International Monetary and Financial Committee

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Statement by Mr. Jaitley
India

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

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(Representing the Constituency consisting of Bangladesh, Bhutan, India and Sri Lanka)

to the International Monetary and Financial Committee

April 22, 2017

Mr. Chairman,

1. Since we met in October 2016, global economic outlook has changed for the better with some silver linings finally emerging. This momentum in global growth is expected to strengthen in 2017 based on gradual improvement in economic conditions in Advanced Economies (AEs), particularly the US, as well as due to the pick-up in growth in some large Emerging Markets (EMs). However, the confidence in global recovery remains weak owing to the risks associated with the future course of economic policies and monetary policy stance of AEs; resurgence of commodity price pressures; and the increasing recourse to protectionism.

2. In these circumstances, it is imperative to fortify efforts to support global recovery by committing ourselves to growth friendly policies and ensuring free and fair trade practices as called for by G-20 leaders at the Hangzhou Summit in September last year. Advanced economies have an important role in stimulating global demand with supportive fiscal and monetary policies and eschewing protectionism.

3. Emerging Market and Developing Economies (EMDEs) are vulnerable to external shocks and must take ample precaution to safeguard ongoing economic recovery. Structural reforms and building buffers constitute the keystones of policy agenda in EMDEs that would ensure sustained growth. Improving the flexibility of labor markets and increasing competition in factor and product markets along with incentives for skill building and innovations are important structural efforts required for boosting productivity and potential growth.

The Role of IMF – Architecture of Global Cooperation

4. The emerging risks to the global economy call for enhanced surveillance by the IMF. The IMF needs to be sufficiently resourced to be able to fully discharge this responsibility. It also needs to function as a quota based institution. Given that there is broad agreement on maintaining the current overall lending capacity of the Fund and that the Fund's existing resource pool is excessively tilted toward borrowed resources, there is a dire need for increasing quotas. Recent work by the Fund also points to the need for realigning quota shares to reflect the changed economic realities. All these must be achieved as part of the 15^{th}General Review of Quotas. We are disappointed that the deadline for completing the 15^{th} GRQ has been pushed back to no later than the 2019 Annual Meetings. Any further delay in the 15^{th} GRQ will erode Fund's legitimacy and credibility, and will be against the spirit of the Articles of Agreement. I do hope that the deadlines now set will be honored and adhered to.

5. We look forward to further work on reforming IMF's toolkit for improving its effectiveness. We fully support any reform of the IMF lending toolkit which better addresses the needs of the EMDEs. We also encourage the Fund to continue working on addressing gaps in the Global Financial Safety Net (GFSN), including improved integration of the different layers of the GFSN for the purpose of establishing a credible crisis prevention mechanism. The IMF should play proactive role by productive engagement with Regional Financing Arrangements (RFAs) by way of sharing information and joint mechanisms for surveillance and policy signaling to build confidence among creditors. Moreover, co-financing arrangements between the IMF and regional financing element(s) would help in mitigating stigma and delay in program financing. We also support IMF's work on prequalified state-dependent lending tools for swift and reliable provision of liquidity for member countries for the full duration of external shocks faced by them.

6. We welcome IMF's role in fostering multilaterally consistent macroeconomic re-balancing and improving the analytical coverage of spillovers from domestic policies to the global economy.

7. In view of the adverse implications of mounting protectionist pressures on global recovery, I call upon the IMF to lend its strong and unambiguous voice in support of free trade and raise awareness about the benefits of rule-based open multilateral trading frameworks.

Developments in the Constituency

Bangladesh

8. Bangladesh has demonstrated resilience amidst global headwinds and domestic challenges. The preliminary estimate of real GDP growth is 7.1 percent in 2015-16 (ending in June 2016) and 7.2 percent in 2016-17. Headline inflation eased further in 2015-16, with annual average CPI inflation reaching 5.9 percent in June 2016, compared to 6.4 percent in June 2015. In 2016-17 so far, inflation has further moderated to 5.4 percent in February 2017 – a five-year low and well within the 2016-17 ceiling of 5.8 percent.

9. Monetary policy stance will continue to remain prudent, and the authorities remain vigilant against upside risks to inflation. Excess liquidity in the banking system has been declining in recent months, as credit growth has picked up. Both food and non-food CPI inflation has moderated, aided by favorable agricultural production, modest rise in global commodity prices, and growth-focused yet cautious monetary policy stance. Projected rise in global commodity prices in 2017, however, may exert some upward pressure on domestic prices.

10. On the external front, the current account balance recorded a small deficit of US$ 1.12 billion during July 2016 -February 2017 as against a surplus of US$ 2.3 billion during the corresponding period in 2015-16 on account of strong import growth (10.15 percent) coupled with a moderate growth in exports (3.31 percent during July-February) and a slowdown in remittance inflows. The recent decline in remittance reflects a combination of global and local factors, but mainly driven by weaker economic activity in the Middle East, which is expected

to recover as oil prices stabilize and manpower exports from Bangladesh increase. Besides, Bangladesh Bank has taken some measures to reduce costs of sending remittance through the formal channels. Bangladesh Bank projects the 2016-17 overall balance surplus at US$ 2.9 billion, which would help the coverage to remain around 7-8 months of prospective imports of goods and services in 2016-17. Despite some moderation, garment exports growth has held up well relative to peers.

11. Fiscal deficit (excluding grants) in 2016-17 is expected to remain broadly unchanged at around 5.0 percent. The increase reflects mainly the increase in public sector wages. Budget financing was mainly done through National Savings Certificates (NSCs). Gross investment as percent of GDP has risen in 2015-16 to 29.7 percent but is expected to be around 28.0 percent in 2016-17. Subsidies as a share of GDP have come down, helped in part by a lower fuel subsidy. With the rolling out of VAT from July 1, 2017, the scope to increase revenue will increase along with improvement in compliance and reduction in tax evasion across the board, and serve as a key building block for future tax policy reforms.

12. In the banking sector, financial stability continues to receive a high priority with intensive monitoring of banks remaining within the statutory limits on their capital market exposures. To improve corporate governance, Bangladesh Bank is further strengthening its supervisory scrutiny, including by IT-based online supervision tools and placement of observers inbanks with governance challenges.

13. The government's reform initiatives to improve the business climate and ease infrastructure bottlenecks, including by developing special economic zones, should help crowd in both private domestic and foreign direct investments that can create more jobs, raise productivity, and potential growth. To undertake the increases in public investment and social spending, so as to boost growth and poverty reduction, while keeping fiscal policy sustainable, the government is committed to boosting revenue and fully implement the VAT by 2017-18.

Bhutan

14. The year 2015-16 saw an acceleration in growth to 6.2 percent from 6.1 percent in 2014-15 and 4 percent in 2013/2014. As in the previous year, the acceleration of growth was mainly driven by a pick-up in services, mining and hydropower-related construction. 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.

15. Consumer price inflation fell further to 3.3 percent in 2015-2016 from 5.2 percent in 2014-15. On account of a gradual pick-up in capital spending, the 2015-2016 fiscal deficit was 1.3 percent of GDP, in contrast to the fiscal surplus of 1.5 percent of GDP in 2014-2015. In 2016-17, because of further acceleration in capital expenditures toward the end of the 11th Five Year Plan, the deficit is projected to reach 5 percent of GDP.

16. The 2015-16 current account deficit increased by about one percent of GDP to 29.1 percent of GDP. The large deficit in 2015/16 and previous years is a result of the imports for the construction of hydropower projects. It is expected to decline after 2017-18 with the

commissioning of new power plants and the resultant export of power. In the longer run, the current account balance is likely to return a surplus.

17. Credit growth picked up to 14 percent in 2015 and has approached 17.4 percent by the end of 2016.

India

18. India continues to be the fastest growing major economy in the world. As per provisional estimates, real GDP grew by 7.9 percent in 2015-16 compared with 7.2 per cent in 2014-15. The second advance estimate for GDP growth for 2016-17 is placed at 7.1 percent. The currency reform initiative will move the Indian economy to a less cash trajectory, increase tax compliance and reduce the threats from counterfeit currency which acts as a source of terror funding. Growth is expected to gain strength in the following years due to externalities derived from deep structural reforms implemented by our Government and robust aggregate demand.

19. CPI inflation which has been easing since August 2016 increased modestly to 3.65 percent in February2017 against 3.17 percent in January 2017.Though it has marginally risen to 3.81 percent in March, 2017, it is well within the medium term CPI inflation target of 4 percent.

20. At the system level, our banks are adequately capitalized. At the same time, we are deeply aware of the problem of non-performing loans (NPLs) which are in the process of being effectively resolved. Policies for resolution of NPLs including optimal structuring of credit facilities, change in ownership/management, deep restructuring of stressed assets and facilitation of speedy exit from unviable accounts have been put in place. Additionally, the amendments to debt recovery laws as well as the enactment of Insolvency and Bankruptcy Code 2016 would provide enabling infrastructure to deal effectively with the recovery of NPLs in a time bound manner.

21. The Government is infusing capital in Public Sector Banks (PSBs) to meet their capital requirements in line with global risk norms and to spur credit growth. Recent announcements made by our Prime Minister for the provision of cost effective credit to farmers and housing loans to the poor including enhanced access of credit for MSMEs would enlarge the scope of institutional credit delivery to the hitherto under-banked segments of the economy.

22. The progress of our financial inclusion efforts has been remarkable with 282 million accounts opened by banks under the no-frills PMJDY so far. The objective of the scheme is to provide all households in the country with financial services, with special focus on empowering the weaker sections of society, including women, small and marginal farmers and laborers, both rural and urban. Attractive low cost life and health insurance and pension plans introduced by the Government have expanded the social safety net for weaker sections of the society. Micro Units Development and Refinance Agency (MUDRA) is active in facilitating structured microcredit deliveries to small scale entrepreneurs for productive activities. Supported by AADHAR, the biometric based unique identity system for individuals, the ongoing rapid expansion of digital payment mechanisms will provide large push to our financial inclusion efforts.

23. The wide ranging liberalisation of the FDI policy in recent years is expected to provide major impetus to employment and job creation. Most of the sectors, except a small negative list, are now under the automatic approval route. India is now the most open economy in the world for FDI. Net FDI inflows during April-February 2016-17 increased to US $ 35.25 billion from US $ 34.49 billion during the same period in the previous year. The increasing strength of economic fundamentals has made India the most sought after destination for investments.

24. India's foreign exchange reserves were placed at US $ 368.99 billion as of April 7, 2017. The Current Account Deficit (CAD) was very much at sustainable level of 1.3 percent and 1.1 percent in 2014-15 and 2015-16, respectively. The CA deficit for the three quarters of 2016-17 improved further to 0.7 percent of GDP.

25. As envisaged, the Gross Fiscal Deficit (GFD) was contained at 3.5 percent in 2016-17 following a steady path of fiscal consolidation without compromising on the public investment requirements of the economy and spending on programs for poverty alleviation. The quality of fiscal adjustment is reflected in the improvement in revenue deficit to 2.1 percent in the revised budgetary estimate vis-à-vis 2.5 percent in 2015-16. Next year the revenue deficit will be reduced further to 1.9 percent to below 2 percent mandated by the FRBM Act. The GFD for the year 2017-18 is pegged at 3.2 percent with a commitment to achieve 3 percent in the following year. The steady approach towards fiscal consolidation is being judiciously adopted to avoid excessive curtailment of public investment- in view of the need for higher public expenditure in the context of sluggish private sector investment and subdued global growth.

26. For the current financial year, the Union Budget 2017-18 has significantly increased resource allocation for infrastructure as well as rural, agricultural and allied sectors. The allocation for the rural employment guarantee scheme has also been increased substantially. The government would continue to increase fiscal resilience through greater focus on the quality of expenditure and higher tax realizations including those that would accrue from large cash deposits made in banks due to demonetization. The Budget for 2017-18 shows our firm resolve to boost investment in agriculture, social sector, infrastructure and employment generation on the one hand and simultaneously pursue the path of fiscal consolidation on the other. The delivery of AADHAAR based direct benefit transfers (DBT) has succeeded in plugging unwarranted leakages resulting in substantial savings to the Government. We are also fully on course to implement the Goods & Service Tax (GST) by July 1, 2017. The GST will deliver significant externalities by way of improved taxation efficiency and the ease of doing business and will convert India into one common market.

27. Since 2014, we have taken efforts to implement deep structural reforms to unlock the full potential of our economy. Widely encompassing reforms have been put in place which, inter alia, include the Goods and Services Tax Act, AADHAAR (Targeted Delivery of Financial and Other Subsidies, Benefits and Services) Act 2016, rationalization of subsidies, enactment of Insolvency and Bankruptcy Code 2016 and operationalization of National Company Law Tribunal (NCLT) and National Company Law Appellate Tribunal (NCLAT) for the new corporate insolvency framework. Other policy initiatives include implementation of the hybrid annuity model for PPP, passage of Mines and Mineral Amendment Act, announcement of National Capital Goods Policy, directions to PSEs for expediting arbitration in construction sector, roadmap for rapid adoption of digital payments system, extensive

liberalization of the FDI regime and improvements in governance processes in infrastructure delivery. Alongside steady progress in India's ranking in Ease of Doing Business, the Government's flagship program 'Make in India' encourages new processes, new infrastructure, new sectors and new mindset to boost entrepreneurial energy. Affirmative policies to arrest declining Child Sex Ratio (CSR) and empowerment of women over the life-cycle continuum and those for enhancing female employment are being vigorously pursued.

Sri Lanka

28. The Sri Lankan economy grew by 4.4 per cent in 2016 compared with 4.8 per cent growth in 2015. During the year, the highest growth of 6.7 per cent was recorded in the industrial sector supported by the increase in construction related activities. Meanwhile, the services sector grew by 4.2 per cent with the expansion of financial services, insurance, and telecommunications. However, agriculture related activities contracted by 4.2 per cent impacted by supply side disruptions due to floods in the second quarter and drought conditions during the final quarter of 2016. GDP is projected to grow by around 5.5 per cent in 2017.

29. Inflation as measured by National Consumer Price Index remained at 4.2 per cent at end 2016. However, it showed an upward trend recording 8.2 per cent in February 2017 which was largely due to the impact of prevailing drought conditions and adjustments to the tax structure. Despite the monetary policy tightening in 2016, the decline in monetary and credit aggregates was slower than expected. The Central Bank of Sri Lanka having considered these developments, further increased its policy interest rates by 25 basis points in March 2017, to contain the buildup of adverse inflation expectations and the possible acceleration of demand side inflationary pressures through excessive monetary and credit expansion. The fiscal deficit of the government was reduced to 5.4 per cent of GDP in 2016, from a deficit of 7 per cent in 2015 through a bolstering of tax revenues and containing recurrent and capital expenditure. Accordingly, the fiscal sector performance was largely on track for the IMF's 3-year extended arrangement under the Extended Fund Facility (EFF) of USD 1.5 billion which was entered in to in 2016.

30. On the external front, deficit in the trade account of the balance of payments (BOP) increased with expenditure on imports increasing and earnings from exports declining in 2016. The declines in export commodity prices, particularly tea and rubber prices as well as low external demand for export commodities lowered the earnings from exports. Earnings from tourism and workers' remittances continued to cushion the adverse impact of trade deficit on the BOP. In the meantime, outflows of foreign investments from the government securities market which was observed in late 2016 and early 2017 appear to have subsided by March 2017. In fact, marginal inflows have been experienced despite the increase in policy interest rates in the United States. The government could raise US$ 2,150 million through issuance of international sovereign bonds during the year. Nevertheless, the overall BOP is estimated to have recorded a deficit of US$ 500 million in 2016. Meanwhile, gross official reserves were estimated at US$ 6.0 billion by end December 2016, which is equivalent to 3.7 months of imports. The rupee, which depreciated against the US dollar by 3.8 per cent in 2016, recorded a further depreciation of 1.1 per cent by end March 2017. The financial sector stability and

soundness improved, supported by adequate capital and liquidity levels and contained non-performing loan ratios.