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EFFECT OF GLOBALISATION ON INDIA'S CAPITAL MARKET AND ECONOMY GROWTH

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INTRODUCTION

"How many millionaires there are who have become wealthy by keeping money in savings accounts?" If we try to find the answer , the most probable answer will be 'no one'

Cash and bank deposits are low risk and fine for near term spending requirements and emergency funds but they would not build wealth over long periods of time. Therefore the earned money must be invested in a place where the person who is investing money can realise maximum profit out of that investment. One of the best example of that place is ' Stock Market or Capital Market'.

The general definition of Capital market is- 'A market where buyers and sellers engage in trade of financial securities like bonds, stocks, etc. The buying and selling is undertaken by participants such as individuals and institutions. It helps channelize surplus funds from savers to institutions which then invest them into productive use'. Generally, this market trades mostly in long-term securities but it pertains high risk.

Capital market is a sub-category of a Financial Market and according to Brighman Financial market is "the place where people and organisation wanting to borrow money are brought together with those having surplus funds for trading of financial products such as stock , bonds, government securities etc."[1].

[1]2 Dr. S. Gurusamy, Capital Markets Tata McGraw-Hill 5,(2d ed. 2009)

Capital market has a very significance role for capital formation. A well functioning stock market may help the development process in an economy through Growth of savings, Efficient allocation of investment resources, better utilization of the existing resources.

Financial resources enable nations to harness economic resources for development. The World Bank (1989) writes that the difference between the rich nations and poor nations is attributed to lack of financial resources to harness the economic resources of poor nations. Financial deepening plays an important role in raising the adaptability and pace of development of an economy through its effects on saving and investment. Thus, an efficient financial system that is supported by a good regulatory system promotes economic growth of a country and its development.

In the 1990s, the term globalization has became a catch-all to describe the phenomenon of an increasingly integrated and interdependent world economy, one that exhibits supposedly free flows of goods, services, and capital. There are many benefits of globalisation, but due to this the global economy also facing a number of serious challenges in the 21st Century. Globalisation has benefitted most participants, but the increasing interconnectedness of the global economy has created a number of problems.

This paper deals with the critical analysis of the effect of globalisation (particularly adverse effect of china's capital market) on India's capital market and economy growth. It deals with the effect of India's economy due to fall in china market.

LITERATURE REVIEW

Joseph Schumpeter (1919)[2]

Substantial academic literature and government strategies support the finance-led growth hypothesis, based on an observation first made almost a century ago by that financial markets significantly boost real economic growth and development. Schumpeter asserted that "finance had a positive impact on economic growth as a result of its effects on productivity, growth and technological change."

World Bank (1989)

The World Bank (1989) writes that the difference between the rich nations and poor nations is attributed to lack of financial resources to harness the economic resources of poor nations. Financial deepening plays an important role in raising the adaptability and pace of development of an economy through its effects on saving and investment.

Bhagwati J.[3]

He defines economic globalization as a "diverse form of international integration such as foreign trade, multi-national direct foreign investment, movements of short-term portfolio funds, technological diffusion and cross-border migration."

Joseph Stiglitz (2002)[4]

[2] olawoye On Impact of Capital Market On Economic Growth Of Nigeria (Oct. 13 , 2016) , http://lekanolawoye.blogspot.in/2011/12/impact-of-capital-market-on-economic.html
[3] 2 C.T.Kurein Indian Economy in Transition Essay in honour 18 (2d ed.2009)

He criticised globalisation for its failures on the basis of transparency and accountability. He suggested that international economic agency must be reformed, made more transparent and accountable, and less dependent on special interest.

Raghuram Rajan (2015, November)[5]

"The Chinese slowdown is a concern for the whole world. There is a lower demand for some of our exports to China. But indirectly too, many of the countries are not exporting to China as much as they did and they are buying less from us,"

"But India being a commodity importer, has been helped a bit by cheaper commodities. So the impact has not been as bad as it could have been. Still, on the whole, we have been adversely affected by the Chinese slowdown because China's slowdown has impacted global growth and India is very well integrated into the global economy".

RESEARCH QUESTION

Globalization has significant role in building India's economy and its capital market structure. Somehow it is beneficial but there are also some negative impact of that. Therefore the following research questions have been critically analyzed to understand the fluctuation or effect of downfall of capital market of China on India's capital market structure and its economic growth.

- What kind of capital market structure in India?
- What is the role of capital market for growth of economy?

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[4] *Id* at 19

[5] China's Economy Slow down , Hindu times, Nov,21,2005

- Impact of globalisation- In the light of fall down of China's economy and its effect on India's capital market and economic growth.

CAPITAL MARKET STRUCTURE IN INDIA

It can be explained under the following headings:-

1. Market- Broadly speaking Indian capital market can be classified into two categories. They are the Primary market and the Secondary market . The primary market helps to raise fresh capital in the market. In the secondary market, the buying and selling (trading) of capital market instruments takes place through a specific medium such as stock exchange.

2.Instruments- To survive and to expand the business, a capital is one of the most important factor. The business house or the companies get the required capital through different instruments present in the capital market. The instruments of capital markets are equity, debt, hybrid, Preference share, Bond, Company Fixed Deposits, Currency exchange.

3. Intermediaries- These people are the back bone for running of a healthy capital market. Intermediaries in Capital Market includes brokers, investment bankers, stock exchanges, underwriters etc..

4. Regulator- For the smooth functioning of the capital market and in order to regulate, promote and direct the progress of the Indian Capital Market, the government has set up 'Securities and Exchange Board of India' (SEBI). SEBI is the supreme authority governing and regulating the Capital Market of India .

5.- Players- The players in capital markets are credit rating agency, corporate, individual, banks/financial institutions, FDI or FII. They are involved in trading of financial products and helps corporate in financial deficiency.

ROLE OF CAPITAL MARKET IN GROWTH OF ECONOMY[6]

The capital market is a highly specialized and organized financial market and definitely essential instrument of economic growth and GDP of a country because of its ability to facilitate and mobilize saving and investment. In Indian market economy, financial market institutions or intermediaries provide the stage by which long-term savings are mobilized and channelled into investments. The economic growth through mobilization and channelization of these long-term savings can be analyzed under the following headings:-

Raising capital- Every companies need capital to run and expansion of the business. Capital market provide this facility by which a company can raise capital for expansion through trading of its shares with investors.

Mobilization of savings for investment- In developing countries like India the importance of capital market is self evident. In this market, various types of securities helps to mobilise savings from various sectors of population. The twin features of reasonable return and liquidity in stock exchange are definite incentives to the people to invest in securities. This accelerates the capital formation in the country.

Distribution of wealth- By giving a wide spectrum of people to become a part owner of a company through buying the shares of that particular company, the stock market helps to reduce

[6] Literature review of stock market (Oct. 13 , 2016), https://nccur.lib.nccu.edu.tw/bitstream/140.119/33947/6/93306406.pdf

large income inequalities. investors invest their money in shares and in returns they get dividends as their profit and that finally result in reduction of economic inequalities.

Corporate Governance- By having a wide and varied scope of owners, companies generally tend to improve on their management standards & efficiency to satisfy the demand of shareholders and more stringent rules for public corporations by public stock exchange and the government. Better corporate governance leads to increase the investors' confidence and in maximum investment & finally result in economic growth of country.

Raising capital by governments- Government also borrow money in order to finance huge infrastructure projects by selling governments bonds. the members of the public can buy these bonds through stock market. The pooled money is invested in development of country's infrastructure and as a result money is mobilized and increase in employment that finally result in economic growth of country.

Barometer of the economy- Stock exchange is place of risk where prices of shares rise and fall depending upon the market condition. If the economy is stable the prices generally remain stable or rise. therefore rise and fall in the price of shares can indicate the general trend of the economy.

Foreign Capital- Capital markets makes possible to generate foreign capital. Indian firms are able to generate capital funds from overseas markets by way of bonds and other securities. Government has liberalised Foreign Direct Investment (FDI) in the country. This not only brings in foreign capital but also foreign technology which is important for economic development of the country.

Policy Making- When policy makers embark on bad policies the equity and bond prices tend to fall. Capital markets anticipate the future prospects of a country thus they reduce politicians incentives to do things that provide short-term gains, but that brings long-term costs that will hurt the economy.

BENIFITS AND CHALLENGES OF GLOBALISATION IN CAPITAL MARKET

As Mundell (2000) argues, the 1970s witnessed the beginning of a new era in the international financial system. As a result of the oil shock and the breakup of the Bretton Woods system, a new wave of globalization began. The oil shock provided international banks with fresh funds to invest in developing countries. These funds were used mainly to finance public debt in the form of syndicated loans. With the disintegration of the Bretton Woods system of fixed exchange rates, countries were able to open up to greater capital mobility while keeping the autonomy of their monetary policies. The capital flows of the 1970s and early 1980s to developing countries preceded the debt crisis that started in Mexico in 1982. To solve the debt crisis of the 1980s, Brady Bonds were created, which led to the subsequent development of bond markets for emerging economies. Deregulation, privatization, and advances in technology made foreign direct investment (FDI) and equity investments in emerging markets more attractive to firms and households in developed countries. The 1990s witnessed an investment boom in FDI and portfolio flows to emerging markets[7].

The potential benefits of financial globalization will likely lead to a more financially interconnected world and a deeper degree of financial integration of developing countries with

[7] Benefits and Risks of Financial Globalisation (Oct. 13, 2016), http://siteresources.worldbank.org/DEC/Resources/BenefitsandRisksofFinancialGlobalizationSchmukler.pdf

international financial markets. Probably, the main benefit of financial globalization for developing countries is the development of their financial system, what involves more complete, deeper, more stable, and better-regulated financial markets.

Globalization has significant role in building India's economy and its capital market structure. Somehow it is beneficial but there are also some negative impact of that. Financial globalization carries some risks. These risks are more likely to appear in the short run, when countries open up. One well-known risk is that globalization can be related to financial crises These are the recent issues to understand the negative impact of financial globalization.

IMPACT OF GLOBALISATION- FALL DOWN OF CHINA'S ECONOMY AND ITS IMPACT ON INDIA'S CAPITAL MARKET AND ECONOMIC GROWTH

China is world's largest manufacturer and holder of foreign reserves; making it essential to the global economy. China is also a major importer of a range of hard and soft commodities and an increasingly important market for manufactures all over the world. Three decades ago China was predominantly a rural and poor society. It allowed China to take advantage of its massive potential and enjoys substantial growth rate. China's growth was largely driven by heavy investment in public infrastructure and manufacturing. The three reasons of china's economic slowdown are:-

1) **Housing Sector slowdown**:- The real estate sector accounts for between 25% and 30% of China's GDP, including industries such as steel, cement, glass, furniture, and appliances. Plunging housing prices are not only hurting affluent Chinese who have poured their fortunes

into investment properties, but it is also triggering defaults by real estate developers. So on the domestic front, China is also struggling to grow, causing further declines for its economy.

2) **Steel Sector**:- There has been a decline in China's automobile sector and construction sector. Both of these industries require steel and iron for their manufacturing. China is the largest producer of steel in the world and it is a major income generator. In fact, its production is seven times that of the second largest producer, Japan. So, if steel prices go down due to over production or lack of demand, the Chinese economy will feel the impact.

3) **Manufacturing Sector** :- It contributes around 59% to China's GDP, with most of production occurring for export. However, the slowdown in the EU, Japan and South Korea has led to reduced demand. These regions are also the largest trading partners of China. So, since these countries have been experiencing their own slowdown this has had a knock-on effect on demand for China. The demand for exports has declined and it doesn't appear that resurgence will happen soon enough to enable China to recover.

Since the growth continues to slow down in the world's second-largest economy, China is at a crossroads. First, it has to prop up the economy the old-fashioned way and also push forward structural reforms to lead the country into growth. The policy changes the government is making need to be used to drive more foreign business into China so it can grow over time.

According to the World Bank, China has made the largest contribution on the growth rate worldwide over 13% on the average since China joined the WTO in 2001. China's economy ranks at the second largest in the world in terms of gross domestic product (GDP) at current exchange rates so therefore any fluctuation or downfall of China's economy affect the global economy. The world's largest consumer of metals and second biggest buyer of oil posted its lowest annual growth in a quarter of a century in 2015[8].

A third of the value of a shares of Sanghai stock exchange was lost within one month of the event. Major aftershocks occurred around 27 July and 24 Augusts' "Black Monday". By 8–9 July 2015, the Shanghai Stock Market had fallen 30 percent over three weeks as 1,400 companies, or more than half listed, filed for a trading halt in an attempt to prevent further losses. Values of Chinese Stock Market continued to drop despite efforts by the government to reduce the fall. After three stable weeks the Shanghai index fell again on 24 August by 8.48 percent, marking the largest fall since 2007[9].

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8 China Stock Market (Oct. 15 , 2016), http://www.starmass.com/china-review/global-economy/contribution-global-economy.html

9 China Stock Market (Oct. 17, 2016) http://www.vox.com/2015/7/9/8917647/china-stock-market-explained

The Chinese Stock crash is going to be mixed with India because India is mostly depended upon the foreign investment in stock market the economy is stable among the EMEs. Besides, traditionally India is slow in quick reforms and this has rescued India in all previous global crisis- the Mexican crisis, the East Asian crisis and the global financial crisis of 2007.

This time also weak policies in China may put a vote of confidence on India. This doesn't mean that fluctuation in global markets is going to be unaffected. Stock prices and value of rupee all will be influenced by Chinese events, but in a moderate manner.

REFORMATIVE ACTIONS TAKEN BY THE CHINESE GOVERNMENT

In an attempt to improve the economic situation in China, the Chinese government has implemented a variety of measures to make it more attractive for countries to buy from China. Overall, the Chinese government is following the lead of many other governments – such as those in Japan – and devaluing the Yuan. It is also providing manufacturing incentives so domestic producers are able to stay afloat and manufacture products at a lower cost. The hope is that this will drive greater exports out of China and restore the demand that it seems to have lost. Since the Chinese government began implementing these measures in August 2015, it doesn't seem to have had a significant impact on the export situation. It also hasn't made much of a dent on declining Chinese indices. The financial news is also focused on worries about how the situation in China could cause wider global impact on the financial markets[10].

Stock market experienced abnormal volatility. SSE strived to stabilize market under CSRC guidance. Revised margin trading rules to release risk, strengthened regulation on abnormal market movement, regulated listed company behaviour, strengthen risk monitoring of new business and public opinion, actively lowered trading fees to bring market back to normal. Improved stock trading mechanism and recovered financing function of market, started market restoration and infrastructure building.[11]

SECTORS IN INDIA THAT AFFECTED DUE TO FALL DOWN OF CHINA'S ECONOMY

Commodities

China is one of the largest consumer of metals in the world. China absorbs 50% of global copper, iron ore and coal exports. A slowdown in China or even a possibility of slowdown means metal

[10] Chinese Economy Slowdown (Oct.16, 2016) https://options.eztrader.com/en/binaryoptions-magazine/reasons-for-chinese-economic-slowdown.aspx?regulationpopup=true

[11] Shanghai Securities Market (Oct. 19, 2016), english.sse.com.cn/indices/publications/factbook/c/4172526.pdf

prices free-fall (because demand for metals is going to reduce substantially). For instance, copper is trading at a 6-year-low. China is the world's top copper consumer, accounting for 40% of global consumption. Further, China has resorted to aggressive selling to clear its inventory of metals and raise cash during these hard times. Despite this, it can also be expected that after the stock market crash, investors would want to park their investments from stocks to commodities especially Gold moving from here, which can again increase prices. Indian metal-producing companies such as Vedanta and Hindalco have seen their stock prices dipping which led to the huge dropping of SENSEX in the month of august 2015[12].

[12] Global Stock Market (Oct. 12, 2016), http://www.aljazeera.com/news/2016/01/analysis-global-stock-market-plunge-2016-160127190807213.html

(Source: Bloomberg Commodity Index[13])

Capital Flow

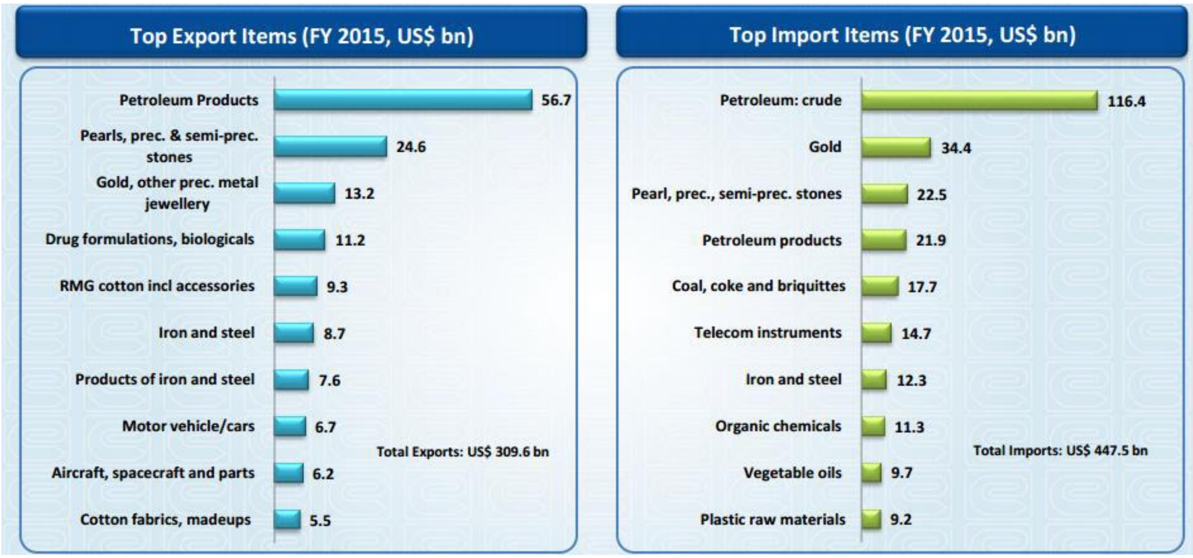
The economic instability in China and its impact on other emerging economies have left the global investors with very limited options. India stands out as a relatively bright spot given its stable macroeconomic conditions, renewed policy momentum, and a business-friendly government. With very few investment options available within China, the investors are looking outside for better returns. China's global stock of outbound foreign direct investment which includes mergers & acquisitions and start ups which will grow by the year 2020.[14] India should attract these Chinese investments to the Indian infrastructure and manufacturing sectors which would be helpful in maintaining a political relation between the two countries.

Trade- Merchandise and Services

The fall in growth of China's effective demand has already hit the global economy hard, through commodity and oil prices. The slackening of demand is likely to make matters worse for Indian exporters also as the purchasing power of other Asian buyers has reduced significantly. India currently faces slowdown in traditional labour-intensive industries, such as cotton, textiles and gemstones[15] along with commodity exports. Knowledge intensive manufacturing industries like automobile and engineering exports will also be greatly affected as China was their fastest growing market.[16] If Chinese officials will further devalue their currency accelerating growth, the global market will be full of Chinese goods at the lowest prices, thereby affecting the

[13] 'Commodities see longest losing streak in 23 years' by Banikinkar Pattnayak for The Financial Express - http://www.financialexpress.com/article/markets/commodities/commodities-see-longest-losing-streak-in-23-years/25201/ (last visited on 23.10.2016)
[14] Paras Parekh What does Chinese Slowdown mean for India 9 (2015)
[15] China slowdown open avenues for India's Economy' by Oxford Analytica - (Oct. 22, 2016) https://www.oxan.com/display.aspx?ItemID=DB205481
[16] Paras Parekh What does Chinese Slowdown mean for India 8 (2015)

economy of other countries including India[17]. Due to the declining prices of the Chinese goods; China would export its overcapacity to the Indian market which will affect the domestic producers. India currently runs a substantial deficit of $48.43 billion with the China.



(Source-Ministry of Commerce & Industry , Government of India)

CONCLUSION

In general, no one can deny the fact that globalisation is inevitable in today's competitive business environment. The issue is on how the countries take the existence of globalisation. Through in the discussion we saw that there are benefits that are being seen from the existence of the phenomenon, but there are also detrimental effects. All of these depend on the nation and hence the context in which globalisation takes place since each country differs from one another in terms of comparative advantages. There are issues that are related to the loss of a country's

[17] Chinese Economic Crisis (Oct. 13, 2016) http://morungexpress.com/chinese-economic-crisis-and-its-impact-on-indian-economy/

freedom and sovereignty that play a key part on whether to embrace or reject globalisation, nevertheless, globalisation will happen. In a brief overview though one can see that there are many economically related benefits that have been associated with emerging market economies and hence probable cause for the increased acceptance in the phenomenon .The aspects of the expanding sales i.e. where by the emerging economies are having a wider market for its products is a notable reason for the acceptance of globalisation. Now the countries with emerging economies are having the markets in practically in many or any country of the world ranging from Europe to Africa, the Middle East and America. Furthermore, they have now been able to acquire resources such as technology and cheap labour from the various countries that they have invested in. The acceptance in globalisation has also reduced the risks that have been associated with the investment in only their country as there are many fruitful opportunities in other countries, but failure of globalisation cannot be denied on the basis of transparency and accountability. Therefore to make globalisation exhaustive, international economic agency must be reformed, made more transparent and accountable, and less dependent on special interest.