

India's Experience During The Current Financial Crisis: A Capital Account Perspective and Policy Response



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to Global Financial Crisis and India-Japan Co-
operation” on 15.02.2010 in Delhi, India***

Dayanand Arora (HTW Berlin Germany)

***Francis Xavier Rathinam (ICRIER, New
Delhi, India)***

Shuheeb Khan (ICRIER, New Delhi, India)

This is our map for the Presentation



1. The Myth of “No Effect” on India
2. Openness of the Indian Economy
3. The Impact of the Crisis on India
4. Policy Response
5. Extent of Exposure (2008-10)
 - A In the Financial Economy
 - B In the Real Economy
6. Concluding Remarks

1. The Myth of “No-Effect” on India



- It is generally believed that the global financial crisis left India virtually unaffected! The arguments given were:
 - No Indian bank went bankrupt (No Systemic Risk)
 - No Indian financial institutions had any exposure to the sub-prime credit market in the US
 - Indian banks did not “search for yield” in the credit default swaps (CDS) and other securitized financial product markets

2. Openness of the Indian Economy (Selected Indicators I)

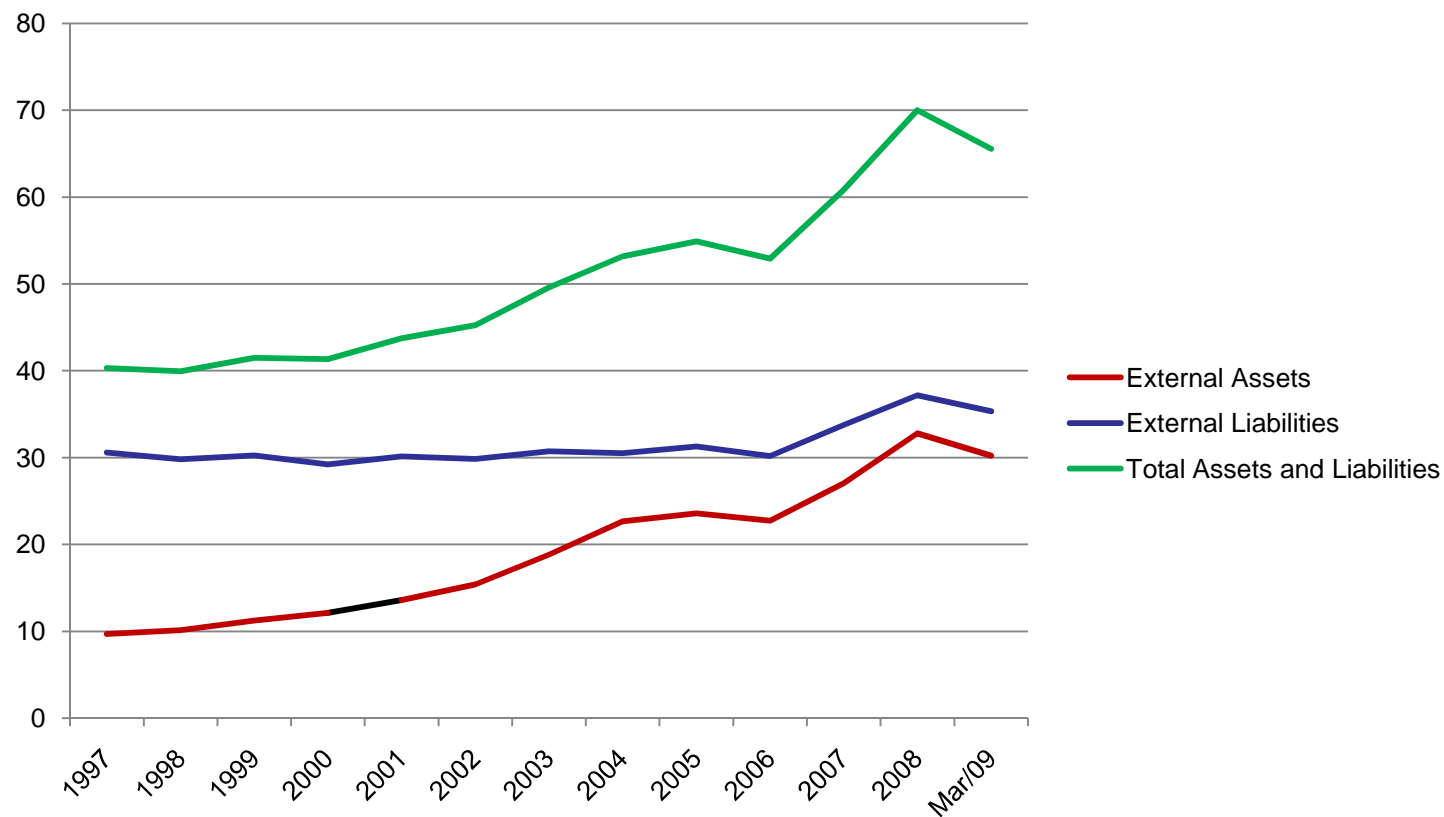


	March 1993	March 1998	March 2003	March 2007	March 2008	March 2009	Sept. 2009
Exports/GDP	7.3	8.7	10.6	14.1	14.2	15.1	14.5
Imports/GDP	9.6	12.5	12.7	20.9	22.0	25.5	24.9
CAD/ GDP	-1.7	-1.4	1.2	-1.1	-1.5	-2.6	-3.3
Gross Flows/ GDP	16.8	16.8	16.1	46.1	64.5	51.4	NA

2. Openness of the Indian Economy (Selected Indicators II)



External Assets and Liabilities (Scaled to GDP)



3. Impact of the Crisis on India (2008)

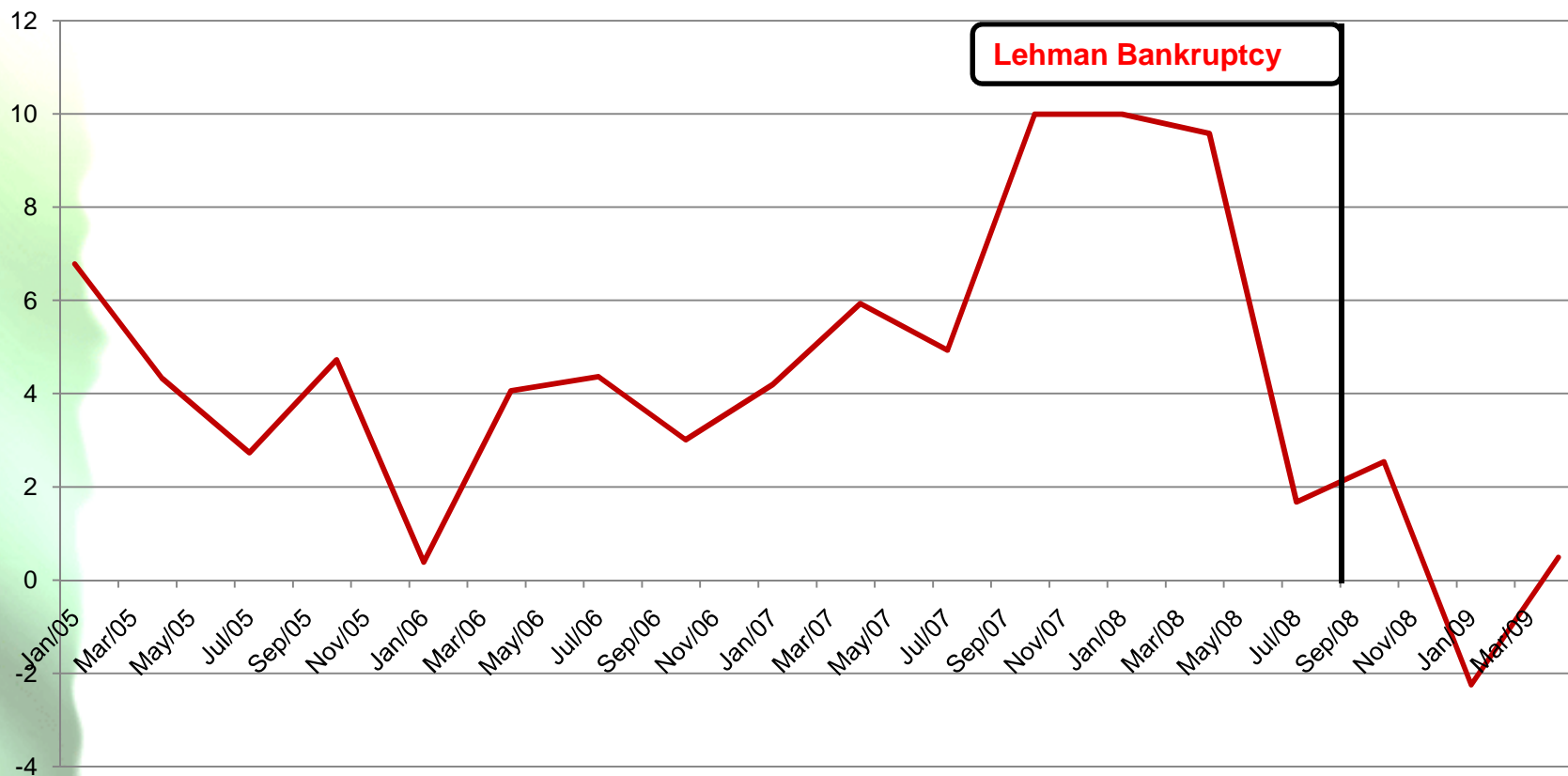


1. Net Capital Flows to India declines
2. Foreign Institutional Investors (FIIs) Withdraw Funds
3. Stock Market reacts strongly!
4. External Commercial Borrowings (ECB) Drop Sharply!
5. Rupee Depreciates
6. Foreign Exchange Reserves Fall

3. Impact of the Crisis on India



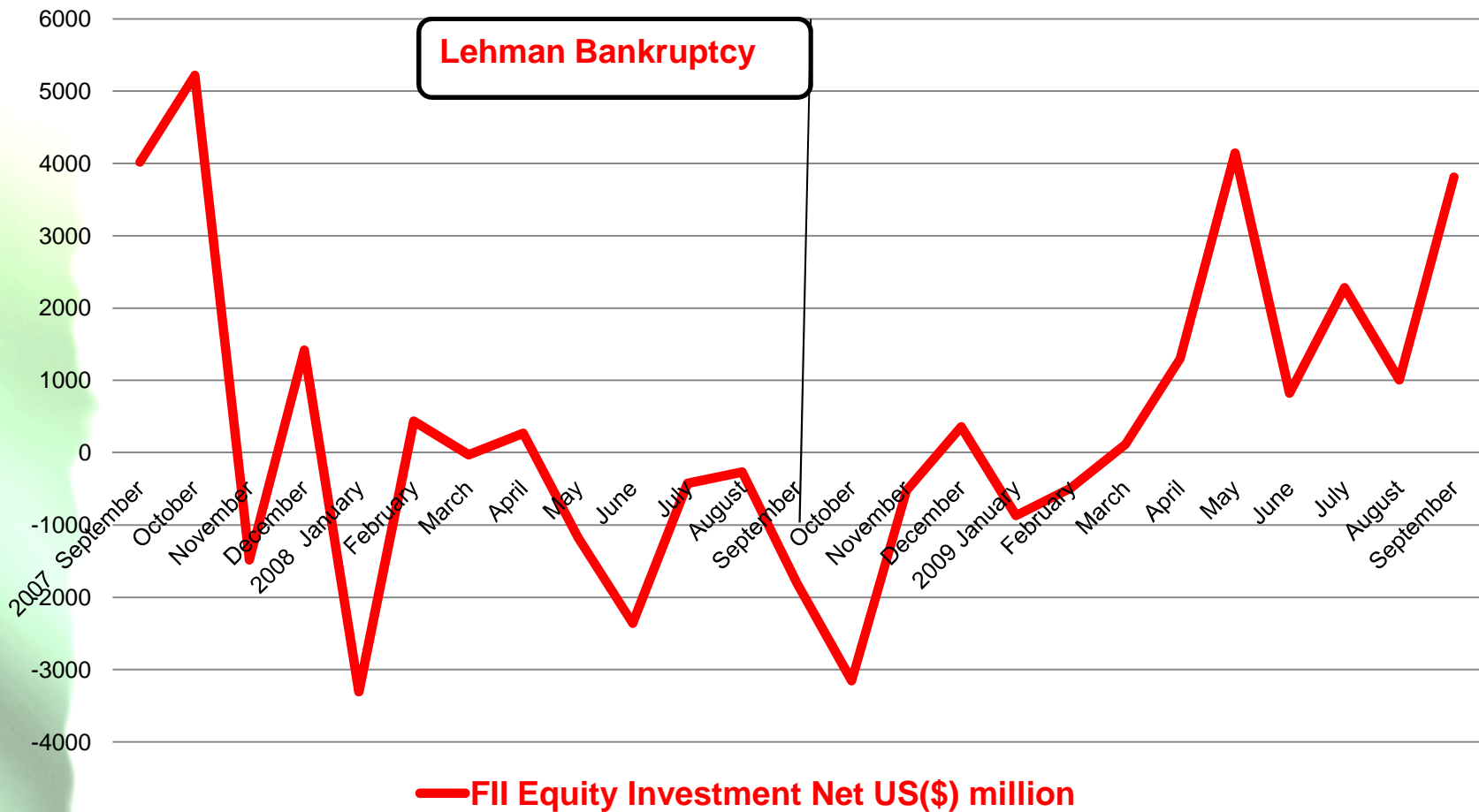
1. Net Capital Flows Decline (Scaled to GDP)



3. Impact of the Crisis on India



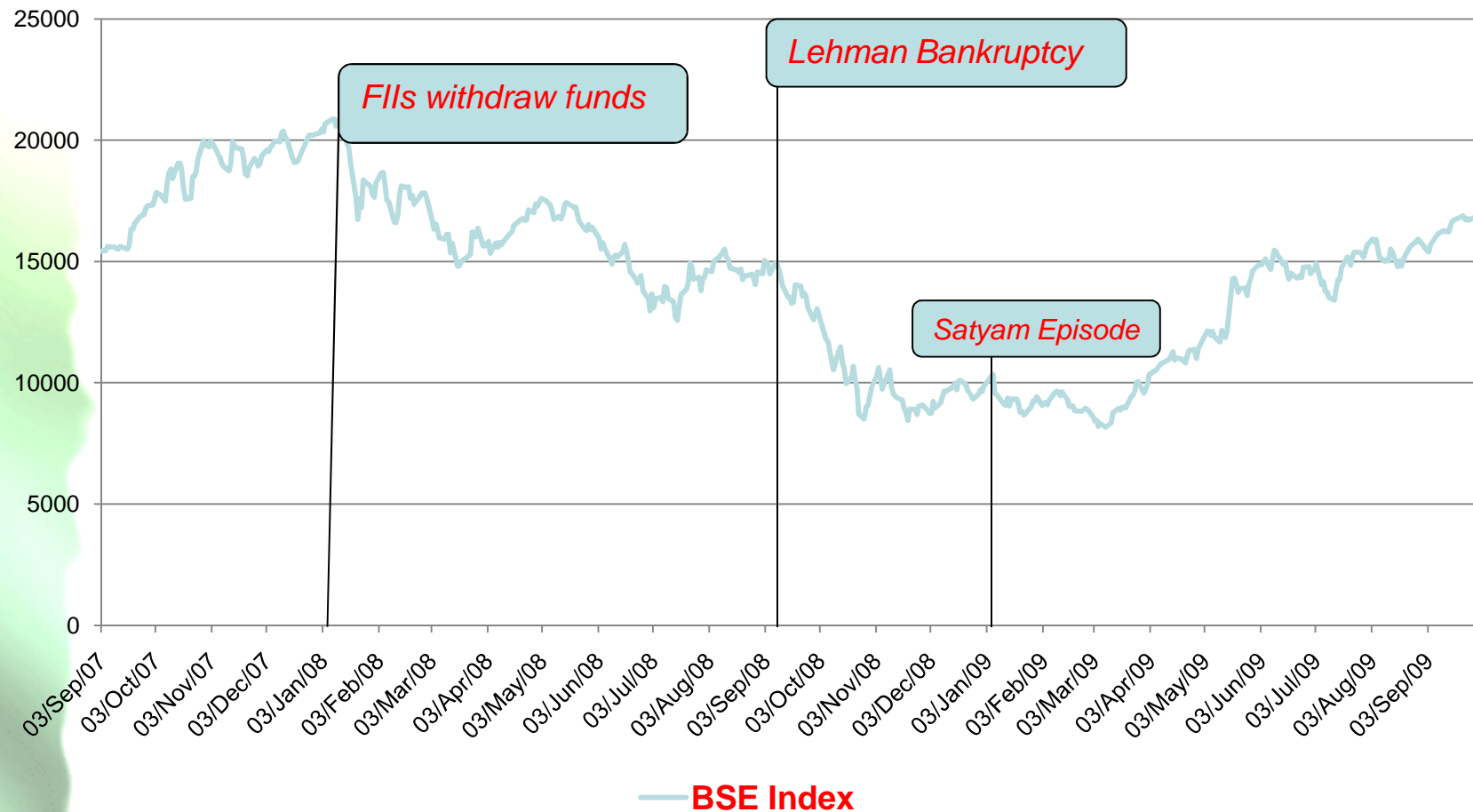
2. Foreign Institutional Investors Withdraw Funds



3. Impact of the Crisis on India



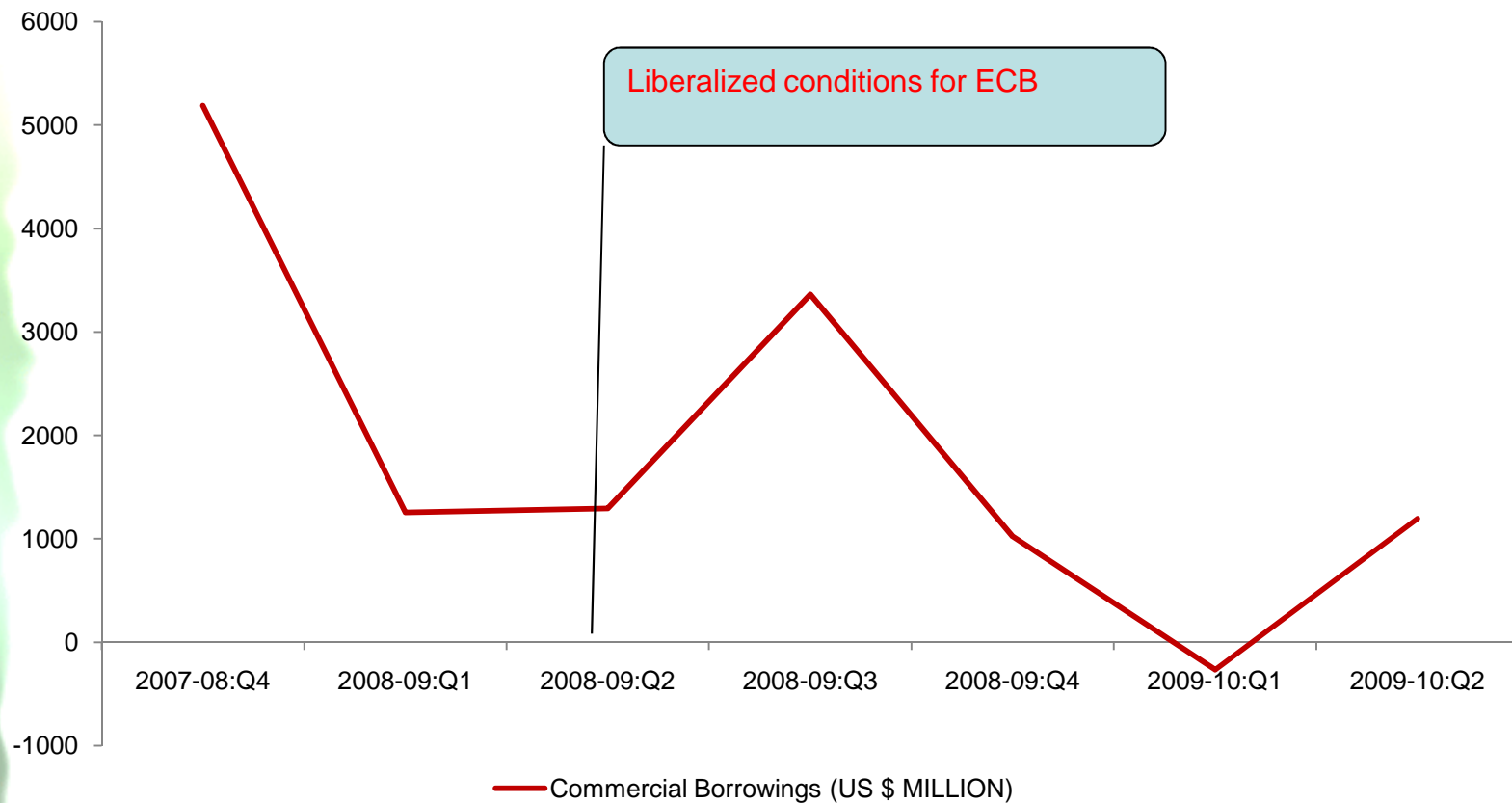
3. India's Stock Exchange Reacts Strongly



3. *Impact of the Crisis on India*



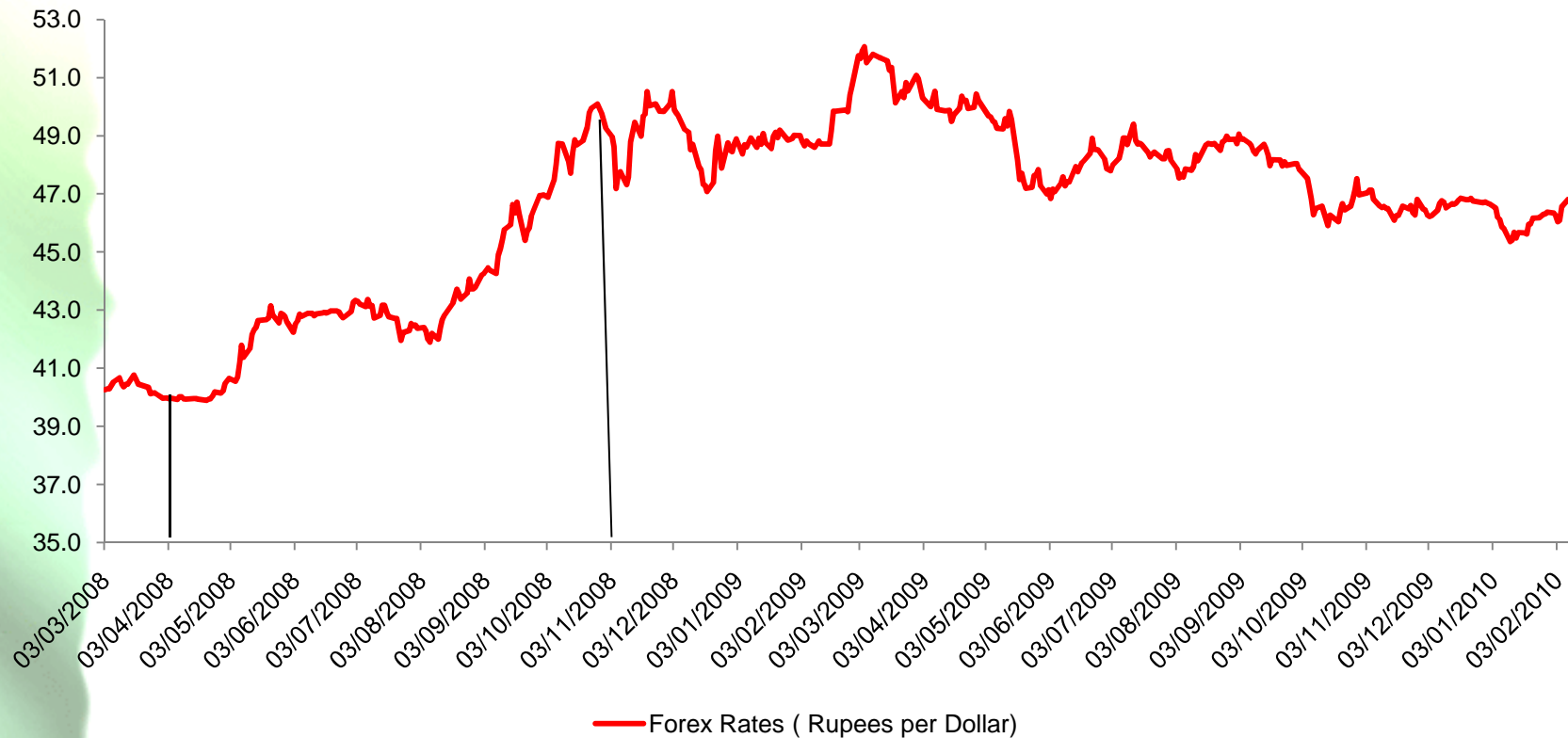
4. External Commercial Borrowings drop Sharply



3. Impact of the Crisis on India



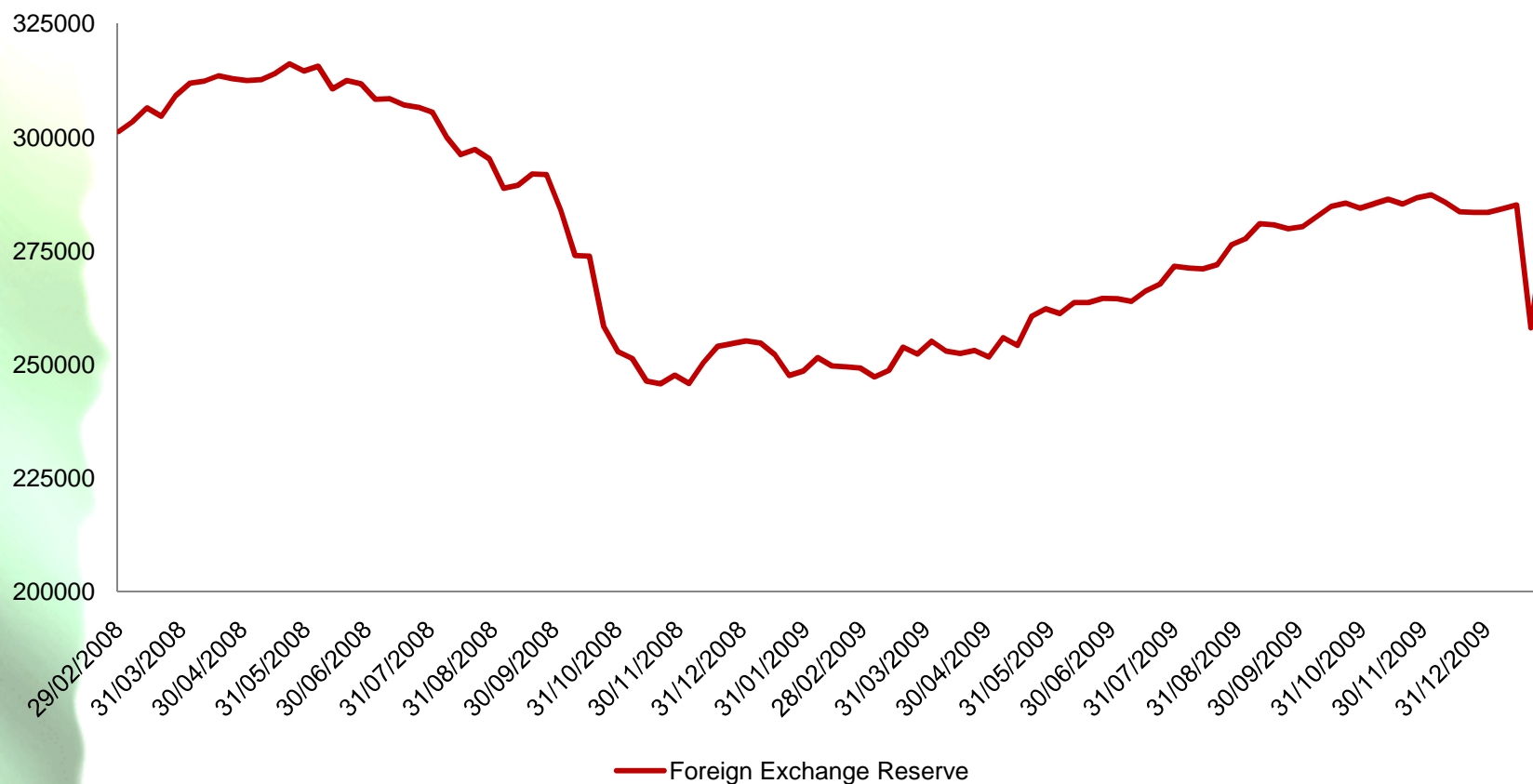
5. Exchange Rate of Rupee Depreciates (Rupees per Dollar)



3. Impact of the Crisis on India



6. India's Foreign Exchange Reserves (US \$ MILLION)



4. *India's Policy Response*



- India's Policy Response was multi-layered:
 - a. Fiscal Stimulus Packages
 - b. Injection of Rupee Liquidity
 - c. Injection of Foreign Exchange Liquidity
 - d. Capital Account Liberalization
 - e. Anti-Cyclical Measures

4.a. Fiscal Stimulus Packages



- Three Fiscal Stimulus packages:
 - a. Fiscal Stimulus Packages in Dec. '08, Jan. '09 and March '09
 - b. Primarily focused at excise duty reduction, additional plan spending, subsidization of export financing, etc.
 - c. Salary hike for government employees: 6th Pay Commission
 - d. The total fiscal burden: about 2% of GDP

4.b. Injection of Rupee Liquidity



Actual/Potential Release of Primary Liquidity since Mid-September 2008 (Rs. billion)		
1	Cash Reserve Ratio (CRR) Reduction	1,600
2	Open Market Operations	801
3	MSS Unwinding /Buyback/ De-sequestering	1,555
4	Term Repo Facility (14 days)	600
7	Increase in Export Credit Refinance	266
6	Special Refinance Facility for SCBs (Non-RRBs)	385
7	Refinance Facility for SIDBI/NHB/EXIM Bank	160
8	Liquidity Facility for NBFCs through SPV	250
Total (1 to 8)		5,617
Memo: Statutory Liquidity Ratio (SLR) Reduction		400

Up to Rs. 5.6 trillion (\$115 bn). Potential Liquidity over 9.5% of GDP was injected

4.c. Injection of Foreign Exchange Liquidity



- Sale of US dollars in the open market
- Special Market Operations to meet public sector oil companies requirements
- Increased Ceiling rates on export credit in foreign currency

4.d. Capital Account Liberalization



- Liberal rules for foreign direct investment in India
- The FIIs investment limits for Government and corporate debt securities increased
- Enhancement of ceilings for external commercial borrowings, both in terms of volume and cost of borrowing
- Increase in interest rate ceiling on remittance by non-resident Indians

4.e. Anti-cyclical Measures



- Dynamic Provisioning: Reduction of all standard asset provisioning
- Increase in the risk weights to banks' exposure to housing and commercial real estate loans

5. Extent of Exposure:

5.A Financial Economy



1. India's Dependence on External Debt
2. Volatile Short-Term Capital Flows
3. International Banking Activity of Commercial Banks
4. Increased Cost of External Financing

5.A.1.India's Dependence on External Debt



(in \$ Bn)	March 06	March 07	March 08	March 09	Sept 09
ECB	2	41.44	62.31	62.42	66.79
NRI Deposits	36.28	41.24	43.67	41.55	45.97
Trade Credit	5.42	7.17	10.36	14.57	15.37
Total long-term	118.59	144.23	178.68	181.23	200.45
Total short-term	19.54	28.13	45.74	43.36	42.38
Total	138.13	172.36	224.41	224.59	242.82

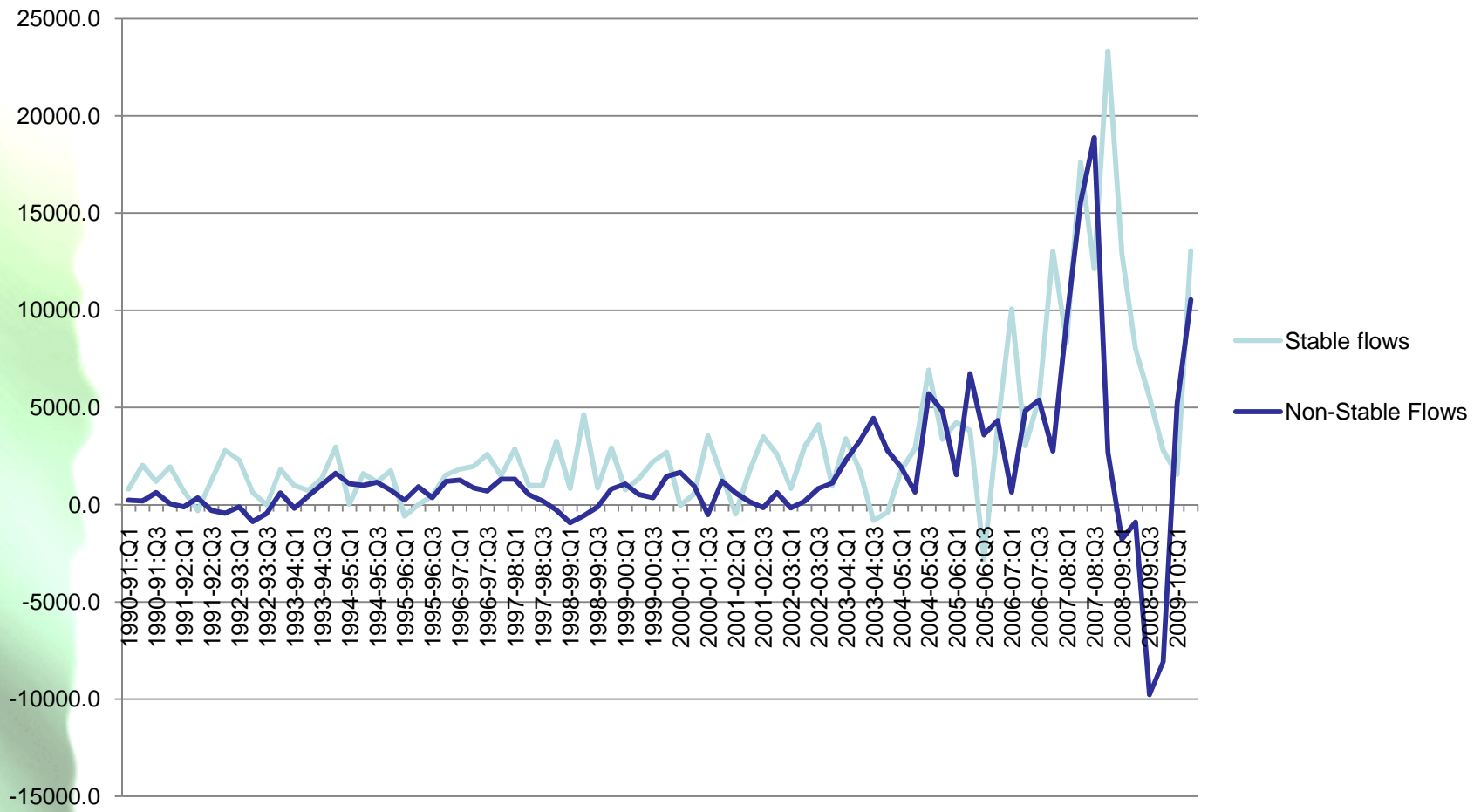
5.A.1. India's Dependence on External Debt



	March 06	March 07	March 08	March 09	Sept 09
Total debt/GDP	17.07	18.86	19.10	19.38	n/a
Short term debt/Total debt	14.15	16.32	20.38	19.31	17.45
Short term debt/Reserves	12.89	14.12	14.77	17.21	15.07
Reserves/Total debt	109.77	115.56	138.01	112.20	115.84
Debt service ratio	10.1	4.7	4.8	4.4	4.9



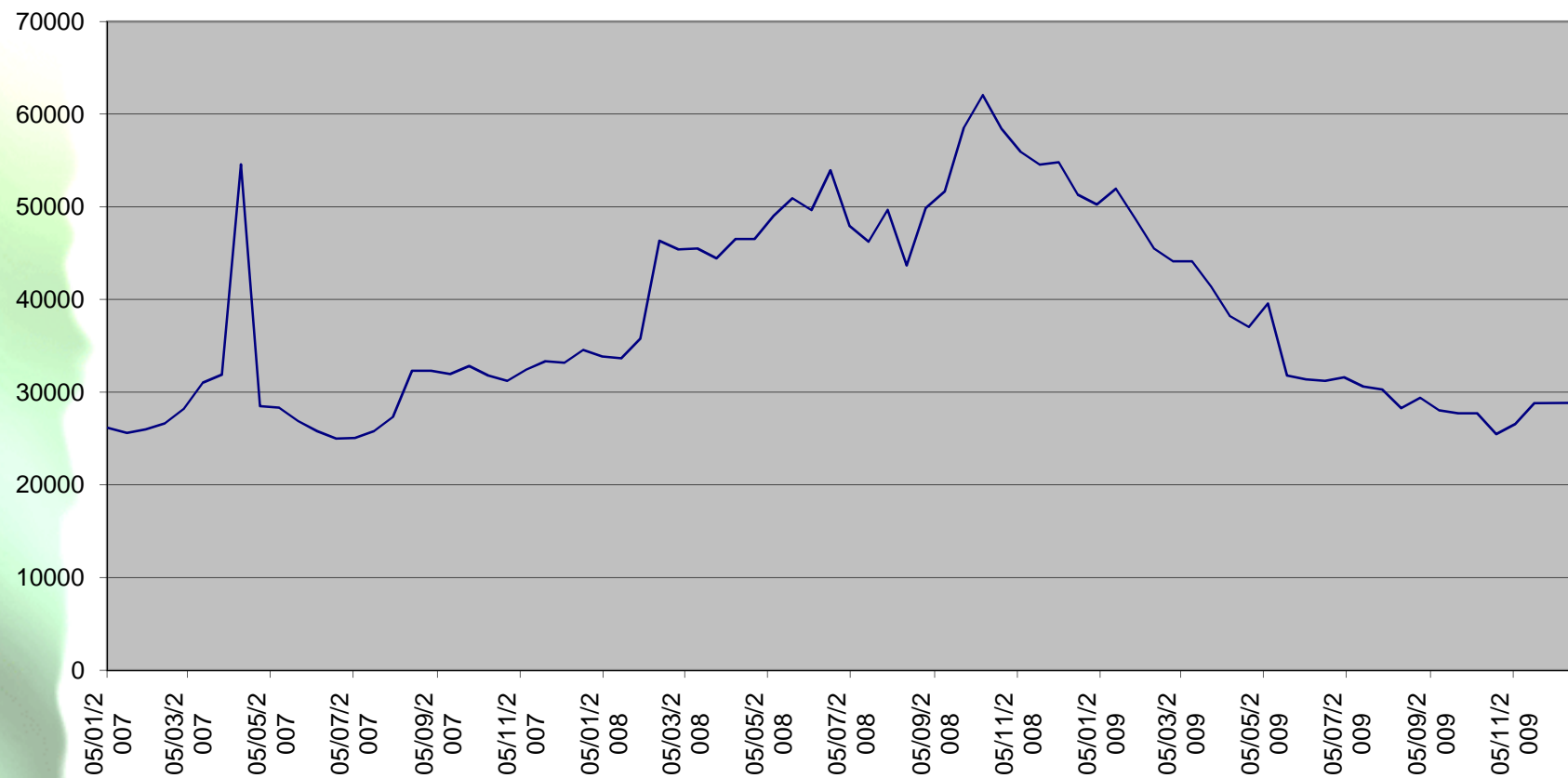
5.A.2. Volatility of Net Capital Flows



5.A.3. International Banking Activities of Indian Banks



Overseas Foreign Currency Borrowings of Commercial Banks (Rs. Crore)



5.A.4 Increased Cost of External Financing



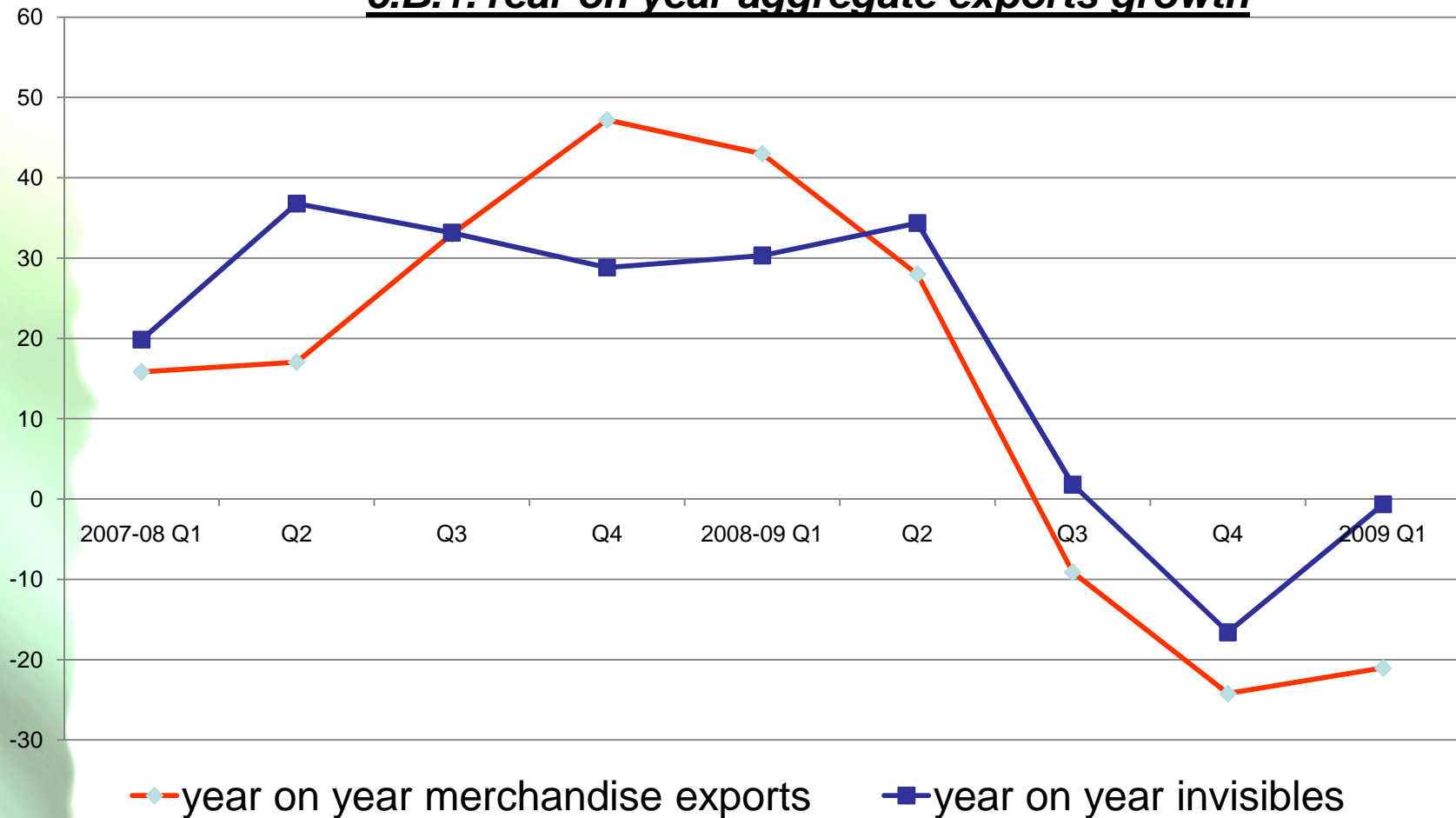
1. India's private companies access to international financial markets, particularly debt market, became expensive
2. Increased repayment burden of foreign debt increased dependence on the domestic financial markets
3. Several projects supported with external funding turned from viable to non-viable!
4. India's sovereign credit rating of BBB, which becomes an implicit ceiling for external borrowing, is questionable!

5. Extent of Exposure:

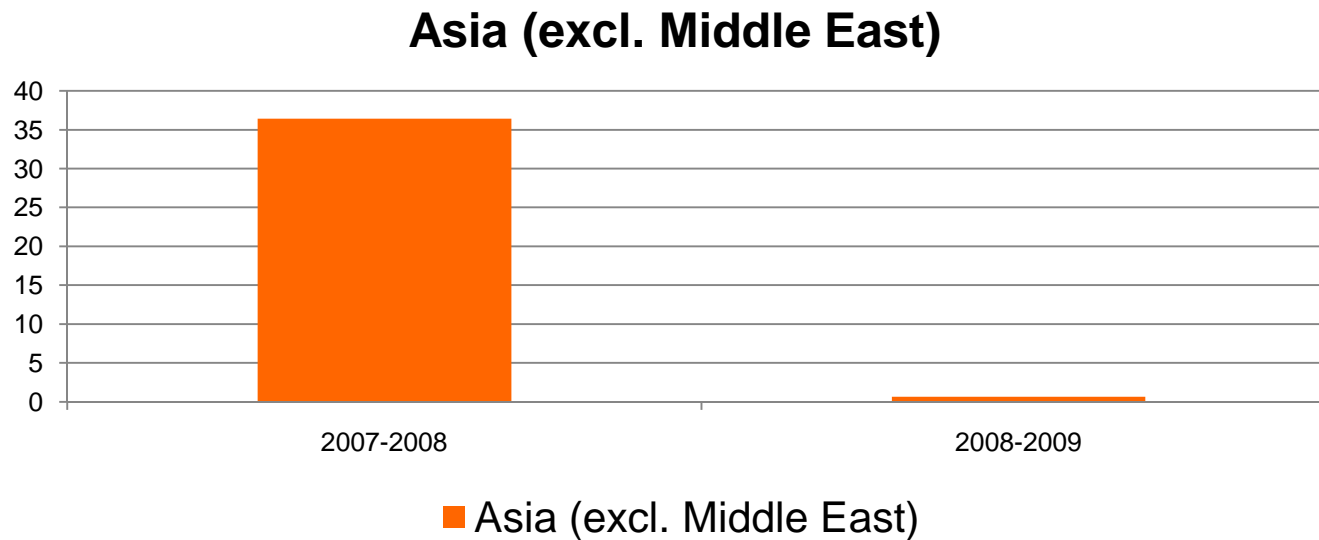
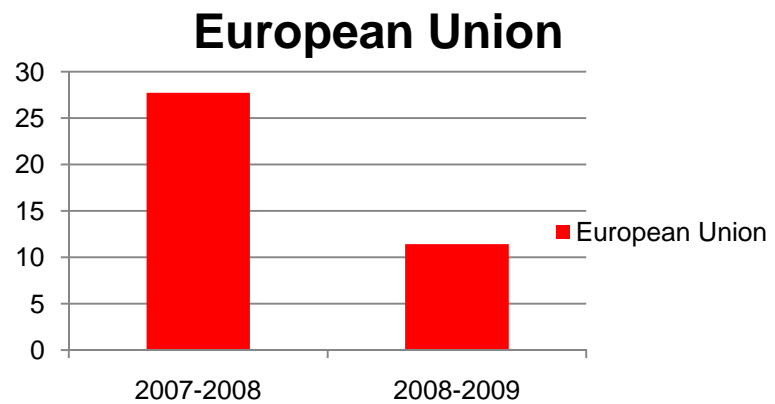
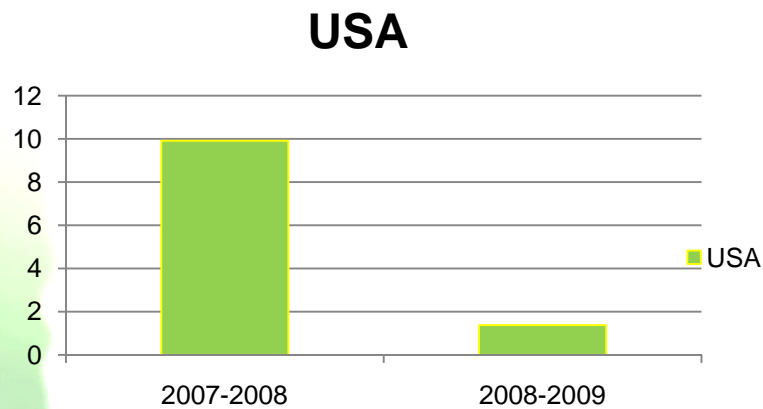
5.B Real Economy



5.B.1. Year on year aggregate exports growth



5.B.2. Growth rate of Merchandise exports from India to:



Concluding Remarks



- Indian financial system did not face any systemic Risk!
- Spillover was largely felt in the capital account and dollar liquidity (leading to other side effects)
- The exposure in terms of short-term external debt is limited
- Volatility of short-term capital flows is a cause of concern