# International Monetary and Financial Committee

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**IMFC Statement by Arun Jaitley**
**Minister of Finance, India**

On behalf of Bangladesh, Bhutan, India, Sri Lanka

**Statement by Mr. Arun Jaitley, Minister of Finance, Corporate Affairs and Information & Broadcasting, India**
**(Representing the Constituency consisting of Bangladesh, Bhutan, India and Sri Lanka)**
**to the**
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Mr. Chairman,

1. Since we met in October 2015, global growth has weakened further and financial market conditions have worsened. Global recovery is affected by subdued growth and low productivity in Advanced Economies (AEs) and elevated risks faced by Emerging Market Economies (EMEs). Many large EMEs are stressed owing to difficult macroeconomic conditions, sharply declining commodity prices and tightening financial conditions amid volatile capital flows. A credible recovery in global growth is dependent on following consistent macroeconomic policies and easing structural impediments to growth. Increasing potential growth and productivity, while remaining vigilant about risks to macro-financial stability are needed to secure a sustainable global recovery.

2. Growing uncertainties and risks of instability of the financial system are unsupportive of global recovery. Flagging trade volumes, softening commodity prices, idle capacities and anemic economic fundamentals, particularly in a number of large EMEs are increasingly impairing their ability to sustain economic and financial resilience against rising risk premiums and credit risks. Moreover, there are the risks of exogenous shocks from asynchronous normalization of Unconventional Monetary Polices (UMPs) that can produce disorderly adjustments in exchange and volatile capital flows- increasing the cost of managing external exposures and balance of payments. In this milieu, risks faced, especially by crisis affected countries and LICs, require the support of a credible multilateral safety net to provide financing necessary to prevent contagion. The IMF is in unique position to take this responsibility but needs to be strengthened further through reforms in its governance. At the same time the IMF should also examine adequacy of its own resources and whether they are sufficient for ‘future proofing’ the global economy against recurrence of financial crisis.

3. It is also a tall order to expect a sustainable economic rebound, given the lack of policy space in major AEs and the existing vulnerabilities, especially, of commodity exporting emerging markets. Low and/or negative policy interest rates in many AEs have increased the risks of volatility in asset prices and capital flows, while increasing the propensity for competitive currency devaluations. UMPs targeted at reviving growth create disruptive spillovers given the growing interconnectedness of the global financial system. UMPs have added huge uncertainty to financial markets, and are harmful to the prospect of maintaining financial stability. As I mentioned last time, advanced economies should be mindful of the consequences of spillovers on other countries that are negatively affected.

4. Structural reforms constitute the backbone of stability and could be pursued by all EMEs and developing countries to increase productivity and potential growth. Besides, countries also should also simplify and incorporate prudence in regulatory frameworks to enhance the ease of doing business to attract knowledge and capital. Consistent fiscal and monetary policies constitute the hallmark of good economic governance by ensuring macroeconomic and financial stability. The IMF should take lead as the knowledge resource in encouraging members to implement sound macroeconomic policies and provide expert analysis and advice on macro structural issues wherever requested. It must be emphasized, though, that the shift towards structural reforms in the overall policy mix being suggested by the IMF for many countries will require deeper thinking on the prioritization, sequencing and institutional capacity required to implement a meaningful structural reform programme.

**The Role of the IMF: Architecture of Global Cooperation**

5. Given the wider implications of ongoing developments in the global economy, we urge the Fund to maintain close oversight upon emerging vulnerabilities, and remain committed to safeguarding the stability of the international monetary and financial system. In order to be a reliable source of contingent financing it is important to assess the sufficiency of Fund's resources in accordance with the changing global realities including levels of global growth, size of trade and capital flows.

6. While we greatly appreciate the implementation of the 14th General Review of Quotas (GRQ) – quicker progress needs to be made to further enhance the Fund's lending capacity to fulfill its mandate of maintaining global stability. We consider that changes in quotas including fresh review of quota formula, is necessary to reflect fairness and equality in the governance of the Fund in order to reinforce its legitimacy. The role of the IMF will become increasingly important as the world becomes more complex, casting greater responsibility on its functioning as sentinel of global economic stability. It is in this regard that we strongly urge for the completion of the 15th General Review of Quotas, including the review of the new quota formula, by 2017 Annual Meetings.

7. Given the urgency of the discussions on 15thGRQ, Board discussions should begin as soon as possible to complete the review in time. Unwarranted delays may create an increased chasm between the Fund's governance and the evolving economic conditions which can be addressed with the presence of a strong global safety net with command over adequate resources. This is particularly important since at present the global financial safety net (GFSN) needs strengthening, owing to uneven coverage, costly access, lack of reliability and predictability. While we believe that all the three potential components – self-insurance, bilateral/regional agreements and the multilateral agreement represented by the IMF – are legitimate and complementary components of a robust and fair GFSN, we consider that there is need to promote cooperation among these various elements so as to make the functioning of GFSN more coherent. The IMF is the best position to share this responsibility by means monitoring and policy signaling to tap the confidence of creditors from various layers by reducing moral hazard. The Fund could also participate in co-financing with other element(s), with agreed coordination protocols to reduce delays in financing. This will reduce the sensitivity of members from availing Fund's help. The Fund could add to the strength of the GFSN by providing predictable and reliable financial support for crisis prevention and

resolution, by earmarking provisions for immediate liquidity support and reliable cover for the full duration of shocks to a wide range of countries to limit contagion. These facilities could be based on pre-qualification and state-dependency to increase reliability. The incorporation of these instruments, apart from those existing at present, may help members to better meet liquidity needs when needed.

8. The global economy is ably supported by the Fund as a knowledge bank in advising members on proficient policies for macroeconomic management and crisis prevention and adjustment. The IMF can also serve as platform for building consensual rules for enhanced cooperation among countries on matters pertaining to global stability. The leadership and participation of advanced economies, especially, the United States in the Fund is a valued source of its institutional strength and credibility. The Fund must continue to evolve as an effective institution in tune with changing character of the global economy, and build ample reserves to prevent the threat of financial distress among its members.

**Developments in the Constituency**

**Bangladesh**

9. Despite global headwinds and domestic challenges, the economy of Bangladesh has continued to do well. Real GDP has been provisionally estimated by the IMF to grow by 6.3 percent in financial year FY16 (ending in June 2016) and further by 6.7 percent in FY17. However, the Government of Bangladesh expects a higher order of growth, topping the medium-term forecast of IMF at 7.05 per cent in FY 16 and 7.2 per cent in FY17. This is a continuation of the robust growth performance over the last three years in which the economy grew at an average of about 6.2 percent, primarily supported by higher public investment and exports.

10. Headline inflation eased in FY15, averaging 6.4 percent, and is expected to remain stable in FY16. While food inflation has eased on the back of a good harvest and declining global prices, non-food inflation has picked up, primarily due to higher minimum wages in the garment industry and electricity and gas tariff hikes. Inflation is expected to moderate further in FY16–18 on accounts of low commodity prices in the international market and reduction in supply bottlenecks. In this regard, the monetary policy stance continues to be prudent, and the authorities remain vigilant against upside risks to inflation. On the external front, the current account balance has again become positive in the first quarter of FY16 after being moderately negative in 2014 and 2015 led by subdued exports due to restructuring in the garment industry and lower external demand. External reserves have risen to a comfortable level of about six months of import cover. Inbound remittances recovered in FY15, but have weakened in the first five months of FY16 due to persistent low oil prices. However, remittances growth is expected to gain momentum shortly as the overseas employment has been increasing in recent months.

11. Fiscal deficit in FY15 is estimated to have risen to 3.8 percent from 3.5 percent in FY14 due to low fiscal revenues reflected in the decline in tax-to-GDP ratio in FY14 and FY15, and fall in nontax revenues due to lower profit transfers from public sector agencies to the government. However, public investment has increased and subsidies as a share of GDP

have come down, helped in part by a lower fuel subsidy. Introduction of the VAT from FY16 would improve the tax-to-GDP ratio. In the banking sector, close supervision of banks continues along with recapitalization and automation of state-owned banks and measures to enhance cyber-security in the banking sector.

12. The Government of Bangladesh envisages the economy to grow at a faster pace over the medium term with the help of higher public investment in infrastructure and measures to enhance private investment. Higher public investment will require an improvement in the low tax/GDP ratio and the necessary microstructure is being put in place to make the introduction of a new VAT by July 2016 a reality, so as to boost tax collections. The Government also intends to make improvements in tax administration and undertake direct tax reforms. The PPP Act passed in September 2015 should enable private participation in public infrastructure projects, particularly in the power and transport sectors, along with future measures to ease the business and investment climate.

**Bhutan**

13. Bhutan's real GDP growth averaged 8.7 percent during the Ninth FYP and 7 percent during the Tenth FYP (2008/09-2012/13). After overheating pressures from large hydropower related investment and imports, the effort to cool down economic activity (chiefly by the moderation of credit growth) contributed to the slowdown in GDP growth which fell to 3.8 percent in 2013/14. However, growth is expected to have recovered to 6 percent in 2014/15, driven by a pick-up in services and hydropower-related construction.

14. Consumer price inflation has eased: after peaking at 11.3 percent in Q4 2013 (y-o-y), it fell to 6.7 percent by Q4 2014 and further to 3.5 percent in Q4 2015. The fiscal deficit rose from 1.2 percent of GDP in 2011/12 to 4.2 percent of GDP in 2012/13, and then turned into a surplus of 3.8 percent of GDP in 2013/14, much stronger than the originally projected deficit of 3.7 percent of GDP. Higher-than-expected project-tied grants from the Government of India (GoI), and spending broadly in line with the original budget plan, have contributed to the stronger fiscal outcome. The 2014/15 (revised) budget envisaged a deficit of 2.3 percent of GDP, however, an updated estimate shows a smaller deficit of 1.9 percent, with somewhat stronger tax and nontax revenues and grants.

15. The current account deficit increased further as interest payments on hydropower-related loans increased, to close to 29 percent of GDP in 2014/15, from 26.4 percent of GDP in 2013/14. As capital inflows moderated somewhat, the overall balance turned slightly negative and international reserves fell marginally to $960 million by June 2015, before recovering to $1,072 million in November.

16. After a period of rapid growth in credit to private sector averaging 35 percent in 2005-2011, credit growth fell to below 10 percent in 2013 and 2014. However, following the September 2014 termination of ban on vehicle and housing loans introduced during the "rupee crisis" in 2011/12, growth of credit to the private sector has increased to 14 percent in June 2015.

**India**

17. India's balanced macroeconomic environment and strong growth prospects make it a 'bright' spot in the global scenario. According to advanced estimates, GDP growth in 2015-16 is likely to attain level of 7.6 per cent, higher than 7.2 per cent in 2014-15. Quarterly growth rates during the first three quarters of 2015-16 have showed consistently strong traction, with the 3rd Quarter registering a growth of 7.3 per cent as compared with 6.5 per cent in the same Quarter in 2014-15. The growth performance is more credible given that it has been achieved despite contraction in our exports due to slowdown in global economy and two consecutive years of monsoon shortfall.

18. Headline Consumer Price Index (CPI) inflation has moderated significantly. In February, 2016 the CPI inflation rate at 5.2 per cent is in line with the glide path set by the Reserve Bank of India. Going by the trend so far, the target of 6 percent for the all important CPI inflation set by the Reserve Bank for 2015-16 is likely to be achieved. On April 5, 2016 the Reserve Bank of India reduced the policy rate by 25 basis points from 6.75 percent to 6.50 percent and would calibrate monetary conditions in line with our objectives of growth and inflation. Efforts are being made by the Reserve Bank to improve the transmission of policy rates to market interest rates, particularly to bank lending rates. At the same time, measures have been taken to capitalize and repair bank balance sheets in order to ease credit delivery. India's foreign exchange reserves rose to US$ 355.95 billion (as of March 18, 2016), up by US$ 14.31 billion from the level on end March, 2015.

19. The Gross Fiscal Deficit (GFD) of the central government at 3.9 percent in 2015-16 was met by recovering higher tax and non-tax revenues without reducing plan spending or reducing allocation for pro-poor schemes, thereby underpinning the quality of fiscal consolidation. Despite the additional burden of pay and pensions on account of 7th central pay commission and defense pensions, the Government is aiming to attain GFD target of 3.5 per cent in 2016-17 as per the medium term fiscal framework. The focus of the Government will be on expenditure prioritization particularly in the farm and rural sector, the social sector, infrastructure and recapitalization of banks. Fiscal policy has to play a vital role in sustaining overall growth in the uncertain global environment. With gains from low commodity prices, manly oil, the current account deficit (CAD) was contained at 1.3 percent of GDP in 2014-15 and is projected to remain stable 1.4 per cent by end of 2015-16. However, there are concerns about export growth which is declining consecutively for more than a year due to slowdown in global demand.

20. The present Government is following the approach of 'Reform to Transform India' through far reaching structural reforms to foster strong and sustainable growth. Measures, *inter alia*, to enhance infrastructure investment, incorporation of Bankruptcy law, improve business climate and significant tax reforms such as GST are being pushed forward. The Government is taking steps to reform institutions, simplify procedures and repeal obsolete laws. A progressive and non-adversarial tax regime incorporating best international practices is being put in place. Initiatives such as Make-in-India, Startup India - Standup India, Mudra bank and Skill India are focused at encouraging innovations, entrepreneurship and job creation. At the same time, novel welfare/social security schemes have been implemented to improve social outcomes. A new crop insurance scheme with attractive premium charge has

been launched to protect farmers from income losses due to crop failures. The scheme protects farmers from losses due to crop failures. The Government is leveraging digital technology to ensure that all eligible persons are included under the direct benefit transfer program. Accordingly, the AADHAAR (unique identification) system with statutory backing will form the backbone for targeted delivery of financial and other subsidies, benefits and services.

**Sri Lanka**

21. The Sri Lankan economy grew by 4.8 per cent in 2015 compared to 4.9 per cent growth in 2014, generally supported by accommodative monetary and fiscal policies and favorable weather conditions. However, growth performance was slowed down due to two national elections held during the year which had some impact on investor sentiment. The growth was supported by all the 3 major sectors of the economic activities. Services sector, the largest contribution to the overall output of the country, grew by 5.3 per cent supported by the expansion in information technology, financial services, and telecommunication and insurance sectors. The agriculture sector also shared strong performance by recording a 5.5 per cent growth mainly on account of paddy and vegetable production. Meanwhile, the industry sector grew moderately by 3 per cent, largely driven by contraction in construction activities. GDP is projected to grow by 5.5 – 6.0 per cent in 2016.

22. Inflation continuously remained at single digit level during recent years supported by appropriate monetary policy actions, low commodity prices in the global market including energy and improved domestic supply conditions. The annual average inflation as measured by the change in national consumer price index was 2.6 per cent in February 2016. However, considering the continued high growth in credit and money supply and high excess liquidity conditions in the market, the Central Bank of Sri Lanka tightened the monetary policy by raising the Statutory Reserve Ratio (SRR) by 1.5 percentage points to 7.5 per cent and raising policy interest rates by 50 basis points, to address build up of demand driven inflationary pressures. Despite the improved performance in government revenue collection during 2015, fiscal management was challenging due to increased recurrent expenditure. Reflecting this fiscal deficit increased to 7.5 per cent from 6.0 per cent in 2014. However, the government is strongly committed to reduce the budget deficit below 6 per cent in 2016 through broadening the tax base, simplifying the tax structure, improving tax administration and rationalizing recurrent expenditure.

23. Sri Lanka's external sector performance was subdued during 2015 largely due to the impact of developments in the global economy. Even though Sri Lanka benefited from low oil prices as an oil importer, declines in export commodity prices, particularly tea and rubber prices as well as low external demand for export commodities lowered the earnings from exports. The faster decline in export earnings than the decline in import expenditure led the widening of trade deficit. However, improvement in services exports, particularly earnings from tourism together with workers' remittances helped to maintain the current account deficit unchanged at around 2.4 percent of GDP. Net inflows to the financial account declined, mainly reflecting outflows in the government securities market and slowdown in foreign direct investments. However, the government was able to raise USD 2,150 million through issuance of international sovereign bonds during the year. Nevertheless, the overall

Balance of Payments is estimated to have recorded a deficit of US dollars 1,489 million in 2015. Meanwhile, gross official reserves were estimated at US dollars 7.3 billion by end December 2015, which is equivalent to over 4.6 months of imports. The rupee depreciated against the US dollar by 9 per cent, as the Central Bank allowed a greater flexibility of determination of exchange rate. The financial sector stability and soundness improved, supported by adequate capital and liquidity levels and contained non-performing loan ratios.