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   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

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# IMPACT OF GLOBAL CRISIS IN INDIAN BUSINESS

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## ABSTRACT
*The Indian economy is experiencing a downturn after a long spell of growth. Industrial growth is faltering, the current account deficit is widening, foreign exchange reserves are depleting, and the rupee is depreciating. The crisis originated in the United States but in Indian government had reasons to worry because there was a potential adverse impact of the crisis on the Indian banks. Lehman brothers and Merrill lynch had invested a substantial amount in Indian banks, who in turn had invested the money in derivatives, leading to exposure of even the derivatives market to these investment bankers. Public sector unit (PUC) banks of India like bank of Baroda had significant exposure towards derivative. ICICI faced the worst hit with Lehman brothers having filed for bankruptcy in the US, ICICI (India's largest private bank), survived a rumor during the crisis which argued that the giant bank was slated to lose $80million (Rs.375 cores), invested in Lehman's bonds through the bank's UK subsidiary. Even axis bank was affected by the meltdown.*

## KEYWORDS
global crisis, Indian Business.

## INTRODUCTION
The Indian economy is experiencing a downturn after a long spell of growth. Industrial growth is faltering, the current account deficit is widening, foreign exchange reserves are depleting, and the rupee is depreciating.
The crisis originated in the united states but in Indian government had reasons to worry because there was a potential adverse impact of the crisis on the Indian banks. Lehman brothers and Merrill lynch had invested a substantial amount in Indian banks, who in turn had invested the money in derivatives, leading to exposure of even the derivatives market to these investment bankers.
Public sector unit (PUC) banks of India like bank of Baroda had significant exposure towards derivative. ICICI faced the worst hit with Lehman brothers having filed for bankruptcy in the US, ICICI ( India's largest private bank), survived a rumor during the crisis which argued that the giant bank was slated to lose $80million (Rs.375 cores), invested in Lehman's bonds through the bank's UK subsidiary. Even axis bank was affected by the meltdown.
The impact of the crisis on the Indian economy has been studied here forth and the study is chiefly focused on 4 major factors which affect the Indian economy as a whole. These are as per following:
1. Availability of global liquidity
2. Decreased consumer demand affecting exports
3. The financial crisis and the Indian IT industry
4. The financial crisis and India's financial markets

## AVAILABILITY OF GLOBAL LIQUIDITY FOR INDIA IN TIMES OF FINANCIAL CRISIS
The main source of Indian prosperity had been foreign direct investment (FDI). American and European companies were bringing in truck-loads of dollars and Euros to get a piece of pie of Indian prosperity. Less inflow of foreign investment will lead to a dilution of the element of GDP driven growth. India is in no position to ever return this money because it has used the same in subsidizing the petroleum products and building low quality infrastructure.
Liquidity is the major driving force of the stock market performances observed in emerging markets. Markets such as those of India are especially dependent on global liquidity and international risk appetite. The initial stage of the crisis witnessed rising interest rates across global economies. Rising interest rates tend to have a negative impact on global liquidity, and subsequently equity prices, as funds may move into bonds or other money market instruments.
Even though there are threats for the Indian economy due to the global liquidity crunch, they are all oriented for the long term. Any short term liquidity concern will be taken care of by the high rate of household and corporate savings in the country. The Indian economy can certainly rely on its 'piggy bank' to address its short-term liquidity demands as the government is taking measures to channelize large sums of household savings lying unused in physical assets into the more productive financial sector. Thus, the Indian economy will be relatively unaffected by the global liquidity crunch.
Indian companies which had access to foreign for financing their trading activities are the worst hit. Foreign funds will be available at huge premiums but will be limited to the blue-chip companies, thus leading to

- Reduced capacity of expansion leading to supply pressure.
- Increased interest rates which will affect corporate profitability
- Increased demand for domestic liquidity which will put interest rates under pressure

## DECREASED CONSUMER DEMAND AFFECTING EXPORTS
Consumer demand has plummeted drastically in developed economies, leading to a reduced demand for Indian goods and services, thus affecting Indian exports.

- Exports oriented units are the worst hit; thus impacting employment
- Trade gap has been widening due to the reduced exports, leading to pressure on the rupee exchange rate.
- In India, It companies, with nearly half of their revenues coming from financial and banking service segment, are close monitors of the financial crisis across the world. The IT giants who had Lehman brothers and Merrill lynch (ML) as their clients are Tata consultancy services (TCS), Wipro, Satyam, and Infosys Technologies. HCL escaped the loss to a great extent because neither Lehman brothers nor ML was its client.

## IMPACT ON FINANCIAL MARKETS
The outflow of foreign institutional investment from the equity market has been the most immediate effect of the crisis on India. Foreign institutional investors (FIIs) have been major sellers in Indian markets as they need to retrench asset in order to cover losses in their home countries, thus being forced to seek havens of safety in an uncertain environment.
The financial crisis has reinstated the notion that in the globalised world, no county can exist as an island, insulated from the twists and turns of the global economy; growth prospects of emerging economies have been undermined by the cascading financial crisis, though there certainly exist significant variations across the countries.

## BACKGROUND OF THE CRISIS

A disorderly contraction in wealth and money supply in the market is the basic cause of a financial crisis, also known as a credit crunch. The participants in an economy lose confidence in having loans repaid by debtors, leading them to limit further loans as well as recall existing loans.

Credit creation is the lifeblood of the financial/banking system. Credit is created when debtors spend the money and which in turn is 'banded' and loan to other debtors. Due to this, a small contraction in lending can lead to a dramatic contraction in money supply.

The present global meltdown is s culmination of several factors, the most important being irrational and unsustainable consumption in the west particularly in united states disproportionate to its income by consistent borrowings fueled by savings and surpluses of the east particularly china and Japan.

The second important factor is the greed of the investment bankers who induced housing loans by uncontrolled leveraging on an optical illusion of increasing prices in the housing sector.

The third important factor is the failure of the regulating agencies who ignored the warning signals arising out of the ballooning debts, derivatives and financial innovation on the assumption that the Collateral Debt Obligation(CDO), the Credit Default Swapping(CDS) and Mortgaged Backed Securities(MBS) would continue to remain safe with the mortgage guarantees provided by Government Sponsored Enterprises(GSEs) namely Fannie Mae and Freddie Mac which had enjoyed the political patronage since inception.

There are other several factors including shadow banking system, financial leveraging by the investment bankers and lack of adequate disclosure in the financial statements leading to fallacious rating by the rating agencies.

## CAUSE OF THE CRISIS

The current crisis has been linked to the sub-prime mortgage business, in which US banks give high-risk loans to people with poor credit histories.

These and other loans, bonds, or assets are bundles into portfolios or Collateralized Debt Obligations(CDOs) and sold to investors across the globe.

Falling housing price and rising interest rates led to high numbers of people who could not repay their mortgages. Investors suffered losses and hence became reluctant to take on more CDOs. Credit markets froze and banks became reluctant to lend to each other, not knowing how many bad loans and non-performing asset could be on their rival's books.

The crisis began with the bursting of the United States housing bubble and high default rates on sub- prime mortgages and adjustable rate mortgages (ARM). The foreclosures exceeded 1.3 million during 2007 up 79% for 2006 which increased to 2.3 million in 2008, an 81% increase over 2007.

## EFFECT THE FINANCIAL CRISIS IN INDIA

The global financial crisis has not left India unscathed. Over the last seven months, growth has slipped dramatically – to 5.3% in the last quarter of calendar year 2008- from over 9% in the previous four years. The contagion of the crisis has spread to India through all the channels- the financial channel, the real channel, and importantly, as happens in all financial crises, the confidence channel.

The slowdown is likely to have a large and immediate impact on employment and poverty informal surveys suggest significant job losses. Job creation is likely to remain a key concern as new entrants to the labor force- relatively better educated and with higher aspirations- continue to put pressure on the job market.

The country has the option of turning the crisis into an opportunity. The most binding constraints to growth and inclusion will need to be addressed: improving infrastructure, developing the small and medium enterprises sector, building skills, and targeting social spending at the poor. Systemic improvement in the design and governance of the public programs are crucial to get result from public spending.

## GLOBAL LIQUIDITY CRUNCH AND THE INIDAN ECONOMY

The Indian banking system was gauged as being relatively immune to the factors that have lead to the turmoil in the global banking industry. The problems of the global banks arose mainly due to the sub-prime mortgage lending and investments in complex collateralized debt obligations (CDOs) whose values were sharply eroded. Confidence- related issues had also affected banks across the globe due to the freeze in the inter-bank market. Indian banks had limited vulnerability on both counts.

The reasons for tight liquidity conditions in the Indian markets during the earlier stages of the crisis were quite different from the factors driving the global liquidity crisis. Large selling by foreign institutional investors (FIIs) and the subsequent interventions by the Reserve Bank of India (RBI) in the foreign currency market, continuing growth in advances, and earlier increases in the cash reserve ratio (CRR) to contain inflation are some of the reasons that accelerated the Indian liquidity crunch.

Thousands of investors, big and small, have been hurt by the downward plunge of the Indian stock market. It will also have broader implication for India's financial system and the future savings and investment patterns.

Cautious investors had started to diversify away from bank deposits and cash over the past few years, and had moved to equities, mutual funds and insurance products. The financial crisis also struck the company at a time when there were growing suspicions related to the Maytas issue.

## CONCLUSION

As the contagion of the financial system collapse across the world spread towards India, and into it, the government and the Reserve Bank of India (RBI) responded to the challenge in close coordination and consultation. The main plank of the government's response was fiscal stimulus while the RBI's action comprised monetary accommodation and counter cyclical regulatory forbearance.

The RBI policy response was to keep the domestic money and credit markets functioning normally and see that the liquidity stress did not trigger solvency cascades. RBI targets can be classified into two prime directions:

- To maintain a comfortable rupee liquidity position
- To augment foreign exchange liquidity

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