



Global Financial Crisis & India: Problems and Recommendations

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ABSTRACT

India an emerging market economy thought it be different this time and they be able to escape the scar, also got affected though to a lesser extent. But the lesson to be learnt is we are living in a global villages, and our sustainable growth as well as our challenges is linked, though to a larger or smaller extent depending upon internal as well as external macros. This is mainly due to the inter linkages between various economies that any such crisis takes global shape and can only be redressed by managing together . Collective efforts of larger number of regulators and governments worldwide are needed for the rescue during the times of crisis.

This leads us to the conclusion that globalization and hence the financial market liberalization has converted the job of regulators to proactively manage macroeconomic policies rather than to controlling or regulating markets. The role of regulator is to keep a close watch on internal as well as external macro-economic developments and manage proactively its foreign trade policies, foreign exchange reserves and fluctuations in currency values, fiscal policies, monetary policies etc. to take the economy on the desired level of economic growth which is sustainable in long run and manage the short term hiccups arising in the way of doing so.

Introduction:

The globalization of world economy in the 20th century has created global linkages like never before. These structural changes have brought some new generation economic facts that every nation has to live and cope with. This global turn ground has enlarged the market liberalization and has lead to a great interdependence and linkage between markets world wide . At the one end , the resource mobilization, their optimal utilization as well as adequate and appropriate end usage and consumption has been ensured and at the other end, the scope for inefficiencies and ineffectiveness has been reduced to minimal as any inefficiency and ineffectiveness can lead to Global Crisis and Global Recession.

Global Financial Crisis :-

The Global recession was initiated with financial crisis in U.Sub Prime Mortgage Market. In 1995, property prices had risen more than rate of inflation. Hence , there were returns in the property sector at that time. Therefore, a property boom was created in 2001. At the time , George Bush , the then President of America, stated that dot com bubble busted.



But to avert the deeper recession in 2001 , the artificial excess liquidity was created and loans were given to Sub Prime sector against the Sub Prime Mortgages. Moreover , due to deregulation of Banking system and change in organization and management model, banks were allowed to issue securities under securitization process .i.e . Banks had further mortgaged the securities to another Bank Holding Companies and even sold these securities to large huge investment banks. These inter-linkages different sectors of US economy and the recession spread to all over U.S.

Faulty Credit Ratings have also plays a significant role in Global Recession. Credit Ratings were done by few companies like fetch, Crisil and these credit rating were done through bribe, Change in leadership in America has also played a role in Global Recession. Obama, the President of America and restricted outsourcing to meet the internal liquidity demands, which leads to withdrawal of investments from other countries and affected almost all the countries of the world wide showing slump in growth and employment due to integrated world economies. IMF estimates of growth rate have shown negative growth in almost all the countries in 2009.

Problems :-

1. Gross Domestic Product and Sectoral Growth :-

The overall impact of Global Recession can be judge from full in GDP from 9% in 2007 to 6.7% in 2009. There was fall in industrial growth rate also. The fall in industrial growth rate from 8% in 2005-06 to 3.9 % in 2008-09 is due to depressed export markets and suppressed domestic demand due to slow generation of employment. Moreover, rise in import prices also adversely affected the manufacturing sector . Service sector also got hampered due to adverse effect on Banking , Insurance and Financial Service Sector. Agricultural sector is also badly affected showing a decrease in growth rate from 5.9 % in 2005-06 to 1.6 % in 2008-09.

2. Foreign Institutional Investment :-

The most immediate effect of recession has been out flow of foreign institution investment from home market . There was decrease in foreign institutional investment from \$ 6409 million in 2006-07 to \$ 15007 million in 2008-09 as foreign institutional investors withdrew their investments from foreign countries to cover losses in the home market.

3. Foreign Exchange Reserve :-

Due to outflow of Foreign Institutional Investment and to meet the external obligations. Government has to releases its foreign exchange reserve. Hence , there was depletion in Foreign exchange reserve from \$ 309 billion in 2008-09.

4. Sensex and Nifty :-

Due to outflow of capital , there was decrease in number of borrowers which resulted in collapse of stock markets i.e. there was sharp decline in sensex and Nifty both from January 2008 to October 2008.



5. Exchange Rate :-

Withdrawal of Foreign Institutional Investment and conversion of funds raised locally to foreign current to meet their external obligations increased the demand for US dollar and as a result exchange rate depreciated.

6. Inflation :-

The Currency depreciation lead to high cost of imported food and imported capital goods, which further affected our domestic prices. Inflation rate on WPI has shown an increase from 4.4 in 2005-06 to 8.4 in 2008-09 . The Commodity exchanges also played a significant role in raising the prices in the economy. Increase in food prices in turn hit the poor individual and houses that spend much of their income on food.

7. Foreign Trade :-

The aggregate decrease in demand in the world market as a result of crisis badly affected the export industries as there is reduction in consumption spending due to job loss. Even the exchange rate depreciation could not increase the exports. On the other hand, due to rise in import prices, import bill increased and hence the gap between imports payments and exports receipts widened and resulted in increase in deficits in Balance of Trade.

8. Leadership :-

The core of the financial crisis in Europe, there is a leadership crisis. Over the weekend, Policy makers and pundits, businessmen and bankers, investors and the lay public waited to see what Greek voters would say about remaining in the eurozone . The very fact that crisis management has to take not of referendums and public opinion were populist rhetoric and base national sentiment rather than cool reasoning would shape perceptions and verdicts about Europe's leadership vacuum.

Europe is clearly adrift in this gathering storm. At a meeting of risk analysts in London , analysts from the United States were shocked to encounter what one called "a dangerous mix of complacency and make-believe. " The decision of eurozone Finance Minister to offer a 100 billion euros bailout package to Spain is viewed as an act of both desperation and bravado. While the fireeeks wonder why Spain gets so much money so easily. French and Italian an assertive Germany and a miffed and hurt German Chancellor says her nation cannot bear too much more of the burden of the eurozone's failure.

9. Employment :-

Confronted with the most severe economic crisis in decades and rising unemployment; government in locations across the global embraced a range of policies to suppress the inflow of migrants, encourage their departure , and protect labor markets for native born workers.

From Malaysia and Thailand to Kazakhstan, Taiwan , Australia , South Korea and Russians many governments have sought to restrict access to their labor markets by halting or at least decreasing the numbers of work permits for foreigners. Others, such as the UK , tightened admission requirements. And while the policy focus of many of these countries was on reducing the entry of low skilled workers. The United States placed restrictions on some companies seeking to bring in the highly skilled.



Swimming against the tide was Canada, which briefly considered the idea of reducing permanent legal immigration rates in response to the global economic downturn, but then proceeded to leave its permanent levels unchanged, and in fact saw employer demand for temporary workers rise. One province, Alberta, saw a 340 % rise in the number of temporary workers from 13000 in 2004 to 58000 in 2008 . Moreover in January 2009 , Alberta sanctioned a program to entice US temporary skilled workers through a fast- track programme for Canadian Permanent residency .

The adjustment of Visa levels and entry requirements was not the only policy tool deployed by countries responding to the economic crisis. Others sought to make it harder for migrants to live and work illegally by stepping up enforcement and curbing access to public services.

10. Aviation :-

The downside of a carbon aviation tax is not just limited to the business risk, it passes to state and private aircraft carriers, but also to global trade in high –value, time-bound commodities that are predicated on the aerial medium. Aviation supports 40% of the total value of international trade and accounts for 8% of global economic activity. The EU is push for taxing airlines that are essential life lines is a misguided one that threatens to slow down trade and changes of recovering form the current economic Crisis.

According to the World Trade Organization (WTO) global trade growth is a barely 3.7% in 2012. Which is way below the long term average growth of 6% between 1990 and 2008. The EU's carbon aviation tax has been painted as a painful but necessary measure to protect the outer environment from airline emissions , but it could undermines that are particularly dependent on aviation-bound merchandise , tourism and overseas workers.

Recommendations :-

1. Fiscal Responsibility Council :-

Fiscal responsibility has to be enforced to ensure that no political party free rides on the fiscal discipline of others. To achieve this, a Fiscal Responsibility Council (FRC) headed by the Prime Minister, and comprising the Finance Minister , and leaders of major political formations in Lok Sabha, has to be constituted. Its mandate could include assessing the soundness of assumptions underlying economic and fiscal policy planning laying down an annual roadmap for the attainment of fiscal goals and monitoring progress , and evolving penalties on the government in case of default. The Budgeting practices in the Union government need to be improved in line with international best practices. The budget manual, can be amended through an executive order to adopt a "top -down" approach to budgeting. Under this system, once the Union Cabinet has approved the overall annual expenditure aggregates of each department , the power to decide on inter- se allocation within a department would vest with the concerned minister. This would encourage every departmental minister to function as the department own Finance Minister and promote intensive infra - department programme scrutiny vis - vis intended outcomes.



2. Ministry of overseas Indian Affairs :-

In order to tackle such situation of crisis and other problems of Indian diasporas, the Indian Government has taken several initiatives. In 2009, a novel initiative, the Government had set up a community welfare fund in 42 Indian missions abroad to facilitate extending help to diasporas community in times on difficulty. Initially, the new welfare fund was envisaged by the Ministry Of Overseas Indian Affairs (MOIA) mainly to support workers who may be returning because they lost there jobs following the global showdown. However, the idea has evolved in to a permanent welfare measure to help overseas workers who may returning for different reasons.

3. Exim Policy :-

A strategy of import compression has to be combined with a drive to push up exports. A lot has been written on the various elements that are key to higher and sustained export growth better infrastructure, diversified markets and easy financing. There is another things that might help export growth in the near term - lifting the ban on export items particularly in agriculture. Clearly, the curbs on agricultural exports can only be lifted after a careful analysis of the impact of lifting them. We can not for example , lift the curbs on the exports of pulses immediately given the current domestic shortage. However the same does not apply wheat (banned since April 2007.) with current buffer stocks running at about 65 million tones or 30 million tones above the optimal stocking norm (a good fraction of which is rotting) , there seems to be no rationale to continue with the ban. In fact, we should export surplus items aggressively to enable us to import items like pulses and oilseeds that are in short supply.

4. Current Account Deficit (CAD) :-

The current account deficit is a structural problem. It is not merely a cyclical upstic that has been driven up by strong domestic growth. A more rational trade policy serves many purposes. It could help bring down the massive CAD and take the pressure of the rupee. This is turn could harness "imported " inflation. The RBI could then think of focusing on ramping up growth through rate cuts and monetary expansion. A revamp of the trade regime would also align our export and import patterns with domestic capacity and resource availability . In short, a win- win situation for the economy.

5. Political Will :-

Political will is a required for big ticket economic reforms. Political will in a good democracy resides in the people. Leaders must have the ability to persuade them. India is a flotilla of ships and boats; Many communities, many political parties and much diversity. They must come together and sail together for India to advance . India is not a navel fleet in which captains of all ships will say " aye, sir " when the admiral commands . The captains and crews with the leader and go along with the fleet. They need a vision of the future into which they are sailing. A number- 7 percent GDP or 9 percent GDP - can not explain what really matters to people . what matters to them is what sort of country will we become ? what will be the experience of daily life for our families ? what opportunities for livelihoods will our children have ?



6. Institutions :-

A nation's economic numbers are an outcome of the quality of its institutions. Institutions channel entry and guide decision that result in inclusive growth. The architecture of institutions follows from " theories – in use" of how things should be organized and done . By 2005 , the ideological divide between pro-markets or pro-government ideas of managing human affairs had widened in India, as it had in the Western World, moreover, market or market institutions come in many forms. For example the northern European model of inclusive capitalism provides institutional roles for labor and civil society for holding to account Democracy requires strong institutions too. The ability to conduct elections is only one. Democracy also needs good institutional capabilities for dialogue and collaboration among diverse stakeholders at many levels of society , national & local.

7. Capitalism:-

The scenarists pointed to the urgency for India to build an inclusive version of capitalism , and the imperative to strengthen local governance . They noted in the churn within India , positive forces pulling in those directions. However, these forces were sidelined by the premature celebration of India's inevitable success. The scenarists noted that the public discourse in India was becoming shriller with tensions within the country needing resolution as well as shallower in public debates designed to entertain rather than resolve. The quality of public deliberation it was feared, could prove to be India's Achilles, heel, In a democracy with great diversity - economic social and political and with an enormous development agenda ahead not only economic growth but also improvement of human development indicators the ability of people to participate effectively in decisions regarding their future is the key to progress. The scenarists forecasted that if India under took the reforms in the institutions that their analysis pointed to, it would not only maintain a percent growth but, with favourable global conditions, exceed it.

8. 12th Five Year Plan :-

As the 12th Five Year Plan was taking shape , many Indians from diverse walks of life voluntarily came together , in a flotilla, to supplement the official planning process. They used the scenario process to get to the heart of the matter. The scenarios explain the choices people must make the strategies the country must adopt and our leaders must commit to unlike economic analysis scenario's are expressed in terms that people understand . They provide seeds for dialogue across the country about how we can shape our future democratically. The scenario's reveal that the keys to Indian's sustainable progress are governance and administrative reforms. For competent and trustworthy institutions. With the EU in turmoil and global markets roiled, we cannot muddle along any longer . It is time to batten down the hatches. So that the Indian flotilla can advance amidst the storm. Internal institutional reforms have become even more urgent.

9. Constitution:-

The Challenger for the EU is to find its Ambedkar , it needs a constitution that will enable a continental political leadership to offer continent -wide solution to a continent



wide problem. Europe needs emotional unity as much as it needs a new strategy for generating employment in a globally competitive way. If this sounds daunting and impossible, then the EU should return to what many in Britain prefer a normal single market, like the South Asian Free Trade Area (SAFTA). A single market with multiple currencies and sovereign member nations. Britain's Eurosceptics in fact advocate this course that the EU should give up idea of a fiscal and monetary union and remain just a single market. But that would also imply the decline of Europe as a geopolitical power.

10. Inflation:-

The coming days will see even more difficult times for monetary policy making. In India is to ward off a high and volatile inflation rate and provide an environment for long term high growth, then apart from the investment climate and all other reforms the government needs to do, it must move towards an inflation targeting Central bank. Otherwise, the political pressure to cut rates in futile attempts to push growth, can plunge India in to years of higher inflation and even lower growth.

11. Financial Literacy :-

Financial inclusion was part of trinity along with consumer protection and financial literacy which would ensure financial stability. Still India needs to do a lot regarding the financial exclusivity with more than half of Indians. Still living in 'unbanked' regions. They have to depend upon the local money lenders who exploit them heavily.

12. Economic Growth :-

From 2004 onwards, the Indian leadership has neglected the foundations of economic growth. The economic policy reforms of previous years, coupled with benign global conditions, gave effortless growth and the focus of the Union was on spending. Now, we need to reevaluate our growth model, and ask how to rebuild the confidence of private investors so as to obtain growth even when global conditions are adverse.

13. Economics of Solidarity :-

Today the capitalist system appears to be the only efficient mode of economic organization. However, there appears to be increasing resistance to the capitalist order, evident in the people's movements witnessed from time to time when the livelihoods of the poor and the marginalized are threatened. This presents an understanding of the new development epistemology of the deprived, the powerless, and those who are at the margins at all levels - local, national and global. It discusses how solidarity economics appears to be paving the way for an alternate, new type of economic development.

14. India's services sector :-

There are various problems in looking at services as the gateway to development in India. First, the sectoral shift of the gross domestic product in favour of services has not been matched by concomitant changes in employment pattern. Second, the services sector has exhibited a dualism where in the fastest growing services are the high productivity, low employment - generating ones. And lastly but significantly; much of the growth in services has necessitated the transfer of resources to the private Corporate sector and destruction of livelihoods of people dependent on such resources.



15. Others:-

But expectations for a short term win have been lowered by Germany's Chancellor, Angela Merkel, who has asserted that big changes such as issuing common debt will have to wait until countries that use the single currency have agreed to a broader revamp of the political architecture of the euro zone. Those change could include surrendering more power over their budgets do Brussels. The Summit, which will be followed by a separate meeting of euro zone leaders which is expected to focus on agreeing on the elements of a banking union , which is seen as a concrete step even through it would not come into operation until 2013 at the earliest. Those elements would include a system to wind up insolvent banks , a central deposit guarantee fund and a bigger supervisory role for the European Central Bank, among other measures.

- a. Government should taking steps to revive investor sentiment, focusing heavily on infrastructure investment and was committed to promote an atmosphere conducive to enterprise and creativity. " Our policies should be transparent stable and designed to provide a level playing field to both domestic and foreign investors. " The Government was focusing on reversing the Fiscal expansion allowed after the global financial turmoil in 2008. " This will require tough decisions , including on controlling subsidies which we are determined to take.
 - b. EBC President Mario Draghi said his bank was ready to step in and fund any viable euro zone bank that gets in trouble, and painted a picture of a deteriorating economy with no inflation danger conditions for monetary easing. Central banks are preparing to take steps to stabilize financial markets if needed by providing liquidity and prevent any credit squeeze.
 - c. Whatever is causing liquidity stress, whether it is foreign exchange market or sometime else , we are focused on maintaining liquidity conditions within the comfort zone, we have stated and that will continue to be the benchmarks. In it's mid-quarter monetary policy review of June 18, the Central bank had said it's open market operations (OMO) have substantially eased liquidity conditions . To further augment liquidity and encourage banks to increase credit flow to the export sector. RBI also raised the export refinance credit limit with to release about Rs. 30.000 crore.
 - d. Referring to the current account deficit, the capital inflows are not matching the expectations and putting pressure on the rupee. As it current account deficit corrects for whatever reasons, whether it is oil prices or exports picking up or imports going down that will obviously have a reverse effect, which will help to stabilize that rupee.
 - e. British officials " Strengthen governance and establish a credible reporting procedure " and ". eliminate incentive to misreport."
 - f. There has been a conflict between the government, the owner of several large banks, and RBI , the regulator, on the issue of micro management of these banks. The conflict should transfer into cooperation.
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Conclusion:-

India an emerging market economy thought it be different this time and they be able to escape the scar, also got affected though to a lesser extent . But the lesson to be learnt is we are living in a global villages, and our sustainable growth as well as our challenges is linked, though to a larger or smaller extent depending upon internal as well as external macros. This is mainly due to the inter linkages between various economies that any such crisis takes global shape and can only be redressed by managing together . Collective efforts of larger number of regulators and governments worldwide are needed for the rescue during the times of crisis.

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" We must plan our economy in such a manner that we cannot expect outside help on a scale which can see us through our difficulties."

" There are problems with regard to management of the balance of payments deficit on the current account. Those problems also we will tackle.

It will not be proper for us to take about these things in details , but , we recognize that we have to work our way to restore the momentum of growth that India needs and which the people of India want the Government of India to work for. "

" Many countries could do more if additional finance and technology were available. Unfortunately, there is little evidence of support from the industrialized countries in these areas (reducing emissions intensity). The ongoing economic crisis has made matters worse." Describing Economic Development social inclusion and environmental sustainability as all equally critical as components of sustainable development. The task before the world community is to give practical shape and content to this architecture in a manner that allows each country to develop according to it's own national priorities and circumstance.

" Difficult though it may seem, we have to summon the imagination to balance the costs that we will incur in the present with the benefits that will accrue to future generations. " For developing countries , inclusive growth and a rapid increase in per capita income levels are development imperatives. " Those living at the subsistence level cannot bear the costs of adjustment and their livelihood considerations are important in determining how scare natural resources such as land , water and forests are used."

Nothing that sustainable development also mandated efficient use of available natural resources, the world community has to be much more frugal in the way it uses natural resources.



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