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CURRENT GLOBAL ECONOMIC CRISIS IN INDIA

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Current Global Economic Crisis in India

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Abstract – India's financial sector is not deeply integrated with the global financial system, which spared it the first round adverse effects of the global financial crisis and left Indian banks mostly unaffected. However, as the financial crisis morphed in to a full-blown global economic downturn, India could not escape the second round effects. The global crisis has affected India through three distinct channels: financial markets, trade flows, and exchange rates.

The Subprime Mortgage Crisis is an ongoing economic problem that has become more apparent in 2008 and has resulted in reduced liquidity in the global credit market and also the banking & financial systems. This crisis has exposed the weakness in the global financial system and also the regulatory framework that is overlooking them.

Some of the reasons for this crisis are:

1. The US Real estate market crash

2. High default rates on Subprime loans &

3. Subprime Mortgage backed securities

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MEANING

Global economic crisis refers to an economic scenario where the economies of countries all over the world have taken a beating. The GDP's of countries are going down are in -ve zone.

There is severe liquidity crunch and countries & governments around the world are frantically taking steps to combat this issue

REASONS OF ECONOMIC CRISIS:

The **Subprime Mortgage Crisis** is an ongoing economic problem that has become more apparent in 2008 and has resulted in reduced liquidity in the global credit market and also the banking & financial systems. This crisis has exposed the weakness in the global financial system and also the regulatory framework that is overlooking them.

Some of the reasons for this crisis are:

1. The **US Real estate market** crash

2. High **default rates on Subprime loans**

3. Subprime **Mortgage backed securities**

A Subprime loan is a loan that is granted to a borrower who does not qualify for loans owing to a variety of risk factors like low income level, bad credit history etc.

THE EFFECTS OF THIS ECONOMIC CRISIS ARE:

1. Banks have incurred huge losses. Their earnings came down.

2. Financial institutions have gone bust or have been taken over by bigger organizations

3. The housing prices have plummeted

4. The liquidity in the financial system has come down

5. High unemployment etc.

IMPACT OF CRISIS ON THE INDIAN ECONOMY

Global Integration of Indian Economy

In response to its balance of payments (BOP) crisis in the early 1990s, India implemented a series of trade, industry, and investment reforms. These reforms effectively liberalized the economy, ending a long period of relative isolation from global markets and financial and technology flows. Since then the Indian economy has become increasingly integrated with the world economy. 6 Consequently, current account flows (receipts and payments of merchandise and invisibles) as a proportion of GDP increased from 20% in FY1990–1991 to 53% in FY2007–2008 (Figure 2). However, the most significant change can be witnessed in the capital account. Due to the rationalization of procedures and conditions for foreign investment, India has emerged as an attractive investment destination. This is reflected as an increase in foreign portfolio investment inflows from US$2 billion in FY2001–2002 to US$29 billion in FY2007–2008. Foreign direct investment (FDI) inflows have also gone up significantly in recent years, having risen to US$34.3 billion in FY2007–2008 from US$6.1 billion in FY2001–2002. At the same time, Indian corporations have also entered the global market for mergers and acquisitions, resulting in some capital account outflow from India. As a result, two-way flows of portfolio and direct foreign capital have gone up from a mere 12% of GDP in FY1990–1991, to 64% of the GDP in FY2007–2008, registering a fivefold increase. Interestingly, these ratios are significantly higher than those in the US, for which trade in goods and services constituted only 41% of GDP in 2007 and capital flows another 25% in the same year.

TRANSMISSION OF THE CRISIS TO THE INDIAN ECONOMY

With India's increased linkage with the world economy, India could not be expected to remain immune to the global crisis or be decoupled from the global economy. While it is true that the Indian banking sector remained largely unaffected because of its very limited operations outside India or exposure to sub-prime lending by foreign investment banks, the global crisis has affected India through three distinct channels. These channels are financial markets, trade flows, and exchange rates.

SEVERITY OF THE CURRENT FINANCIAL CRISIS

Banking and financial crises have been a regular feature of modern economic history. According to one estimate, there have been 86 banking crises since the Great Depression that have spread beyond national borders. According to a World Bank study in 2001,[2] the world has witnessed as many as 112 systemic banking crises from the late 1970s to early 2001. Most crises, including the current one, share some common features. Some general examples include a search for increasingly higher yields in financial markets, a lax regulatory regime, a mismatch in appetite for risk and the capacity for bearing it, and the consequent buildup of asset bubbles, usually in the real estate sector, which for various reasons is overlooked by the regulators.

CONCLUSION

The effects of the global financial crisis have been more severe than initially forecast. By virtue of globalization, the moment of financial crisis hit the real economy and became a global economic crisis; it was rapidly transmitted to many developing countries. India too is weathering the negative impact of the crisis. There is, however, an important difference between the crisis in the advanced countries and the developments in India. While in the advanced countries the contagion traversed from the financial to the real sector, in India the slowdown in the real sector is affecting the financial sector, which in turn, has a second-order impact on the real sector

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