IMPACT OF RUSSIA-UKRAINE WAR ON INDIAN ECONOMY: A STUDY

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ABSTRACT:

History has demonstrated that following a conflict, markets do recover. History has not taught us how to foretell how a battle will end or what its repercussions will be. The Russian invasion of Ukraine has sent tremors across world markets. Less than 2% of global trade is conducted between Russia and Ukraine, although they generate a sizable part of several commodities, including 37% of the world's palladium, 17% of its natural gas, 13% of its wheat, 12% of its oil, and 9% of its nickel. The supply chain connections and the sanctions imposed on Russia will undoubtedly have an impact on international trade and finance. The main source of worry for the Indian economy is the impact on commodities, especially energy.Rising oil costs eventually cause the rupee to lose value, inflation to rise, the budget deficit to widen, and GDP growth to slow. A 10% increase in oil prices is expected to aggravate the current account deficit, slow GDP growth by 20 basis points, and boost inflation by 40 basis points. This article examines how the Russian-Ukrainian War affected the Indian Economy.

Keywords: *Russia, Ukraine, War, Crude Oil, Economy, Inflation, Investors*

INTRODUCTION:

All diplomatic efforts to prevent a future armed conflict between the two nations were unsuccessful when Russia declared a "special military operation" in Ukraine. Studies of Russian tactics in times of war indicate that coercive diplomacy may be involved. Along with a moderate ascent the current Russian military deployment and the takeover of Crimea. These are actual examples of the strategy in action, along with Ukraine. The global conflict has gotten worse. posed a serious threat to European security and slowed down world economic expansion. He is weak as a result of the pandemic's recessive effects. What can be considered a likely scenario?A resumption of the Cold War would probably have an adverse effect on the West's economy. Internationally, commodity prices have increased while the financial market has contracted. The European region will experience these consequences with extreme polarisation. Being net oil importers, most Asian nations will be able to withstand the effects over time. However, in a shorter amount of time, the hasty purchases of crude oil will maintain the price per barrel high for a while due to the race to fill up storage capacities, meet rising oil demand, and avert the beginnings of an energy crisis. India is essentially at the centre of the power dynamics that develop during and/or after the current conflict.This year, India is a permanent member of the United Nations Security Council, in contrast to the last Russia-Ukraine conflict in the Crimean peninsula in 2014–15. Both dismay on Kiev's part by New Delhi's lack of expected support and its initial move of tacitly criticising Moscow for violating the territorial integrity of another country are factors in its decision to abstain from voting on the UNSC resolution.

The omission could suppress criticism to China's expansionist intentions in the Indo-

Pacific at a time when India wishes to improve relations with the United Kingdom, the United States, and the European Union. There is an argument going on at the same time. The conflict takes place shortly after India purchased the S-400 missile system from Russia. The Western sanctions would hamper Russia's defence industry and restrict its exports of and imports of technology to India. Payment in US dollars is hindered by the absence of two significant Russian banks and their 90 subsidiary subsidiaries from the well-known SWIFT global banking system. With bilateral commerce worth $2.5 billion in FY 2020–21, India is Ukraine's main Asian export market.

In contrast, the value of bilateral commerce between Russia and India in the 2020–21 fiscal year was 8.1 billion dollars. Exporters are closely monitoring the severity and duration of the ongoing issue since it has a lot on its plate. The Federation of India Exports (FIEO) has advised traders to stop or divert their goods away from the Black Sea route. In addition, the imposition of sanctions will impede international trade and worsen supply shortages.

International rules cannot be avoided in a globalised society, which has a cascading influence on the economy at the national level. Crude oil price increases, turbulence on the financial markets, the potential for growing current account deficits, which would weaken the rupee further against the dollar, and a likely increase in inflation as measured by the WPI-CPI indexes are all having an immediate negative impact on the Indian economy. The current high P/E ratio will have further effects on the stock markets. The continuing sanctions will unavoidably increase oil prices, which were already about $105 on the day Russia invaded Ukraine, the highest since 2014. Russia is the second-largest exporter of crude oil in the world.India's current account deficit, which is currently 1.3 percent of GDP, would grow if import costs increased. The RBI estimates that a $10/barrel increase in oil prices has a 49 basis point impact on inflation.

The budget deficit as a percentage of GDP will increase by 43 basis points as a result of this. On the other hand, if it is passed on to consumers, a $10 increase in the price of a barrel will lead to a 50 basis point increase in the CPI. Nomura estimates that a 10% increase in oil prices will result in a 0.2 percentage point decline in GDP growth and a 0.3 percentage point worsening of the current account. According to the Economic Survey, growth is expected in 2022–2023, with an assumed oil price of $75 per barrel. Additionally, the RBI faced pressure to hike interest rates to battle inflation, which will impede economic growth, because the RBI's most recent monetary announcement did not mention an increase in oil prices.The RBI's 4.5 percent inflation target for FY23 appears to be at danger of 90-100 basis points (bps) if oil prices average $90 per barrel and 100-130 bps if oil prices average $100 per barrel, according to comments made by the State Bank of India's group's top economic advisers. Gas prices are expected to grow because India imports 55% of its natural gas and Russia is a key natural gas exporter. The daily adjustment of the price of gasoline, diesel, and natural gas has been suspended because elections are soon to be held in five states.

The gap between selling and cost prices, which industry sources estimate to be over Rs 10/litre due to the current push and international price pressure, has grown. If passed on to consumers, this would result in extremely high inflation that would already be above the

Reserve Bank of India's tolerance shield of 6%. The Indian stock markets plunged 3% on February 24 as a result of the financial sector's inability to avoid the world's unrest, and it is expected that volatility will continue as tensions escalate. The NIFTY dropped 816 points to 16,248 on the same day that the SENSEX dropped nearly 2,700 points to 54,529, marking the biggest drop in a single day in SENSEX history.In response to the increase in gasoline prices, foreign portfolio investors switched to sellers and withdrew a net amount of Rs51,703 crore from Indian shares. $177 billion in investments were lost from the Indian market after the SENSEX collapse. The firms have kept a close eye on things and postponed their IPOs in response to the depressing market conditions. 90% of India's sunflower oil imports come from Russia and Ukraine in terms of exports. India got 1.89 million tonnes of sunflower oil in 2021, of which 70 percent came from Ukraine; this month, not a single cargo has been sent.Our country would experience a setback because it is one of the biggest exporters of pharmaceutical products to Ukraine, and because rising input costs for the auto industry are expected to lead to higher vehicle prices.

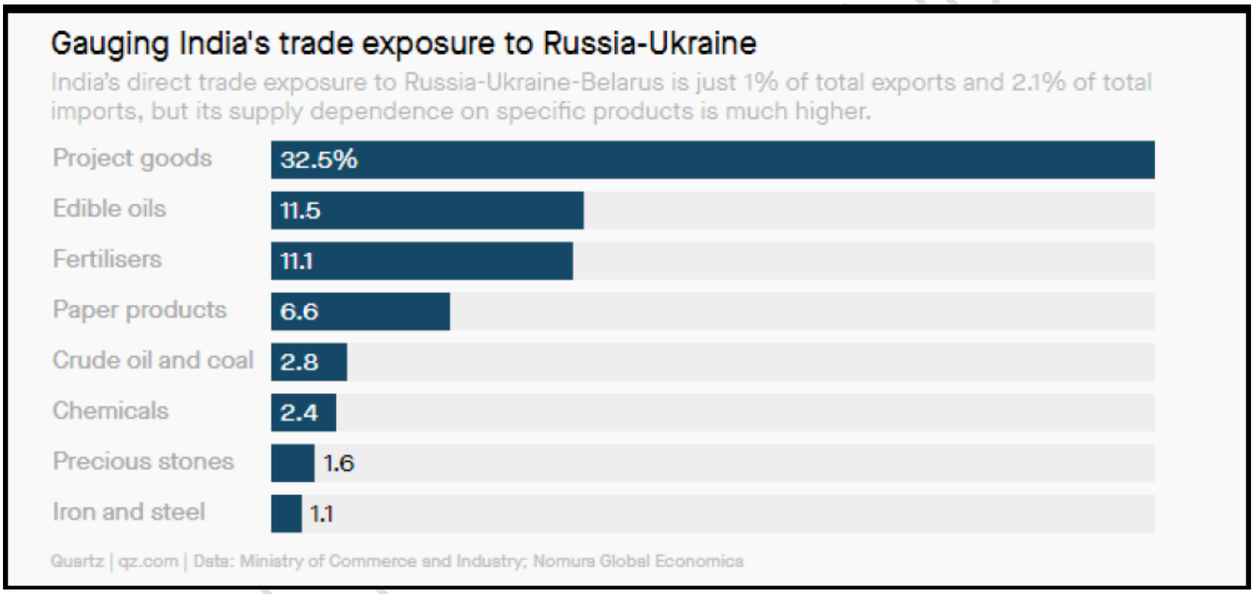

Figure 1: India's Trade Exposure

Here are several ways that India could suffer from a war between Russia and Ukraine without taking part in it.

Exports of Russian crude are forbidden:

Due to the United States' ban on all Russian oil and gas imports, Brent crude prices skyrocketed to nearly $130 per barrel last week, up 43% from the beginning of February.This is a significant setback for the expansion of the international economy because Russia is one of the biggest producers of crude oil. Even if only 1% of India's trade is comprised of oil imports from Russia, there may be a spillover effect in the form of high pricing and sluggish growth. According to the paper, there may be more issues if conditions in the global economy continue to deteriorate and India's export and capital investment cycles are hampered.

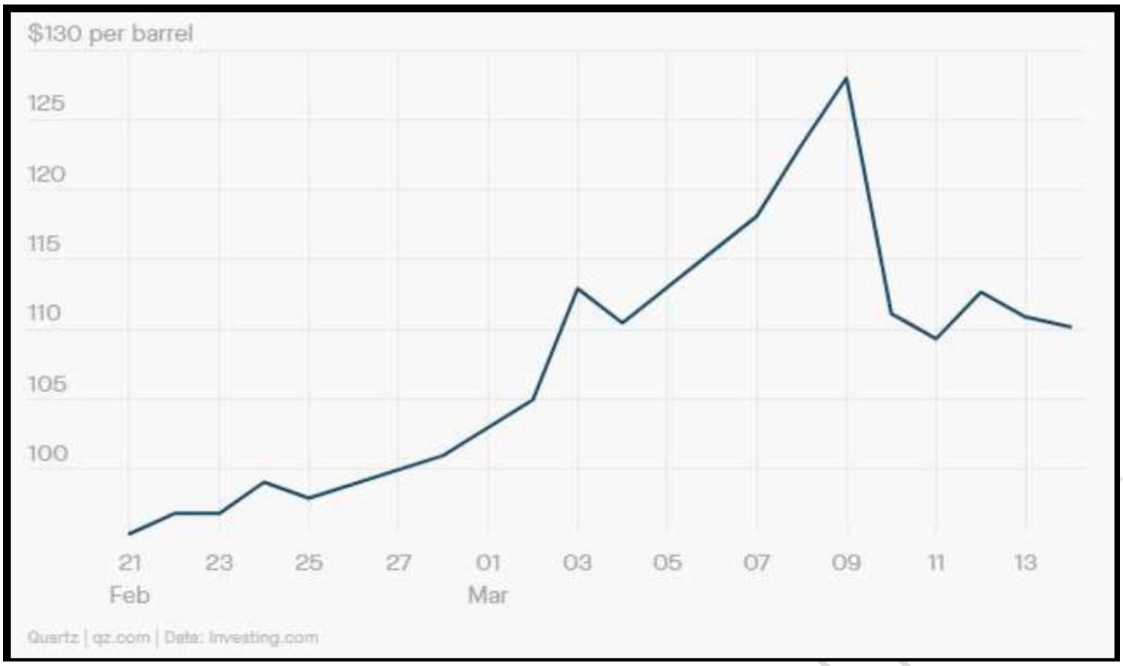

Figure 2: Brent crude oil prices since Ukraine invasion

Worries about inflation

India imports enough crude oil to satisfy up to 85% of its needs. Wider price pressures have been brought on by the 14-year high in international oil prices. Analysts predict that the impact on India's economy would mostly manifest as rising cost-push inflation, which will have an impact on all economic players, including consumers, businesses, and the government. According to the sources, consumer inflation rises by 0.4 percentage points for every 10% increase in crude oil prices.The likelihood that India's import bill would increase and that its current account deficit will worsen as a result has increased (CAD). A study predicts that the CAD will increase from 1.7 percent of GDP last year to 2.6 percent of GDP in the fiscal year 2023. The rupee, which just touched a new low of 76.98 against the dollar, will likely suffer as a result of this.

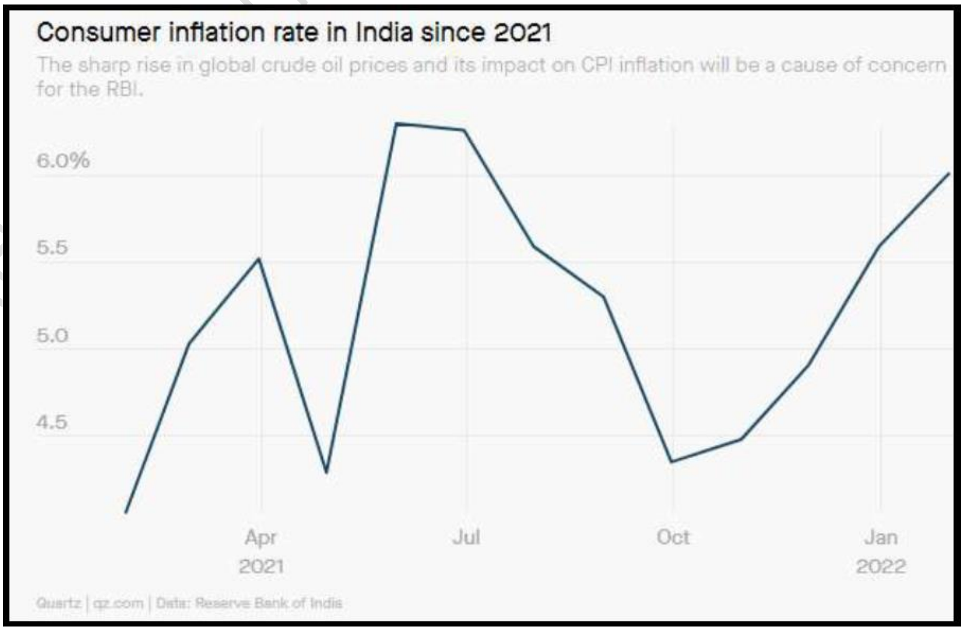

Figure 3: Inflation Rate

India's military hardware

Since the invasion of Ukraine, India has reportedly frequently abstained from UN votes out of a desire to safeguard its supply of defense technology, the majority of which is supplied by Russia. The Stockholm International Peace Research Institute's statistics shows that between 2016 and 2020, India received about 25% of all Russian weapon shipments. This explains why a sizeable chunk of India's annual budget is allocated to defense spending. In its union budget for 2022–23, India allocated $70.2 billion for military spending, an increase of almost 10% from the initial allocation for the prior fiscal. One of the most significant defense contracts in doubt is the delivery of the $5 billion S-400 air missile system, which was constructed by Russia.The Congressional Research Service reported in October 2021 that the Indian military requires Russian technology in order to function effectively. The Russian T-72M1 and T-90S combat tanks, which make up 66% and 30% of all units, respectively, of the Indian Army's main battle tank force. India will continue to rely on Russian weaponry in the medium term, despite the US threat of sanctions over the S-400 purchase hanging over it heavily.

Macro Effects

(i) First, inflation is a cause for concern. Early in February, the rhetorical assault started, and since then, commodities prices have risen. The struggle has arguably had the most noticeable effect on the price of crude oil, but it has also increased the cost of metals, gas, and edible oils at a time when it was anticipated that prices would level off this year after a bull run in 2021. For instance, since late December, manufacturers in India have been gradually raising prices and passing along growing input costs. The pressure will increase across the board with this latest round of pricing increases. The Indian government has not increased fuel prices since November, citing state elections as justification.This round of price hikes was inevitable even before the crisis. Simply put, the situation is aggravating the issue.

(ii)The rupee is the second area of concern. Since the commencement of the war, currency markets have experienced significant volatility. War and sanctions have contributed to currency devaluation, and the rupee has not been exempt. This occurs at a time when the current account balance has changed to the negative, and a higher CAD is anticipated due to increased oil prices.

(iii) The third concern is with payments. The payment issue worries those conducting business with Russia. As a result of Russia's removal from SWIFT, exporters are in a bind. Worse, shipping companies are reluctant to send goods to Russia. All entities in other countries that are counterparties to these transactions are impacted in an effort to hurt Russia. India can enter into a government-level rupee-rouble agreement, but receiving roubles in exchange for exports may not be as tempting to individual businesses.

(iv) The fourth is a lower GDP. War has a significant impact on commodities in India, especially energy, which is the main cause for concern for the Indian economy. Rising oil costs eventually cause the rupee to lose value, inflation to rise, the budget deficit to widen, and GDP growth to slow. Oil prices are expected to rise by 10%, inflation will rise by 40 basis points, and the current account deficit will widen by 30 basis points, resulting in a 20 basis point decline in GDP. Fortunately, the Indian economy can withstand the anguish of rising oil prices and the disruption brought on by the crisis in Russia and Ukraine.Undoubtedly, growth will slow down, but it will be bearable. There will be great caution used when central banks around the world stop providing monetary support.

Sectoral and Market Impact

Rising prices, a weaker GDP, and a declining rupee will all have a negative impact on corporate profits. On the other side, there are some bright spots in the stormy skies. The route of long-term growth is still in place. It is a good idea to create policies that encourage growth. The number of domestic investors has increased. With prices close to historical averages, this market is evolving into a buy-on-dip opportunity with modest return expectations. Due to concentrated holdings and a small number of floating companies, markets where values are still high might not provide the expected return.With some volatility, it is anticipated that capital goods, home improvement, pharmaceuticals, large-cap IT, and some select financials will outperform the market. The car industry lost 9% of its value, followed by banking and real estate, in a sector with a mixed trajectory. On the other hand, IT, energy, and metal worked to keep the damage to a minimum. While the smallcap index outperformed but ended 0.3 percent lower, the midcap index concluded in line with the benchmark.

War benefits for the Indian economy

1. The supply of semiconductor chips will be impacted by disruptions in the supply of metals like palladium, which will have an effect on the ailing automotive industry. Different enterprises could encounter a "tail wagging the dog" situation. On the other side, the expansion of business from Ukraine and Eastern Europe may benefit the Indian IT sector. India's farm exports can continue to grow despite disruptions to the supply from Russia and the Ukraine. Our granaries hold three times as much stock as is required by law. Given recent research on the reliability and quality of India's food grains, this is an extremely important opportunity.Increased grain prices elsewhere in the world shouldn't have much of an influence on inflation because Indian local prices are greater than global prices.

2. If India can resuscitate the Rupee-Ruble trade and turn into Russia's favoured supplier, there is a bright spot in the gloom. In order to fill the economic gaps caused by the sanctions and large economies like India, Russia would need their assistance. There will be enough loot to split with China, which will be Russia's preferred choice due to its size and proximity. India needs to make a concerted effort to entice Russian investment in GIFT City. Compared to investments made in western markets, these investors would find their investments to be much safer and more profitable.

3. The sanctions imposed on Russia may help India's travel and tourism industries, since India may become a popular vacation spot and a hub for Russian travellers. We should work to create numerous tourism destinations like Goa for Russian visitors.

4. A lot of students from India travel to Russia and the Ukraine to complete their higher education. This demand need to be used to strengthen our educational system. There are currently billions of dollars being used as foreign exchange to fund education abroad. Instead, we have the ability to increase the scope and size of the educational sector.

5. The conflict between Russia and Ukraine will enable us to keep up our export momentum and further our integration into global supply networks. We must increase the ease of doing business and the rule of law if we want to encourage our entrepreneurs to take advantage of this chance. Russia diversified its foreign currency assets by purchasing gold as a means of preparing for sanctions. China might easily employ a similar strategy while keeping in mind its long-term goals for Taiwan. Indians will experience a significant increase in wealth if Chinese purchasing helps to maintain gold prices, as they are the largest holders of the yellow metal. Faster development will arise from increased consumption and available funds for investment.

6. Investing over the long run Opportunity is present. Despite being unfortunate occurrences, wars do offer chances for long-term investment. Every time investors anticipate a correction or experience one, they are overcome with fear. Long-term investors should take this opportunity to steadily expand their investment portfolio. Anyone with funds and a time horizon of three to five years can start investing at least one-third of the corpus right away, and the remaining funds during the following three to six months. Foreign Institutional Investors (FIIs) have withdrew capital from Indian markets due to worries over overvaluation, rising inflation, and the country's sluggish economic growth. Concerns have increased as a result of rising crude oil prices and geopolitical tensions between Russia and Ukraine.On the other hand, domestic institutional investors (DIIs) have consistently provided funding for the market. Future FII inflows are anticipated to be influenced by decreased crude oil prices, decreased interest rates, enhanced economic growth, and increased earnings.

What ought we to do?

1. Asset Allocation: The price of shares and other asset classes has fallen sharply since the news of the war surfaced. As bond yields have increased, gold and other precious metals are selling at a premium, while equities have dropped sharply in value, investors should rebalance their portfolios in light of the stock market's wild swings.

2. Systematic Approach: Due to the unpredictability brought on by the conflict in Russia and Ukraine, it is impossible to predict when the markets will rebound following a decline. The best approach is to make an investment in a low-risk debt fund or exchange-traded fund (ETF) and then use a systematic withdrawal plan (SWP) to transfer money into your equity funds at a predetermined date. This is preferable than going all-in. For investors with a lesser risk tolerance in the current market, we would suggest a Flexi-cap fund or a big and mid-cap vehicle among equity funds. However, during this procedure, the investor's medium-term asset allocation should also be taken into account. Depending on the investor's risk tolerance and current asset allocation, we advise increasing equity allocation levels as the equity markets recover.

3. Keep an eye on the long term: Market reversals present opportunities for investment; however, this tactic works best when investors are buying for the long run. Market fluctuations and geopolitical unrest cannot be the key driver of investment decisions." Keep it straightforward and keep in mind that discipline, patience, and luck are the three cornerstones of successful stock investment." If you possess the first two, good fortune must intervene. As a result, avoid basing your investing decisions on changes in the market, the state of the economy, or global politics.

Conclusion :

If the Ukraine issue worsens, the stock market is likely to suffer severe losses because high oil prices are predicted to continue. Although the US Federal Reserve will convene the next month to discuss whether to restrict liquidity and hike interest rates, it is anticipated that the Fed won't take any drastic action. The effect of rising crude oil prices on the Indian economy at a time when inflation is close to 6%, well above the Reserve Bank of India's upper limit, is another cause for concern.

Analysts advise investors to stick with their long-term investment plans and advise mutual fund clients to keep up their SIP plans without stopping them. On the other hand, the severe fall will give investors the chance to purchase premium equities at competitive rates. Investors should wait and let the situation develop before making any significant decisions. Only invest in stock market segments that are fairly valued or have optimistic profit projections. The fourth consecutive week of losses for Indian stock markets was caused by the escalating Ukraine crisis, which drove up oil prices and fueled concerns about inflation. Sensex and Nifty consequently decreased by 2.7 and 2.5 percent, respectively.

Investor apprehension increased as a result of the Russia-Ukraine situation, fresh sanctions put in place against Russia by powerful nations, and concerns that Russia may have attacked the biggest nuclear power plant in Europe in Ukraine. While DIIs work to support the market, FIIs are constantly selling, and their selling momentum has increased over the past few trading sessions with over 22,000 crores transacted. However, 34,000 is a key support level, and if it can hold it, we can anticipate a bounce back to 35,000-35,500 as an immediate resistance area, and 36,300-36,600 as a significant resistance zone. Banknifty's structure is also fragile. With crude oil prices surpassing $120 per barrel, soaring commodity costs are severely hampering the Indian economy.As a result, the market will be paying close attention to crude oil prices. Investors are on a roller coaster, but they shouldn't get off in the middle, to put it simply. Investors will look back on the experience with gratitude.

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