

# Global Financial Crisis: Implications for India's Development

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# Introduction

- ▶ **Global Financial Crisis: Background Information**
  - What is happening on the global financial markets?
  - What does it mean for developing countries in Asia?
- ▶ **Implications for India**
  - Economic impact
  - Social and development sectors
- ▶ **Policy responses and recommendations**
- ▶ **Role of the civil society: what can be done from the development perspective?**



# What is happening on the global financial markets?

- ▶ **Rapid growth of speculative lending and deregulation of financial market over the past couple of decades**
- ▶ **Increase in global liquidity and risk appetite e.g. subprime lending and mortgage-backed securities**
- ▶ **Comprehensive and global crisis, encompassing the banking sector, securities and currency markets, and institutional and individual investors in most parts of the world**
- ▶ **Impact of the crisis on growth in the United States and its global spillovers to other parts of the world through international trade and financial system**



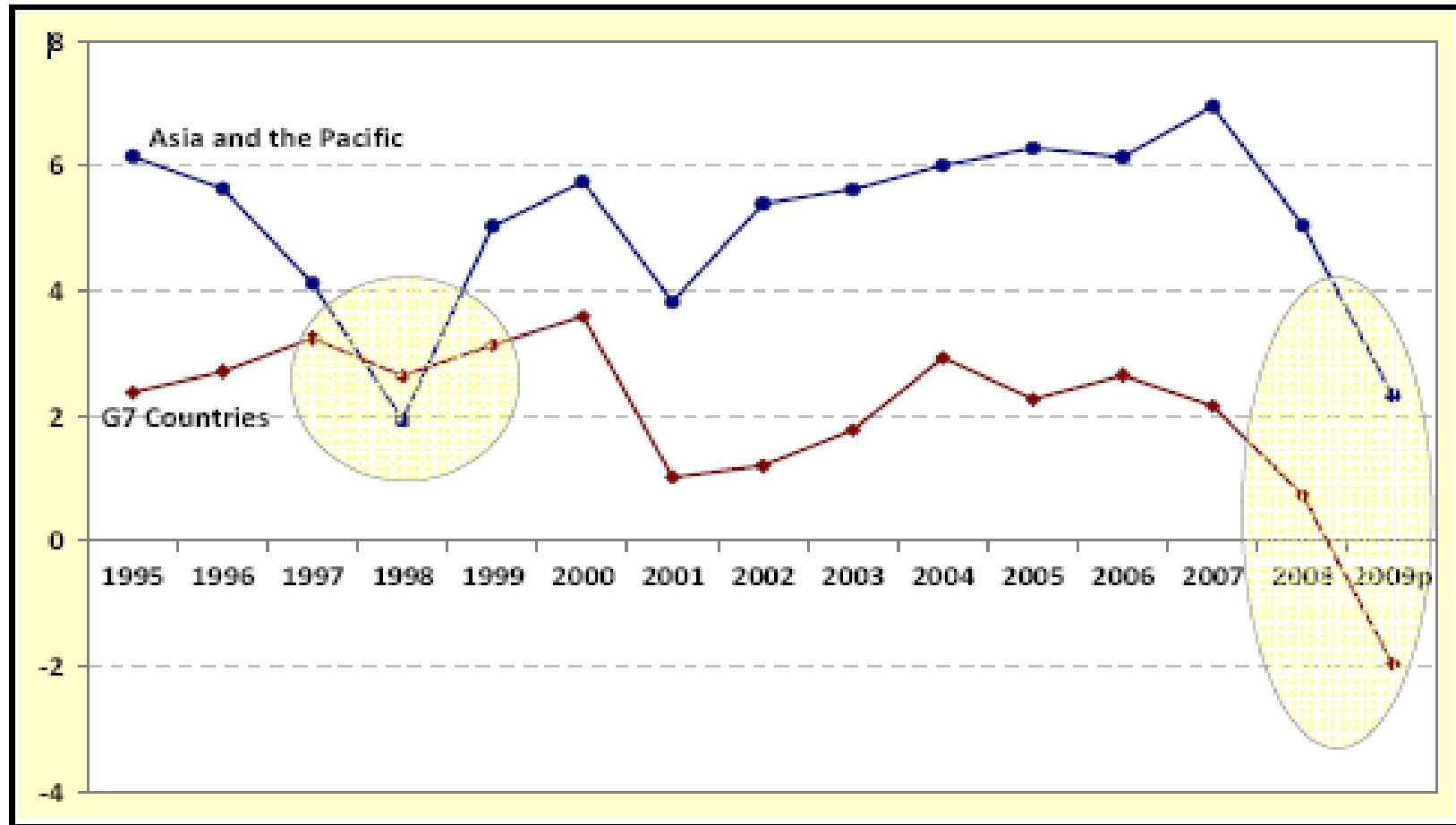
# Transmission mechanisms to Asian economies

- ▶ **Asian economies do not have large direct exposure to securitized assets linked to high-risk lending.**
- ▶ **Nevertheless, the slowdown in the global economy and key channels for transmission of the crisis from developed to developing countries has been:**
  - **Massive reversal of private capital flows, which has been more severe in emerging markets than lower income countries**
  - **Declining trade volume i.e. decreasing demand in industrialized economies for Asian exports and lowered industrial output**
  - **Remittances at risk, depending on remittance share of GDP: Nepal (17%), Philippines (11.7%), Bangladesh (9.7%), Sri Lanka (8.3%)**
  - **Pressure on domestic investment**

*\*Source: UNDP Working Paper, The Financial Crisis and Its Impact on Developing Countries, 18 January 2009*



# Annual GDP Growth (%) 1995-2009, Asia versus the G7 Countries



\*Source: ILO calculations, Responding to Economic Crisis 18-20 February 2009



# What does it mean for developing countries

## Degree and nature of impact depend on the following factors:

- ▶ Degree of financial markets integration in the global market e.g. Brazil, China, India are likely to experience immediate impact
- ▶ Particular sectors e.g. tourism and mining, as well as informal sector
- ▶ Whether economies depend on remittances
- ▶ Level of dependency on food and fuel imports
- ▶ Pressure on government budget expenditure due to falling revenue as a result of the economic slow down
- ▶ Vulnerabilities of particular social groups and/or populations

\*Source: PR-Net, Consolidating Online Discussion on *Impact of Financial Crisis on Developing Countries*, 14 January 2009



# Implications on India

## ***Economic Impact*** – implications on growth and employment

- ▶ **Service sector, including banking, finance and IT sectors**
- ▶ **Real sector such as manufacturing and exports**

## ***Social and development Impact***

- ▶ **Employment and poverty reduction efforts**
- ▶ **Government's fiscal position, particularly development expenditures**
- ▶ **The achievement of the Millennium Development Goals (MDGs)**



# Impact on India's Economy

- ▶ **Growth declined to 7.3% in 2008, down from 9.3% in 2007**
- ▶ **Current Government estimates are for approx 6.5% to 7.5% growth in 2009, but the IMF forecast is for growth to fall to 5.1%**

## As economic growth contracts...

- ▶ **Demand for labour has fallen**
  - **Large-scale job losses in some sectors**
  - **Rising unemployment & underemployment**
  - **Downward pressure on wages**
- ▶ **SMEs have been hit hard**
- ▶ **Informal economy has expanded**
- ▶ **Reverse migration has increased**



Source: ILO, The fallout in Asia: Assessing labour market impacts and national policy responses to the global financial crisis, 18-20 February 2009



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# Impact on India's Economy (Con't)

- ▶ **Global financial crisis affects credit and confidence of the banking and financial markets**
  - **The capital market – capital has become more expensive as banks are lending to each other at higher rates**
  - **The stock market – fall in value of stocks and real estate as a result of credit, assets and investment bubbles**
  - **The reversal of portfolio flows in India was large and have immediate impact**
- ▶ **Service sector, particularly the IT sector**
  - **Companies in the IT and financial sectors continue to downsize and cut costs and will not likely hire more people**



# Impact on India's Social and Development Sectors

## Three key aspects:

- ▶ Impact on employment and poverty
- ▶ Funding for development or development expenditure
- ▶ Achievement of the Millennium Development Goals (MDGs)



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# Impact on rural employment and poverty

- ▶ **Although the main transmission channels have primarily affected urban labour markets, the consequent effect on the rural economy, employment and household income cannot be underestimated.**
  - **Job losses in export manufacturing often affect the rural-to-urban migrants and their income support to their rural families.**
  - **Workers who are not able to find new urban employments, whether in formal or informal sector seek rural work opportunities**
  - **Process of reverse migration has already begun in India**
  - **This shift will often coincide with reduced wages and household income.**



# Rising unemployment

- ▶ **Rising unemployment in the Asia-Pacific Region**
  - **Low estimate: 7.2 million additional unemployed**
  - **High estimate: 23.3 million additional unemployed**
- ▶ **The number of unemployed in the region is projected to increase in 2009**
- ▶ **Over 2009 and 2010, an estimated 20.3 million additional jobs will be needed to absorb India's growing labour force**
- ▶ **There is very little chance that a sufficient number of new jobs will be created to keep up with expected labour force growth.**

**Source:** ILO, The fallout in Asia: Assessing labour market impacts and national policy responses to the global financial crisis, 18-20 February 2009



# Most vulnerable social groups

- ▶ **Marginalized and vulnerable populations**
- ▶ **Migrants and migrant workers**
- ▶ **Workers in the informal sector**
- ▶ **Youth**
  - **At least 3 times as likely as adults to be unemployed**
- ▶ **Women and children are among the most vulnerable social groups**
  - **Women likely to face larger increase in unemployment**
  - **Concerns of school drop-out and rise in child labour**



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## Most vulnerable social groups (Con't)



- ▶ **Indian workers in sectors with high exposure to the global market which employ millions of women workers have already faced job cuts:**

- **Civil aviation; Textiles; Leather; Gems; and Jewellery**

- ▶ **With the country's sub regional diversity, tailored assistance is critical to states with high global integration**

- **In Kerala, tens of thousands of workers are expected to face job losses in key export industries such as marine products and textiles**



# Fall in Development Funding/Expenditures

There is a major concern that the global financial crisis will:

- ▶ **Decline in financing for development through**
  - **Public channels** e.g. reduction in ODA and domestic resources following the global economic slow down
  - **Private channels** as NGOs and development organization are less able to raise funding
- ▶ **Reduce overall investments in social services and infrastructure**
  - **Over half of India's planned highway-improvement projects of more than \$6 billion could be delayed as much as two years. India expected private investment to fund around half of the more than \$100 billion a year in planned infrastructure development\***
- ▶ **Government budgets are also under constraints on the revenue side as the economies slow down.**

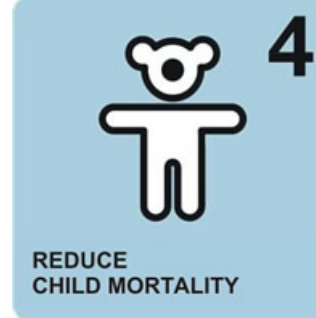
Source: The Wall Street Journal, "India Reins In Ambitious Building Plans",  
12 November 2008



# Achievement of the MDGs in India

*The global financial crisis could reverse progress in poverty reduction and MDG achievement.*

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# Global Financial Crisis: Implications for the MDGs

- ▶ **Facing a global economic slowdown in consumer demand, India's unemployment will rise along with a likely fall in total household income.**
- ▶ **The financial crisis could worsen the existing level of inequality in India**
- ▶ **Formalization of employment and reduction of working poverty will slowdown**
- ▶ **Despite lower inflation, the prices of many food items remain much higher in recent years. This means that the poor face a double crisis – high costs for basic necessities on which they spend the majority of their income, along with economic stagnation that threatens their livelihoods.**
- ▶ **Slowdown in eradicating poverty and extreme hunger will likely impact the achievement of other goals\***



# Nevertheless...

- ▶ **The impact of the global crisis on India has not been as sharp as in some other Asian economies because:**
  - **India is a relatively closed economy**
  - **Impact is limited to the urban industrial areas. India's urban areas are not closely integrated with the country's vast rural economy, the overall impact has been muted.**
  - **India has already put in place country-wide rural poverty alleviation programmes, which require government spending outside the fiscal stimulus packages.**



# India's policy response to the crisis?

- ▶ Rapidly deteriorating economic situation shifted the policy focus to **fiscal measures**
- ▶ By December 2008, India had already rolled out bold policies to increase aggregate demand. Within less than a month, it announced a second fiscal stimulus package.
- ▶ India's two fiscal packages together accounted for USD 8.1 billion represent 0.7% share of the country's GDP in 2008.
- ▶ Fiscal measures place greater emphasis on
  - Supporting particular industries, including labour-intensive and export-oriented businesses.
  - Ensuring liquidity in the financial system
  - Encouraging investment in infrastructure



# Key Policy Recommendations

- ▶ **Employment and incomes should be a central focus of the government's fiscal stimulus packages**
  - **Give priority to public spending programmes that have high multiplier effect on employment**
  - **Spread public spending and job creation broadly (including education, health, pension systems)**
  - **Target credit-constrained businesses (including SMEs) and consumers (the poor and low-income households)**



# Key Policy Recommendations (Con't)

- ▶ **Protect the poor and the vulnerable:**
  - **Social transfers serve dual purpose of stimulating domestic spending while also protecting the poor**
  - **Building effective social safety net programmes**
  - **Supporting poor families to keep their children in education**
  - **Increasing the scope and responsiveness of unemployment benefit system**



# Role of Civil Society: What can you do?

- ▶ **Studying the core issues and the impact of the global financial crisis on India's development**
- ▶ **Identifying and enhancing the voice of the most vulnerable social groups, particularly women and youth**
- ▶ **Enabling sound policy responses from the government:**
  - **Involving social partners in policy design**
  - **Promoting governance and accountability through social audit of government's social programmes**
- ▶ **Strengthening policy dialogue between government and civil society**
- ▶ **Campaign and advocacy to for programmes that protect the poor and vulnerable groups**



## Closing Remarks

***"Now more than ever we must be bold. In these times of crisis, when we are tempted to look inward, it is precisely the time when we must move pursuit of the common good to the top of the agenda. While recently we have heard much in the US about how problems on Wall Street are affecting innocent people on Main Street, we need to think more about those people around the world with no streets,"***

**Ban Ki-moon**

**UN Secretary General**

