India Economic Outlook
2014 Article IV Report

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Outline

1. Global backdrop
2. Growth and inflation
3. India’s external sector
4. Fiscal policy
5. Corporate and financial sector
6. Structural issues
7. Conclusion: main messages

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Global backdrop

**WORLD ECONOMIC OUTLOOK UPDATE JANUARY 2014**

**UPSIDE**
- Strengthened global activity during second half of 2013
- Euro area moving from recession to recovery
- Higher export demand in emerging markets
- U.S. budget deal to boost final demand in 2014

**TO ENSURE GROWTH, IMF RECOMMENDS:**

**Advanced economies:**
- Avoid premature monetary policy tightening
- Repair balance sheets
- Implement structural reforms to boost growth

**Emerging market and developing economies:**
- Manage vulnerabilities from capital flow volatility
- Safeguard financial stability after rapid credit growth
- Implement structural reforms to boost growth

**RISKS**
- Possible deflation in advanced economies
- Weak domestic demand in emerging markets
- Stagnation in euro area
- Capital flow volatility to some emerging markets

**GROWTH**

- **2012**
  - World: 3.1
  - Advanced: 1.4
  - Emerging Markets & Developing: 1.3

- **2013**
  - World: 3.0
  - Advanced: 1.3
  - Emerging Markets & Developing: 2.2

- **2014**
  - World: 3.7
  - Advanced: 3.9
  - Emerging Markets & Developing: 4.7

- **2015**
  - World: 5.1
  - Advanced: 5.4
  - Emerging Markets & Developing: 5.4

**INTERNATIONAL MONETARY FUND**

www.IMF.org #WEO
India: Growth and inflation

GDP Growth
(In percent, yoy)

Sources: CEIC and IMF staff calculations.
We’ve all been too optimistic for India

India: Growth Forecast Revisions
(In percent)

Sources: IMF; and Consensus Economics.
Have we hit bottom yet?
(Consensus: 4.7% in 2013/14 and about 5.5% in 2014/15)

Source: Consensus Forecasts, WEO
There is a domestic component to India’s slowdown

Spillovers from Advanced Economies

Sources: IMF, *World Economic Outlook*; and IMF staff calculations.
Note: Unexpected growth denotes real GDP growth in 2013 minus the forecast. AE partner unexpected growth denotes export-weighted average of growth of advanced-economy trading partners in 2013 minus the forecast, multiplied by the economy’s share of exports in real GDP. Forecasts are taken from the September 2011 WEO.
India’s growth slowdown began with investment stalling ...
... but the slowdown has become broad-based, ...

**Demand Components of GDP**
(In percent, yoy)

Sources: CEIC and IMF staff calculations.
... and the investment pipeline remains thin
Inflation is too high (and it has become stuck in expectations)

Household Inflation Expectations and Food Inflation
(In percent)

Sources: CEIC, Haver Analytics and IMF staff calculations.
Food inflation is certainly part of the story

CPI Food Inflation: Contributions
(In percent, yoy)

Sources: CEIC and IMF staff calculations.
Role of monetary policy?
Normalization since September, but real policy rate still very low
Bottom line for EMs: getting macro fundamentals right is crucial.
India’s external sector

Nominal and Real Effective Exchange Rates
(Index, 2005=100)

REER

10yr Average of REER

NEER [RHS]

Sources: IMF, Information Notice System and IMF staff estimates.
Equity flows have been more stable than debt flows since May.
CAD has been squeezed, but mainly due to gold measures?

Current Account Balance
(In percent of GDP)

Sources: CEIC and IMF staff calculations.
How durable are the measures to reduce gold imports?

**Imports: Principle Commodities**
(In millions of US Dollars, 3mma)

Sources: CEIC; and IMF staff calculations.
Financing the CAD has become more difficult in recent years...

Financial Account
(In percent of GDP)

Sources: CEIC; and IMF staff calculations.
... and composition has shifted toward debt (at least until the last few months)

Inward FDI and Debt Financing
(In percent of Current Account Deficit)

Source: Haver Analytics.
India had ample reserves (even before Sept measures) ...
Reserves Coverage

Sources: IMF staff calculations.

... but the trend has worried some analysts
Government Balance
(In percent of GDP) 1/

1/ Includes subsidy-related bond issuance.
Source: IMF staff data.
After the post-global crisis expansion, fiscal stance has been broadly neutral.

General Government Fiscal Impulse 1/
(In percent of GDP)

1/ Defined as difference between current and previous year budget deficits, using business cycle-adjusted revenues.
Source: IMF staff calculations.
Revenue mobilization has not recovered...
... and current spending, which reached a plateau during the crisis, has fallen only slowly
Subsidy reform is therefore a high priority.

Government Subsidies
(As a percent of Current Expenditure)

Sources: IMF staff data.
Government capital investment has taken the brunt of adjustment.
Corporate and financial sector

**Corporate Borrowing**
(As percent of GDP)

- Non-food bank credit
- External commercial borrowing

Sources: CEIC Data Company
Leverage ratios are particularly high for construction; manufacturing; transport, communications & utilities; and the public sector.
NPAs have been rising in recent years, but remain at levels well-below the early 2000s.

**Commercial Banks NPAs**

(In percent)

<table>
<thead>
<tr>
<th>Year/Year</th>
<th>Public gross</th>
<th>Private gross</th>
<th>Foreign gross</th>
<th>Public net</th>
<th>Private net</th>
<th>Foreign net</th>
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<tbody>
<tr>
<td>2002/03</td>
<td>9.3</td>
<td>5.2</td>
<td>2.6</td>
<td>4.8</td>
<td>2.6</td>
<td>2.2</td>
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<tr>
<td>2003/04</td>
<td>8.5</td>
<td>4.9</td>
<td>2.7</td>
<td>4.4</td>
<td>2.4</td>
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<td>2004/05</td>
<td>6.7</td>
<td>4.5</td>
<td>2.0</td>
<td>3.7</td>
<td>2.0</td>
<td>1.7</td>
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<tr>
<td>2005/06</td>
<td>5.9</td>
<td>3.6</td>
<td>1.6</td>
<td>3.2</td>
<td>1.6</td>
<td>1.2</td>
</tr>
<tr>
<td>2006/07</td>
<td>5.1</td>
<td>3.0</td>
<td>1.4</td>
<td>2.7</td>
<td>1.3</td>
<td>1.0</td>
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<tr>
<td>2007/08</td>
<td>4.3</td>
<td>2.6</td>
<td>1.2</td>
<td>2.4</td>
<td>1.1</td>
<td>0.8</td>
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<tr>
<td>2008/09</td>
<td>3.7</td>
<td>2.2</td>
<td>0.9</td>
<td>2.1</td>
<td>0.9</td>
<td>0.6</td>
</tr>
<tr>
<td>2009/10</td>
<td>2.9</td>
<td>1.9</td>
<td>0.7</td>
<td>1.8</td>
<td>0.7</td>
<td>0.4</td>
</tr>
<tr>
<td>2010/11</td>
<td>2.4</td>
<td>1.6</td>
<td>0.5</td>
<td>1.6</td>
<td>0.5</td>
<td>0.3</td>
</tr>
<tr>
<td>2011/12</td>
<td>2.0</td>
<td>1.4</td>
<td>0.4</td>
<td>1.4</td>
<td>0.4</td>
<td>0.2</td>
</tr>
<tr>
<td>2012/13</td>
<td>1.8</td>
<td>1.2</td>
<td>0.3</td>
<td>1.2</td>
<td>0.3</td>
<td>0.1</td>
</tr>
</tbody>
</table>

Sources: Reserve Bank of India and IMF staff calculations.
PSU banks have higher NPAs and greater exposure to restructured loans

**Commercial Banks: Restructured Advances & NPAs**
**(In percent)**

- **Restructured Advances (% of outstanding advances)**
- **Gross NPAs (% of outstanding advances)**

Sources: Reserve Bank of India and IMF staff calculations.
Ease of Doing Business Ranking: BRICS and South Asia

Note: South Asia Group includes Bhutan, Maldives, Nepal, Pakistan and Sri Lanka.
Labor market: demographic dividend or demographic bomb?

**Labor Market Efficiency Ranking and Young Population Ratio: BRICS and South Asia**
(Young population ratio: in percent of working-age population)


Note: 1/ Young, defined as people younger than 15; working-age population as 15-64.
2/ South Asia Group includes Bhutan, Nepal, Pakistan and Sri Lanka.
Conclusion: main messages

**Inflation is too high**
- Not only food inflation;
- Undermining competitiveness;
- Tight monetary policy appropriate

**Management of external volatility**
- Exchange rate volatility is key;
- Use of reserves to smooth;
- Tighten monetary, but also fiscal;
- Don’t try to curb capital outflows

**Fiscal consolidation needed**
- Need to control subsidy bill
  - *Fuel subsidies are regressive*
- Revenue mobilization important over medium term
Conclusion: main messages

Corporate and financial sector
- Better monitoring of asset quality is needed;
- More info on corporate vulnerabilities

Structural bottlenecks
- Competitiveness concerns;
  - Labor market rigidities
- Power linkages;
- Land / environmental clearances

Other issues?
- What have we missed?
Thank you

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