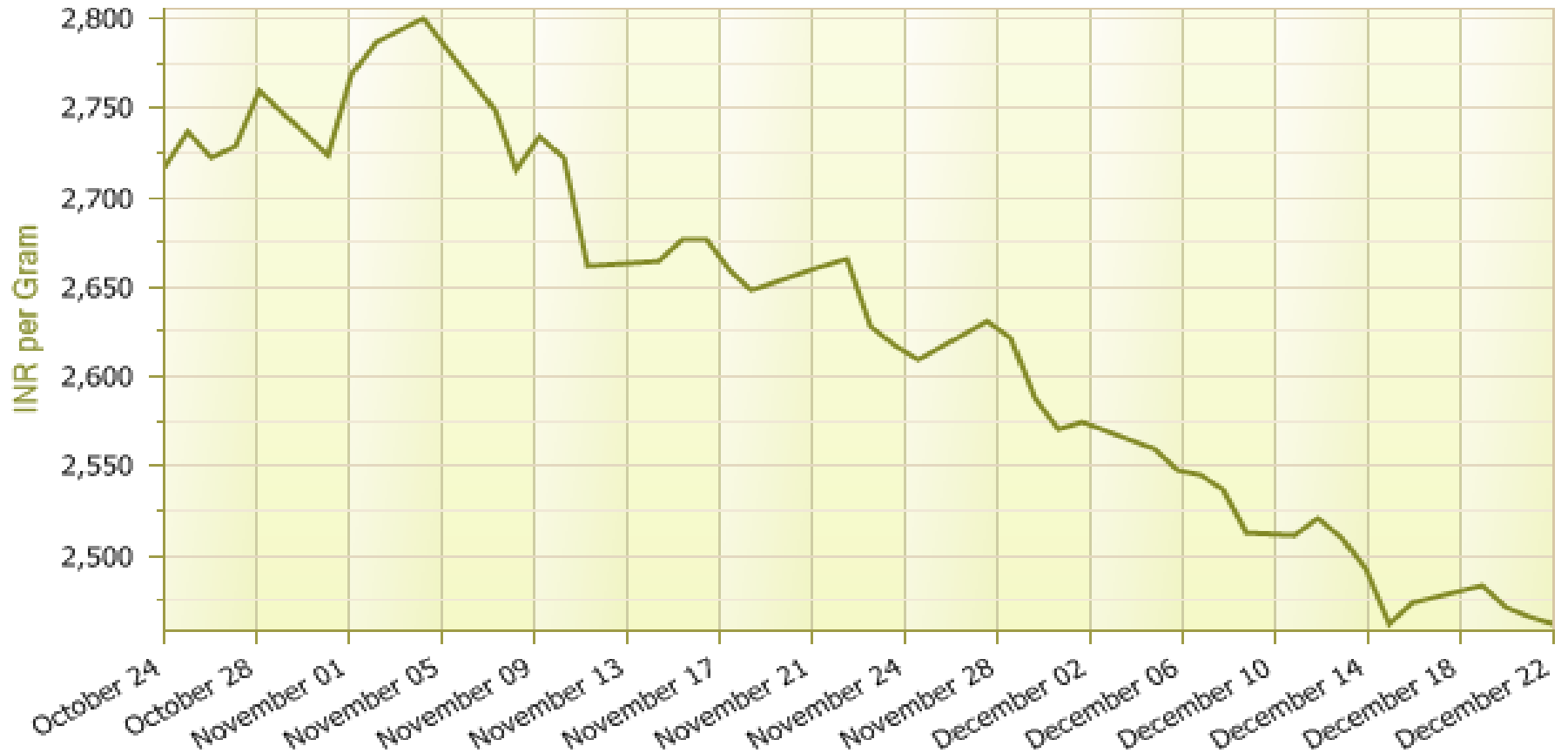


GOLD 18 Kt in Mumbai

www.Bullion-rates.com

60 Day Gold Prices in Indian Rupees (price per gram)

23-12-16 15:25



New Delhi Time (GMT+5:30) * www.bullion-rates.com

According to a Assocham research on Cybercrimes:

-Mobile frauds are expected to grow up to 65% in India by 2017.

-Credit and debit card fraud cases have topped the charts of cybercrimes and increased six times in just last three years.

- about 46 per cent complaints of online banking are related to credit/debit card fraud,

Senior RBI Official Arrested For Allegedly Money Laundering A Crore (12.12.2016), AXIS bank case.

Amendment in Section 44AD

Individual, HUF, Partnership Firm (Other than LLP)

Any Business other than Tpt, Agency, Brokerage, Commission

		Cash 100%	50%+50%	Digital 60%	Digital 100%
Total Turnover	Lakhs	200.00	200.00	200.00	200.00
Cash Turn Over	Lakhs	200.00	100.00	80.00	-
Digital Turnover	Lakhs	-	100.00	120.00	200.00
Profit @8%	Lakhs	16.00	8.00	6.40	-
Profit@ 6%	Lakhs	-	6.00	7.20	12.00
Total Profit	Lakhs	16.00	14.00	13.60	12.00
Deduction u/s 80C	Lakhs	1.50	1.50	1.50	1.50
Taxable Income	Lakhs	14.50	12.50	12.10	10.50
Tax incl Cess	Rs.	267800	206000	193640	144200
Tax Savings	Rs.	0	61800	74160	123600

PARTICULARS	EXISTING PROVISIONS	AMENDED PROVISIONS
Taxation and Investment Regime for Pradhan Mantri Garib Kalyan Yojana, 2016' (PMGKY)	New Taxation and Investment Regime	<p>Undisclosed income in the form of cash & bank deposit can be declared:</p> <p>(A) <u>Tax, Surcharge, Penalty payable</u></p> <p>Tax @30% of income declared;</p> <p>Surcharge @33% of tax;</p> <p>Penalty @10% of income declared</p> <p>Total @49.9% of income (approx.)</p> <p>(B) <u>Deposit</u></p> <p>25% of declared income to be deposited in interest free Deposit Scheme for four years.</p>

<p>Provisions for taxation & penalty of unexplained credit, investment, cash and other assets</p>	<p><u>TAX (Section 115BBE)</u> Flat rate of tax @30% + surcharge + cess (No expense, deductions, set-off is allowed)</p>	<p><u>TAX (Section 115BBE)</u> Flat rate of tax @60% + surcharge @25% of tax (i.e. 15% of such income). So total incidence of tax is 75% <u>PENALTY (Section 271AAC)</u> If Assessing Officer determines income referred to in section 115BBE, penalty @10% of tax payable in addition to tax (including surcharge) of 75%.</p>
<p>Penalty for search seizure cases</p>	<p><u>Penalty (271AAB)</u> (i) 10% of income, if admitted, returned and taxes are paid (ii) 20% of income, if not admitted but returned and taxes are paid (iii) 60% of income in any other case</p>	<p><u>Penalty (271AAB)</u> (i) 30% of income, if admitted, returned and taxes are paid (ii) 60% of income in any other case</p>

Coordination Gap Affects Smooth Implementation Of Some Steps

Times of India / 22.12.2016

NOT ON SAME PAGE

Quality of ₹500 Notes »

Difference in quality of notes raised fears of counterfeit. RBI confirms notes are genuine but can't explain as notes were not printed at RBI presses. Government keeps mum



Withdrawal for Weddings »

Government says those getting married or their parents can withdraw ₹2.5 lakh. RBI puts pre-conditions

Deposit of Scrapped Notes »

RBI discontinues announcing numbers after government contests the figures, citing double-counting

Merchant Discount Rate »

Government waives merchant discount rate on card transaction. RBI thinks it will hurt banks

Deposits »

Government seeks to put onus of vetting legality of deposited notes on banks. RBI tells banks to seek reasons for deposits above ₹5,000


Sources in RBI Feel »

- ▶ There is an attempt to put tax compliance responsibility on RBI
- ▶ RBI's image is being tarnished by frequent changes in circulars suggested by the government

WHAT'S THE REAL REASON FOR THE CASH CRUNCH?

Everyone's been under the impression that the shortage of new Rs 2,000 and Rs 500 notes has been on account of the printing presses not being able to keep pace with demand. But data from the RBI seems to suggest otherwise. **Till Dec 19, the central bank had not released for distribution to the public all the Rs 2,000 notes it had printed before demonetisation was announced on Nov 8.** So who, or what, has created the cash crisis that has led to so much hardship and slowed the economy? Here are some numbers

220 crore (2.2 billion) is the number of ₹2,000 and ₹500 notes released by the RBI to banks for distribution to public between November 10 and December 19

 If **90%*** of these notes were of ₹2,000 denomination and the remaining of ₹500...

...then **₹4.07 lakh crore** is the value of new high-value currency released till Dec 19 (last available remonetisation figure)

But **₹4.94 lakh crore** is the value of ₹2,000 notes RBI had ready by November 8, according to its reply to an RTI query. This is nearly ₹1 lakh crore more than what it had released till Dec 19. Why?

*Based on survey of banks. RBI didn't give break-up

Story Doesn't End Here...

1 Printing of new notes has continued after Nov 8 too, presumably at full capacity. Based on the capacity of the four presses, ₹2 lakh cr worth of ₹2,000 and ₹500 notes should have been printed since Nov 2nd week (a conservative estimate). This would take total value of new currency available by Dec 19 to nearly **₹7 lakh crore** (original ₹4.94 lakh cr + ₹2 lakh cr)

2 So, why was only ₹4.07 lakh cr released when up to ₹7 lakh cr was available?

TOI requested RBI and the finance ministry for an answer, but no response had been received after 48 hours. Here's what RBI officials informally told the paper:

- ATMs had to be recalibrated to disburse new notes
- Printing of ₹500 notes had to be stopped and shifted to another mint after faults were detected in a few lots
- The shift slowed printing at two mints (out of four) for nearly three weeks
- There was a belief in a section of government that sudden release of large cash could lead to excessive rush, possibly even a run on banks

Losers:

- Economy to take hit in short term with lesser demand
- Common people/ households
- Small farmers and labourers
- Lower interest on FDs for Retired Persons
- Real Estate
- Discretionary Exp.: Luxuries, Gold, Tourism
- Expensive weddings, parties
- Black money hoarders
- GST on backstage

Gainers:

- Economy in long term
- Municipal Corp., Elect.Cos., Shopping Malls
- E-Wallets,
- Genuine buyers of property
- Inflation down- overall downturn in prices
- Lower interest rates to Industries
- More funds for Industries
- Widening Tax base, higher fiscal revenue
- Reduction in tax rates
- Tracking of flow of funds in Digital transactions
- Reduction in corruption level

“There will be short term pains, for laying foundation for a better future” - K V Kamath, Chairman, BRICS

Whether Objects of Demonetisation achieved...

- Fake Currency
- Terror funding
- Black money

Way Forward:

1. Revamp tax system by offering huge incentives to encourage cashless economy
2. 100% cashless donations to Pol.parties & Rel.places
3. Tax on Pol.parties, Rel.places, Agriculture, Educational Institutions(Trusts)
4. Limit on cash transactions,
5. Cash carrying limit
6. Withdraw Rs 2,000 notes asap
7. Forensic Audit of Banks by CMAs



Thank you very much.

Have a great learning.

Subhash Agrawal

CMACS.SA@GMAIL.COM

Mobile 9717494767