

A Multidisciplinary Indexed International Research Journal

ISSN: 23203714

Volume: IX



ADHYAYAN
INTERNATIONAL
RESEARCH
ORGANISATION



A Study on effect of banks due to demonetization

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Abstract:

Stock markets are very sensitive to events and information. There could be volatility in the stock prices either side based on the news. Events might be Natural disasters like Earthquakes and Manmade attacks like terrorism. For instance, the market today is interconnected. That is the earthquake which was occurred in the Indian ocean on December 26, 2004, showed an impact on THE stock market by reducing the percentage of stock up to 3.8%. And also, from Oslo to London to Brazil to Brussels terrorist attacks would puncture the relative calm working the world to enormous irregularity. It was November 8th, 2016 where there was an announcement that 500 and 1000 rupee notes can no longer be used. This torpedoed Indian economy which led a huge impact on the people living in rural and urban areas. BSE's SENSEX and NSE's NIFTY has shown a huge volatility due to demonetization of Indian currency. The stock market also got affected due to the subsequent event which was Donald Trump's victory in states. The Banking sector took an immediate hit on a day when demonetization happened. However, the main focus of demonetization was to eradicate black money in the Indian economy which would benefit the banking sector in long term. Though demonetization of money has happened and the economy suffered overdue, the economy would be free from black money and cashless transactions happen in long term. Hence the present study deals with how stock prices of Indian banks are performing after demonetization and would these prices benefit long term success of various banks. On this regard we have chosen five public sector banks such as Andhra Bank, Bank of India, IDBI bank, UCO bank and Syndicate bank, and five private sectors such as Bank of Punjab, Federal bank, HDFC bank, ICICI bank and Karur Vysya bank. India has lost 86% of its monetary base. The government has attempted to tackle all the issues affecting economy i.e a parallel economy, counterfeit currency in circulation and terror financing. The problem is that investment is not taking place in the economy and the rate of growth of capital formation is down. A way to bring up capital is to divert funds into investments when the total cost of capital comes down

The paper also focuses on Comparing the average risk and return of the stock prices of various banks and also spot which bank has given highest and lowest returns after demonetization.

Introduction:

Stock markets are very sensitive to events and information. There could be volatility in the stock prices either side based on the news. Events might be Natural disasters like Earthquakes and Manmade attacks like terrorism. For instance, the market today is interconnected. That is the earthquake which was occurred in the Indian ocean on December 26, 2004, showed an impact on THE stock market by reducing the percentage of stock up to 3.8%. And also, from Oslo to London to Brazil to Brussels terrorist attacks would puncture the relative calm working the world to enormous irregularity. After Paris attack on November 13, 2015, the CAC 40 has dropped to 1% just after it opened. There was an illusion that the victory of Donald Trump would likely cause the stock market DJIA¹, -0.02% to crash and plunge the world into recession. Hence there would be the impact on stock markets due to many reasons. Prior to the above examples, one among the causes of fluctuations in stock prices of banks is due to demonetization².

It was November 8th, 2016 where there was an announcement that 500 and 1000 rupee notes can no longer be used. This torpedoed Indian economy which led a huge impact on the people living in rural and urban areas. BSE's SENSEX³ and NSE's NIFTY⁴ has

shown a huge volatility due to demonetization of Indian currency. The stock market also got affected due to the subsequent event which was Donald Trump's victory in states.

The Banking sector took an immediate hit on a day when demonetization happened. However, the main focus of demonetization was to eradicate black money in the Indian economy which would benefit the banking sector in long term. Though demonetization of money has happened and the economy suffered overdue, the economy would be free from black money and cashless transactions happen in long term. Hence the present study deals with how stock prices of Indian banks are performing after demonetization and would these prices benefit long term success of various banks. On this regard we have chosen five public sector banks⁵ such as Andhra Bank, Bank of India, IDBI bank, UCO bank and Syndicate bank, and five private sector⁶ such as Bank of Punjab, Federal bank, HDFC bank, ICICI bank and Karur Vysya bank. The paper also focusses on Comparing the average risk and return of the stock prices of various banks and also spot which bank has given highest and lowest returns after demonetization.

Literature Review:

and sound companies listed in Bombay stock Exchange

⁴ NSE Nifty 50: NSE stands for National Stock Exchange. The NSE nifty 50 is an index of National stock exchange which holds the stock prices of top 50 companies of India. NSE is world's 12th largest stock exchange as of march 2016.

⁵ Public sector banks: These are the banks where majority of the stake is held by government (51% of the stake).

⁶ Private sector banks: These banks are held by private shareholders but not by the government.

¹ Dja: Dow Jones industrial average the Dow, is a stock market index, and one of several indices created by Wall Street Journal editor and Dow Jones & Company cofounder Charles Dow.

² Demonetization: The process of stopping the circulation of present money in order to bring new notes and coins into circulation.

³ BSE Sensex: BSE stands for Bombay Stock Exchange. The BSE Sensex is a free-float market weighted stock market index of 30 well established

According to Chirag Singal (18th November 2016), Everyone is aware of demonetization of 500 and 1000 rupee notes. It would have a pretty bad impact on SME's, small traders, real estate, transport sector, consumer durable goods industry and rural business where the majority of transactions are made in the form of cash. Few industries got benefitted due to demonetization. One among them is banking industry. The reason behind this beneficiary is a lot of people deposit their cash at banks. Hence there will be a lot of liquidity with the bank. As the deposits with the bank's increases, the current account savings account(CASA) will increase, so will increase the net interest income and net earnings of the banks.

According to InsightsIAS (16th November 2016) due to demonetization, India has lost 86% of its monetary base. The government has attempted to tackle all the issues affecting economy i.e a parallel economy, counterfeit currency in circulation and terror financing. The problem is that investment is not taking place in the economy and the rate of growth of capital formation is down. A way to bring up capital is to divert funds into investments when the total cost of capital comes down

According to HDFC bank Investment Advisory group (11th November 2016) from an equity market perspective, demonetization is beneficial for sectors like banking and insurance in medium to long term. This could be non-beneficial for sectors like consumer durables, luxury items, gems, jewelry, real estate and allied sectors near to medium term. Demonetization has improved tax compliance, fiscal balance, lower corruption, lower inflation and complete elimination of fraud currency.

According to G R Hari – chief executive partner of Manohar Chowdary & Associates (11th December 2016) due to a decrease in bank lending rates, the sales might be boosted as the bike and car EMI's become much affordable and short-term impact due to purchase deferment: demand will revive in a medium term.

According to Invesco Mutual fund, the demonetization initiated by the government is going to have a far impact on Indian economy. RBI says, 86% of 17.54 lakh crores is of INR 500 and INR 1000. It is being estimated that 20% of the currency is black. The banking sector went to see a surge of liquidity as deposits collected. Based on the assumptions that there would be tendering of currency from the public to the tune of INR 12 lakh crores. The sudden surge in the deposit of 6% of current aggregate deposits helped in the improvement of liquidity and also would help in long run. It will also lead to demand for fixed income securities, particularly government securities.

From all the prior studies and articles, our study deals about how the top five public and private sector banks of India got affected due to demonetization. As part of our research, it is revealed that the banks were affected about 1% for the first month after demonetization and the recovery of banks were uneventful after demonetization. So, the aim of our study is to compare either of the banks i.e public and private sector banks and show which bank has got more affected due to demonetization.

Research methodology

The present study is a descriptive study which deals with stock prices of various public and private sector banks. The public sector banks which we have taken are Andhra bank, Bank of India, IDBI bank,

syndicate bank and UCO bank. The private sector banks which we have taken are ICICI bank, HDFC bank, Bank of Punjab, Karur Vysya bank and Federal bank.

Steps of research methodology:

- a. The historical stock data of both public and private sector banks are taken from various sources like yahoo finance and investing .com of one month, two months and three months’ data after demonetization has been collected. The collected data is secondary data.
- b. The collected data is kept in spreadsheet and return on close price and risk on close price have been calculated using the following formulas

i. Return

$$\text{Daily return} = (\text{price}_1/\text{price}_0)-1$$

ii. Risk

Variance:

$$\text{Var}(R) = \sigma^2 = \sum_{i=1}^N p_i (R_i - E[R])^2$$

Standard deviation:

$$\text{SD}(R) = \sigma = \sqrt{\sigma^2} = (\sigma^2)^{\frac{1}{2}}$$

- c. The data after performing risk and return for all the banks is compared and then the result is determined.

Data Interpretation:

These are the results obtained after performing the analysis. In public sector banks, as part of analysis, it was found that most of the banks like Bank of India, Andhra bank, IDBI bank, Syndicate bank and UCO bank have shown a huge return on the first month of demonetization and gradually the banks enjoyed more benefits after the second and third month. When it

comes to comparison of the five public sector banks, the Andhra bank has shown the huge returns due to demonetization in the first month. When the INR 500 and INR 1000 got demonetized, people started investing in stocks of various banks which indeed benefited the share prices of the banks.

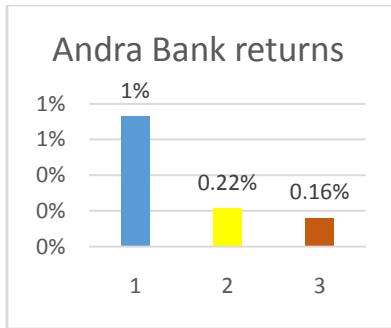


Fig: the graph depicts about the returns of Andhra bank, I; the bank showing benefits and returns in various months due to demonetization.

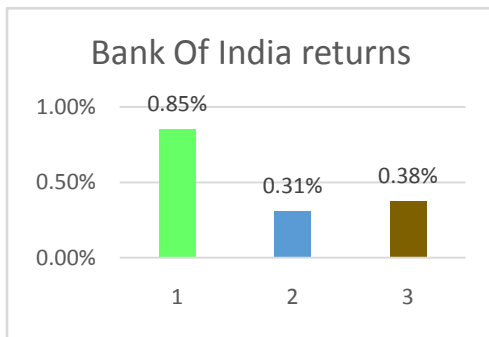


fig 2: bank of India returns

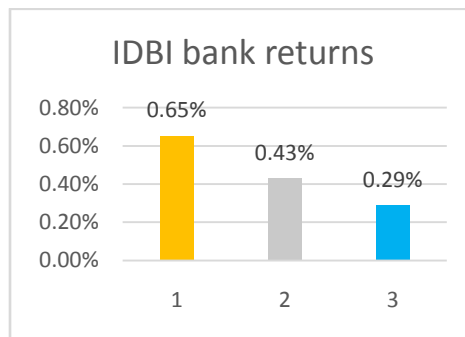


fig 3: IDBI bank returns

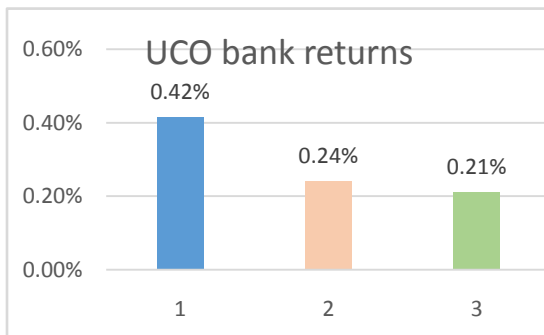


Fig 4: UCO bank returns

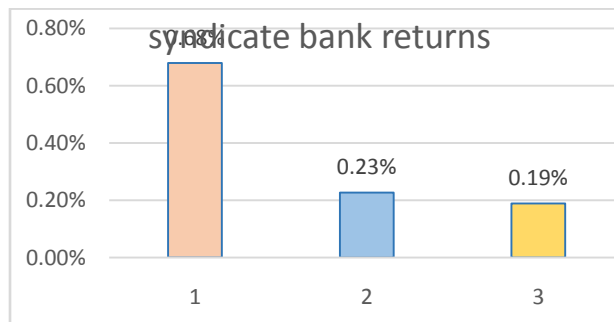


Fig 5: syndicate bank return

When it comes to the private sector banks like ICICI bank, HDFC bank, federal reserve bank, bank of Punjab and Karur Vysya bank, the analysis shows that ICICI bank, federal reserve bank and bank of Punjab has got huge returns in the first

month of demonetization and in the second and the third month there were no returns. HDFC bank and Karur Vysya bank has no returns. HDFC bank has reduced its interest rate up to 0.25% that is from 7% to 6.75% due to demonetization.

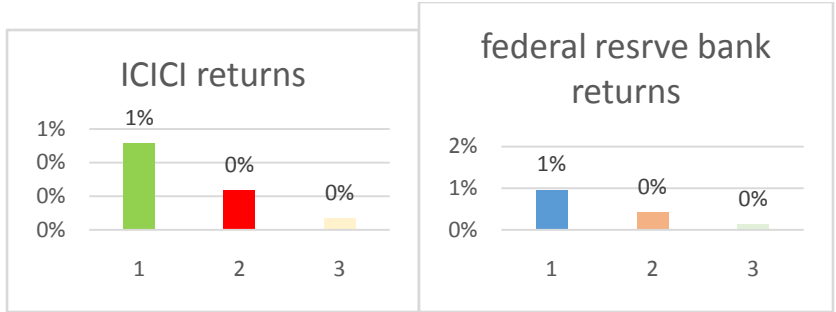


Fig 6: ICICI bank returns

Fig 7: federal reserve bank returns

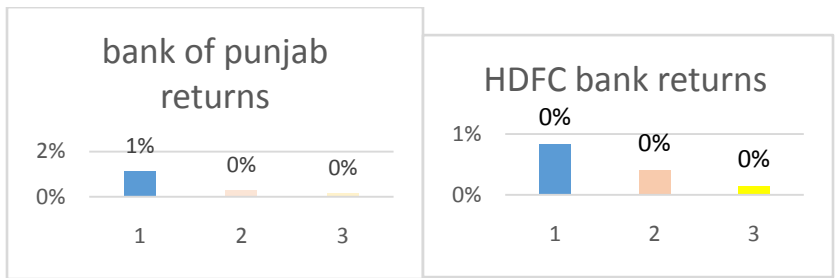


Fig 8: bank of Punjab returns

Fig 9: HDFC bank returns

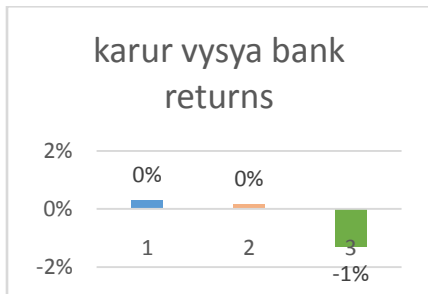


Fig 10: Karur vysya bank returns.

Conclusion:

Demonetization has created huge fluctuation in the Indian economy. Many sectors such as consumer durable goods, SME's, transport services, real estate and rural areas where many of the transactions happen through cash only. Though the scale of difficulty is high, it would benefit Indian economy in the long run as the main aim behind demonetization of INR 500 and INR 1000 is to eradicate black money and to make digital

transactions. This can be seen in future which might be down the line of 20years. As of now the only sector which was benefitted due to demonetization is banking sector. As demonetization happened people started depositing their tangible asset (cash) into banks and investing them into stocks which indeed gave huge returns to the public and private sector banks in India. When it comes to the stock prices, it a good opportunity for the public to invest in stocks of banks for a long term. The interest rates also got lower

because of low liquidity and hence banks will lend money to people at lower rates. Hence demonetization of Indian currency is a good measure when it comes to the banking sector.

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