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India

On behalf of
Bangladesh, Bhutan, India, and Sri Lanka

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Global Economy

1. I am happy to join this forum to discuss about global economic developments at this juncture. This platform provides a unique opportunity to present different perspectives and learn about the critical issues confronting the member countries. Our economies are inter-connected much more than earlier. Hence, the decisions and actions we take will have ramifications on the life of one and all on this planet. We have achieved rapid growth in world trade over the last few decades but trade seems to be stalling of late. After rapid financial integration across borders, the capital flows have also ebbed post-crisis. In this backdrop, the multilateral institutions, especially the IMF, need to reorient themselves to handle the complexities and concerns arising therefrom.

Growth Prospects and Downside risks

2. Global economic activity has weakened since Q3 of 2018 sans Q1 of 2019. Elevated trade tensions, uncertainty about Brexit, volatility in oil prices, and geo-political developments are leading to subdued sentiments and demand conditions across the globe. As per the latest World Economic Outlook, global growth is projected to decline from 3.6 per cent in 2018 to 3.0 per cent in 2019. The slowdown appears pervasive and broad-based and runs across advanced economies (AEs) and emerging market and developing economies (EMDEs). The risks and imbalances underlying the growth slowdown call for the need to strengthen global cooperation at multilateral level.

3. Notwithstanding the downturn, we need to be careful in interpreting and communicating on the growth slowdown. We need to recognize the policy levers that we have to stem the rot that seem to be setting in due to growing trust deficit. As we move towards the decade of 2020s, I find that there are reasons to be hopeful and cautiously optimistic. But, that would require a calibrated and balanced approach in deploying a mix of fiscal, monetary and structural measures by countries to help achieve their growth potential. We need to guard against evolving financial sector vulnerabilities reinforced by prolonged accommodative stance across economies and the need to use macro-prudential measures to mitigate adverse spill overs.

4. We, in India, have taken frontloaded action using diverse policy levers. Notwithstanding the very recent slowdown, our potential growth rate in the coming years is much higher. With a prudent mix of policies, we are committed to having a sound macro-economic environment conducive to fuel growth and ensure inclusive development.

5. We have provided impetus to growth by rationalizing and reducing corporate tax rates that will stimulate private sector investment in infrastructure and industry. We have also taken a number of sector specific measures to support growth. The Reserve Bank of India has also reduced policy rates five times this year by a cumulative 135 basis points recognizing the policy

space it had. Supported by fiscal and monetary actions, an inflation trajectory in line with the inflation target and progressive structural reforms, we expect investment to revive, consumption to remain robust and growth to return to a higher trajectory soon. Having said this, there are risks at various levels which can adversely affect the growth momentum. In a globalized economy, it is pertinent to mention that external factors like trade tensions and other geopolitical uncertainties can have overwhelming deleterious effects. We need to think of ways whereby the IMF and other international organizations including the WTO, as also this forum and the member governments can work towards evolving a mechanism to mitigate these risks and boost mutually beneficial engagements. As a dynamic economy, we believe that we have a key stake in nurturing global cooperation. Hence, we reiterate our faith in the multilateral system to provide a platform for equitable partnership.

IMF's role in ensuring global economic stability

6. The international monetary and financial system, of which IMF is the core, is facing a host of significant challenges such as global imbalances amongst certain advanced economies, spillover effects of policy actions of AEs, especially on the EMEs, risks of financial sector vulnerabilities coming to fore as growth slows down, and generally limited fiscal space amid continued fiscal sustainability concerns amongst AEs as well as EMDEs. There is need for cooperative solutions to overcome these risks and a strong coordination amongst member countries through multilateral institutions and fora and otherwise.

7. The Fund plays a significant role in assisting the member countries to assess their macro-economic stability and mitigate financial vulnerability. The IMF's proposal to come up with an Integrated Policy Framework is a step in the right direction. An effective surveillance mechanism helps countries to identify risks, both global and domestic, and suggest ways to prevent such risks and mitigate their adverse effects. We will look forward to how the IMF proposes to factor in the interactions between monetary, exchange rate, macro-prudential, and capital flow management policies in its policy advice. In this context, it is very important to build in sufficient policy flexibility for the EMEs, not just because they are heterogeneous group, but also because they need a wide array of tools which can be contextually used as per needs. This has been the case especially when there has been fundamental misalignment of exchange rate, caused by surges in capital flows. Often sudden stops and reversals of capital flows follow these surges that erode macro-financial stability very quickly. We believe that the policy option of EMEs to preemptively use macro-prudential measures (MPMs) and capital flow measures (CFMs) need to be fully recognized in any integrated policy framework.

8. As with trade, the growing global financial integration is bringing in huge opportunities but is also introducing uncertainties and risks. Capital flows benefit countries in terms of higher investment and risk sharing, but at the same time, it can have adverse effect on countries with weak policies and institutions. The macro-prudential policies' interface with anti-money laundering (AML) and countering financing of terrorism (CFT) could be useful in strengthening the integrated policy framework. The IMF's remit may not be as direct as of the Financial Action Task force (FATF) in this respect. However, integrating AML-CFT with IMF lending policies can significantly enhance member's compliance on these issues that pose threat to the global economy. The IMF work can also cover elements such as secrecy jurisdictions, cyber-risks and tax havens.

Highly Indebted Economies and IMF's role

9. Debt levels are rising alarmingly amongst low income, emerging and the AEs. Unsustainable and opaque lending conditions are weakening the economic fundamentals, eroding governance and unsettling growth prospects. Multilateral institutions must focus more on capturing the external debt correctly and the risks the debt build-up pose. Only then can one consider the right steps to mitigate debt problems. Debt transparency and sustainability are central to the macro-financial stability and the IMF must take on a larger leadership role and enforce delivery.

IMF resources and governance

10. To ensure the stability of the international monetary and financial system, it is imperative that the IMF continues to remain at the centre of the Global Financial Safety Net. For this to happen, the IMF should be able to maintain its current lending capacity to meet the needs of its members as well as meet such needs should a financial crisis occur. In this backdrop, there have been concerns about its resource adequacy, given that the 15th Round of the General Review of Quotas (GRQ) is likely to conclude this year without any quota increase. This could seriously hamper the effectiveness of the IMF's role in a crisis, as the only source which IMF could rely upon with certainty is its permanent resources, i.e. quotas. Moreover, IMF was conceived as a quota-based organization and its legal as well as economic basis is enshrined in that concept. Although we acknowledge that Fund's borrowed resources (New Arrangements to Borrow and Bilateral Borrowing Agreements) have played a role in building its buffer, these remain temporary and backstop arrangements, As such, creditor nations may themselves be in stress in a crisis and may not able to come to the aid of IMF and its wider membership, thereby rendering these buffers ineffective. That this category of resources is going to remain valid for 1-3 years from now, unless extended or new agreements reached, is hardly comforting.

11. A more permanent solution in the form of a quota increase is in order. We, therefore, view the lack of adequate support for a quota increase under the 15th GRQ as somewhat disappointing. We, however, consider this as a temporary setback. We hope that the discussions in the next (16th) Round of the GRQ would achieve success in terms of quota increase to take care of the Fund's resource adequacy. It should also address the long-pending issue of under-representation of the EMDEs and the dynamic economies in the IMF's quota shareholding. The representation of member countries in the IMF should be in line with the changing economic realities for this institution to continue staying relevant. Quota increases under the 16th Round and also in the future rounds should be seen as an opportunity to realign quota shares in favour of EMDEs to allow them a more meaningful role in the governance of this Institution.

DEVELOPMENTS IN THE CONSTITUENCY

A. BANGLADESH

12. Growth momentum in Bangladesh economy continues gaining pace, clocking 8.13 percent real GDP growth estimated for FY2019 (July2018-June 2019) against 7.86 percent growth in preceding FY2018; supported by both external (export) and domestic demand.

13. Cautious monetary and fiscal stances have helped drive down headline (y-o-y annual average) CPI inflation from 5.74 percent at end August 2018 to 5.48 percent by end August 2019, well within the targeted 5.6 percent FY2019 ceiling. However, robust domestic demand driven by rapid GDP growth gain has nudged point-to-point and core (non-food, non-fuel) CPI inflation upward since January 2019, indicating need of continued caution against buildup of inflationary pressures.

14. Fiscal deficit (including grants) of 5.0 percent of GDP projected for FY2020 remains within its typically moderate lower single digit trend level, with a more than half (2.8 percent of GDP) of it to be funded by domestic borrowing. A substantial sustained boost in tax receipts is expected from the revamped new VAT law coming into force from July 2019, widening fiscal space for larger fiscal expenditure outlays without widening deficit in GDP percentage terms.

15. The BOP current account deficit almost halved at the end of FY2019 and reached 1.7 percent of GDP, which stood at about 3.2 percent of GDP at the end of FY2018. CAB was in surplus of USD 240.0 million in July 2019. Besides post-flood rebound in domestic food crop output and project related imports coming down to normal trend levels, healthy growth in exports and workers' remittance inflows in FY2019 and market-based adjustments in exchange rate of Taka have also helped in rapid substantial narrowing down of bop current account deficit.

16. Bangladesh authorities are pursuing quickest feasible graduation of Bangladesh to Upper Middle-Income economy status on an inclusive environmentally benign development path fully in tune with the UN SDGs. To that end the authorities are focusing on broad based inclusive human development, with adequate fiscal expenditure outlays for healthcare, education and job oriented training; besides ample outlays for expansion and maintenance of physical infrastructure to crowd in domestic and foreign private investments in job rich, environmentally benign output initiatives.

17. Also, the country's financial sector is being shored up towards getting it ready and able to respond adequately to the larger domestic and external financing needs of an Upper Middle-Income economy, with institutional strength and soundness to withstand volatility shocks from increasing exposures to global markets. Activation of markets in corporate bonds and asset backed securities, introducing crop insurance schemes and other risk mitigation and hedging instruments are also high on priorities in Bangladesh's financial sector development agenda.

18. Sustained steady GDP growth is enabling Bangladesh to finance much of her ambitious multifaceted development initiatives out of domestic resources; the once dominant role of external ODA has dwindled to a minor one. Nonetheless, substantial need still persists for external financing in softer terms (particularly from the multilateral global institutions), including inter alia for attaining some of the key UN SDGs like climate change risk mitigation and adaptation, and for larger physical infrastructure projects. Bangladesh looks forward to continuing role of the Breton-Woods Institutions and their subsidiaries in catalyzing such external financing support. Finally, for an emerging economy like Bangladesh, ongoing trade war between major economic powers may present new scope to further bolster its external economic activities, while potential slowdown in global growth poses uncertain risk.

B. BHUTAN

19. Bhutan's economic growth slowed down to at 4.63 percent in 2017, in line with the performance of the preceding three years where growth averaged a little over 6 percent. The slower growth was driven by the secondary and tertiary sectors. The medium-term outlook is also promising, with the commissioning of new hydropower projects expected to provide further impetus to output and exports, as well as to fiscal revenues.

20. The overall CPI inflation (measured by the year-on-year change of the consumer price index) recorded at 2.74 percent in June 2019 compared to 2.55 percent during the same month of previous year. The small increase in inflation was mainly due to increase in the prices of non-food commodities. On the other hand, the domestic inflation during June 2019 was recorded at 3.36 percent while imported inflation was recorded at 2.13 percent. The higher domestic inflation of was due to the increase in food prices.

21. During the FY 2017/18, the actual expenditure was Nu. 52,113.16 million, with the total realized resources of Nu. 56,331.36 million, resulting in the fiscal deficit of Nu. 4217.81 million, which is 2.42 percent of GDP. With election of new democratic Government and launch of 12th FYP, the revised budget for the FY 2018/19 was Nu. 42,949.11 million. Despite decrease in the revised budget, the fiscal deficit improved from 2.42 percent of GDP to 1.96 percent with the higher improvement in the resources.

22. On the external front, both the trade and current account deficits deteriorated in FY 2018/19. The current account deficit slightly increased from 24.11 percent of GDP in FY 2017/18 to 25.10 percent of GDP in FY 2018/19, mainly on the account services payment, which increased to Nu. 8,654.07 million from Nu. 3,885.80 million in the previous year. At the same time, trade deficit also increased from Nu. 27,573.1 million to Nu. 29,109.7 million in FY 2018/19. At the end of June 2019, the gross international reserves recorded at USD 1,063.18 million. Reserves were sufficient to finance 13.36 months of merchandise imports.

23. The broad money (M2) was recorded at 5.60 percent as of June 2019, a decrease of 4.83 percent point from 10.43 percent in June 2018. The growth in the broad money was contributed by growth in narrow money (M1) and other deposits. The narrow money and other deposits growth recorded at 4.39 percent and 7.26 percent respectively as of June 2019. On the other hand, net foreign assets recorded negative growth of 3.16 percent and domestic credit recorded

growth of 13.13 percent. Credit to private sector growth remained at level of 20.54 percent in June 2019 with increase from 15.69 percent in June 2018. The growth in credit was mainly contributed by the access to credit transmitted through financial inclusion initiatives.

C. INDIA

Growth performance and prospects

24. The Indian economy has shown resilience against the global headwinds. However, with the continuing subdued global demand conditions and a cyclical downturn in India that was exacerbated by some sector-specific issues, it has witnessed some slowdown in recent quarters. The idiosyncratic sector-specific issues have since been substantially resolved. The expected recovery has been reflected in IMF projections. The authorities have taken a series of growth supporting measures including resolution of impaired assets of banking sector, bank recapitalization, cut in the corporate income tax rate, resolution of NBFC liquidity stress and monetary easing that are expected to provide significant boost to investment as well as consumption. During the FY2019-20, the IMF projections as well as RBI's monetary policy projections show that the Indian economy will clock a growth rate of 6.1 per cent. India's growth is expected to strengthen next year and the October WEO has projected it at 7 per cent. Further, India's continued commitment to fiscal discipline, sound external position, liberalized FDI inflows and enhanced emphasis on financial inclusion would provide ground for sustaining robust growth, going forward.

Fiscal consolidation

25. On the fiscal front, the Government is firmly committed to the path of fiscal consolidation. Fiscal deficit has been budgeted to be 3.3 per cent of GDP in FY 2019-20 compared to the 3.4 per cent in the preceding year. The Government's adherence to the fiscal glide path will provide adequate headroom for private sector investment and supplement the growth supporting measures initiated.

External sector

26. Notwithstanding the adverse global economic environment, India's external sector has continued to be resilient. The current account deficit has stayed on average below 1.5 per cent of GDP during the past 5-year period. The level of foreign exchange reserves has gradually increased to USD 434.6 billion as on October 1, 2019, equivalent to 10 months of imports cover. The Indian economy remains one of the preferred destinations for foreign direct investment (FDI). Even though global FDI flows have slackened in recent years, net FDI flows to India during the current year (April-July) have grown by 55 per cent over the preceding year.

Monetary policy

27. The conduct of monetary policy is guided by the objective of achieving the medium-term target for consumer price index (CPI) inflation of 4 per cent with a tolerance band of +/-2 per cent, while supporting growth. Sensing the policy space in terms of current and projected inflation being below the inflation target, the RBI acted in a forward-looking manner and, taking into consideration its assessment of domestic and global slowdown, started cutting its policy rates since February 2019. It has since lowered its policy rates by 135 bps and the

transmission is expected to gather speed ahead. The CPI inflation has edged up a bit, largely in line with the trajectory anticipated by RBI and was at 3.2 per cent in August 2019. The benign inflation outlook provides headroom for policy action to close the negative output gap. Addressing growth concerns by boosting aggregate demand, especially private investment, assumes the highest priority at this juncture while remaining consistent with the inflation mandate.

Financial sector

28. Turning to the financial sector, with persistent efforts, the overhang of stressed assets in the banking system has declined. The Insolvency and Bankruptcy Code is proving to be a game changer. Recoveries have gradually improved and as a result, deadlocks in the potential path of the investment cycle are easing. New norms for resolution of stressed assets framed in June 2019 by the RBI provide incentives for early resolution, with discretion to lenders on resolution processes. Capital buffers have been strengthened by recapitalisation of state-owned banks to the order of INR 2.7 trillion, including the budgetary allocations for 2019-20. The abatement of stress has rekindled bank credit flows, which are getting broad-based.

Ease of doing business

29. Several investor-friendly measures have been taken, including a highly liberalized FDI regime, to realize our endeavour of 'Make in India'. In the World Bank's Ease of Doing Business Rankings, India jumped from 130 to 100 in 2018; and from 100 to 77 in 2019. This jump of 53 places in just two years reflects an evolving facilitative business environment for investors and business professionals in the country and outside.

Infrastructure sector

30. The growth dynamics of our economy are perhaps best captured by our thrust on improving infrastructure, particularly physical infrastructure connectivity. We are rapidly developing industrial corridors; national road corridors and highways (***Bharatmala***); enhancing port connectivity, port modernization and port-linked industrialization (***Sagarmala***); augmenting the navigation capacity of National Waterways (***Jal Marg Vikas***); creating dedicated railway freight corridors; and improving air connectivity to smaller cities (***UDAN***). As these initiatives will improve logistics and reduce cost of transportation, they will increase competitiveness of domestically produced goods in the international market. Again, a step ahead towards Make in India!

31. As we envisage becoming a 5 trillion-dollar economy by 2024-25, our focus on creating world-class infrastructure has become even more resolute. If we spent USD 1.1 trillion on infrastructure in the last ten years (2008-17), we now are going to invest about USD 1.4 trillion in the next five years. A task force has been constituted in the Ministry of Finance that will draw up a National Infrastructure Pipeline for the next five years.

32. We have taken various steps to enhance infrastructure investment by launching innovative financial vehicles such as Infrastructure Debt Funds (**IDFs**), Real Estate Investment Trusts (**REITs**), Infrastructure Investment Trusts (**InvITs**) and laying down a framework for municipal bonds. We are already applying novel Public Private Partnership (**PPP**) models in

the country. We have adopted the **Asset Recycling** model to modernize existing infrastructure like highways while providing government with upfront capital to support new infrastructure.

33. We are also trying to develop **brownfield assets** as a separate asset class for infrastructure investment. Such assets, having passed the stages of land acquisition and environmental and forest clearances, are considerably de-risked and hence, institutional investment from pension, insurance and sovereign wealth funds are forthcoming in such assets. Another initiative is the National Investment and Infrastructure Fund (**NIIF**), which is aimed at channeling investments from both domestic and international sources into infrastructure. India's experience with such innovative modes of funding holds an important example in financing of infrastructure for other developing countries.

Schemes to benefit the common man, especially the poor

34. The rural economy is vital for a country like India, which also depends heavily on agriculture. We have achieved high food grains production but returns in the sector are somewhat subdued due to a dip in agricultural commodity prices globally and depressed food prices domestically. To provide relief by way of income support to the farmers, the Government announced the ***Pradhan Mantri Kisan Samman Nidhi*** (PM-KISAN) this year. Gauging the success of implementation and its benefit potential, the Government has already approved the extension of this scheme to all the eligible farmer families in the country. With 20 million more farmers being covered, nearly 145 million beneficiaries in total will stand covered under this scheme.

35. The Government has also approved the ***Pradhan Mantri Kisan Pension Yojana*** (Prime Minister's Farmers Pension Scheme) for small and marginal farmers of age 18-40 years, who will get a minimum fixed pension of Rs. 3,000 (or about 45 US Dollars) per month on attaining the age of 60 years. The scheme will initially cover 50 million farmers in the first three years of launching of the scheme.

36. We are adopting **Zero Budget Natural Farming** model to promote the use of organic seeds and natural fertilizers by our farmers. This will reduce their expenditure and remove their dependence on credit. Such a step would contribute to our goal of doubling farmers' income by 2022.

37. We have been implementing a **micro irrigation** scheme to enhance water use efficiency in the agriculture sector by promoting appropriate technological interventions like drip and sprinkler irrigation technologies and encouraging farmers to use water-saving and conservation technologies. Micro irrigation would ensure '**Per drop-More crop**'. Water being a precious resource, we are also according high priority to water security. To complete all irrigation projects in the pipeline on time, we launched the '***Pradhan Mantri Krishi Sinchayee Yojana'*** (Prime Minister's Agriculture Irrigation Scheme) with the motto '***Har Khet Ko Paani'*** (water to every farmland).

38. In India, we have actively promoted the use of latest technology in agriculture. For instance, **drone technology** based unmanned aerial vehicle has the ability for smooth scouting over farm fields, gathering precise information and transmitting the data on a real time

basis. The Indian Agricultural Research Institute and others have formulated a research project on **Sensor Based Smart Agriculture**, which envisages the development of indigenous prototype for drone based crop and soil health monitoring system.

39. The Government has laid focused attention on rural infrastructure, on account of which, the urban-rural divide in the country is fast disappearing. Targeted expenditure is aimed at providing urban facilities in villages and improving the quality of life. Under the ***Pradhan Mantri Gram Sadak Yojana*** (Prime Minister's Rural Roads Scheme), construction of rural roads has been taken on a war footing. Over 140,000 out of a total of 158,000 habitations have already been connected with *pucca* (concrete) roads, with work on-going to complete the rest very soon.

40. The **Digital India** programme aims to transform India into a digitally empowered society and knowledge economy. To take care of the digital rural-urban divide, **Bharat Net** is targeting to provide internet connectivity in local bodies at every village in the country. Under the ***Pradhan Mantri Gramin Digital Saksharta Abhiyan*** (Prime Minister's Rural Digital Literacy Mission), over 20 million rural Indians have so far been made digitally literate. These initiatives are already acting as engines of growth and development.

41. Two schemes that have had a huge direct impact on the lives of the common people are ***Prime Minister's Ujjwala Yojana*** that has increased households' access to clean cooking gas through 70 million LPG connections so far, and the ***Saubhagya*** scheme through which almost 100 per cent households in the country have been provided with electricity connections. By providing 1.43 billion LED bulbs with the participation of private sector, annual savings of about USD 7 billion in electricity bills of the poor and middle class families have been achieved. Thanks to efficient implementation of these schemes and outstanding reception by their beneficiaries, access to energy for household consumption no longer remains an issue.

42. We are working towards ensuring ***Har Ghar Jal*** (piped water supply) to all rural households by 2024 under the ***Jal Jeevan Mission***.

43. Our country's future rests on the genius of her people. Our large young population will translate into demographic dividend only if they are endowed with good health, education and skill. We have established a multi-dimensional healthcare system - ***Ayushman Bharat*** - that is far more accessible and affordable than schemes implemented in the past. Under the ***Pradhan Mantri Jan Arogya Yojana*** (Prime Minister's Health Protection Scheme) of Ayushman Bharat, an annual health cover of Rs. 0.5 million is provided to over 107 million families belonging to the poor and vulnerable sections of population. A programme was also initiated to set up 0.15 million **Health and Wellness Centres** (HWCs) by 2022, of which over 17,000 have become functional. We are not only expediting the setting up of these centres, but also equipping them with all modern facilities. Health of our citizens is of utmost importance as good health leads to better productivity in the long run. We have launched the **Fit India Movement** to take our country towards a healthier future.

44. Our youth rightfully aspire for better livelihood opportunities. To enable about 10 million youth to take up industry-relevant skill training, the ***Pradhan Mantri Kaushal Vikas Yojana***

(Prime Minister's Skill Development Scheme) was instituted. This is helping to create a large pool of skilled manpower with speed and high standards.

Financial Inclusion

45. India has taken social infrastructure to the next level through robust government programmes, aided by technology. ***Aadhaar*** or biometric identification has helped beneficiaries access their rights without leakages from the system. The ***Jan Dhan Yojana*** has brought the unbanked population into the fold of formal banking system through the opening of bank accounts. Under the **Direct Benefit Transfer** (DBT) mechanism, subsidies are transferred directly to the bank accounts of beneficiaries. This has reduced delays and pilferages, and improved transparency. The DBT today has over 430 schemes of the Central Government under its ambit. In the context of the digital revolution ushering in good governance in the country, more than 0.3 million Common Service Centres (CSCs) employing about 1.2 million people are digitally delivering various services to the citizens. These CSCs are not only expanding their services but also creating digital infrastructure in the villages, including connectivity, to convert these villages into Digital Villages.

46. The mobile telephony penetration has helped empower rural India to leverage digital technology for financial access. The retail payment systems powered by Universal payment Interface (UPI) work seamlessly 24 hours X 365 days in India. India has 560 million internet users, which is the second highest in the world. India also has 1.2 billion mobile phones in use, which is again the second highest. Building on the high penetration of internet and mobile use in the country, we have taken the forward leap to develop India into a digitally active economy. We are promoting the use of **e-payment gateways**, which are more efficient means of transactions. To achieve a cashless society, **RuPay** has been conceived to offer a domestic, open-loop, multilateral system, which will allow all Indian banks and financial institutions in India to participate in electronic payments. The **BHIM App** is also playing an important role in promoting digital transactions. Through the **UMANG App**, more than 100 public services have been made available using the mobile phone. The **Unified Payments Interface** (UPI) is an instant real-time payment system developed by the National Payments Corporation of India to facilitate inter-bank transactions. It is fast catching up with a monthly volume of 800 million transactions valued at Rs. 1.4 trillion or USD 20 billion. This has helped in spreading the use of cashless transactions in the country ushering in an era of digitalization at the ground level.

C. SRI LANKA

47. The Sri Lankan economy, which recorded a growth of 3.7 per cent in the first quarter of 2019, experienced a sharp setback in its growth performance in the second quarter of the year, impacted by the Easter Sunday terrorist attacks in April 2019, which killed and wounded hundreds of civilians, including tourists. Consequently, economic growth in the second quarter was limited to 1.6 per cent, resulting in a modest growth of 2.6 per cent, in real terms, during the first half of 2019, compared to 3.9 per cent growth recorded during the corresponding period of the previous year. Nevertheless, growth during the first half of the year was supported by all three major economic activities, namely, Services, Industry and Agriculture. The growth in Services activities was mainly supported by the expansion in financial services and

wholesale and retail activities. However, the growth in accommodation, food and beverages services activities was adversely affected by the Easter Sunday attacks. Growth in Industry activities was largely supported by the recovery in the construction and mining sectors, and the continuous growth in manufacturing activities. The recovery in the production of rice and oleaginous fruits aided the growth in Agricultural activities. The economy is envisaged to regain its growth momentum gradually in the medium term with the implementation of pro-growth policies and ongoing structural reforms aimed at enhancing trade and investment, supported by stabilization measures adopted by the authorities in the past few years. Accordingly, the Sri Lankan economy, which is projected to grow by around 3.0 per cent in 2019, is expected to move towards its potential over the medium term.

48. Headline inflation broadly remained in or below the desired mid-single digit levels during the first nine months of 2019 reflecting muted demand pressures, amidst some volatility that emanated from food inflation. Meanwhile, core inflation, which experienced a one-off increase in January 2019 mainly due to adjustment in house rentals after a lapse of several years, is expected to remain elevated until the beginning of 2020. The Colombo Consumer Price Index (CCPI) based headline and core inflation was at 5.0 per cent and 5.6 per cent, respectively, on a year-on-year basis in September 2019, while the National Consumer Price Index (NCPI) was at 3.4 per cent and 5.9 per cent respectively, on a year-on-year basis in August 2019.

49. The Central Bank reduced the Statutory Reserve Ratio (SRR) applicable on all rupee deposit liabilities of commercial banks by 2.50 percentage points, in total, in November 2018 and March 2019 to ease the market liquidity conditions. These measures helped the domestic money market to record surplus liquidity. Nevertheless, market interest rates, in both nominal and real terms, remained elevated. Against this backdrop, the Central Bank provided forward guidance to the market on possible future reduction in policy interest rates in April 2019. Thereafter, capitalising on muted inflationary pressures, decelerating monetary growth, a relatively stable external sector and the increasingly accommodative global monetary policy stance, the Central Bank relaxed monetary policy by reducing policy interest rates, namely the Standing Deposit Facility Rate (SDFR) and the Standing Lending Facility Rate (SLFR) by 50 basis points to 7.50 per cent and 8.50 per cent, respectively, by end May 2019. Considering the available monetary policy space to support productive economic activity, the Central Bank further reduced the SDFR and the SLFR by 50 basis points to 7.00 per cent and 8.00 per cent in August 2019, respectively. Further, the Central Bank imposed interest rate caps during the year to expedite the monetary policy transmission mechanism and revive economic activity amidst rigid market lending rates. Meanwhile, the Central Bank has made substantial progress in the institutionalization of key reforms with initiatives taken to introduce necessary legislative changes for a smooth transition to a full-fledged flexible inflation targeting framework by 2020.

50. Impacted by the Easter Sunday attacks, uncertainties caused by political developments, and subdued economic activity as a result of stabilization measures taken in the previous year, the fiscal performance remained weak during the first seven months of 2019. Lower than expected government revenue and a rise in government expenditure, resulted in an expansion of the budget deficit. Policy measures imposed to curtail the surge in import of personal vehicles, deceleration in economic activity following the Easter Sunday attacks and the delay in the implementation of certain revenue proposals announced in the Budget 2019 largely

contributed to the subdued revenue performance. Government expenditure increased during the first seven months of 2019 owing to higher recurrent and capital expenditure, particularly the rise in expenditure on interest payments, and subsidies and transfers. Hence, fiscal performance is likely to deviate in 2019 from the original estimates. However, the government is committed to return to the envisaged fiscal consolidation path in the medium term assisted by revenue enhancement measures, including the newly enacted Inland Revenue Act and other administrative reforms. Further, the government is expected to strengthen the framework for fiscal rules in the near term with a view to enhancing fiscal discipline while taking measures to accomplish structural reforms envisaged under the IMF-EFF programme. The enactment of the Active Liability Management Act (ALMA) and the implementation of the Medium-Term Debt Management Strategy (MTDS) would facilitate debt management, while reducing the level of debt to a sustainable level over the medium term.

51. Sri Lanka's external sector strengthened during 2019, supported by decisive measures to address vulnerabilities experienced in 2018. The trade deficit contracted significantly in the first half of 2019, due to a significant reduction in import expenditure and a growth in export earnings. Despite the improvement in the trade deficit, the impact on earnings from tourism, following the Easter Sunday attacks, and the moderation of workers' remittances resulted in the current account recording a marginal deficit in the first half of 2019. In particular, the Easter Sunday attacks are projected to cause a reduction in earnings from tourism from the originally envisaged US dollars 5 billion to US dollars 3.7 billion in 2019. The financial account of the Balance of Payments (BOP) recorded significant inflows due to successful issuances of International Sovereign Bonds (ISBs) on two occasions so far in 2019 amounting to US dollars 4.4 billion. Meanwhile, the government repaid two maturing ISBs amounting to US dollars 1.5 billion in the first half of 2019. Other flows to the financial account remained moderate owing to lower than expected Foreign Direct Investments (FDI) and foreign investments in the Colombo Stock Exchange (CSE), while foreign investment in the government securities market recorded a net outflow during the first half of 2019. The proceeds from the ISB issuances in 2019 and other inflows increased the gross official reserves, strengthening external sector resilience in 2019. The Sri Lankan rupee, which recorded a significant depreciation in 2018, remains appreciated so far in 2019 mainly benefiting from the contraction in import expenditure and other inflows to the domestic foreign currency market. The improved liquidity conditions in the domestic foreign exchange market permitted the Central Bank to purchase foreign exchange on a net basis to build up gross official reserves so far during 2019.

52. The performance of the financial sector remained subdued during 2019 in the backdrop of sluggish economic growth. Slow growth in credit due to dampened investor sentiments stemming from political uncertainties and the Easter Sunday attacks, as well as stabilization measures, added some stress on financial institutions, particularly in the non-bank sector. Banking sector assets continued to expand, albeit at a slower pace, while deposits continued to be the main source of funding. The banking sector continued to comply with enhanced capital requirements under Basel III and reported a strong liquidity position and maintained other prudential ratios at satisfactory levels. Longstanding issues with a few weak non-bank financial institutions are being resolved with the support of the stronger resolution and enforcement framework that has been introduced for this purpose.

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