IMPACT OF GLOBAL ECONOMIC CRISIS ON INDIAN ECONOMY: AN ANALYSIS

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Abstract - Economic crises and there spread are increasing with the increase in globalization. The origin may be different but the tremors are being felt in different parts of the world including India. The present paper seeks to analyze the impact of global economic on Indian economy which is one of the fast growing economies of the world. Currently Indian economy is facing a challenge due to global melt down. Consequently, economic activities are bound to slow down. The global economic crisis or US Meltdown, has its origin in the United States housing sector back in 2001-02, but gradually extended over a period of time and eventually brought the entire world under its grip. Though in the beginning Indian officials denied the impact of global economic crisis affecting the Indian economy but later the government had to acknowledge the fact that economic crisis will have some impact on the Indian economy. The present paper confirms that various sectors of Indian economy are affected by global recession, to a certain extent.

Key words: Global economic crisis, Slow down, Indian economy, Macroeconomic indicators.

I. INTRODUCTION

Economic crises and there spread are increasing with the increase in globalization. The origin may be different but the tremors are being felt in different parts of the world. The new economic policy of 1991 which is based on Liberalization, Privatization and Globalization (LPG), increased the rate of economic development in India. During post economic reforms Indian economy grew at the rate of 8 to 9 per cent. As a result, all macro economic indicators such as saving, investment export and import, foreign exchange reserve and level of employment increased in a considerable manner. The waves of global economic crisis are giving some trouble to India also but we do not see intensive atmosphere of recession in internal India. Though it is true in some way but till Indian economy has received a great blow of economic crisis, and it restricted our fast run of development completely. The economic crisis that developed around 2006-07 in United States of America (USA) due to which economies all over the world are considered to be entering into prolonged slowdown in economic activities. The intensity of present economic crisis is so high that is being compared with global economic recession in 1873, great depression of 1930s and East Asian crisis of 1990s. The present economic slowdown is considered to be sub-prime mortgage crisis in the financial sector of the US. As a result, the sub prime lending crisis led to the collapse of booming US housing sector. Keeping in above backdrop, the paper is organized as follows. Global economic crisis is explained in section II. Impact of global economic crisis on Indian economy is presented in section III. And lastly, Section IV concludes the paper with policy implications.

II. GLOBAL ECONOMIC CRISIS

Recession or crisis is a form of the normal business cycle. The crisis may be a traumatic or stressful change in, political, social, economic, military affairs and large-scale environmental event. The recent economic crisis is widely viewed as a glaring example of limitless pursuit of greed overindulgence at the expense of caution, prudence, due diligence and regulation. The origin of current economic crisis back to mid 2007, when three things became clear - Low income or sub prime US households that had borrowed heavily from banks and financial companies to buy homes, the size of this sub prime housing loan market was huge at about $ 1.4 trillion and Wall Street financial engineers had packaged these loans to really complicated financial instruments.

Since 2001 to 2006 U.S.A. economy was economically sound and the interest rate prevailing in various sectors were low, prices of houses were continuously increasing because of lower rate of interest and

banking sector was incurring lower profit. Therefore the banks and financial institutions in USA had thought a new idea regarding the lending, in which high rates of interests were charged and loans were given to the sub-prime lenders for purchasing the houses. These were fully aware about the risk involved in sub prime lending for housing but they have taken such risk on the belief that housing prices would never fall.

Investment in housing sector was found to be profitable to the speculators as well as banks, due to the continuously rising prices of houses. Americans have made huge speculative investment in housing sector. It caused a rise in demand for houses and housing loans in US. In order to fulfill the demand for huge loans for housing, the funds available with banks and financial institutions were found insufficient. Therefore, American banks and financial institutions introduced a new credit weapon called Mortgage Bonds. The basis of these mortgage bonds was the houses already mortgaged by the people for borrowing housing loans were again mortgaged by artificially increasing the price of houses more than their actual prices. These mortgage bonds were sold in international market. Large amounts of funds were collected by American banks by selling these mortgage bonds. These funds were utilized for financing the housing loans in US.

This housing bubble based on sub-prime loans burst in 2006-07. In the same year housing prices had declined after 15-16 years. It adversely affected the speculative investment made in housing sector. Those who had invested in houses to earn more profit, have to face losses. Therefore, they started to sell the houses but due to lack of demand, houses could not be sold. Huge over dues of housing loans were not repaid by the borrowers. Banks and financial institutions did not succeed in the recovery of these loans. The price of mortgage bonds started a steep fall resulting in loss for those who invested in mortgage bonds. Hence, the liquidity problem in America became very serious. Meltdown set in the third quarter of the year 2007. The large banks like Lehman Brothers, Merrill Synch had declared bankrupt. In USA, 19 large banks and 100 private financial institutions were declared bankrupt. Thus, the default in mortgage loans for housing is the primary reason for the financial crisis sweeping the world.

III. IMPACT OF GLOBAL ECONOMIC CRISIS ON INDIAN ECONOMY

The Indian economy had performed well during the last two decades, resulting in high growth rate of real Gross Domestic Product (GDP), besides increase in domestic savings and increase in investment and productivity. Though the epicenter of the economic crisis was the US sub prime mortgage market, its agitations are being felt in financial markets all over the world. Though in the beginning Indian officials denied the impact of global economic crisis affecting the Indian economy but later the government had to acknowledge the fact that global crisis will have some impact on the Indian economy.

The US meltdown which shook the world had little impact on India, because of India's strong fundamental of the economy, well regulated banking system and less exposure of Indian financial sector with the global financial market. Perhaps this has saved Indian economy from being swayed over instantly. Unlike in US where capitalism rules exist, in India, market is closely controlled by the government. The meltdown in the U.S. has not created any credit crunch in Indian economy but the credit crunch in U.S. led to panic in India. After a long spell of growth Indian economy experiencing a downturn, faltering of industrial growth, double digit inflation, widening of current account deficit etc.

The global crisis affected the health of several sectors of Indian economy through distinct channels: financial markets, trade flows, export & inport and exchange rates. The following table-1 presents the impact of global economic crisis on the growth rate of Gross Domestic Product (GDP) in various sectors of Indian economy. To analyze the impact of global slowdown for the Indian economy, a comparative analysis is made between the growth rates of sectoral GDP during pre meltdown and meltdown years.

TABLE 1: GROWTH RATE OF GDP (SECTOR WISE) IN INDIA

	Pre-Meltdown Years		Meltdown Years	
Sectors	**2006-07**	**2007-08**	**2008-09**	**2009-10**
1.Agriculture, Forestry & Fishing	3.7	4.7	1.6	-0.2
2.Mining & Quarrying	8.7	3.9	1.6	8.7
3.Manufacturing	14.9	10.3	3.2	8.9
4.Electricity, Gas & Water Supply	8.5	10.0	3.9	8.2
5.Trade, Hotels & Restaurants	11.2	9.5	5.3	8.3
6.Construction	10.6	10.0	5.9	6.5
7.Transport, Storage & Communication	12.6	13.0	11.6	N.A.
8.Finance,Insurance,RealEstate&Business Services	14.5	13.2	10.1	9.9
9.Community, Personal & Social Services	2.6	6.7	13.9	8.2
Total GDP from all sectors	**9.7**	**9.2**	**6.7**	**7.2**

The above table 1 depicts that among all sectors of the Indian economy, mining, and manufacturing and to some extent trade was affected by the economic meltdown in 2007-08. It occurred due to fall in the demand for India's iron ore and decline in exports particularly garments exports. Despite that Indian economy sustained an impressive growth rate of 9.2 per cent in 2007-08. This was the second highest growth rate next only to China in the whole world. And this is in contrast to the shrinking of the real economies of many western economies. However, the Indian economy could not withstand the impact of global meltdown beyond 2007-08.

In 2008-09 there was an all round decline in the growth rates of GDP from almost all sectors except from community, personal and social services. Consequently, the GDP of the country could grow only at 6.7 per cent in 2008-09, a decline of 2.5 per cent over the previous year. But the Indian economy started recovering from the slowdown towards the end of the fiscal year 2009-10. This is evident from the 7.2 per cent growth rate of GDP. Except agriculture which suffered a negative growth rate of 0.2 per cent and transport, real estate, finance and community and social services, all other sectors have shown recovery. Notably, mining, manufacturing, construction and electricity generation have shown remarkable recovery.

Apart from GDP, the bigger concern is the employment implications of economic crisis. The Ministry of Labour and Employment conducted a survey on a fairly large sample size across sectors such as Textiles, Automobiles, Gems & Jewellery, Metals, Mining, Construction, Transport and BPO/ IT sectors and states that five lakh workers lost jobs in the last quarter of 2008. The employment in these sectors went down from 16.2 million during September 2008 to 15.7 million during December 2008. However, in the manual contract category of workers, the employment has declined in all the sectors/ industries covered in the survey. Employment had declined in the Automobiles and Transport sectors by 12.45 per cent and 10.18 per cent respectively. The overall decline in employment in the manual contract category was 5.83 per cent. In the direct category of manual workers, the major employment loss reached to 9.97 per cent in case of Gems & Jewellery, followed by 1.33 per cent in Metals. The continuous process of job losses in exports and manufacturing, particularly the engineering sector and even the services sector was a big challenge for the government.

International trade declined as a result of the financial and economic crisis. Between July, 2008 and May, 2009 the value of world trade declined by 37 per cent, of which 16 per cent was due to the fall in prices. The WTO estimates projected that global trade is likely to decline by 9 per cent in volume terms and the IMF estimates projected a decline of over 11 per cent for 2009. Though India has not been affected to the same extent as other economies of the world during this phase, yet the declining trend in the growth rate of our exports and imports, have started in second and third quarter of the year 2008-09 respectively. The quarterly growth performance of exports and imports of India are shown in the following table-2

TABLE 2: QUARTERLY GROWTH RATE OF EXPORTS & IMPORTS IN INDIA

	2008-09		2009-10	
Quarters	**Exports**	**Imports**	**Exports**	**Imports**
I	57.0	38.7	-38.6	-35.0
II	39.5	73.8	-21.0	-33.6
III	-4.0	7.4	6.0	1.2
IV	-20.3	-24.0	N.A.	N.A.

The table-2 shows that growth rate of exports and imports declined in 2008-09 and turned to be negative significantly in the IV quarter of the year 2008-09. During, first quarter of 2009-10 growth rates of both exports and imports become highly negative. But due to the export specific stimulus measures adopted in Indian economy, started stimulating the exports and as a result the growth rate of exports turned positive at 6 per cent in the third quarter.
The overall effect of the global economic crisis on country's external sector can be well analyzed through the Balance of Payments position of the economy. BoP comprises current account, capital account, errors and omissions and changes in foreign exchange reserves. Under current account of the BoP, transactions are classified into merchandise (exports and imports) and invisibles. Under capital account, capital inflows can be classified by instrument (debt or equity) and maturity (short or long-term). The main components of capital account include foreign investment, loans and banking capital. Thus, the BoP summary gives a clear picture of the overall performance of the economy especially the external sector. The following figure-1 represents the BoP position of Indian economy during 2005-06 to 2010-11

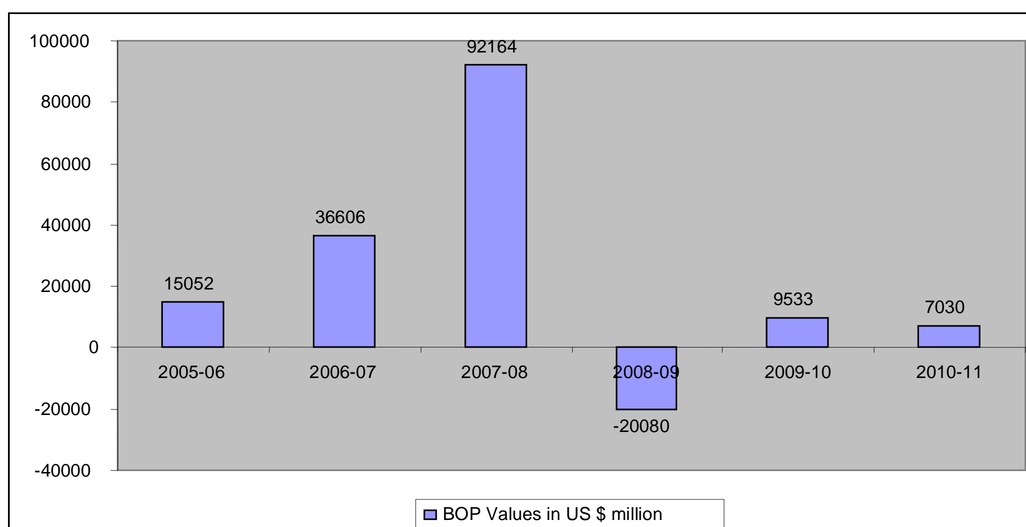

FIGURE 1: INDIA'S BALANCE OF PAYMENT POSITION- OVERALL BALANCE

The above figure clearly indicates that the overall balance of BoP has been improving since 2005-06. But during 2008-09, the overall BoP balance turned negative i.e., -20080 US $ million showing that global financial crisis severely hit the flow of capital into the country. However, the economy recovered from the sudden shock of the crisis thereby making positive balance in country's BoP account by the year 2009-10 and onwards.
In the present global scenario, India has been considered as the most promising and fast growing economy in the world. Due to the liberalized rules for Foreign Direct Investment (FDI) in Indian economy, the real estate, telecommunication, service sector, construction activities, power etc have become very attractive investment avenues for both the domestic as well as foreign investors. Similarly, due to the increased activities of Foreign Institutional Investors (FIIs) like mutual funds, pension funds etc, the Foreign

Portfolio Investment in the country has witnessed tremendous upswing during 2000s. The overall foreign investment in India met serious setback during the global economic crisis. The following table-3 reveals the position of income flow and foreign investment in India.

TABLE 3: FOREIGN INVESTMENT & INCOME FLOW IN INDIA

Years	Foreign Investment in India		Income Flow to India	
	Values in Crores	Percentage Change	Values in Crores	Percentage Change
2001-02	73435	---	16080	---
2002-03	67401	-8.22	17049	6.03
2003-04	148811	107.84	17909	5.04
2004-05	210047	41.15	20638	15.24
2005-06	341818	62.73	28426	37.74
2006-07	597139	74.69	42016	47.81
2007-08	1082001	81.19	57300	36.38
2008-09	737696	-31.82	65512	14.33
2009-10	N.A.	---	62016	-5.44

It is cleared from the above table-3 that the foreign investment in India has been growing at a faster rate since 2003-04. However, during 2008-09, the very year hit by the crisis, the foreign investment declined significantly showing a negative growth rate of 31.82 per cent. A similar trend of decline in growth is found in case of income flow to India during 2008-09 and 2009-10.

The Indian financial sector was not untouched from the impact of global economic crisis. As the stock markets collapsed in USA and Europe, there was panic in the Indian stock markets. The foreign institutional investors (FIIs) who had invested in Mumbai stock market suddenly withdrew their investment. This naturally dipped the BSE sensex. The value of sensex which reached 17,578 on February 2008 declined to 16,371 on March 28th, 2008. It further declined to 14,043 on July 6th, 2009 because of the net selling by the foreign institutional investors (FIIs). Such decline was noticed in many other Asian stock markets also and this can be shown through the following table-4

TABLE 4: CUMULATIVE CHANGE OF EQUITY INDEX OVER 2003 LEVEL IN ASIAN STOCK MARKETS (POINTS)

Equity Index	2007	2008	2009	2010
BSE Sensex (India)	247.4	65.2	199.1	251.2
Hang Seng Index (Hong Kong)	121.2	1.1	74.2	83.2
Nikkei 225 (Japan)	43.4	-22.9	-5.3	-4.2
TSEC Weighed Index (Taiwan)	44.4	-25.2	32.3	35.3
SSE Composite Index (China)	251.5	43.7	116.9	87.6

Table- 4 reveals the change in equity index value of share indices of major Asian economies in major Asian Stock Markets after the financial crisis. It may be observed that the downward pressure on the share values was severe in 2008. But the recovery in share values had occurred in 2009 and 2010 in some Indian and Chinese stock markets because of economic stimulus measures announced by their governments.

Last but not least, the economic crisis significantly affected the poverty scenario in India. The increased job losses in the manual contract category in the manufacturing sector and continued lay offs in the export sector have forced many to live in penury. The World Bank has served a warning through its report, “The Global Economic Crisis: Assessing Vulnerability with a Poverty Lens,” which counts India among countries that have a “high exposure” to increased risk of poverty due to the global economic downturn. Thus, Indian economy was severely hit by the global economic crisis. Almost all sectors faced the negative consequences of crisis to a certain extent in India.

IV. CONCLUSION & POLICY IMPLICATIONS

In the concluding words we can say, India cannot escape unscathed present crisis because its economy has become more integrated with rest of the world over the past two decades. In order to overcome the global economic crisis, monetary and fiscal stimulus package are essential. More transparency is required in the process of setting bank rate, repo rate, reverse repo rate, CRR, SLR etc. The RBI must lower the policy rates further to bring down the costs of funds and boost the growth momentum. The link between monetary policy and financial stability need to be understood and more autonomy to the central bank should be given to maintain the enviable reputation earned by RBI. Monetary & fiscal policy both should be co-ordinated for overall better performance of Indian economy.

India has huge domestic demand which need to be tapped.There should be quick and consistant policy making which can transmit positive signals to the private sector for boosting the investment levels in the economy. Black money should be brought back and corruption should be controlled.Ethical and moral standards should be enhanced. To speed up the pace of economic development and to attract foreign direct investment in Indian economy, there is an urgent need to ensure the protection of investors, their lives and money through maintaining the proper law and order. For a country like India, there is a rationale to protect the rural economy from adverse effects of global crisis by protecting agriculture, local business and services so that projected growth rate would be maintained. The protection of rural economy increases the purchasing power of 70% of the total population which provides sound base to the Indian economy. Entrepreneurship development in both rural & as well as urban areas should be focused. The amount of budget deficit should be increased in the field of infrastructure projects viz. national highway, airport, electricity sector etc. to boost the overall performance of Indian economy.

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