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Economic Recession-(2008 to 2010) Its Impacts on Indian Economy

Abstract

The term Business cycle or Economic cycle refers to the fluctuations of economic activity (business fluctuations) around its long-term growth trend. The cycle involves shifts over time between periods of relatively rapid growth of output (recovery and prosperity), and periods of relative stagnation or decline (contraction or recession). These fluctuations are often measured using the GDP. Traditional business cycles undergo four stages: expansion, prosperity, contraction, and recession. The phases of the business cycle are characterized by changing employment, industrial productivity, and interest rates. Some economists believe that stock price trends precede business cycle stages. Despite being termed cycles, these fluctuations in economics growth and decline do not follow a purely mechanical or predictable periodic pattern.

After the disintegration of the USSR there has been a Consistent effort by the US to project that the world is no more bipolar but it is unipolar and the pole is none but the US. Besides the great depression of 1929-1933 the US has seen seventeen recessions. And the Recession of 2008 is the next Globalization, privatization and Industrialization has made the counties so interdependent that a change in any economic barometer, in any country especially which is economically strong, is felt in other countries too.

In the light of above states facts this article deals to understand: what is an economic recession? How it has affected the Indian industries? What are the remedies to get rid off this problem/How to respond to a recession?

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Introduction

History of Economic Recession

Economic recessions have occurred all throughout the history of modern economics. The National Bureau of Economic Research defines economic recession as a significant decline in the economic activity spread across the economy, lasting more than a few months. An average of more than 5,00,000 business failed in United States during each of the 10th recession that have occurred since the end of IInd world war. The United States is not the only county to suffer from them but any country that has similar modern economic structure has suffered from economic recession.

The United States suffered from first recession in the years between 1797 and 1800. It was called the ‘Panic of 1797’, and it was primarily caused by the deflating effects of the Bank of England as they crossed the Ocean to American soil.

The next recession occurred in the years between 1807 and 1814, and it was called the ‘Depression of 1807’. This depression was primarily caused by the Embargo Act of 1807. This act destroyed a good part of the shipping related industries.

The ‘Panic of 1819’ soon followed. This panic brought with it widespread foreclosures, failing banks, huge unemployment rates, and a gigantic slump in manufacturing and agriculture that caused havoc among Americans.

Economic recessions in America continued with the ‘Panic of 1837’. This recession can really be attributed to failing banks and the lack of confidence people had in paper currency, which was becoming popular at the time. Banks stopped paying out in gold and silver, which really took its toll on American confidence.

The ‘Panic of 1857’ was not longer. This panic affected the railroads and U.S. banks, causing over 5,000 businesses in America to fail in the first year of the panic alone. Unemployment rose, and protest meetings became popular.

Recessions continued to plague not only America, but the rest of the world too. Countries like Germany, U.K., China, and Japan all had trouble with recessions. In fact, economists say that Germany is in for what might be the biggest recession in all of German history. Japanese economic recession has also played a huge part in their history.

In the year 2001, the early 2000s recession hit America. The attacks that occurred on September 11th on the 'World Trade Center Towers' in New York City accounting scandals also ran rampant, contributing to the overall downward financial spiral that America faced. Everyone remembers the attacks on America's soil, and nobody will forget how, despite economic trouble, the attacks brought Americans together, more united than ever. And with that kind of perseverance, America was led out of that struggle to a new future of prosperity.

The modern economic cycle again comes around to purge itself of the problems put on it by humanity, and unfortunately, that purge is known to us as recession.

Aim of the Study

The main aim of present research study is to analyze the impact of global financial crisis on Indian economy in terms of growth rates of real Gross Domestic Product (GDP) and examine the sector-wise impact of the crisis in the Indian economy.

Review of Literature

Mohanty (2010) in his speech has commented about the impact of global financial crisis of 2008 on the Indian economy, he comments as the crisis showed that while increasing globalization and trade integration have brought enormous economic and financial benefits to the Emerging Market Economies (EMEs), they have also widened the channels through which slowdown in economic activity in advanced economies could spread to the EMEs. Mohan (2009) in his speech has commented about the impact of global financial crisis on the various sectors of the Indian economy. Prasad and Reddy (2009) have assessed the impact of financial crisis on India; they say that the impact of the crisis on the Indian economy relatively has been less when compared to USA, UK and European Union. Sengupta (2008) has observed that surplus inventory of houses and increase in interest rates led to decline in housing prices in 2006-07 resulting in an increased defaults and foreclosure activity that collapsed the housing market. Onaram (2008) has viewd that due to the failure of a few leading institutions in US, the entire financial system in the world has been affected.

What is Recession?

National Bureau of Economic Research (NBER, US. Based) defines Economic Recession as: "a significant decline in the economic activity spread across the economy, lasting for more that a few months, normally visible in Real GDP growth, Real Personal Income, Employment (non-farm payrolls), Industrial Production, and Wholesale-Retail Sales."

In economics, the term Recession is- The reduction of a country's Gross Domestic Product (GDP) for at least two quarters. The dictionary definition of recession is "a period of reduced economic activity, a Business Cycle contraction".

Thus when the growth rate of GDP (Gross Domestic Product) is increase it implies that economy is growing and its indicate the profits and when the GDP growth rate is slowed down its implies that it is a period of recession. It is the period of slowdown and it indicates the losses.

Investment decrease and people invest less since they are not sure of the returns. The amount of profit made by the business sector decrease substantially since their investment does not yield any profit. A large number of people are jobless due to economic recession. Some companies may also close their operation for an indefinite period of time due to heavy losses even government level recovery packages cannot bail them out from such scenario. There may be a general decrease in the price level of some commodities and services. Oil prices may fall down due to lack of demand. The price of property and cars also go down since the demand for these things decrease during a period of recession. Many major companies around the world suspend their production in order to cope up with the stress which they receive due to economic recession.

The demand and supply shows the parameter. The increase in demand indicates the level of general consumer satisfaction and they feel safe to go for various expenditure. The decrease in demand implies that the general consumer is not satisfied with the economic scenario and does not feel safe in investment. Thus it can be said that when the demand falls then supply chain is also affected due to the initial phase of decline.

What is Economic Recession?

Economic crisis of lesser intensity is referred to as a recession. Recession marks a downward trend in business and it is caused by an imbalance between the quantity and quality of goods and the consumer feels his inability to buy them. If a recession continues for a long period, it can turn into depression. Economic downturn is characterized by lack of confidence in business. Recovery from economic depression is normally slow. In the modern time, consumer demand has been reduced a major reason for such depression. Million of people have become insolvent and their balance sheets have gone bust. This time is to restore consumer confidence in the market. There are many industries in jobs that have been not affected by the economic downturn. Food, household goods, essential commodities, telecomm, health care, military and security sectors generally have robust demand. These sectors can generate employment to a large number of people.

Causes of Economic Recession

Economic recession depends on demand. The fate of modern economics is determined by four types of demand. The demand for consumer goods, the demand for money, demand for investment goods and the demand for assets which represents the expected utility of money.

Economic recession is unavoidable in a perpetual fluctuation of economic boom and decline. Not a single nation is affected for recession nor are they blessed with forever booming. An individuals and business expenditures is an effort to trim cost. It happens when GDP declines and the unemployment rate rises because companies lay off workers to cut their costs. It is a combine factor that causes the economy to fall into a recession.

Effect o Economic Recession

An economic recession can usually spot before it happens. When the economy sees extending periods of economic recession, the economy can be referred to as being in an economic depression. During a mild economic recession, one can focus on being invested in recession proof sectors in the market such as gold, silver, agriculture, bonds and consumer stocks.

The most apparent and straight forward result of an economic recession is the reduction in overall national output. Where in all people suffer from a decline standard of living compared with normal output or full potential output.

Recession Effects of the Recession Cycle

The recession effects of the recession cycle can be discussed under the separate heads mentioned below:

Consumer Spending Might Go Down

As consumers tight their purse strings and spend their money just on essential items, there can be a decrease in your sales, especially if you are dealing in non-essential items. Even if you do manage to maintain your sales, your profit margins may still come down. You may have to devise new and innovative methods to attract customers towards your business.

Competition could Get Fierce

As the economic cycle enters into a recession, the competition will get fiercer since there will now be many competitors fighting over a smaller pie. But take heart and don't be puzzled, because this cycle will also result in your weaker competitors closing their shutters.

EXPENSES WILL GO UP

Along with your sales coming under pressure, your expenses will also go up as inflation starts pinching your wallet. This will result in you tightening your financial belt, as your business becomes part of this downward cycle. You will have to ensure that you give priority only to those expenses that directly affect your business over those that do not. Moreover, if you don't have a lot of savings, then spending on luxury items through your credit card can not be advisable.

Business will become Unpredictable

The downside of this economic fluctuation is that your business will become unpredictable. At times, you will find that customers have vanished into thin air - while during other times, you might think that you are experiencing a sales boom. It pays to have a cool and calm head during such fluctuating periods.

Interest Rates may Come Down

During a recession, interest rates may come down; and in case you need to apply for a loan, then you may not be faced with high interest rates. The only problem is, since there will be a liquidity crunch in the monetary markets, you may have a tough time qualifying for a loan as lenders' qualifying standards go invariably higher.

Get A Chance to Invest Outside Business

A recession may induce the stock markets and property markets to fall drastically. This can offer you a chance to invest in stocks or property due to lower prices. And once the economy moves back into the boom cycle, then your investments will be worth quite a lot more.

Employees can Demand Higher Salaries

As inflation attacks on the pockets of your employees, they can ask for higher salaries in order to maintain their lifestyles. You may then have to let go inefficient employees in order to maintain your payroll at the same level.

Impact of Us Recession 2008 in India

Though recession is altogether unwanted, almost everyone appears reconciled to one in the United States. Meanwhile, politicians continue to downplay any fears of global recession but what is the reality for countries like India?

It would be naïve to imagine that a recession in the United States would have no Impact on India. The United States accounts for one-fourth of the world GDP and any significant slowdown is bound to have impacts elsewhere. On the other hand, interdependencies between the US economy and emerging economies like India and China has reduced considerably over the last two decades. Thus, the effect may not be as drastic as would have been the case in the 1980s.

Irrespective of above stated facts, fears of a US recession led to panic in the Indian stock market. January 21 and 22 saw a huge loss of US$450 billions. An unprecedented interest cut by the Fed led to a bounce-back on January 23, the benchmark index (BSE) has gained 2.5%, almost in line with Hang-Seng, Nikkei, and Kospi. History holds a clue and a co-relation here. The last time bubble burst (2001-2002), the DJIA went down by 23%, while the Indian fell by 15%.

But the situation has changed between then and now. The Indian economy has shown a robust and consistent growth trajectory and to add the projection for 2008 is 9% Indian exports to the United States account for just over 3% of GDP. India has a healthy trade surplus with the United States. In other words, the effects of this recession on India may be quite distinct from those of the past.

Here are some areas worth following:

1. A credit crisis in the United States might lead to a restructuring of asset allocation at pension funds. It has been suggested that CALPERS (California Public Employees' Retirement System) is likely to shift an additional US $ 24 billion to its international portfolio. A large portion of this is likely to flow into India and China. Along with the already significant dollar funds available, the additional funds could be deployed to create Infrastructure-roads, airports, and seaports-and is ready for a rapid takeoff when normalcy is restored.

2. In 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 (as opposed to merely providing services). If this is done, India can emerge as a major player in the IT products category as well.
3. The Manufacturing sector has to ramp up scale economies, and improve productivity and operational efficiency, thus lowering prices, to offset the loss of revenue from a possible US recession. The demand for appliances, consumer electronics, apparel, and a host of products is huge and can be exploited to the advantage by adopting appropriate pricing strategies. Although unlikely, a prolonged recession might see the emergence of new regional groupings-India, China, and Korea.
4. The tourism Sector could be affected. Now is the time to aggressively promote healthy tourism. Given the availability of talented professionals, and with a distinct cost advantage, India can be the destination of choice for healthy tourism.
5. A recession in the United States 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 the 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 (Reserve Bank of India) can intervene anytime and cut interest rates, increasing the liquidity in the economy, and catalyzing domestic demand. A strong domestic demand would also help in competing globally when the recession is over.

To summarize, at the macro-level a recession in the US may bring GDP growth, but not by much. At the micro-level, specific sectors could be affected. Innovation now may prove to be the engine for growth when the next boom occurs. For US firms, who have long looked at China as a better Investment destination, this may be a good time to look at India as well. After all, 350 million people with purchasing power cannot be ignored.

Conclusion

In the end it can be said that as evolution in animals dictates that only the fittest survive in an economic downturn, the cycle dictates that it is the survival of the smartest. You will need to adapt, save and earn more if you want your small business to come out of the recession unscathed and stronger than ever.

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