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ORIGINAL ARTICLE

INDIAN STOCK MARKET REACTION TO GLOBAL CRISIS

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Abstract:

It is believed that Indian stock market is not affected from the global crisis. The paper seeks to look into the reaction of Indian stock market to global crisis. It is concluded that India stock market is indirectly affected to the global crisis because India is globally connected and integrated with global markets. The stock market falls by more than 50 % between January 2008 and December 2008. The reversal of capital flow through foreign institutional investors and also, reduction in export are the possible reasons for downfall of the Indian stock market.

KEYWORDS:

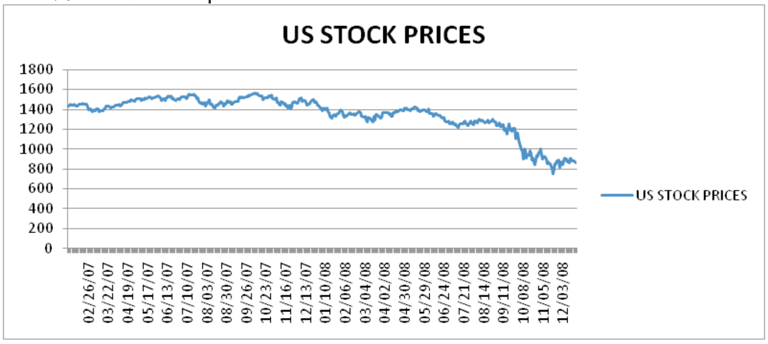
Global Crisis, Indian Stock Market, Reactions.

1.INTRODUCTION:

The Global Financial crisis of 2007–2008 initially referred to in the media as a "credit crunch" or "credit crisis" The belief of investors in the securitized mortgage market shattered in August 2007 due to liquidity crisis which further contingent by credit rating agencies. The year 2007 was the disclosing of the scam, but its evolution is even before it. The main reasons for the scam are housing scam alongside uses of over leveraged contracts. Excessive lending and underwriting with high risk securitizations are the main reasons to boost housing bubbles. The prices of houses went very high. But failing of securitizations to not provide funds for the mortgage, leads to dumping of the houses to the market and fall in the prices of the houses. Initially, home construction and mortgage companies suffers huge losses it led to fall in the stock prices of varius prestigious companies and ultimately leads to crashing of internationals banks to became a global crisis. The integration of stock market due to globalizations leads to domino effect and contagion effect

Reaction of Indian stock market to global crisis

The US stock prices start falling from August, 2007 from 1600 dollars to 800 dollars in November, 2008 with a fall of 50 %. It led to steep stock market crash



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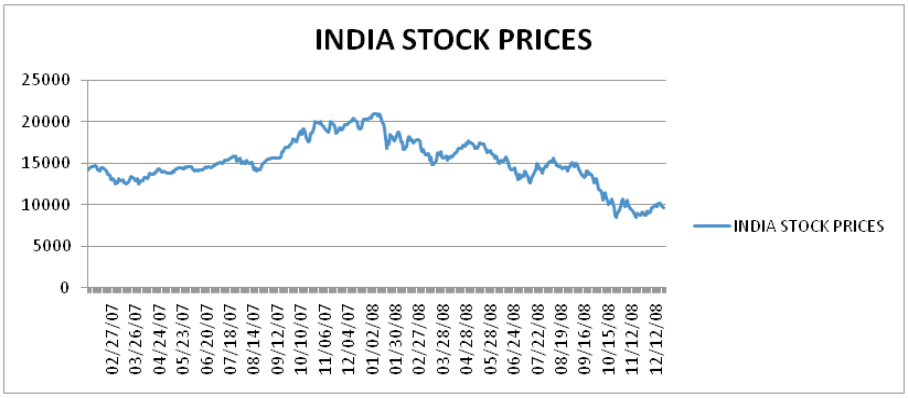
Indian stock market was moving up before the scam gets disclosed, but it also falls more than 50 % steeply from January 2008 to December 2008



As we can see from the above two charts of Indian stock market and US stock market. Indian stock market also reacts to the global crisis in a deferred manner later on after 4 months. It suggests that Indian stock market integrated with US stock market. This has been tested also by conducting an impulse response function

Impulse response graph given below shows that Indian stock market changes in the same direction to a shock in the US stock market within 2 days and then it starts normalize to that shock. The response of American stock market to any shock in the Indian stock markets seems to vary from positive to negative, which is not clear. (kumar, V, 2014)

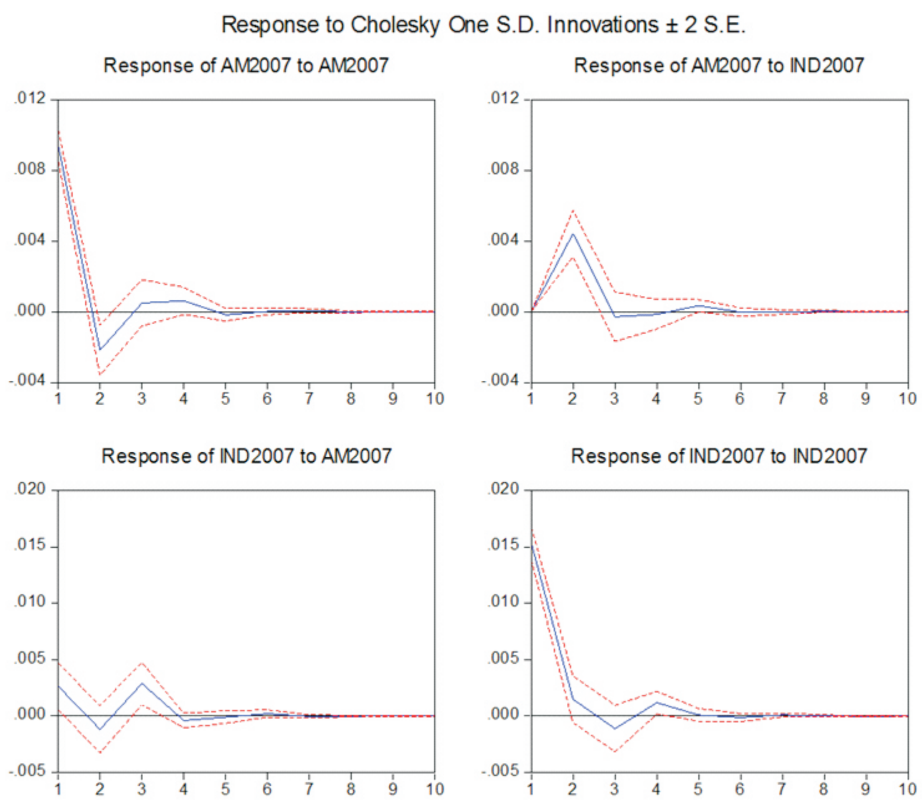


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Figure 1 Impulse Response Graph between Indian and USA Returns in Crisis period

Data compiled by Securities and Exchange Board of India (SEBI) shows that after receiving record $ 45.07 billion between 2004 and 2007, Indian economy witnessed reversal in FII equity flows in 2008 with an outflow of $12.03 billion because of global financial crisis. The global crisis has affected India through three distinct channels: financial markets, trade flows, and exchange rates.

The reversal in capital inflows, which created a credit crunch in domestic markets along with a severe deterioration in export demand, contributed to the decline of gross domesticProduct by more than 2 percentage points in the fiscal year 2008–2009. (Kumar, 2009)

CONCLUSION AND IMPLICATIONS

It is concluded that India stock market is indirectly affected to the global crisis because India is globally connected and integrated with global markets. The stock market falls by more than 50 % between January 2008 and December 2008. The reversal of capital flow through foreign institutional investors and also, reduction in export are the possible reasons for downfall of the Indian stock market. The impulse response function conducted by Kumar (2014) also shows that Indian stock market reacts to any disturbance taken place in the USA stock market. Therefore India is equally sensitive to any crisis that takes place in USA.

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