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Research Papers

Global Recession And India

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Abstract

The Indian Economy is liked to global market through LPG policy. We accept the policy in 1991. Globalization has ensure that the Indian Economy and financial market cannot stay insulate from the present financial crisis in the developed economies.

Keywords: Global Recession , global integration , developed economies.

INTRODUCTION

Global financial crisis that stated with sub-prime woes in United States has shaken the whole world in this era of global integration. Economists claimed that it is not affected to the extent other nations have been.

I) What is Recession:-

A recession is a decline in a country's gross domestic product growth for two or more consecutive quarters of a year. A recession is also preceded by several quarters of slowing down.

In economics, the term recession is generally used to describe a situation in which a country's Gross Domestic Product, sustains a negative growth factor for at least 2 consecutive quarters. I say generally because recession can be defined differently by different economists. Just as there is an agency to define the measure of inflation; the official agency in charge of declaring that the economy is in a state of recession is the National Bureau of Economic Research (NBRE). NBRE's define recession as a "significant decline in economic activity lasting more than a few months". For this reason, the official designation of recession may not come until after we are in a recession for six months or even longer. Some economists also suggest that a recession occurs when the natural growth rate in GDP is less than the average of 2 %. Typically, a normal economic recession lasts for approximately 1 year.

II) Thoughts of Ronald Reagan:-

"Recession is when a neighbor loses his job. Depression is when you lose yours".

III) History of Recession:-

a) Global Recessions:-

There is no commonly accepted definition of a global recession. The IMF estimates that global recessions seem to occur over a cycle lasting between 8 and 10 years. During what the IMF terms the past three global recessions of the last three decades, global per capita output growth was zero or negative. Economists at the International Monetary Fund state that a global recession would take a slowdown in global growth to three percent or less. By this measure, three periods since 1985 qualify; 1990-1993, and 2001-2002.

b) 2008 Recession in some countries:

Since 2007, there had been speculation of a possible recession starting in late 2007 or early 2008 in some countries. In January 2008, the IMF predicted that 2008 global growth would fall from 4.9 per cent to 4.0 per cent however 2 months later it was announced that this projection was not low enough. There was significant speculation about a possible U. S. recession in 2008. If such a recession happened, it was expected to have a global impact. The U. S. represents about 21 per cent of the global economy, and impact of a U. S. recession could spread through the following.

- Less spending by American consumers and companies reduce demand for imports.
- The crisis of the U. S. subprime- mortgage market has pushed up credit costs worldwide and forced European and Asian banks to write down billions of dollars in holdings.
- Dropping U. S. stock prices drag down markets elsewhere.

c) United States:

The United States housing market correction and subprime mortgage crisis had significantly contributed to anticipation of a possible recession. U. S. employers shed 63,000 jobs in February 2008, the most in five years. Former Federal Reserve chairman Alan Greenspan said on April 6, 2008 that "There is more than a 50 per cent chance the U. S. could go into recession. "On October 1st, the Bureau of Economic Analysis reported that an additional 156,000 jobs had been lost in September. On April 29, 2008, nine U.S. states were declared by Moody's to be in a recession. Although the U. S. Economy grew in the first quarter by 1 % by June 2008 some analysts stated that due to a protracted credit crisis and "rampant inflation in commodities such as oil, food and steel", the country was nonetheless in a recession.

d) India:

India has seen the rate of growth of GDP decrease, generally attributed to reduced liquidity, sector price inflation in food and energy, and the USA slowdown.

IV) Causes of Recessions:-

1- Currency crisis:

A currency crisis, which is also called a balance-of-payments crisis, occurs when the value of a currency changes quickly, undermining its ability to serve as a medium of exchange or a store of value. It is a type of financial crisis and is often associated with a real economic crisis. Currency crisis can be especially destructive to small open economies or bigger, but not sufficiently stable ones. Governments often take on the role of fending off such attack by satisfying the excess demand for a given currency using the country's own currency reserves or its foreign reserves. Recession attributed to currency crises include the 1997 Asian Financial Crisis and the Argentine economic crisis (1999-2002).

2- Inflation:

In economics, inflation or price inflation is a rise in the general level of prices of goods and services in an economy over a period of time. The term Inflation once referred to increase in the money supply; however, economic debates about the relationship between money supply and price levels have led to its primary use today in describing price inflation. Inflation can also described as a decline in the real value of money – a loss of purchasing power. When the general price level rises, each unit of currency buys fewer goods and services. A chief measure of price inflation is the inflation rate, which is the percentage change in a price index over time.

Inflation can cause adverse effects on the economy. For example, uncertainty about future inflation may discourage investment and saving. Inflation may widen an income gap between those with fixed incomes and those with variable incomes. High inflation may lead to shortages of goods as consumers begin hoarding them out of concern their prices will increase in the future.

3-National Debt:

Government debt is money owned by any level of government; central government, federal government, municipal government or local government. As the government for the people, government debt can be seen as an indirect debt of the taxpayers. Government debt can be categorized as internal debt, owed to lenders within the country, and external debt, owed to foreign lenders. Governments usually borrow by issuing securities, government bonds and bills. Less credit worthy countries sometimes borrow directly from supranational institutions. Some consider all government liabilities, including future pension payments and payments and payments for goods and services the government has contracted but not yet paid, as government debt. Another common division of government debt is by duration. Short term debt is generally considered to be one year or less term is more than ten years. Medium term debt falls between these two boundaries.

4- Speculation:

Speculation, in a financial context, is making an investment that increases the overall risk in a portfolio. The opposite of speculation is hedging, which is making investments that decrease the overall risk in a portfolio. The reason the context of a portfolio is important can be illustrated by example; investing in futures contracts to buy oil is generally considered to be risky and speculative; however, if your portfolio predominantly contains airlines, investing in oil could very well reduce or hedge your risk. Investment is the assumption of the risk of loss, in return for the uncertain possibility of a reward. Financial speculation involves the buying, holding, selling, and short-selling of stocks, bonds, commodities, currencies, collectibles, real estate, derivatives, or any valuable financial instrument to profit from fluctuations in its price as opposed to buying it for use or for income via methods such as dividends or interest. Speculation represents one of three market roles in western financial markets, distinct from hedging and arbitrage.

5- War:

War is an international relations dispute, characterized by organized violence between national military units. War is "continuation of political intercourse, carried out with other means". War is an interaction in which two or more militaries have a "struggle of wills". When qualified as a civil war, it is a dispute inherent to a given society, and its nature is in the conflict over state governance rather than sovereignty. War is not murder or genocide because of the usually organized nature of the military's participation in the struggle, and the organized nature of units involved. War is also a cultural entity, and its practice is not linked to any War is a universal phenomenon whose from and scope is defined by the society that wages it. The conduct of war extends along a continuum, from the almost universal tribal warfare that began well before recorded human history, to wars between city states, nations, or empires.

Depending on the amount of damage and the weapons used, farmlands may become infertile and certain regions may be uninhabitable due to radiation contamination. In other cases, a victory and little damage to industrial capacity at home might pull the country out of a depression as happened to the United States in World War II.

V)Effects of Recession:-

a-Bankruptcy:

Bankruptcy is a legally declared inability or impairment of ability of an individual or organization to pay their editors. Creditors may file a bankruptcy petition against a debtor in an effort to recoup a portion of what they are owed or initiate a restructuring. In the majority of cases, however, bankruptcy is initiated by the debtor "voluntary bankruptcy" that is filed by the bankrupt individual or organization. The current example of Lehman Brothers and other.

b-Deflation:

Deflation is the opposite of inflation. Therefore, under the usual contemporary definition of inflation, deflation means a decrease in the general price level. Alternatively, the term was used by the classical economists to refer to a decrease in the money supply and credit; some economists, including many Austrian school economists, still use the world in this sense. The two meanings closely related, since a decrease in the money supply is likely to cause a decrease in the price level. Deflation is considered a problem in a modern economy because of the potential of a deflationary spiral and its association with the Green Depression, although not all episodes of deflation correspond to periods of poor economic growth historically.

c- Foreclosure:

Foreclosure is the legal professional proceeding in which a mortgagee, or other line holder, usually a lender, obtains a court ordered termination of a mortgagor's equitable right of redemption. Usually a lender obtains a security interest from a borrower who mortgages or pledges an asset like a house to secure the loan. If the borrower defaults and the lender try to repossess the property, courts of equity can grant the owner the right of redemption if the borrower repays the debt. When the equitable right exists, the lender cannot be sure that it can successfully repossess the property, thus the lender seeks to foreclose the equitable right of redemption. Other lien holders can and do use foreclosure, such as for overdue taxes. The foreclosure process as applied to residential mortgage loans is a bank or other secured creditor selling or repossessing a parcel of real property after the owner has failed to comply with an agreement between the lender and borrower called a mortgage or deed of trust. Commonly, the violation of the mortgage is a default in payment of a promissory note, secured by a lien on the property. When the process is complete, the lender can sell the property and keep the proceeds to pay off its mortgage and any legal costs, and it is typically said that the lender has foreclosed its mortgage or lien. If the promissory note was made with a recourse clause then those if the sale does not bring enough to pay the existing balance of principal and fees the mortgagee can file a claim for a deficiency judgment.

d- Stock Market Crash:

A stock market crash is a sudden dramatic decline of stock prices across a significant cross-section of a stock market. Crashes are driven by panic as much as by underlying economic factors. They often follow speculative stock market bubbles. Stock market crashes are in fact social phenomena where external economic events combine with crowd behavior and psychology in a positive feedback loop where selling by some market participants drives more market participants to sell.

e- Unemployment:

Unemployment occurs when a person is available to work and currently seeking work, but the person is without work. The prevalence of unemployment is usually measured using the unemployment rate, which is defined as the percentage of those in the labor force who are unemployed. The unemployment rate is also used in economic studies and economic indexes such as the states as a measure of the state of the macroeconomics. There are a variety of different causes of unemployment, and disagreement on which causes are most important. Different schools of economic thought suggest different policies to address unemployment. Monetarists for example, believe that controlling inflation to facilitate growth and investment is more important, and will lead to increased employment in the long run. Keynesians on the other hand emphasize the smoothing out of business cycles by manipulating aggregate demand. There is also disagreement on how exactly to measure unemployment. For example, the conservative government, when in power in the United Kingdom, changed the way in which employment was measured several times. Each time, the figure reduced. Different countries experience different levels of unemployment; the USA currently experiences lower unemployment levels than the Union, and it also changes over time throughout economic cycles.

VI) How United State Recession Comes:-

The US economy, as well as the world economy, is proving to be most resilient. This has persuaded most observers to expect moderate economic growth of 2 to 3 per cent and a moderate inflation around 2 per cent for years to come, while unemployment remains at a thirty year low. Let us remember that the US gross domestic product is the largest in the world at more than $ 13 trillion, that Americans have a net home equity equal to about $ 14 trillion, while American households have a net ownership of corporate equities of about $ 10.5 trillion.

Thus, what could be the reasons for slower economic growth in the coming months?

1- First, the artificial short term stimulus that the Bush-Cheney administration gave the economy before the 2004 and 2006 elections, through a combination of large tax cuts and large increases in military outlays, is about to run its course, and the piper will have to be paid.

2- Record budgetary and current account deficits have severely neutralized the Fed's monetary policy stance because interest rates cannot be reduced substantially for fear of a collapse of the US dollar; while fewer stimuli is expected from the federal budgetary deficits as they are being slowly reigned in.

3-All this is taking place at the same time that the construction industry is in disarray and housing prices have tapered off or are declining.

4-During the years of the housing boom, consumer spending was driven by the accumulating of wealth and record consumer indebtedness, most of it in the form of mortgages, as the price of houses increased. Now that the reveres is occurring and foreclosures are on the way up, a retrenchment in consumer spending cannot be ruled out. Logically, especially with consumer confidence crumbling. This should be expected.

5-A fifth factor is now entering the picture to make matters potentially worse: The protectionist push from the democrat controlled congress risks putting in jeopardy the flow of capital of about $2 billion a day that the US economy is borrowing from abroad, mainly from China and Japan.

Looming trade frictions between the US and China could force the Fed to raise interest rates, and not lower them as most observers expect-in any case, the Fed would surely not lower them as much as it would be warranted to alleviate the housing crisis.

6-As a sixth factor, would be the collapse of one and possibly several major financial institutions under the pressures of bad loans and record foreclosures. Particularly at risk is the some $ 2.5 trillion mountain of debt concentrated in subprime. Others are likely to follow, because 2007 is the year when a large number of prime real estate loans have to be renegotiated at higher interest rates.

7-A seventh geopolitical factor could also throw fuel on the fire. Indeed, if the clumsy Bush-Cheney regime goes ahead with its bomb and attack Iran, the coming US economic slowdown could be transformed into something much worse. Indeed, during the coming years, the word economy will have to adjust to a peak in oil production and to higher energy prices, after the current lull. If geopolitical mistake turn the richest oil producing region into a hot war zone for many years to come, the worldwide economic consequences will be disastrous.

VII) Impact on a US Recession on India:-

A slowdown in the US economy is bad news for India. Indian companies have major outsourcing deals from the US. India's exports to the US have also grown substantially over the years. The Indian economy is likely to lose between 1 to 2 percentage points in GDP growth in the next fiscal year. Indian companies with big tickets deals in the US would see their profit margins shrinking.

The worries for exporters will grow as rupee strengthens further against the dollar. But, experts note the long-term prospects for India are stable. A weak dollar could more foreign money to Indian markets.

1-A credit crisis in the US might lead to a restructuring of asset allocation at pension funds. A large portion of this is likely to flow into India and China. If other funds follow suit, a cascading effect can be expected. Along with the already significant dollar funds available, the additional funds could be deployed to create infrastructure-roads, airports, and seaports- and be ready for a rapid takeoff when normalcy is restored.

2-It terms of specific sectors, the IT Enabled Services sector may be hit since a majority of Indian IT firms derive 75 % or more of their revenues from the United States – a classic case of having put all eggs in one basket. If Fortune 500 companies slash their IT budgets, Indian firms could be adversely affected. Instead of looking at the scenario as a threat, the sector would do well to focus on product innovation. If this is done, India emerges as a major player in the IT products category as well.

3- The manufacturing sector will be hit. This sector has to ramp up scale economies, and improve productivity and improve productivity and operational efficiency, thus lowering prices, if it wishes to offset the loss of revenue from a possible US recession.

4- The tourism sector could be affected. Now is the time to aggressively promote health tourism. Given the availability of talented professionals, and with a distinct cost and vantage, India can be the destination of choice for health tourism.

5- A recession in the United Nation may see the loss of some jobs in India. The concept of Social Security, that has been absent until now, may gain momentum.

6- The Indian Rupee has appreciated in relation to US dollar. Exporters are pushing for government intervention and rate cuts. What is conveniently forgotten in this debate is that a stronger Rupee would reduce the import bill, and narrow the overall trade deficit. The Indian central bank can intervene anytime and cut interest rates, increasing liquidity in the economy, and catalyzing domestic demand. A strong domestic demand would also help in competing globally when the recession is over.

VIII)CONCLUSION:-

1-We saw the definition of recession occurs when the natural growth rate in GDP is less than the average of 2% typically a normal economic recession lasts for approximately 1 year. US economy grew in first quarter by 1% by June.

2-India is an emerging economy and effect of recession in our growth is slowdown.

3-There is liquidity problem many countries gives liquidity to market. We should try to make the trade cycle functional.

4-The Indian government has already injected Rs 1,80,000 corers of liquidity into the economy through RBI and fiscal measures. Other governments have been proactive too.

5-At the macro-level, a recession in the US many bring down GDP growth, in India too, but not much. At the micro-level, specific sector could be affected.

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