# Indian Economy · GS - III

**A sharp correction in the valuation of a major technology company can generate global financial-market volatility without necessarily developing into a systemic banking crisis. Examine the factors that determine whether a market shock becomes a systemic financial crisis.**

| EXAM YEAR | PAPER | SUBJECT |
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| MARKS | WORD LIMIT |
|---|---|
| 10 | ~150 words |

## Answer Hint

**Systemic risk, market capitalisation, leverage, debt exposure, financial interconnectedness, liquidity crisis, asset-price correction, contagion effect, banking-sector resilience, regulatory oversight, macroprudential supervision.**

## Model Answer

### Introduction

A sharp fall in the valuation of a major technology company can trigger investor losses, market volatility and a wider reassessment of asset prices. However, a market correction does not automatically constitute a systemic financial crisis.

### Factors Determining Systemic Risk

The extent of leverage is crucial because highly indebted institutions may face severe losses when asset prices decline. Interconnectedness among banks, investment funds and financial markets can transmit shocks across the economy. Liquidity mismatches, concentrated exposures and counterparty defaults can further amplify instability.

### Lessons from the 2008 Financial Crisis

The global financial crisis involved excessive leverage, subprime mortgage exposure, complex financial products and interconnected financial institutions. These channels transformed losses in the housing market into a broader banking and economic crisis.

### Way Forward

Stronger capital requirements, stress testing, transparent disclosures, effective risk management and macroprudential regulation can reduce systemic vulnerabilities. Regulators must also monitor emerging exposures in technology and private financial markets.

### Conclusion

The systemic impact of a corporate collapse depends less on its market valuation alone and more on its debt linkages, financial interconnectedness and potential to disrupt credit and liquidity channels.

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