The Global Financial Crises (2008) and It’s Impact on Indian Economy

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Abstract

The global financial crisis of 2008

The term financial crisis is applied broadly to a variety of situations in which some financial institutions or assets suddenly lose a large part of their value. In the 19th and early 20th centuries, many financial crises were associated with banking panics, and many recessions coincided with these panics. Other situations that are often called financial crises include stock market crashes and the bursting of other financial bubbles, currency crises, and sovereign defaults. The crisis led to a liquidity problem and the de-leveraging of financial institutions in the United States and Europe. In this paper, an attempt has been made to study the impact of Global crisis on the Indian economy.
Origins

The roots of the credit crisis stretch back to another notable boom-and-bust: the tech bubble of the late 1990’s. When the stock market began a steep decline in 2000 and the nation slipped into recession the next year, the Federal Reserve sharply lowered interest rates to limit the economic damage.

Lower interest rates make mortgage payments cheaper, and demand for homes began to rise, sending prices up. In addition, millions of homeowners took advantage of the rate drop to refinance their existing mortgages. As the industry ramped up, the quality of the mortgages went down. And turn sour they did, when homebuyers had to leverage themselves to the hilt to make a purchase. Default and delinquency rates began to rise in 2006, but the pace of lending did not slow. Banks and other investors had devised a plethora of complex financial instruments to slice up and resell the mortgage-backed securities and to hedge against any risks — or so they thought.

Crisis in the US

The United States entered 2008 during a housing market correction, a subprime mortgage crisis and a declining dollar value.

In February, 63,000 jobs were lost, a 5-year record.
In September, 159,000 jobs were lost, bringing the monthly average to 84,000 per month from January to September of 2008.

On September 5, 2008, the United States Department of Labor issued a report that its unemployment rate rose to 6.1%, the highest in five years.
The defaults on sub-prime mortgages (homeloan defaults) have led to a major crisis in the US.
Foreclosures spread like wildfire putting the US economy on shaky ground. This, coupled with rising oil prices at $100 a barrel, slowed down the growth of the economy.
The housing market soared on the back of easy availability of loans.
The realty sector boomed but could not sustain the momentum for long, and it collapsed under the gargantuan weight of crippling loan defaults.
Sub-prime is a high risk debt offered to people with poor credit worthiness or unstable incomes. Major Banks have landed in trouble after people could not pay back loans.

**Liquidity Crisis**

In early July, depositors at the Los Angeles offices of Indy Mac Bank frantically lined up in the street to withdraw their money.

On July 11, Indy Mac - the largest mortgage lender in the US - was seized by federal regulators. The mortgage lender succumbed to the pressures of tighter credit, tumbling home prices and rising foreclosures.

Bank of America agreed to purchase Merrill Lynch, the insurance company AIG sought a bridge loan from the Federal Reserve and a consortium of 10 banks created an emergency fund of at least $70 billion to deal with the effects of Lehman's closure. The biggest bank failure in history occurred on September 25 when JP Morgan Chase agreed to purchase the banking assets of Washington Mutual.

The year 2008 as of September 17 has seen 81 public corporations file for bankruptcy in the United States, already higher than the 78 in 2007. Lehman Brothers being the largest bankruptcy in U.S. history also makes 2008 a record year in terms of assets with Lehman's $691 billion in assets all past annual totals.

The year also saw the ninth biggest bankruptcy with the failure of Indy Mac Bank. On September 29, Citigroup beat out Wells Fargo to acquire the ailing Wachovia's assets will pay $1 a share, or about $2.2 billion. In addition, the FDIC said that the agency would absorb the company's losses above $42 billion; in exchange they would receive $12 billion in preferred stock and warrants from Citigroup in return for assuming that risk.

**Federal fund rate**

In the United States, the federal funds rate is the interest rate at which private
depository institutions (mostly banks) lend balances (federal funds) at the Federal Reserve to other depository institutions, usually overnight. It is the interest rate banks charge each other for loans. Changing the target rate is one form of open market operations that the Chairman of the Federal Reserve uses to regulate the supply of money in the U.S. economy.

**Impact of federal funds rate cuts**

The Federal Reserve has responded to a potential slow-down by lowering the target federal funds rate during recessions and other periods of lower growth. In fact, the Federal Reserve lowering has recently predated recessions because as interest rates are increased to slow economic growth, interest payments on all debts rise. To the extent these increases in debt service leads to defaults and forced selling, this can be extremely destructive to asset values and the financial system, as seen in 2008. The charts show the impact on S&P 500 and short- and long-term interest rates. Bill Gross of Pimco has suggested that in the past 15 years, every time the fed funds rate was higher than the nominal GDP growth rate, assets such as stocks and/or housing always fell. He even suggested that the best way to price the fed funds rate would be 100 basis points below the nominal GDP growth rate.
Federal rate list

<table>
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<tr>
<th>Date</th>
<th>0.00–0.25%</th>
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<tbody>
<tr>
<td>Dec 16, 2008</td>
<td>0.00–0.25%</td>
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<tr>
<td>Oct 29, 2008</td>
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<td>Oct 8, 2008</td>
<td>1.50%</td>
<td>1.75%</td>
</tr>
<tr>
<td>Apr 30, 2008</td>
<td>2.00%</td>
<td>2.25%</td>
</tr>
<tr>
<td>Mar 18, 2008</td>
<td>2.25%</td>
<td>2.50%</td>
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<tr>
<td>Mar 16, 2008</td>
<td>3.00%</td>
<td>3.25%</td>
</tr>
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<td>Jan 30, 2008</td>
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<td>3.50%</td>
</tr>
<tr>
<td>Jan 22, 2008</td>
<td>3.50%</td>
<td>4.00%</td>
</tr>
</tbody>
</table>

Table 1.1

Methodology

The study of research methods provides you with the knowledge and skills you need to solve the problems and meet the challenges of the past paced decision making environment. We define business research as a systematic enquiry whose objective is to provide information to solve the managerial problems. The present study attempts to analyses the 2008 global financial crises and its impact on Indian economy.

OBJECTIVES

1. To study the global financial crises

2. To analyse the impact of global financial crises on world economy

3. To analyse the impact of global financial crises on Indian industry

4. To measure the impact of global financial crises on Indian stock exchange.

Method of Data Collection:

Information for any research has been gathered from the primary and the secondary sources. Primary data is to be collected originally, the entire scheme of the plan starting with the definitions of various terms used, units to be employed, type of enquiry to be conducted, extent of accuracy aimed at, etc. is to be formulated whereas the collection of secondary data is in the form of mere compilation of the existing data.

A proper choice of the data (primary or
secondary) needed for any statistical investigation is to be made after taking into consideration the nature, objective & scope of the enquiry. As the data was not collected from any original source, so source of data collection here was secondary.

3.4 Secondary Sources:

The secondary data included the study of the various research papers in the field of project financing and the credit appraisal. The secondary research primarily dealt with the advanced mathematical model used in appraising the projects.


IMF report
World Bank report
RBI monthly report
FICCI report
ILO report

3.6 Published Sources:

There are a number of national organizations (govt. semi govt. and private Organizations) and also international agencies which collect statistical data related to business, Trade, labour, prices, consumption, production, industries, income etc. and publish the findings in statistical reports on a regular basis. These publications of various organizations serve as a very powerful source of secondary data, like CMA data issued by RBI for checking the industry scenario of the project.

Data of economy and stock markets.
Limitation of study:

Every research study has its own loophole which are able to affect the findings of it. This study also has its own limitation. These are given below:

1. Regular changes in economic condition of the country because of recession in the global market

2. Current data is not available because of the ongoing financial year

3. One of the basic limitations of the research is that the research only consist of a limited number of sectors under study, this is due to the time constraint and also due to the fact that a large number bottleneck in collecting the data on accurate bases.

4. Furthermore, the research attempts only on qualitative aspect and thus views can differ and no precise accurate conclusion can be derived.

Impact of Global crisis on India: The Good, Bad & Ugly

<table>
<thead>
<tr>
<th>Least Impact</th>
<th>Mildly Impact</th>
<th>Most Impact</th>
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<tbody>
<tr>
<td>Pharmaceuticals</td>
<td>Power equipments &amp; Services</td>
<td>Bank</td>
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<tr>
<td>Oil &amp; Gas</td>
<td>Retail</td>
<td>Financial Services</td>
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<tr>
<td>FMCG</td>
<td>Hospitality</td>
<td>Real Estate</td>
</tr>
<tr>
<td>Media &amp; Entertainment</td>
<td>Logistics</td>
<td>Infrastructure</td>
</tr>
<tr>
<td>Auto</td>
<td>Information technology</td>
<td></td>
</tr>
<tr>
<td>Hospitality &amp; Tourism</td>
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</tr>
</tbody>
</table>
Indian Financial Services

Impact: Most impacted

① The US sub-prime market crisis, which so far caused losses worth $181 billion to the world’s top 45 banks by the end of FY08, has started hitting Indian banks also.

② India’s large the world’s top 45 banks by the end of FY08, has started hitting Indian loss of about Rs. 1056 crores owing to the sub prime crisis of US in the FY08 results.

③ The public sector banks have had a limited position in the structured products and therefore impact is expected to be minimal. However negative sentiments will hit harder.

④ Punjab national Bank, Bank of India, State Bank of India, Bank of Baroda were major banks having an exposure to the instruments issued by Lehman and Merrill Lynch.

⑤ However the banking sector in general will have to face tight liquidity conditions apart from further mark-to-market losses. The net non performing assets of entire banking sector is less than 2% and it is well capitalized the capital adequacy ratio is around 13% as against the statutory requirement of 8 to 9%.

Financial market

Indian Stock Markets are one of the oldest in Asia. Its history dates back to nearly 200 years ago. The earliest records of security dealings in India are meagre and obscure. The East India Company was the dominant institution in those days and business in its loan securities used to be transacted towards the close of the eighteenth century.

At the end of the American Civil War, the brokers who thrived out of Civil War in 1874, found a place in a street (now appropriately called as Dalal Street) where they would conveniently assemble and transact business. In 1887, they formally established in Bombay, the "Native Share and Stock Brokers' Association" (which is alternatively...
known as "The Stock Exchange"). In 1895, the Stock Exchange acquired a premise in the same street and it was inaugurated in 1899. Thus, the Stock Exchange at Bombay was consolidated.

India's oldest and first stock exchange: Mumbai (Bombay) Stock Exchange. Established in 1875. More than 6,000 stocks listed.

Total number of stock exchanges in India: 22

They are in: Ahmedabad, Bangalore, Calcutta, Chennai, Delhi etc.

There is also a National Stock Exchange (NSE) which is located in Mumbai.

There is also an Over the Counter Exchange of India (OTCEI) which allows listing of small and medium sized companies.

The regulatory agency which oversees the functioning of stock markets is the Securities and Exchange Board of India (SEBI), which is also located in Bombay. SEBI's website location is at http://www.sebi.gov.in but you need a password to access it.

There are mainly two stock exchanges which is important because of liquidity availability and no of company register in it.

NSE (national stock exchange)
BSE (Bombay stock exchange)

**National stock exchange**

With the liberalization of the Indian economy, it was found inevitable to lift the Indian stock market trading system on par with the international standards. On the basis of the recommendations of high powered Pherwani Committee, the National Stock Exchange was incorporated in 1992 by Industrial Development Bank of India, Industrial Credit and Investment Corporation of India, Industrial Finance Corporation of India, all Insurance Corporations, selected commercial banks and others.

Trading at NSE can be classified under two broad categories:

(a) Wholesale debt market and
(b) Capital market.

Wholesale debt market operations are similar to money market operations - institutions and corporate bodies enter into high value transactions in financial instruments such as government securities, treasury bills, public sector unit bonds, commercial paper, certificate of
There are two kinds of players in NSE:
(a) Trading members and
(b) Participants.
Recognized members of NSE are called trading members who trade on behalf of themselves and their clients. Participants include trading members and large players like banks who take direct settlement responsibility.
Trading at NSE takes place through a fully automated screen-based trading mechanism which adopts the principle of an order-driven market. Trading members can stay at their offices and execute the trading, since they are linked through a communication network. The prices at which the buyer and seller are willing to transact will appear on the screen. When the prices match the transaction will be completed and a confirmation slip will be printed at the office of the trading member.
NSE has several advantages over the traditional trading exchanges. They are as follows: NSE brings an integrated stock market trading network across the nation.
Investors can trade at the same price from anywhere in the country since inter-market operations are streamlined coupled with the countrywide access to the securities.
Delays in communication, late payments and the malpractice's prevailing in the traditional trading mechanism can be done away with greater operational efficiency and informational transparency in the stock market operations, with the support of total computerized network. Unless stock markets provide professionalized service, small investors and foreign investors will not be interested in capital market operations. And capital market being one of the major sources of long-term finance for industrial projects, India cannot afford to damage the capital market path. In this regard NSE gains vital importance in the Indian capital market system.
## Nifty and Dow Jones one year comparison (2008)

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<th>DOW JONES</th>
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</tr>
<tr>
<td>Feb</td>
<td>5223.5</td>
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<tr>
<td>May</td>
<td>4870.1</td>
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<td>June</td>
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<td>July</td>
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<td>Aug</td>
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<td>Sep</td>
<td>3921.2</td>
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<td>Dec</td>
<td>2959.15</td>
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**TABLE: 1.2**
COMPARISON OF NIFTY AND DOW JONES

FIG: 1

INTERPRETATION:

This figure shows the how nifty is directly linked with American exchange Dow Jones. Both these index show similar pattern of fall and rise with in a year from Jan 2008-mar 2009.this chat show that how NSE NIFTY is positively correlated with DOW JONES.

Both these index show similar patter of movements. This show that how our market is affected with the fall of American DOW index because of recession.
Bombay stock exchange:
Today, BSE is the world’s number 1 exchange in terms of the number of listed companies and the world’s 5 in transaction number. Of the 23 stock exchanges in the India, Bombay Stock Exchange is the largest, with over 6,000 stocks listed. The BSE accounts for over two thirds of the total trading volume in the country. Established in 1875, the exchange is also the oldest in Asia. Among the twenty-two Stock Exchanges recognized by the Government of India under the Securities Contracts (Regulation) Act, 1956, it was the first one to be recognized and it is the only one that had the privilege of getting permanent recognition ab-initio. Moreover, The BSE SENSEX is not only scientifically designed but also based on globally accepted construction and review methodology. The index is widely reported in both domestic and international markets through print as well as electronic media. The "Free-float Market Capitalization" methodology of BSE index construction is regarded as an industry’s best practice globally. All major index providers like MSCI, FTSE, STOXX, S&P and Dow Jones use the Free-float methodology. Due to its wide acceptance amongst the Indian investors; SENSEX is regarded to be the pulse of the Indian stock market. As the oldest index in the country, the SENSEX has over the years become one of the most prominent brands in the country. The paper therefore emphasizes mainly on BSE sensex and major fluctuations related to it from time period of 2006 to 2008. The paper also put the light on how various factors such as inflation, investments made through participatory notes, rising crude oil prices, the sub-prime mortgage woes in US, concerns over a slowing down US economy and big role of Foreign Institutional Investors (FIIs) determines market’s situation and operate SENSEX.
Sensex and Dow Jones one year comparison (2008)

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<th>DOW JONES</th>
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<tr>
<td>Dec</td>
<td>9647.31</td>
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</tr>
</tbody>
</table>

TABLE: 1.3

COMPARISON OF BSE SENSEX AND DOW JONES

FIG: 2

The Global Financial Crises (2008) and It’s Impact on Indian Economy
INTERPRETATION:
This graph shows the movement of two indexes in blue line show BSE sensex index of India movement and red line show DOW JONES of America index movement. This figure shows how BSE move in the similar direction where the DOW index moves throw out a year from Jan 2008-Mar 2009.

Govt sets up top body to handle impact of global financial crisis
A day after an interactive session with top honchos of industry to get their feedback on tackling the impact of global financial crisis on the country, Prime Minister Manmohan Singh today set up an apex group headed by him to coordinate government’s response to various issues raised by industry from time to time.

Ministers of Finance
Commerce and Industry, Deputy Chairman of Planning Commission and Reserve Bank Governor will be members of the top body, an official statement said this evening.

The apex group will meet regularly to coordinate and decide government’s response to points raised by industry from time to time with regard to the current global financial crisis and its impact on India, the statement added. Industry has been demanding cut in interest rate, relaxing norms for external commercial borrowing, and more government expenditure on infrastructure to tide over the crisis which has hit hard various sectors of the economy.

The Prime Minister has also approved a committee of officers headed by Finance Secretary that will meet daily or as often as required to consider issues raised by Industry. Commerce Secretary, Secretary of Department of Policy and Promotion, Secretary of Planning Commission will be members of the committee, the statement said, adding Joint Secretary(banking) will be government’s contact person to get industry’s suggestions.

INSTITUTIONAL INVESTOR:
An institutional investor is an investor, such as a bank, insurance company, retirement fund, hedge fund, or mutual fund that is financially sophisticated and
makes large investments, often held in very large portfolios of investments. Because of their sophistication, institutional investors may often participate in private placements of securities, in which certain aspects of the securities laws may be inapplicable.

**Type of institutional investor**

**Domestic institutional investor**

It is used to denote an investor - mostly of the form of an institution or entity, which invests money in the financial markets of its own country where the institution or entity was originally incorporated. In India, there are broadly four types of institutional investors.

![Diagram of Institutional Investors]

**FIG: 3**
FOREIGN INSTITUTIONAL INVESTOR (FII)

It is used to denote an investor - mostly of the form of an institution or entity, which Invests money in the financial markets of a country different from the one where in the institution or entity was originally incorporated. FII investment is frequently referred to as hot money for the reason that it can leave the country at the same speed at which it comes in. In countries like India, statutory agencies like SEBI have prescribed norms to register FIIs and also to regulate such investments flowing in through FIIs.

- Pension Funds
- Mutual Funds
- Investment Trust
- Insurance or reinsurance companies
- Endowment Funds
- University Funds
- Foundations or Charitable Trusts or Charitable Societies
- Asset Management Companies
- Nominee Companies
- Institutional Portfolio Managers
- Trustees

The sources of these FII flows are varied. The FIIs registered with SEBI come from as many as 28 countries (including money management companies operating in India on behalf of foreign investors).

US-based institutions accounted for slightly over 41%; those from the UK constitute about 20% with other Western European countries hosting another 17% of the FIIs. It is, however, instructive to bear in mind that these national affiliations do not necessarily mean that the actual investor funds come from these particular countries. Given the significant financial flows among the industrial countries, national affiliations are very rough indicators of the ‘home’ of the FII investments. In particular institutions operating from Luxembourg, Cayman Islands or Channel Islands, or even those based at Singapore or Hong Kong are likely to be investing funds largely on behalf of residents in other countries.

SOURCES OF FII IN INDIA:
FII REGISTERED IN INDIA:
Let’s look at some of the data to get an
idea about the trend of FIIs in India, and
also to see the future direction of their
movement. India had 528 FIIs were
registered with SEBI by end of 2001 and
by end of Feb-2008 the number
increased to 1303. The trend in the
number of registered FIIs has been
consistently on the rise as can be seen
from the table; showing the significant
amount of confidence that Indian Capital
market has developed in the last few
years.

CONCLUSION
As we started our research works with
the aim to find out the global financial
crises causes and its impact on Indian
economy and Indian stock market. To
achieve this aim we started with the
analysing
The subprime mortgage financial crisis,
which has yet to be resolved, is the sharp
rise in foreclosures in the subprime
mortgage market that began in the
United States in 2006 and became a
Rising interest rates increased the
monthly payments on newly-popular
adjustable rate mortgages and property
values suffered declines from the demise
of the United States housing bubble,
leaving home owners unable to meet
financial commitments and lenders
without a means to recoup their losses.
The effects of the meltdown spread
beyond housing and disrupted global
financial markets (see financial
contagion and systemic risk) as
investors, largely deregulated foreign
and domestic hedge funds, were forced
to re-evaluate the risks they were taking
and consumers lost the ability to finance
further consumer spending, causing
increased volatility in the fixed income,
equity, and derivative markets.
Under the present conditions, banks may be expected to be shy in advancing credit. Despite the massive amount of liquidity injection resorted to by the US Federal Reserve credit growth has barely responded. However, there is a world of difference between the financial conditions of banks in the US, many of which still face prospects of making further large provisions on their bad asset portfolio and the banks in India – and for that matter in many other parts of Asia. However, it is difficult for Indian banks to completely escape the environment and not to be influenced by fears of loan losses. Thus, policy has to try and also use other channels for making sure that funds flow to meet the needs of commerce and business. One method of doing so is to create adequate financing for non-bank channels that are of particular importance in the financing of commercial vehicles, two and three wheelers, construction equipment and passenger cars.

The aggregate of measures taken since September through early January has resulted in a reduction of the CRR to 5.0 from 9.0 per cent; of the repo rate to 5.5 from 9.0 per cent; and of the reverse repo rate to 4.0 from 6.0 per cent.

The number of people out of work in Asia could surge by 23.3 million this year as the global financial crisis continues to batter the region’s economies, according to a study released on Wednesday.

After the collapse of Lehman Brothers, equity markets across the world took a nose dive. The plunge proceeded within a tight range, with little apparent discrimination between markets. In the North America, West Europe, Japan and Australia stock indices fell by 30–40 per cent.

After hitting bottom in late October and then further lows in late November 2008, equity markets seem to be trying to move towards a kind of stabilisation at lower levels. Most markets, including India’s, have recovered between 10 and 20 per cent from their post-Lehman bottom with Latin American and some Asian markets making up more ground.

The trend in the decline, plunge and the recovery seems to have had a generic character and was not closely related to the extent these markets had gained prior...
to 2008. However, the equity markets remain vulnerable and it will take some time before they may be regarded to have stabilised. It would appear that significant improvement will have to await some signs of economic recovery and improvement in corporate earnings which cannot be reasonably expected before the second half of 2009.

Foreign investment certainly are influencing the Indian stock market but the extent of this influence cannot be determined or rather the extent of India’s dependence on the FIIs is a subjective issue as on no clear grounds can we see a permanent relationship between the stock market returns and the Foreign inflows. But to generalize they have shown a positive relation most of the time apart from a few occasions where the behavior of their relation was difficult to explain.

It expects that in 2009/10, the Indian economy is likely to remain relatively weak in the first quarter (April–June) and slowly pick up thereafter; that the economy would show fairly strong recovery in growth in the second half of the fiscal (Oct 2009 to Mar 2010) assuming an improvement in international economic and financial conditions in the second half of 2009. Overall, growth in 2009/10 would be between 7.0 and 7.5 per cent or somewhat above that, with the first half of the year averaging growth close to 7.0 per cent and the second half with average growth of close to 7.5 per cent or higher. This outcome factors in the impact of monetary easing, fiscal stimulus and other administrative measures to keep the growth engine running in the economy

The direct impact of funding constraints on the investment plans of Indian corporates and hence on growth and job creation, together with the second order effects of this development, coupled with the compression in export markets and the second order effects on this count, are the two principal channels through which the impact of the global financial and economic crisis are being felt in India. addition, there is of course the intangible, but not insubstantial, impact of weaker investor and business confidence due to the bad news and uncertainty flowing out of the advanced
economies and the lack of clarity regarding how long it would take for the resolution of the underlying problems.

To summarise, the US, the EU and Japan, there will be a prevalence of recessionary conditions for at least the first half of 2009, with the possibility that this may extend into the third quarter, with some recovery in the fourth quarter of 2009. Furthermore, although the IMF has not yet put out estimates of growth for 2010, the feeling seems to be that when the advanced economies do return to recovery it may not be very vigorous, as some of the financial workout will remain to be completed. This is captured by the European Commission when it sees the EU growing at 1.1 per cent in 2010, with another major institution placing EU prospects below 1 per cent and that of the US at the long-term trend rate of growth of 2.8 per cent.

**Recommendation**

However the many months of tight monetary policy and its consequent effect on drying up domestic liquidity had forced Indian companies to look externally for financing. This forced and increased International exposure has seriously compromised the Indian industry because of turmoil in the International Financial Markets and the rapid devaluation of the Indian Rupee. In addition the risk aversion that has suddenly crept into the Domestic banking sector on account of the International Banking crisis have created a situation of deep concern and threat for the real economy and all the players in it.

Do not focus on stock market alone; focus on “Real Economy”

Liquidity that has been infused into the market following the recent CRR cuts would be quickly absorbed to meet the outstanding commitments. Given this scenario it is important to inject a fresh dose of liquidity much ahead in time. Central bank must further bring down the CRR from the present 6.5% to 4.5% - the same level as was seen in the year 2004.

Cut repo rate by another 50 basis points immediately and bring it...
down to 5% in the near term. This would send a strong signal to the banks to revise their PLR downwards.

Banks must completely deliver on all sanctioned loan limits to corporates.

Protecting against systemic defaults by NBFCs by converting them to Banks and bringing them under regulation

Government to lift foreign investment restrictions and review caps in sectors like insurance, telecom, multi-product retail and aviation

Focus on agricultural loans immediately.

Public investment needs to be accelerated to pump prime the economy through increased infrastructure projects.
After analyzing the nature and behavior of the foreign institutional investment in the past and its influence on the Indian stock market it would be safe enough to say that foreign funds are one of the most volatile instruments floating in the market and needs to be handled cautiously.

Inflation control factor implemented regularly

Inflation should be measured on consumer price index.

Control over the working of stock market

**Lessons from the Global Financial Crisis with special reference to Emerging Market Economies and India***

Since the collapse of the leading US investment banks in August-September 2008, there has been a breakdown of trust in inter-bank and inter-institutional lending. Given that this kind of extreme risk perception will be reversed only slowly, the full resolution of the crisis will inevitably take time.

Financial supervision has drawn widespread critique. The stereotype perception is that risk management and supervisory practices lagged behind financial innovations and emerging new business models. The present crisis underscores the need for regulation staying ahead of the curve, and for continually upgrading the skills and instruments for financial regulation and supervision. However, there is need for a note of caution here. There is a distinct risk that in trying to stay ahead of innovation, regulation may get so stringent that it stifles innovation. This is a risk we must guard against.

The origins of the current crisis can be traced to both the build up of macro-global imbalances as well as the mispricing of risks in the financial system, which in turn, was encouraged by prolonged easy monetary policy and excess liquidity. We endorse the IMF view that the respective roles of central banks, regulators, supervisors, and fiscal...
authorities regarding financial stability needs to be revisited.

Central banks should play a central role in maintaining financial stability and should have the necessary informational base to do so effectively. This implies close cooperation among all the agencies entrusted with the task of maintaining financial stability.

The fifth lesson is that the large scale bail-out packages will have implications for the regulatory architecture of the financial system and for the fisc of countries. Besides, the rescue packages offered by one country could have ramifications for other countries, even when they are far from the epicentre of the crisis. A relevant issue in this context is the efficacy and coverage of deposit insurance.

The unfolding crisis has revealed the weaknesses of structured products and derivatives in the credit markets. This throws up questions about the appropriateness of various structured product like credit derivatives and their financial stability implications. Are exchange traded derivatives superior to over the counter (OTC) derivatives? Do we need to focus on prescribing and instituting appropriate clearing and settlement practices even for OTC products?

Finally, the near meltdown of the US financial sector is seen by some as evidence that markets and competition do not work. This is clearly the wrong lesson to draw. The right lesson to draw is that markets and institutions do succumb occasionally to excesses, which is why regulators have to be vigilant, constantly finding the right balance between attenuating risk-taking and inhibiting growth.

Comment on India.

India, with its strong internal drivers for growth, may escape the worst consequences of the global financial crisis. Indian banks have very limited exposure to the US mortgage market, directly or through derivatives, and to the failed and stressed financial
Institutions. The equity and the forex markets provide the channels through which the global crisis can spread to the Indian system. The other three segments of the financial markets - money, debt and credit markets - could be impacted indirectly.

Reduced investor interest in emerging economies could impact capital flows significantly. The impending recession will also impact on Indian exports.

It is heartening that there is coordination among developed countries in the management of the crisis. That is welcome and necessary, but not sufficient. In as much as emerging and developing economies are likely to be increasingly impacted.
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