



India Economic Outlook

2014 Article IV Report

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ICRIER, New Delhi
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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

2014 Report posted to
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February 20

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

Possible deflation in advanced economies

Weak domestic demand in emerging markets

Stagnation in euro area

Capital flow volatility to some emerging markets

RISKS

GROWTH

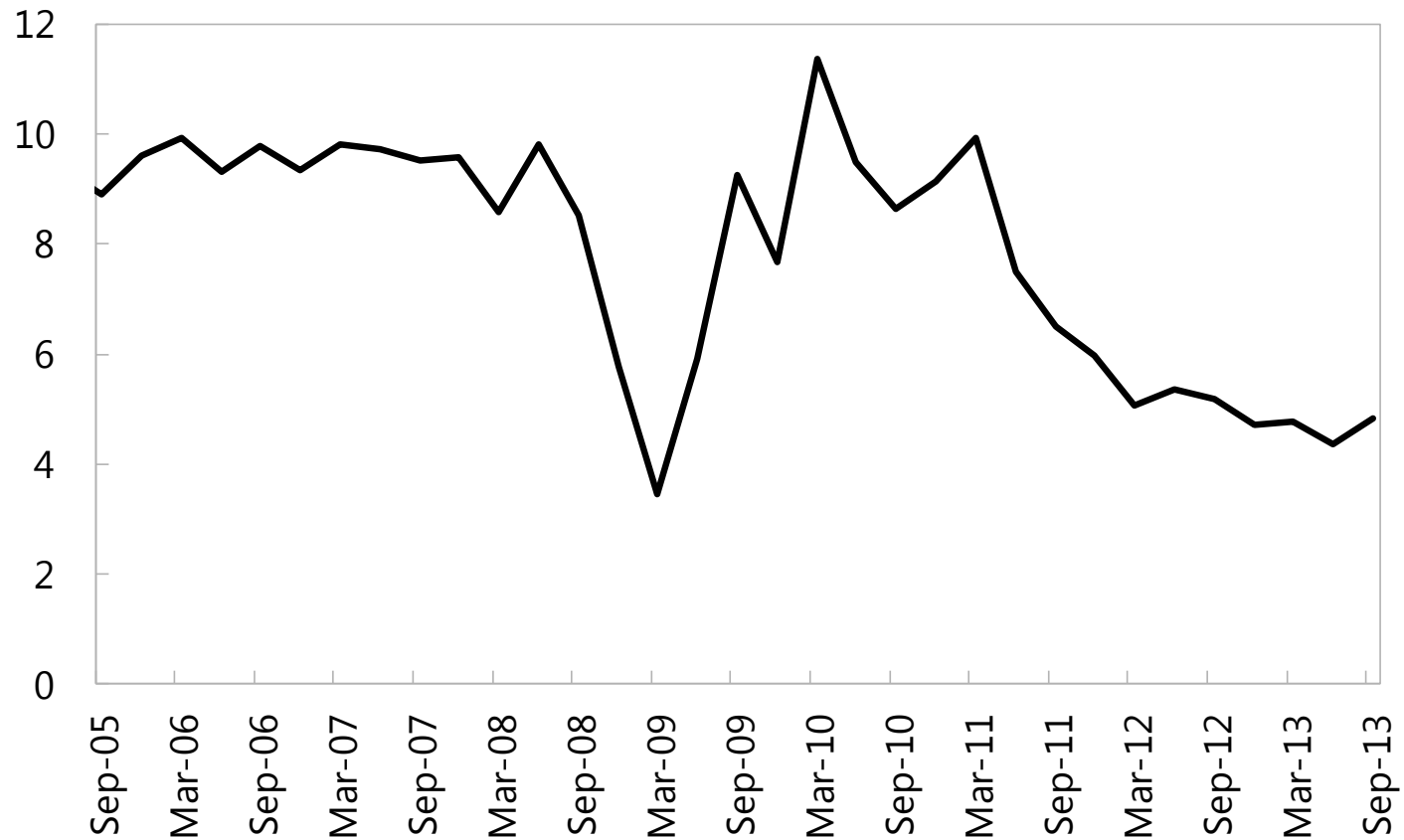


World Advanced Emerging Markets & Developing

India: Growth and inflation

GDP Growth

(In percent, yoy)

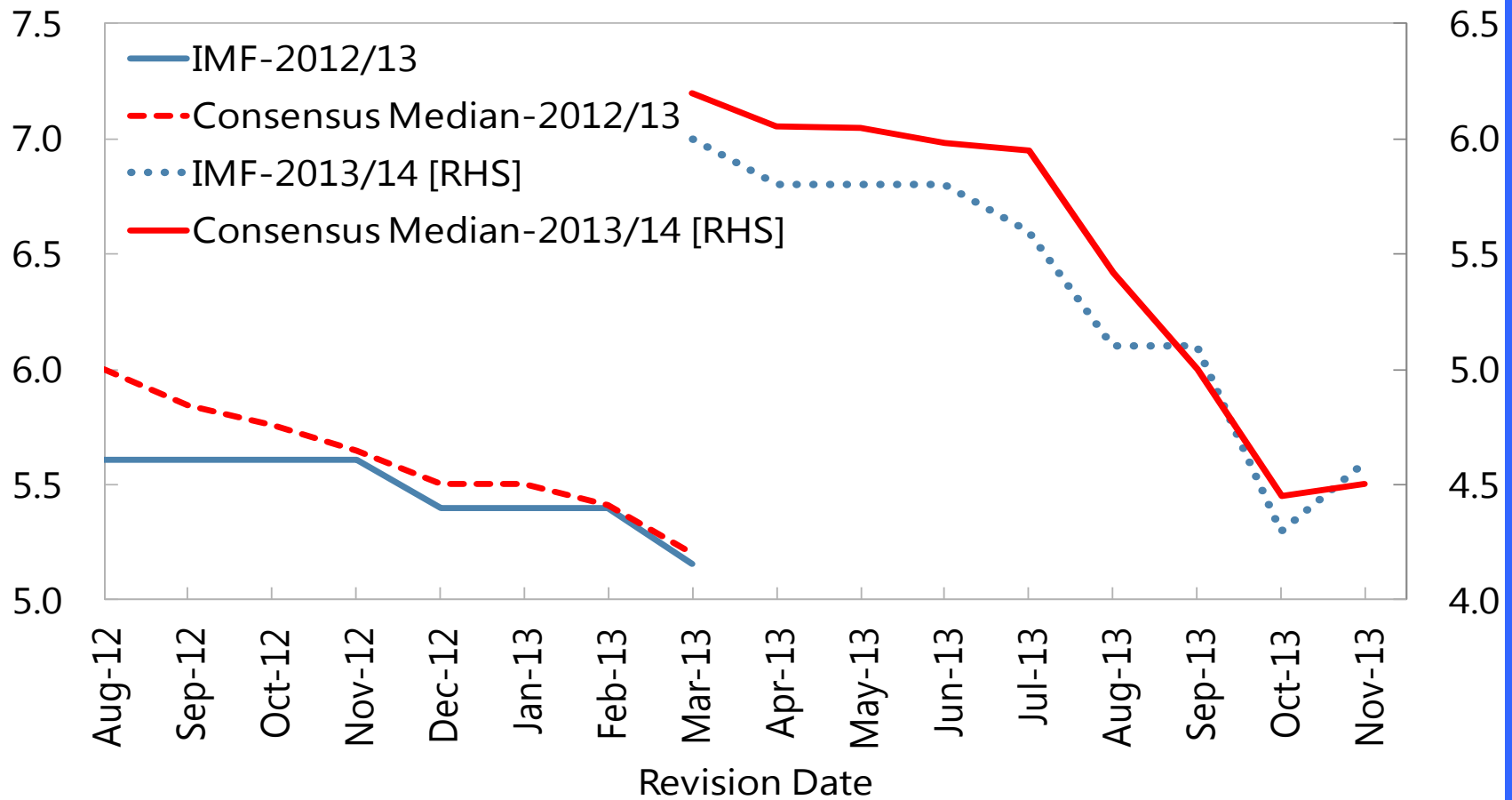


Sources: CEIC and IMF staff calculations.

We've all been too optimistic for India

India: Growth Forecast Revisions

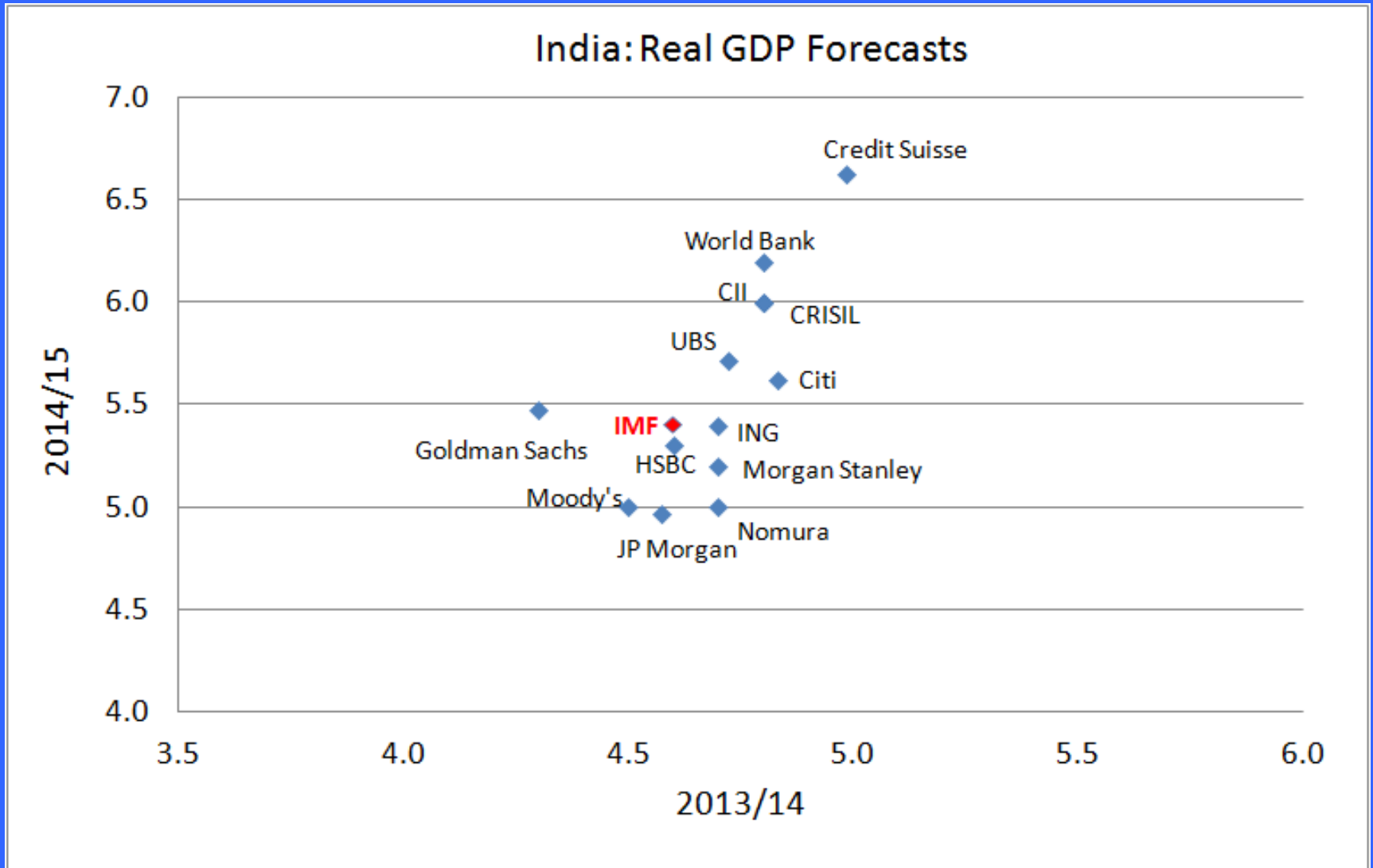
(In percent)



Sources: IMF; and Consensus Economics.

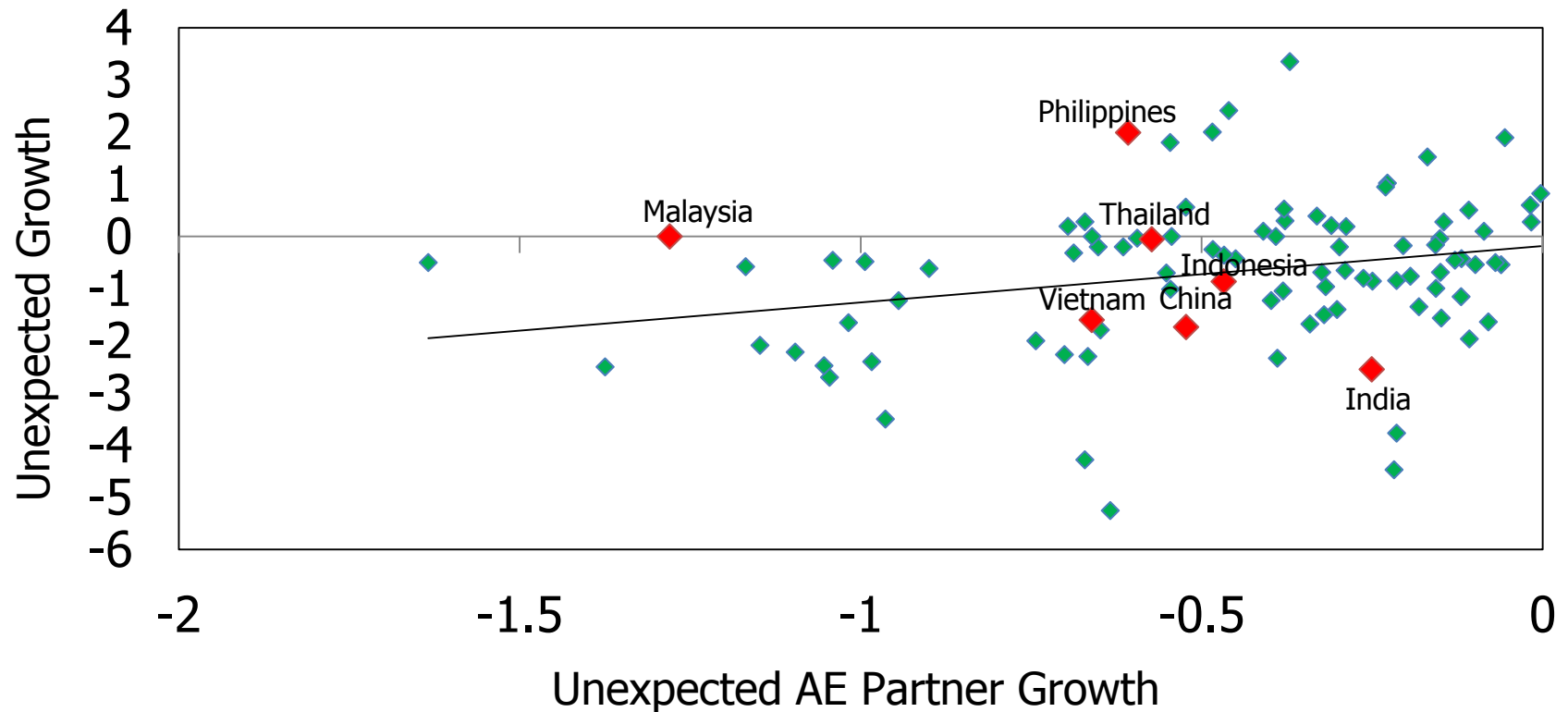
Have we hit bottom yet?

(Consensus: 4.7% in 2013/14 and about 5.5% in 2014/15)



There is a domestic component to India's slowdown

Spillovers from Advanced Economies



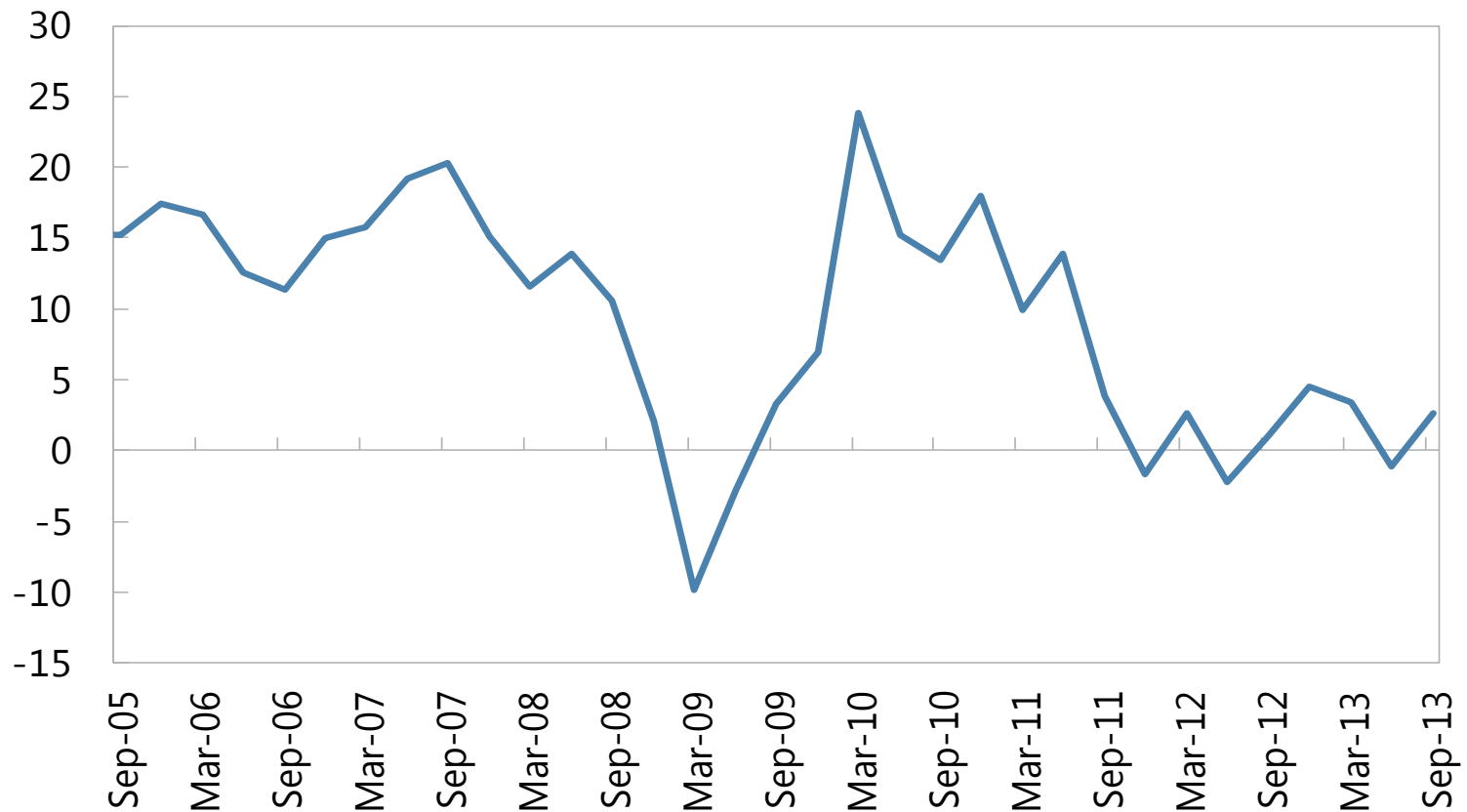
Sources: IMF, *World Economic Outlook*, and IMF staff calculations.

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 ...

Gross Fixed Capital Formation, Real

(yoy percent change)

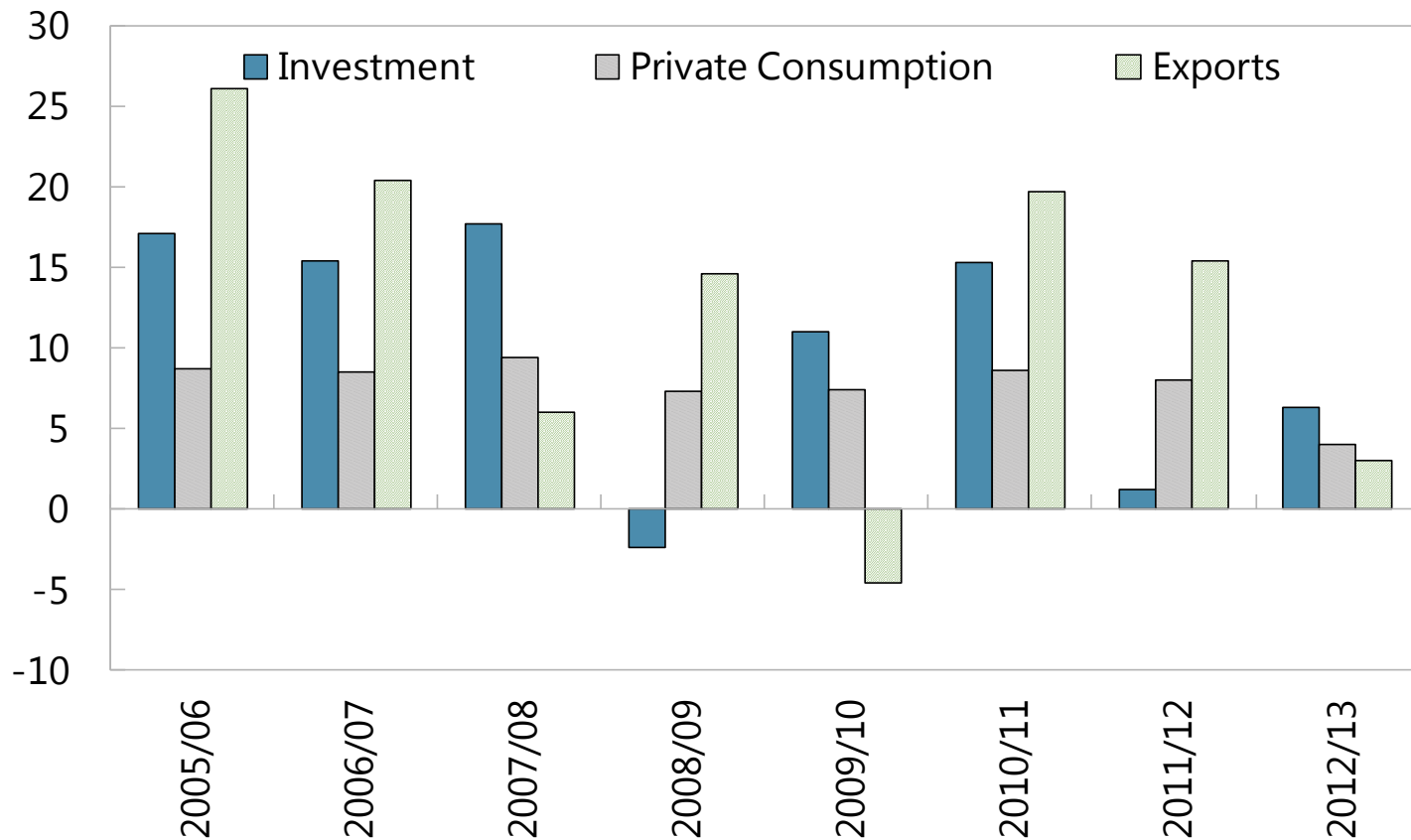


Source: Haver Analytics.

... but the slowdown has become broad-based, ...

Demand Components of GDP

(In percent, yoy)

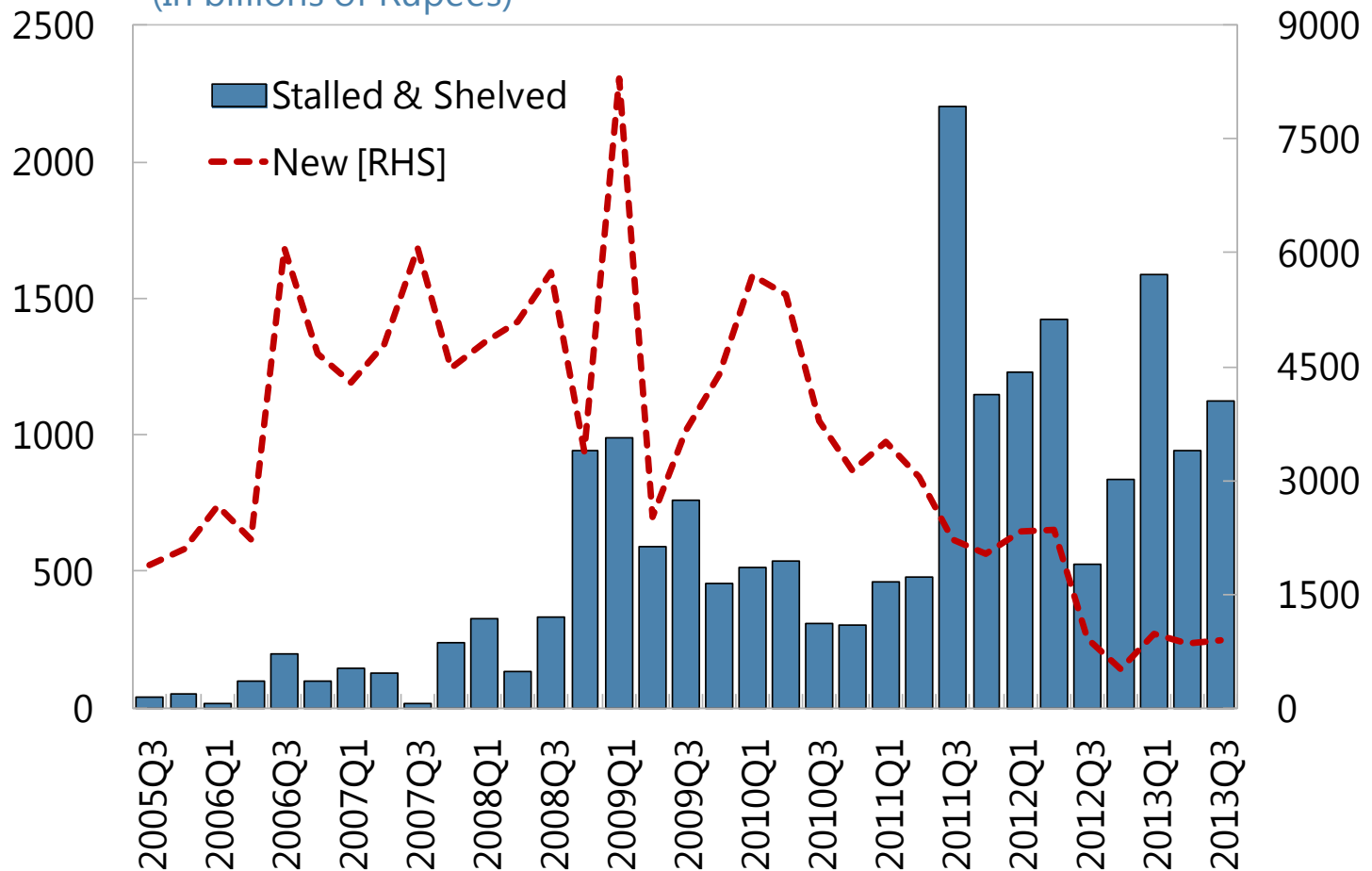


Sources: CEIC and IMF staff calculations.

... and the investment pipeline remains thin

Investment

(In billions of Rupees)

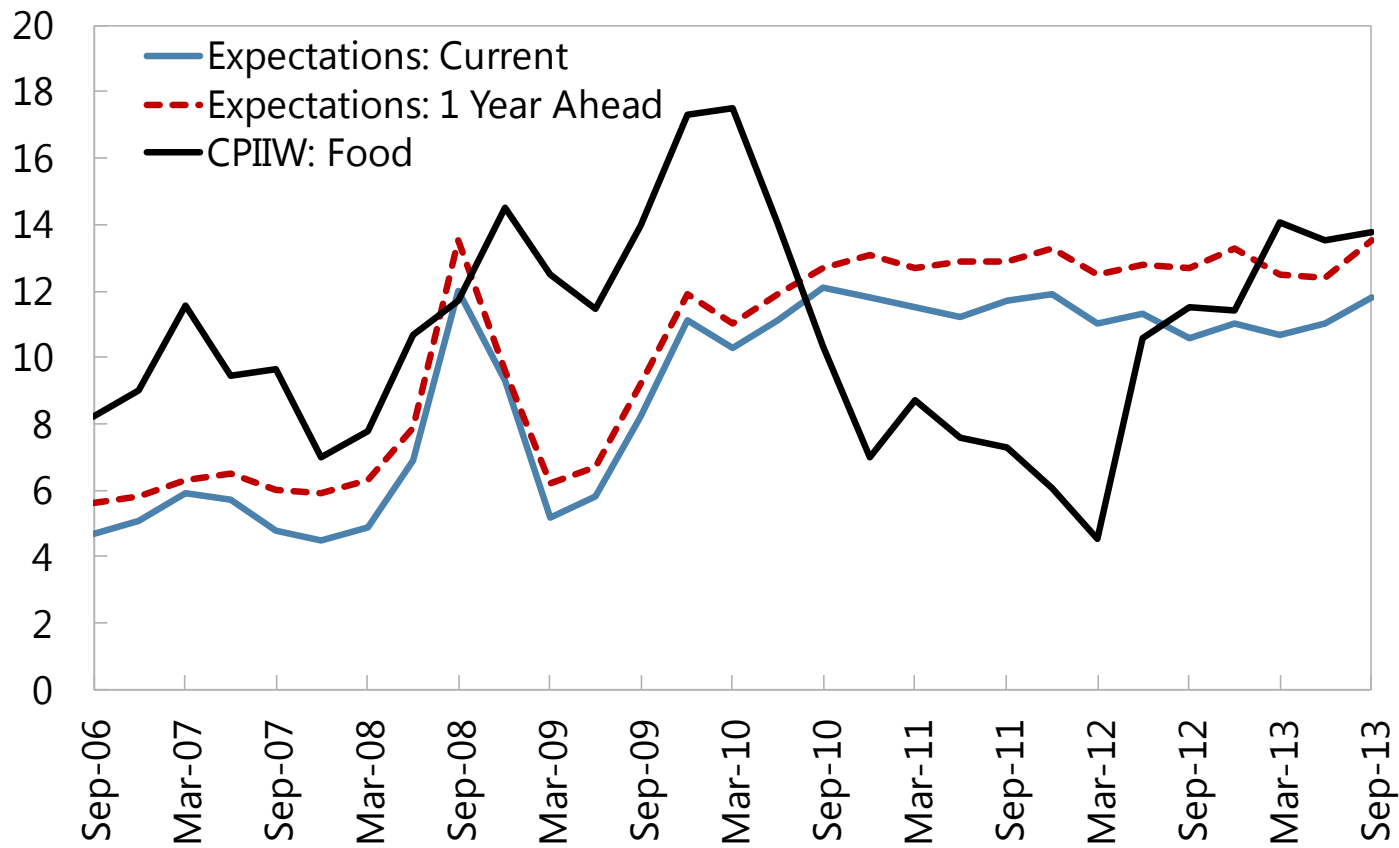


Sources: CAPEX and IMF staff calculations.

Inflation is too high (and it has become stuck in expectations)

Household Inflation Expectations and Food Inflation

(In percent)

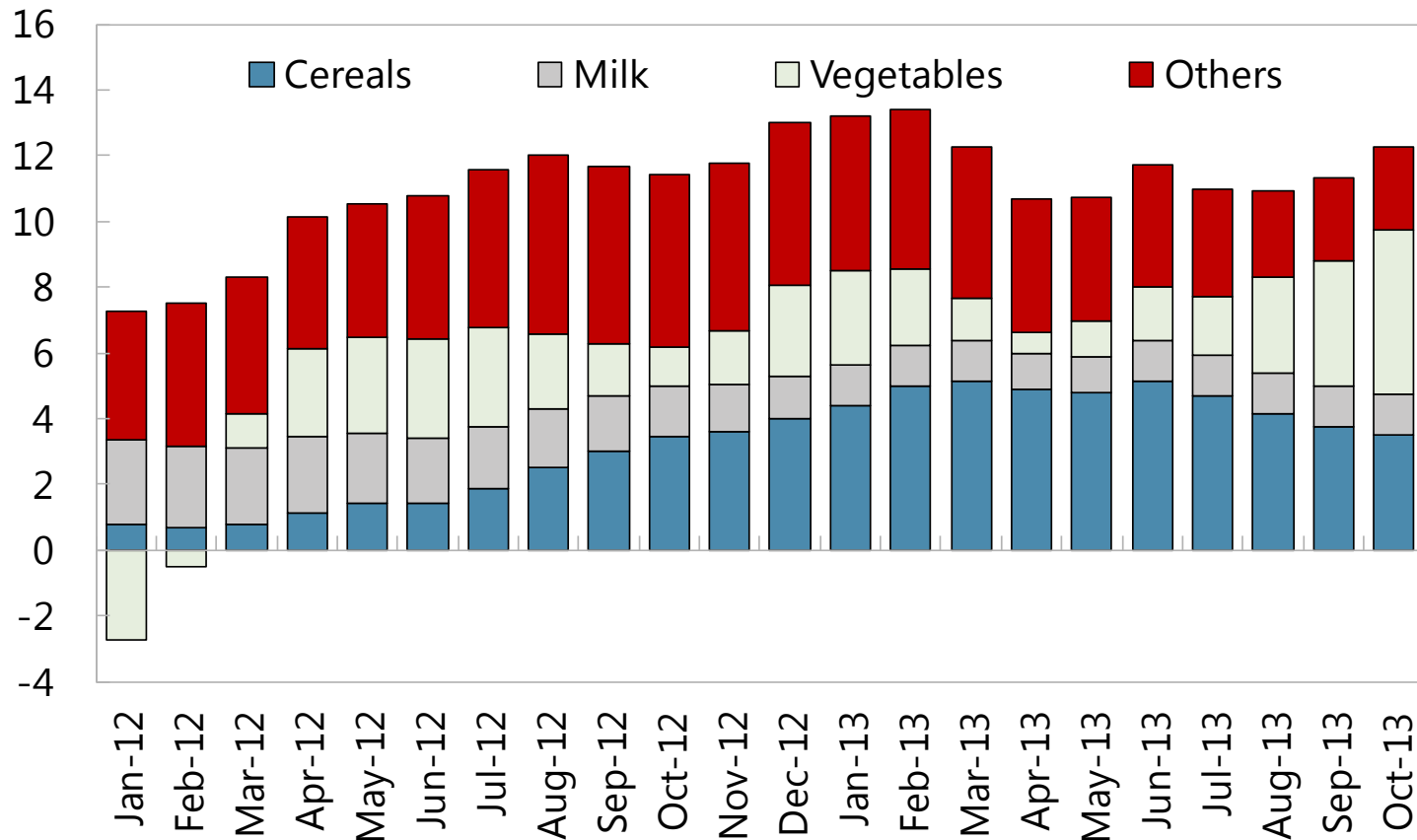


Sources: CEIC, Haver Analytics and IMF staff calculations.

Food inflation is certainly part of the story

CPI Food Inflation: Contributions

(In percent, yoy)



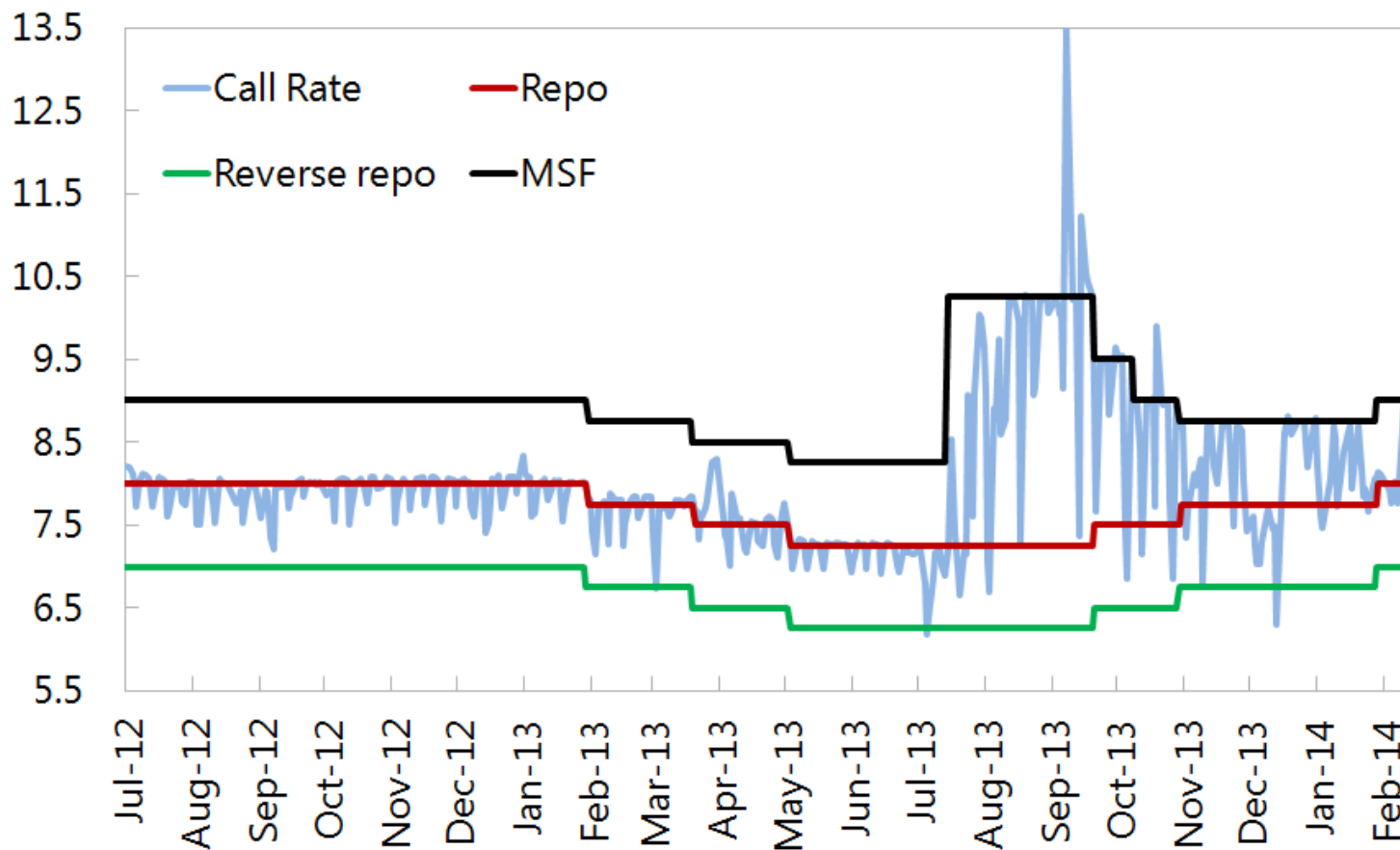
Sources: CEIC and IMF staff calculations.

Role of monetary policy?

Normalization since September, but real policy rate still very low

India: Policy and Call Market Interest Rates

(In percent)

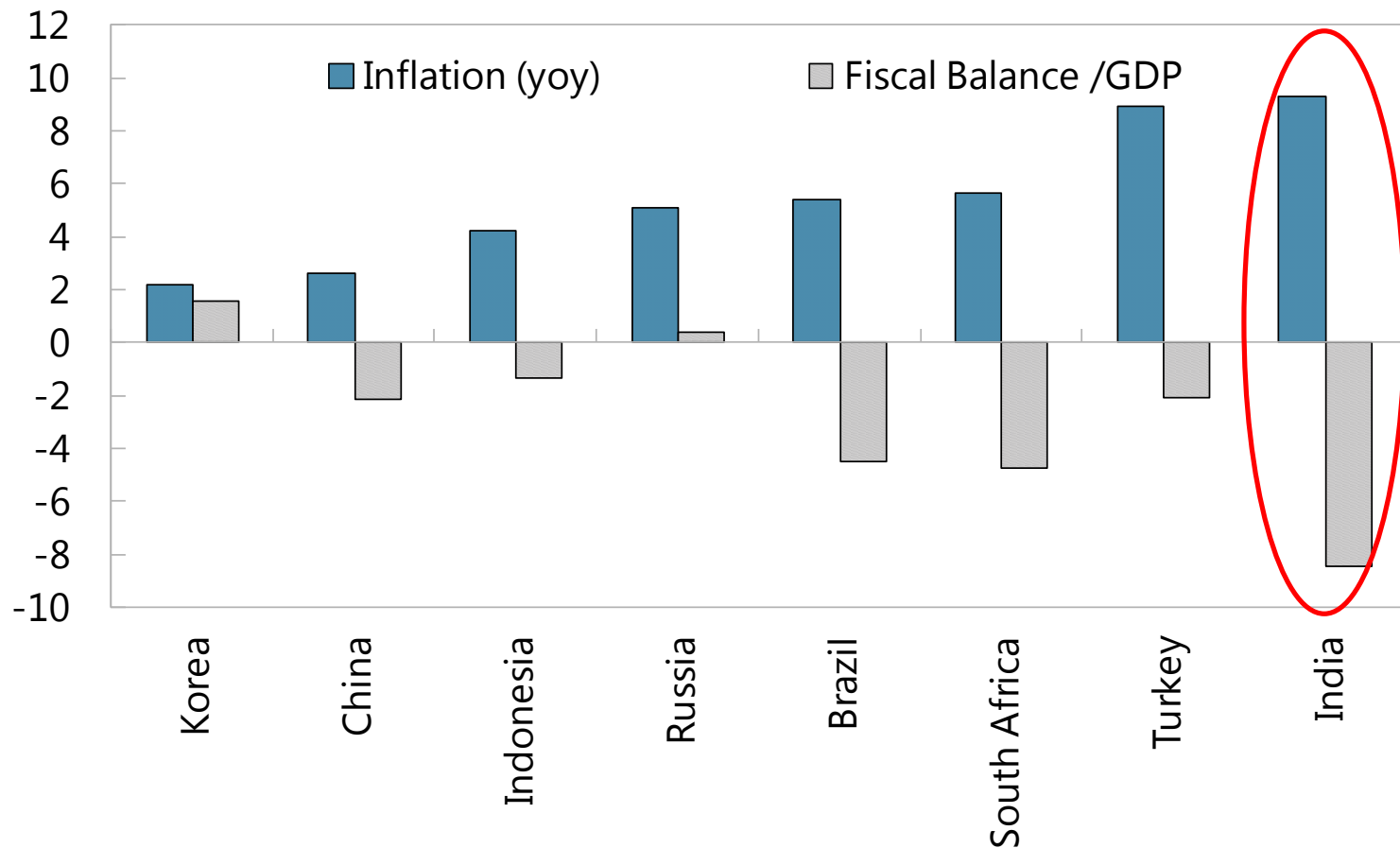


Sources: RBI and IMF staff calculations.

Bottom line for EMs: getting macro fundamentals right is crucial

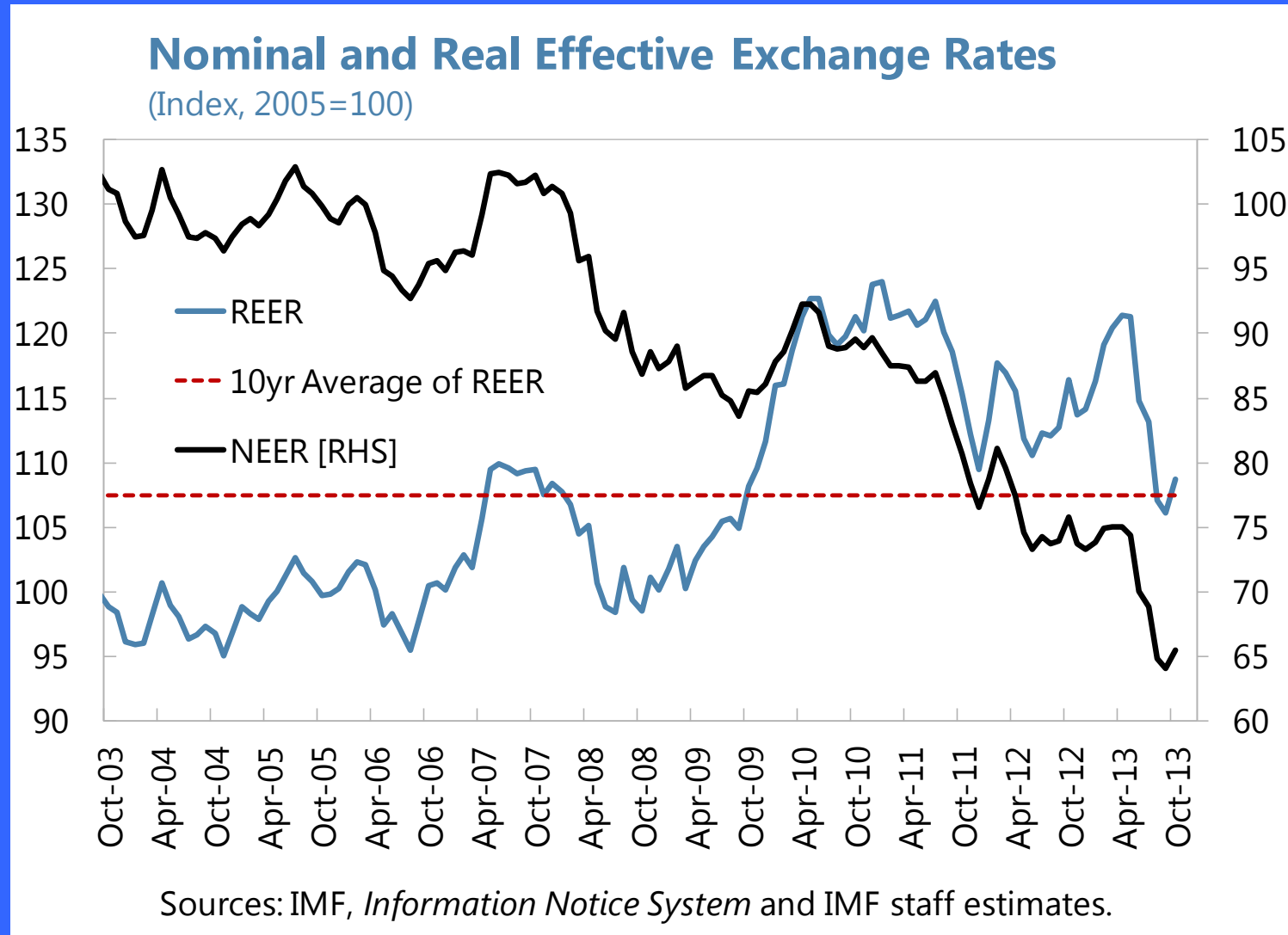
Inflation and Fiscal Balance, 2012

(In percent)



Sources: IMF, *World Economic Outlook*; and IMF staff calculations.

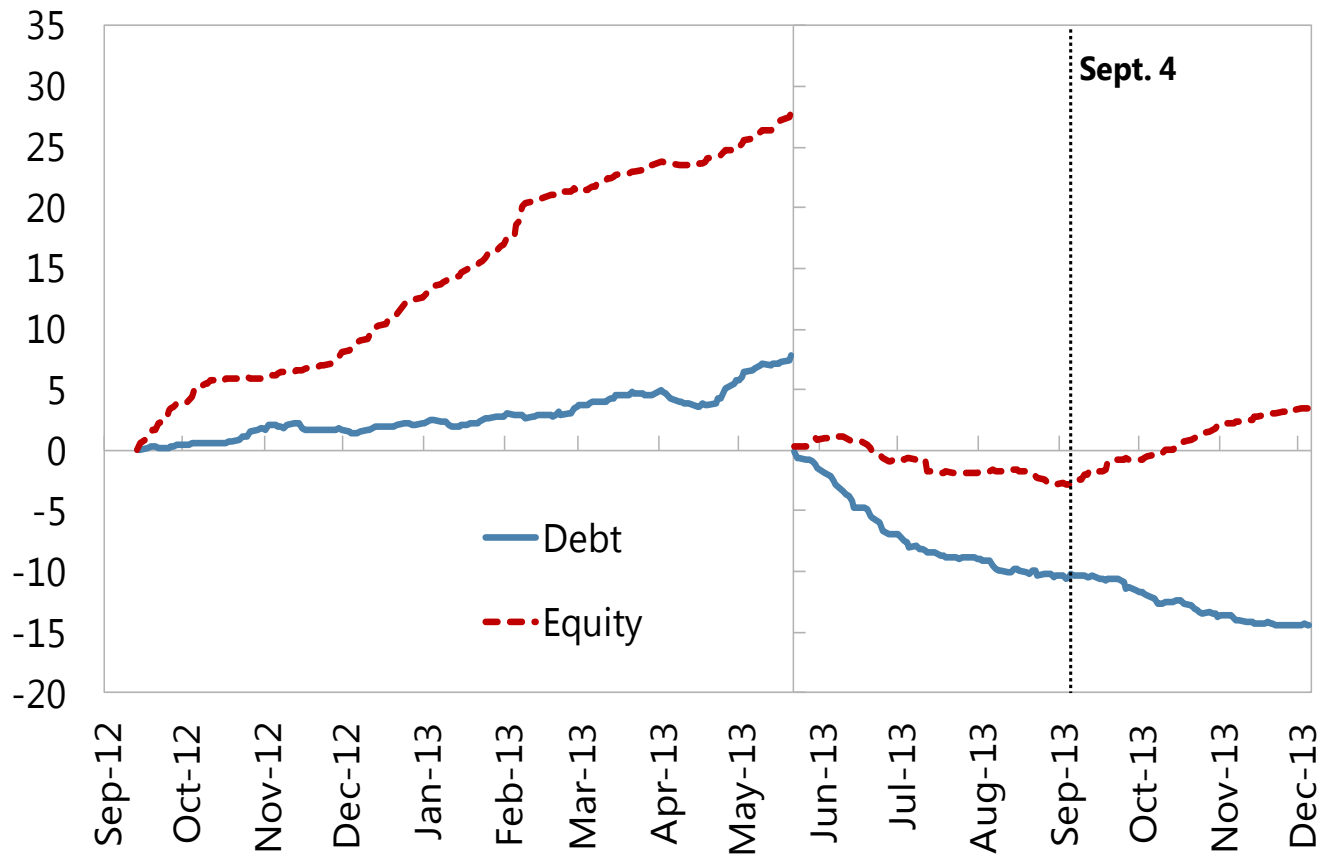
India's external sector



Equity flows have been more stable than debt flows since May

Debt and Equity Inflows

(In billions of US Dollars, cumulative)

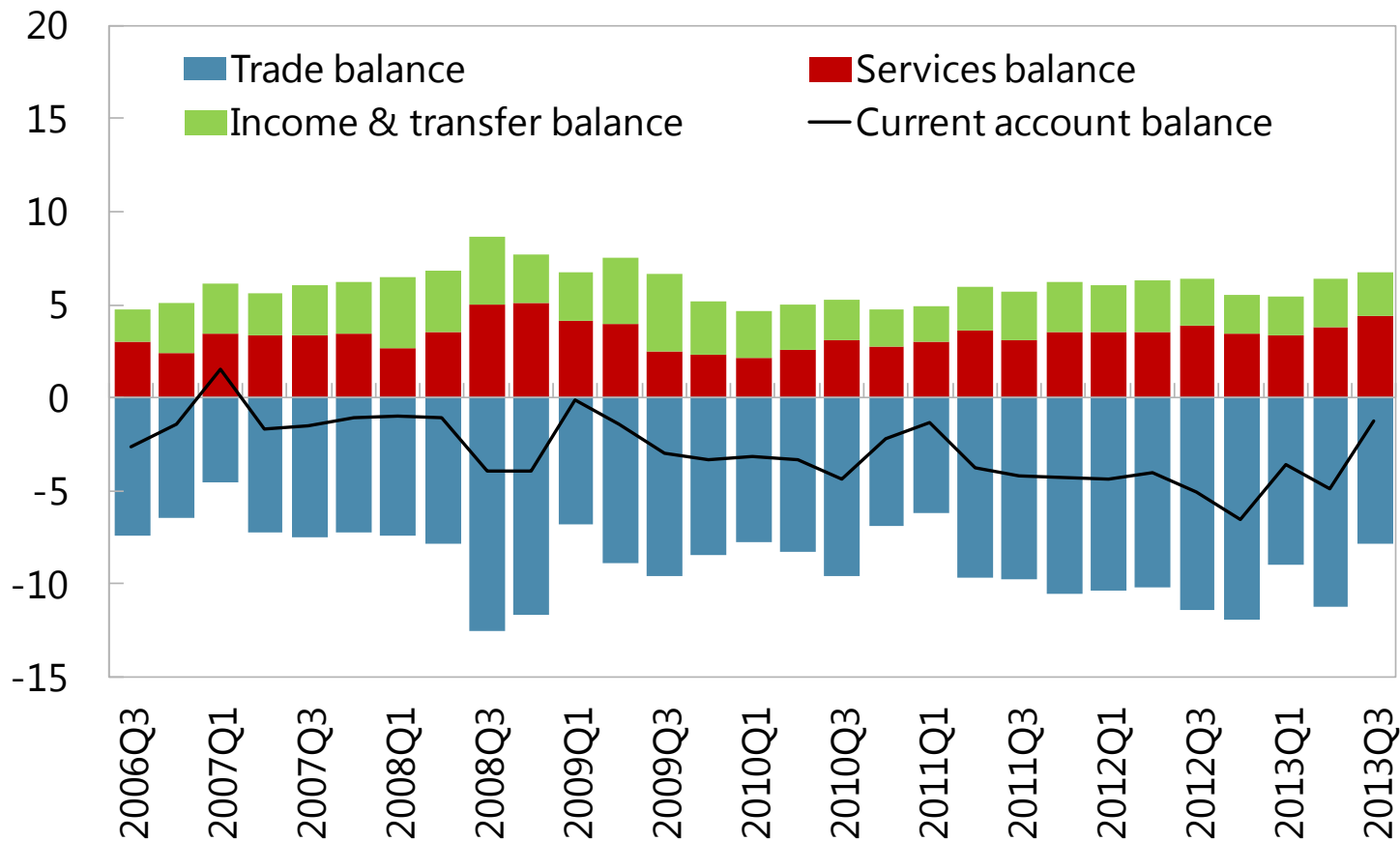


Source: Bloomberg.

CAD has been squeezed, but mainly due to gold measures?

Current Account Balance

(In percent of GDP)

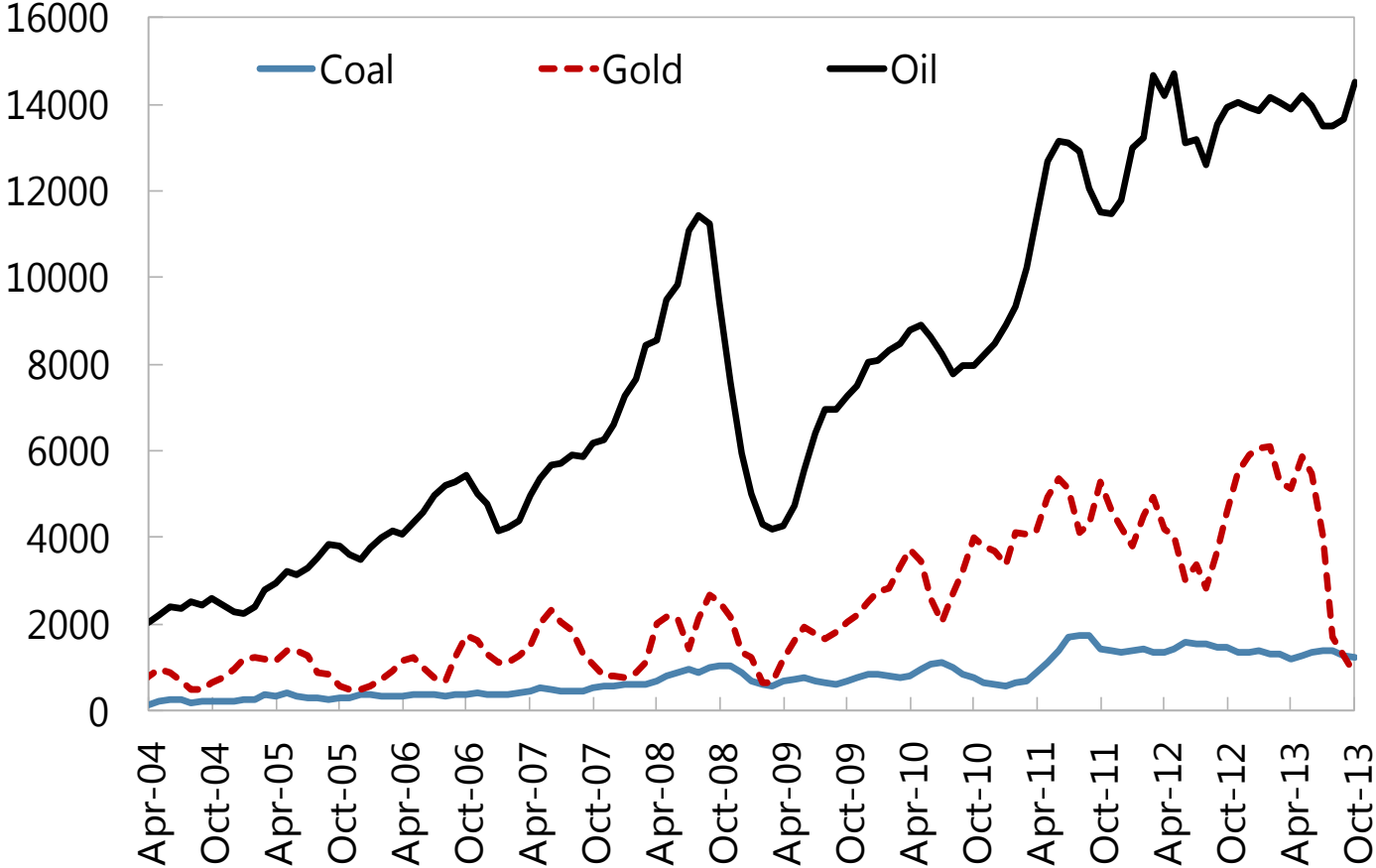


Sources: CEIC and IMF staff calculations.

How durable are the measures to reduce gold imports?

Imports: Principle Commodities

(In millions of US Dollars, 3mma)

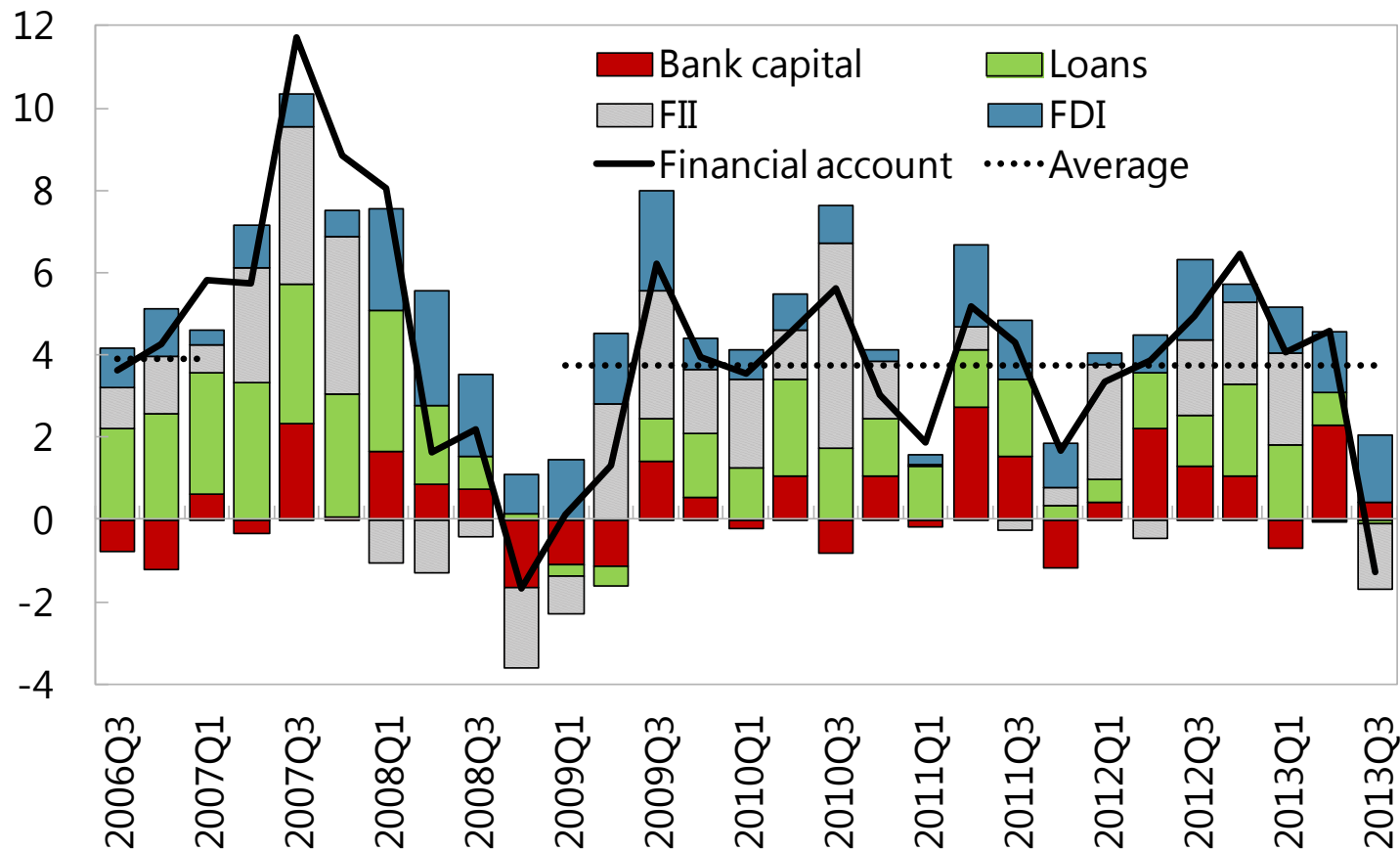


Sources: CEIC; and IMF staff calculations.

Financing the CAD has become more difficult in recent years...

Financial Account

(In percent of GDP)

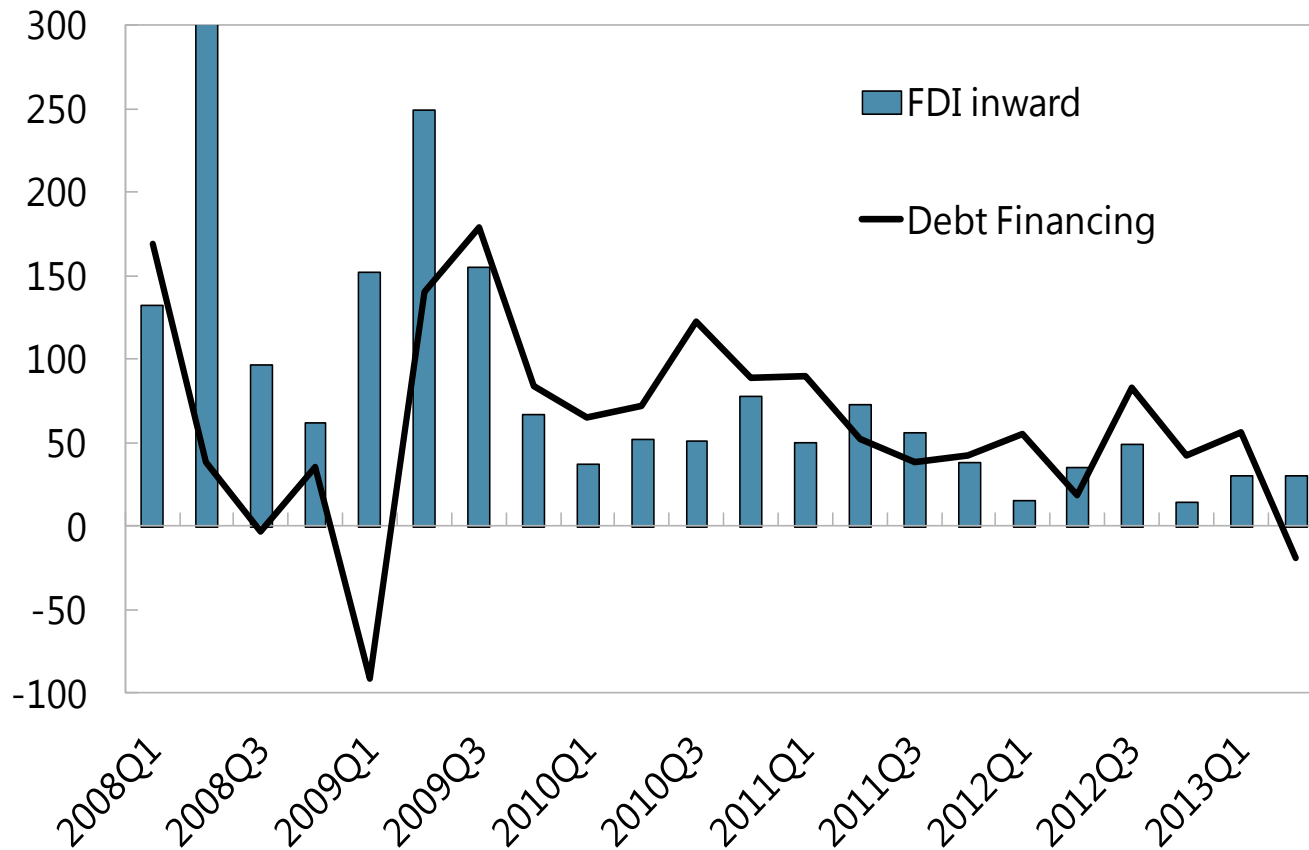


Sources: CEIC; and IMF staff calculations.

... and composition has shifted toward debt
(at least until the last few months)

Inward FDI and Debt Financing

(In percent of Current Account Deficit)

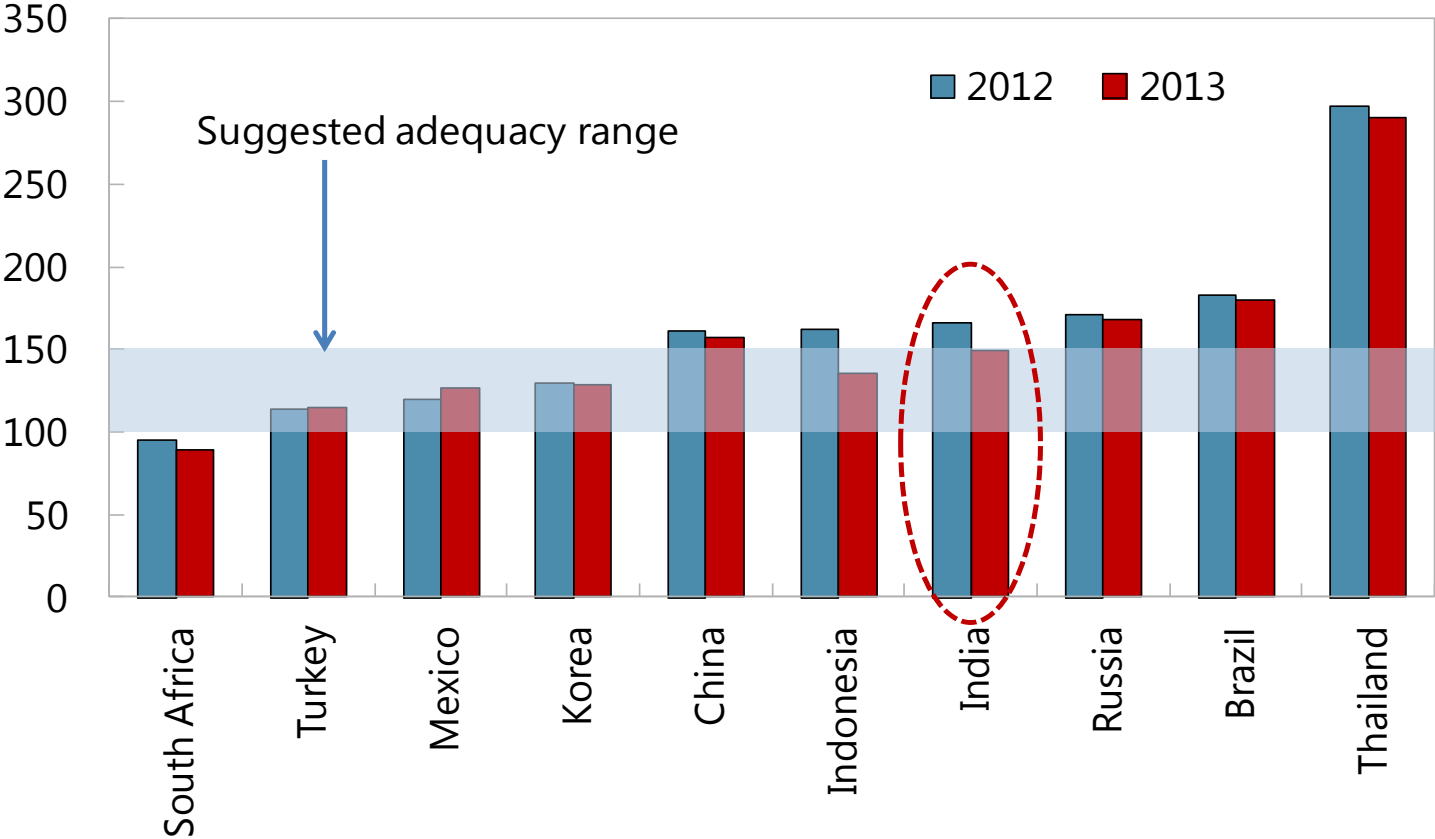


Source: Haver Analytics.

India had ample reserves (even before Sept measures) ...

Estimated Reserve Adequacy

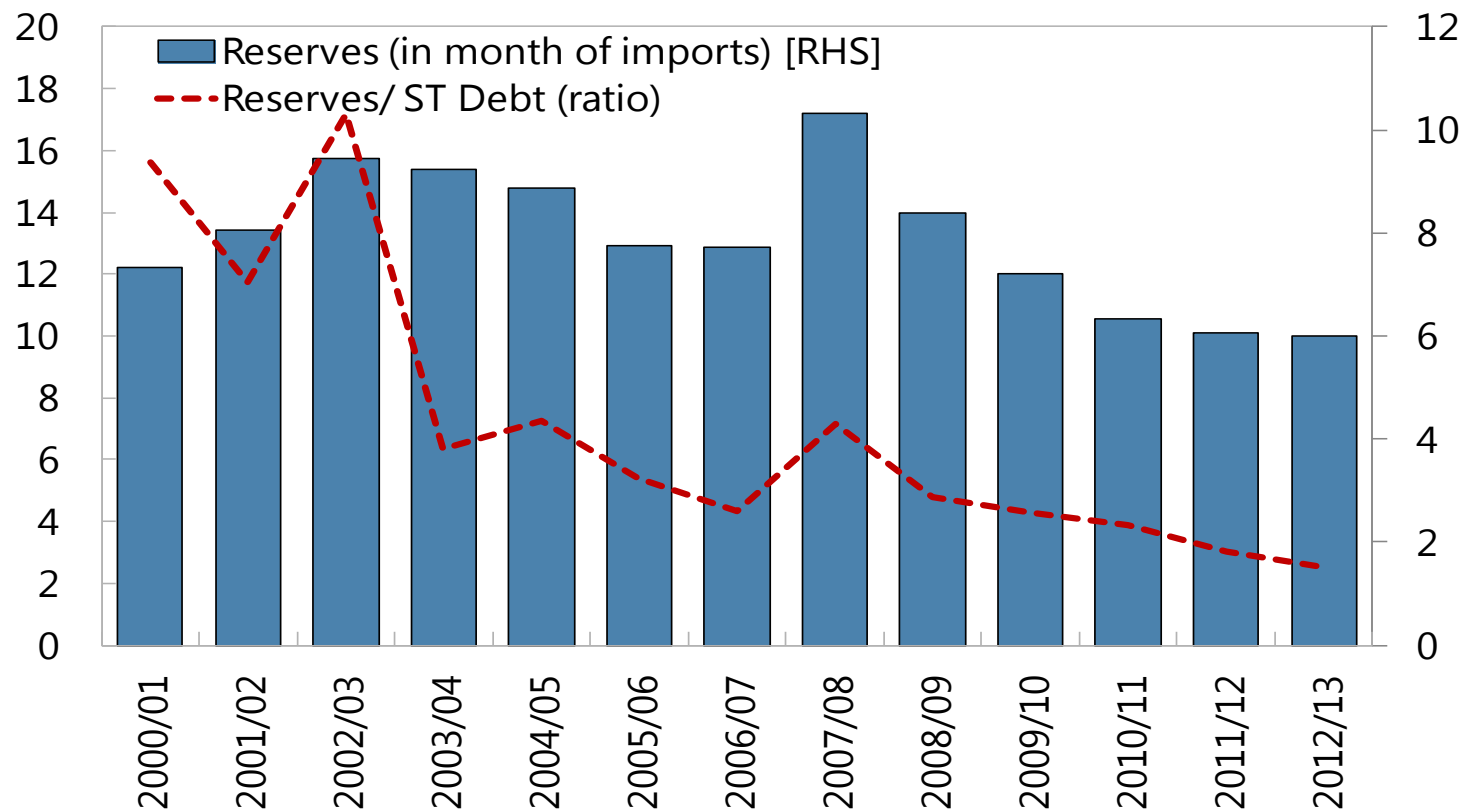
(Official reserves as a percent of IMF country-specific metric)



Sources: IMF, *International Financial Statistics*; and IMF staff calculations.

... but the trend has worried some analysts

Reserves Coverage

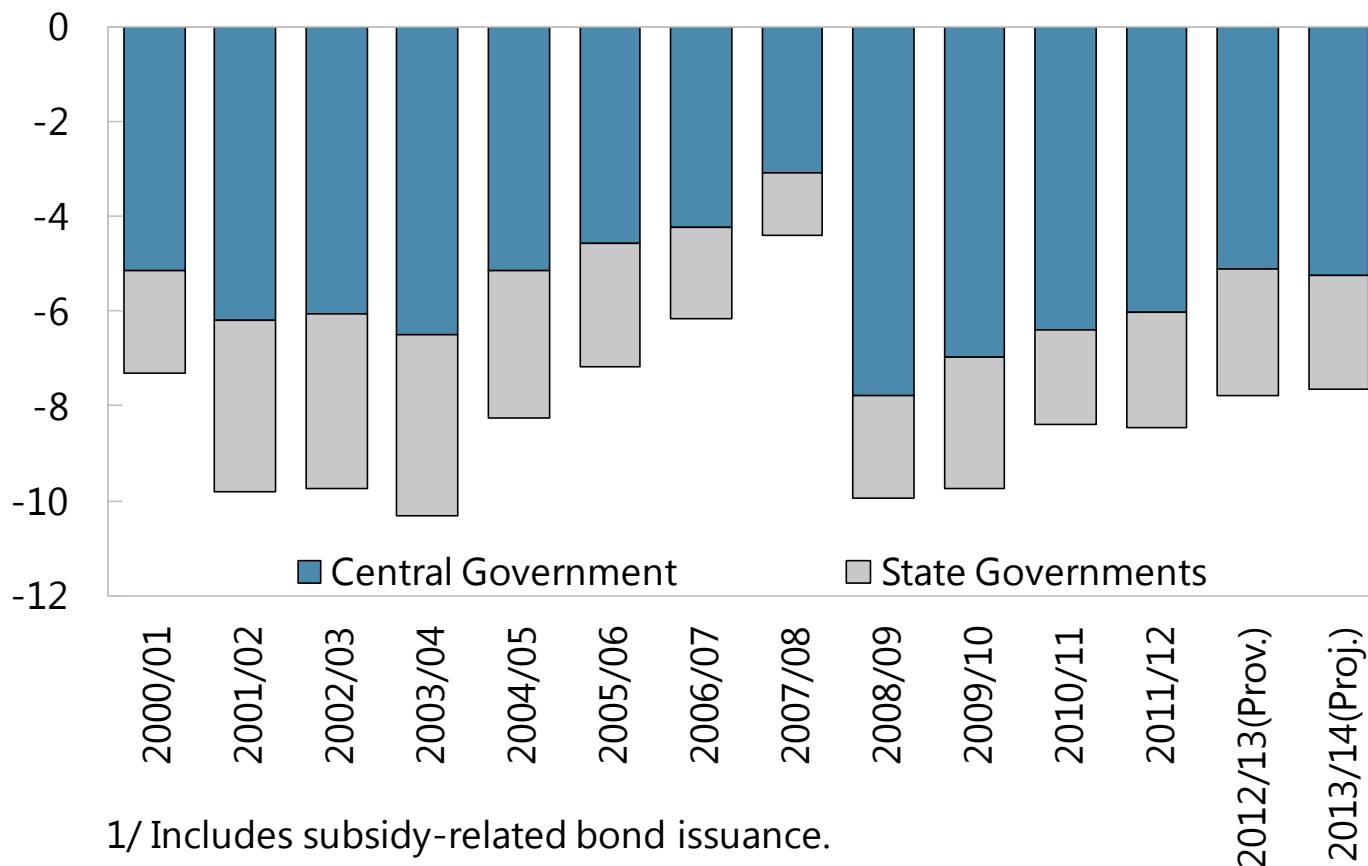


Sources: IMF staff calculations.

Fiscal policy

Government Balance

(In percent of GDP) 1/



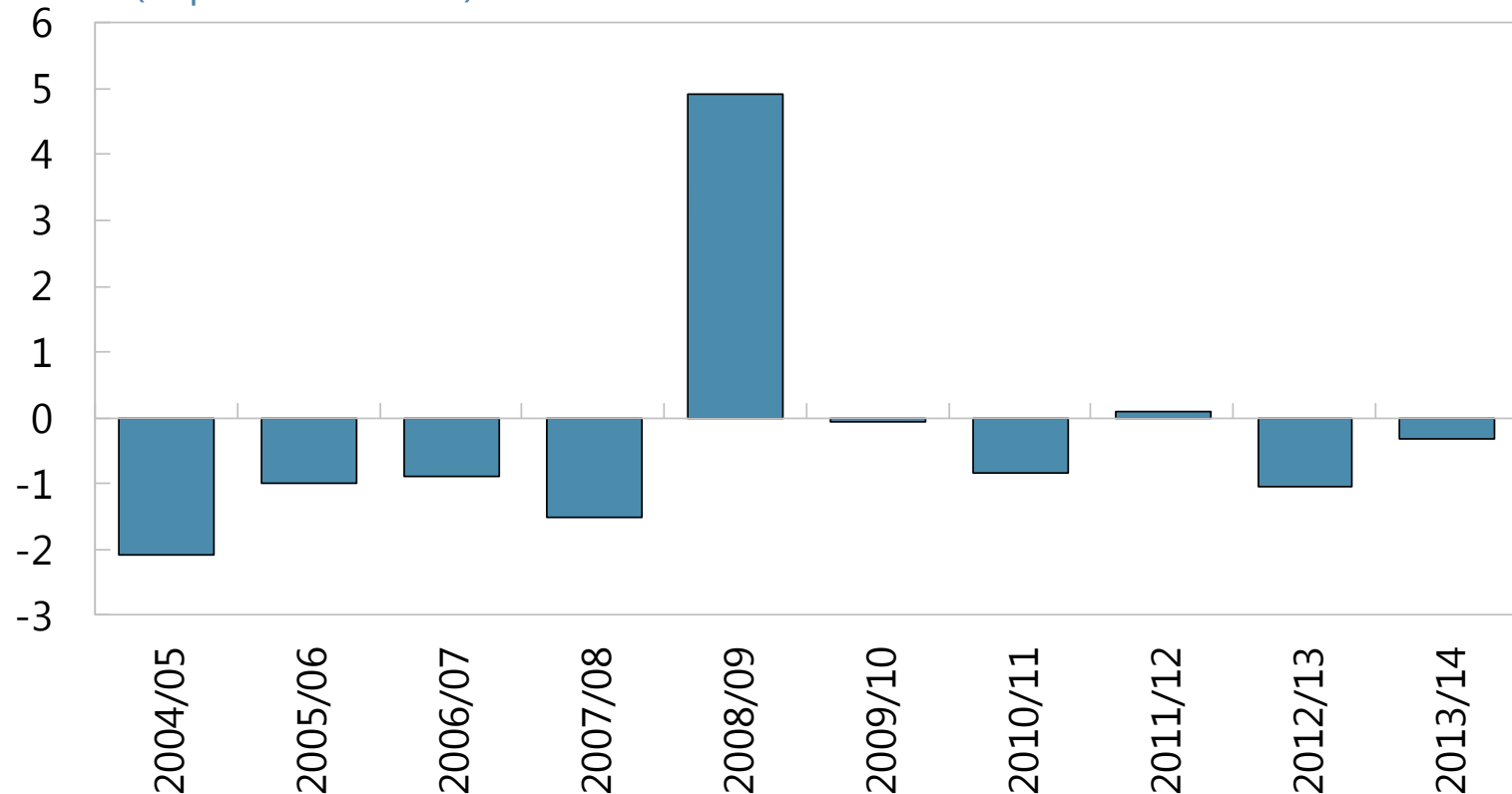
1/ Includes subsidy-related bond issuance.

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)



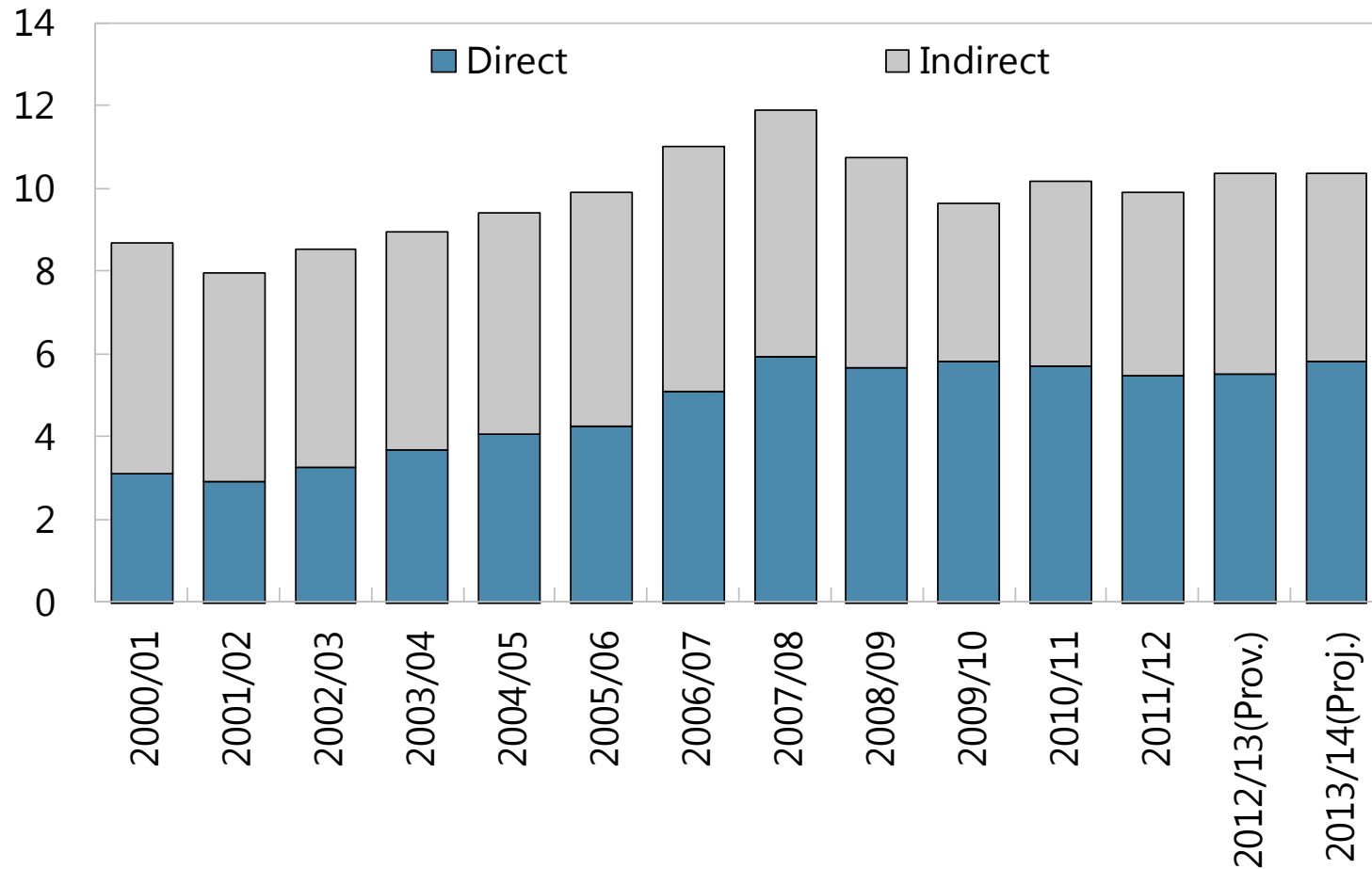
1/ Defined as difference between current and previous year budget deficits, using business cycle-adjusted revenues.

Source: IMF staff calculations.

Revenue mobilization has not recovered...

Central Government Revenue

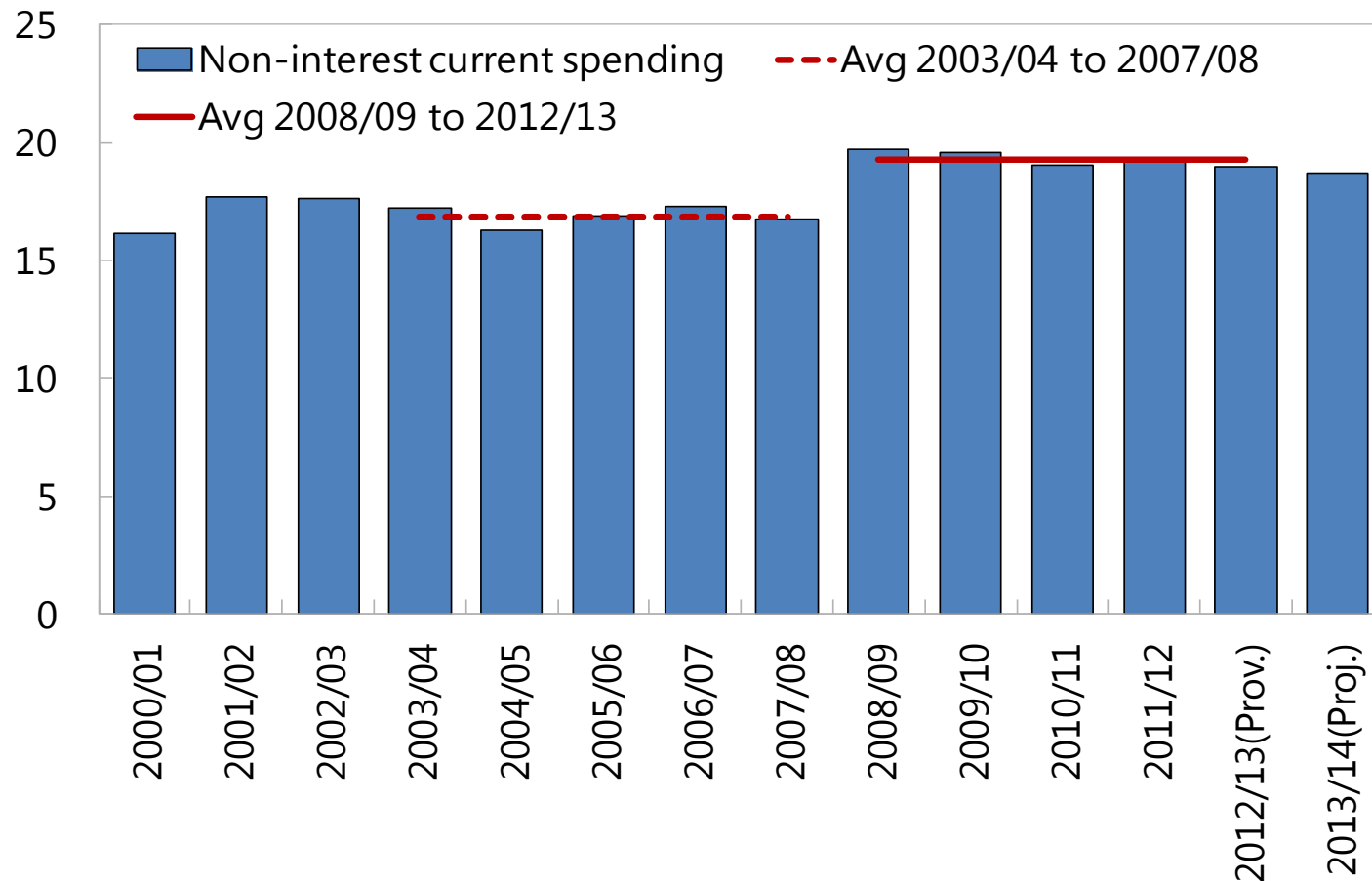
(In percent of GDP)



... and current spending, which reached a plateau during the crisis, has fallen only slowly

General Government Non-interest Current Spending

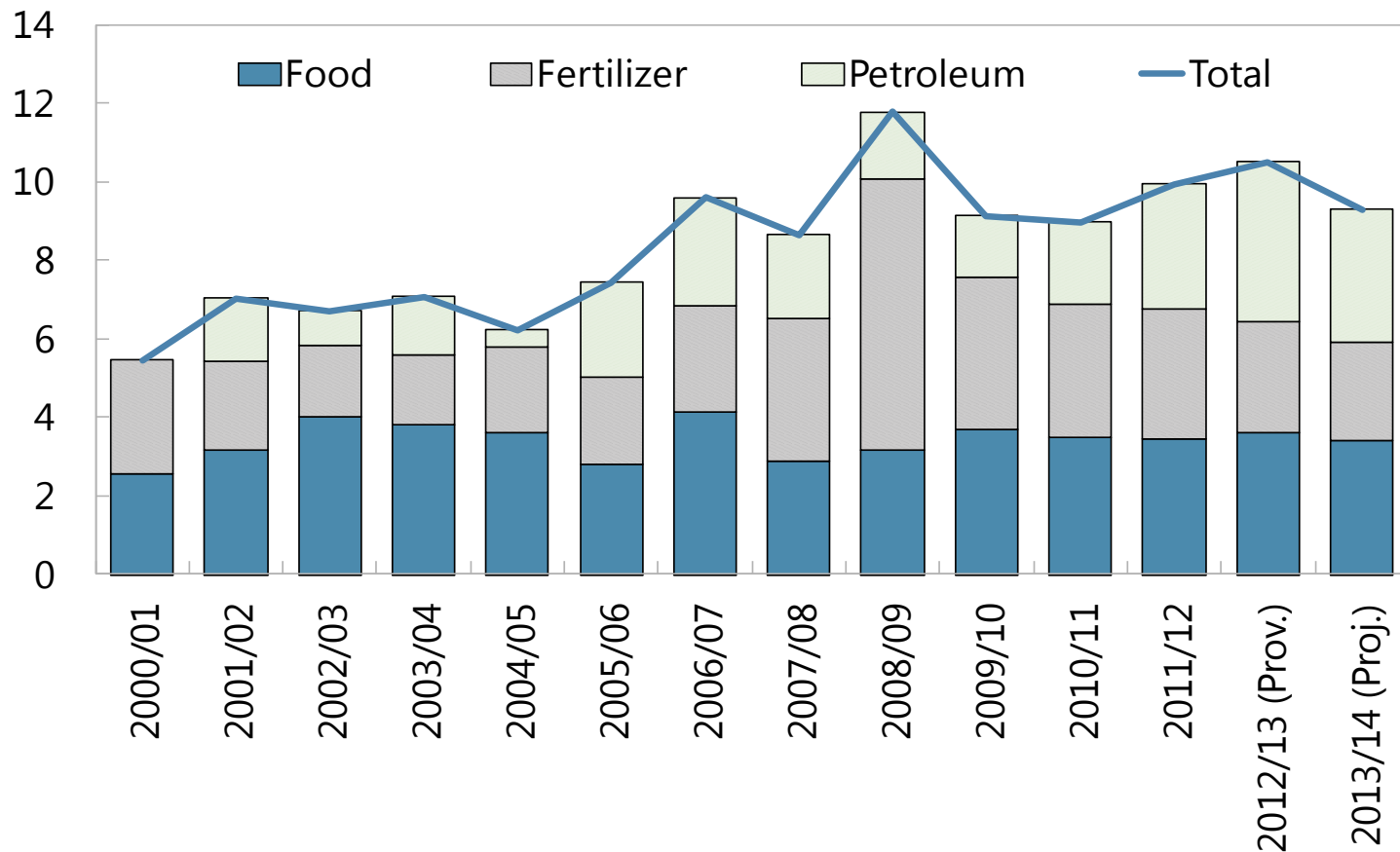
(In percent of GDP)



Subsidy reform is therefore a high priority

Government Subsidies

(As a percent of Current Expenditure)

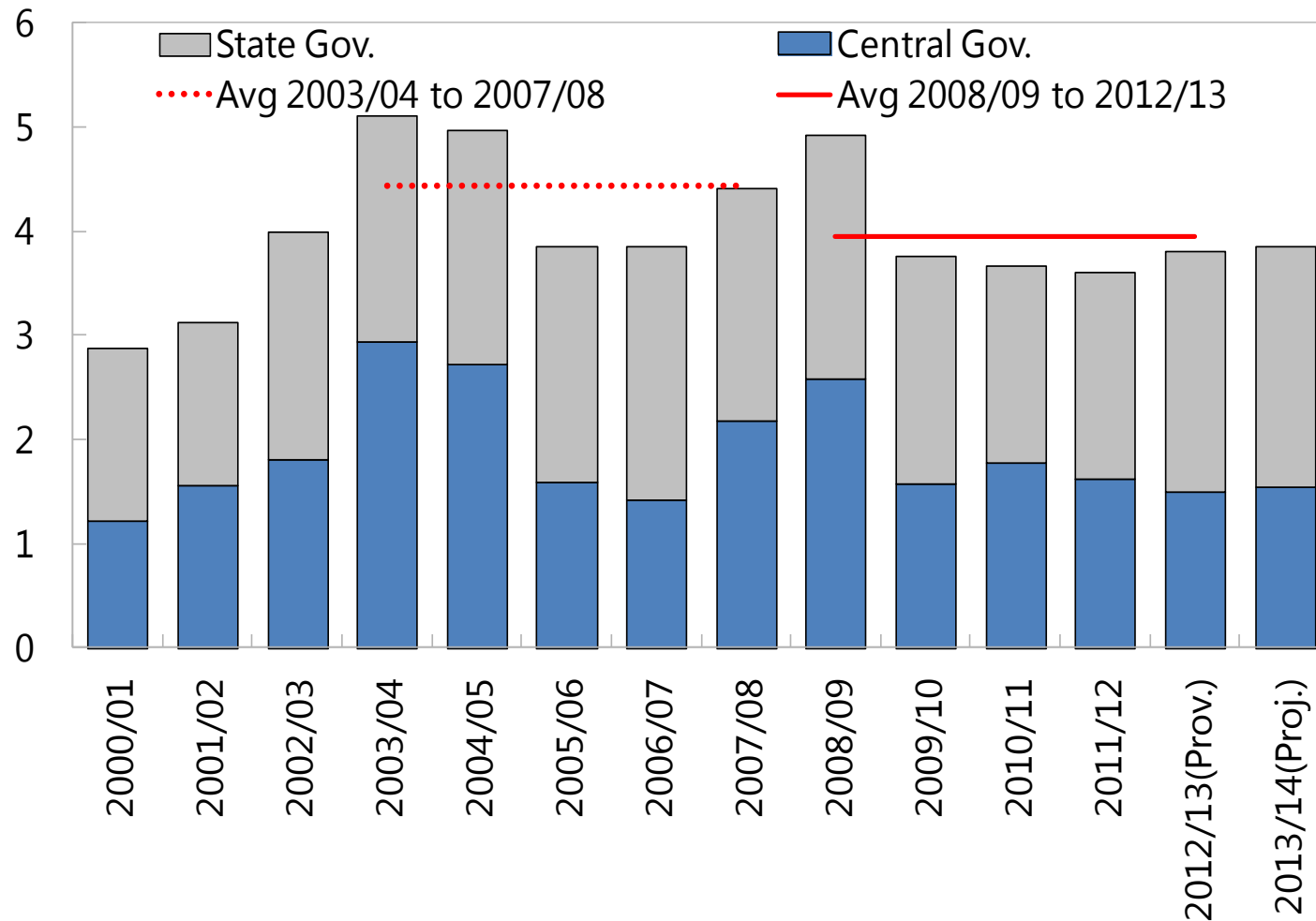


Sources: IMF staff data.

Government capital investment has taken the brunt of adjustment

Capital Spending

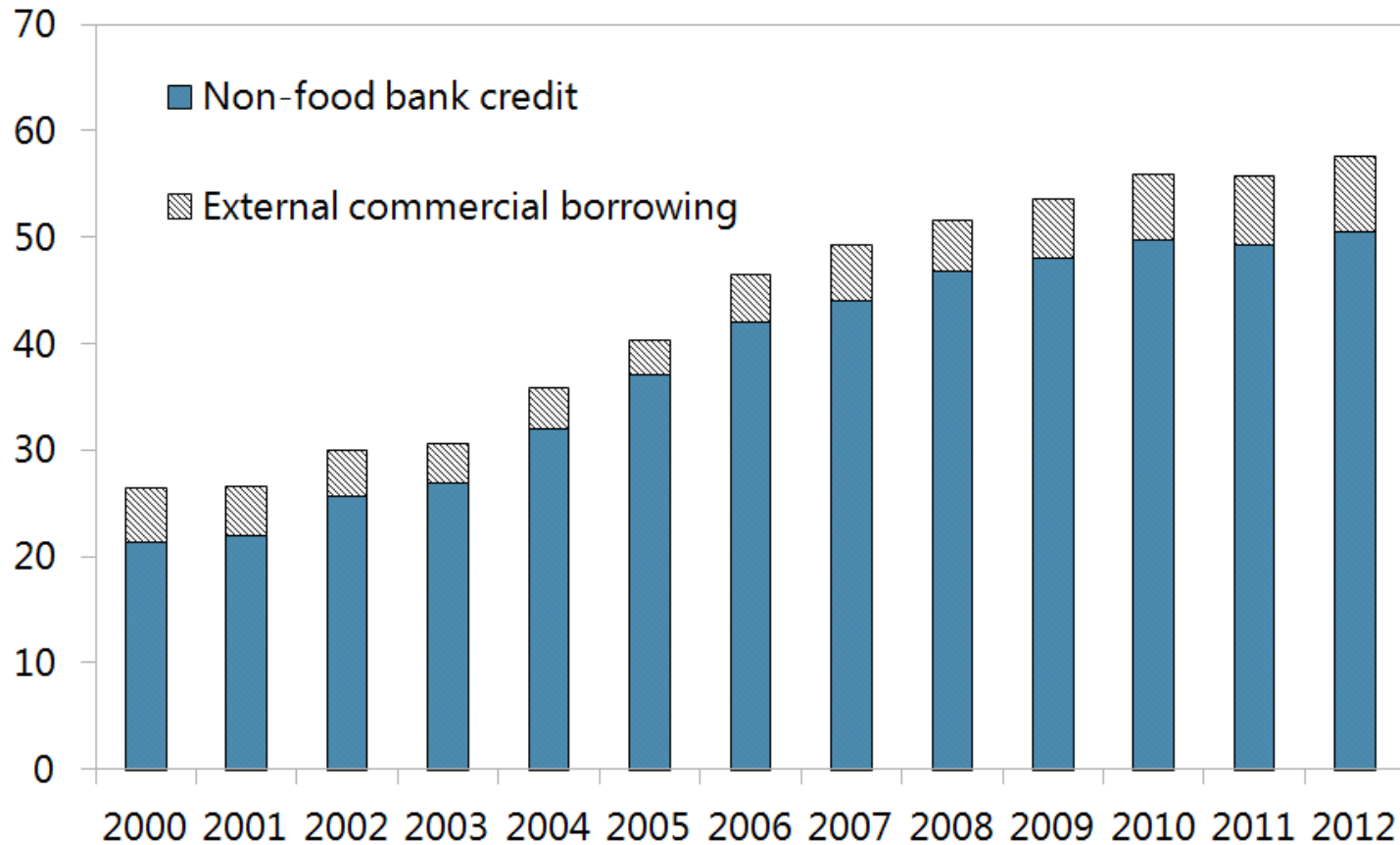
(In percent of GDP)



Corporate and financial sector

Corporate Borrowing

(As percent of GDP)

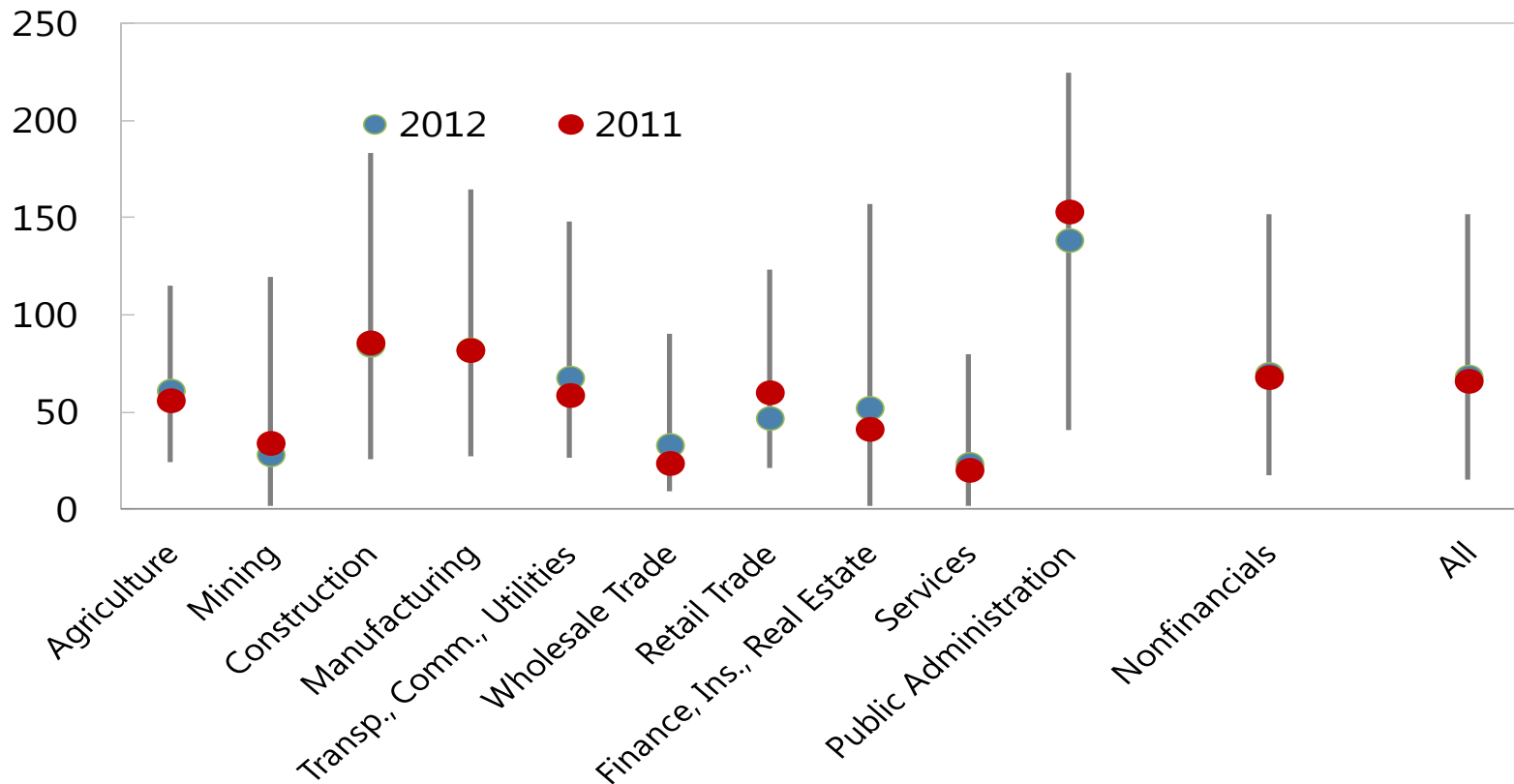


Sources: CEIC Data Company

Leverage ratios are particularly high for construction; manufacturing; transport, communications & utilities; and the public sector

Leverage Ratios by Sector

(Ratio of Debt to Equity - Median, 25th and 75th percentiles by sector)

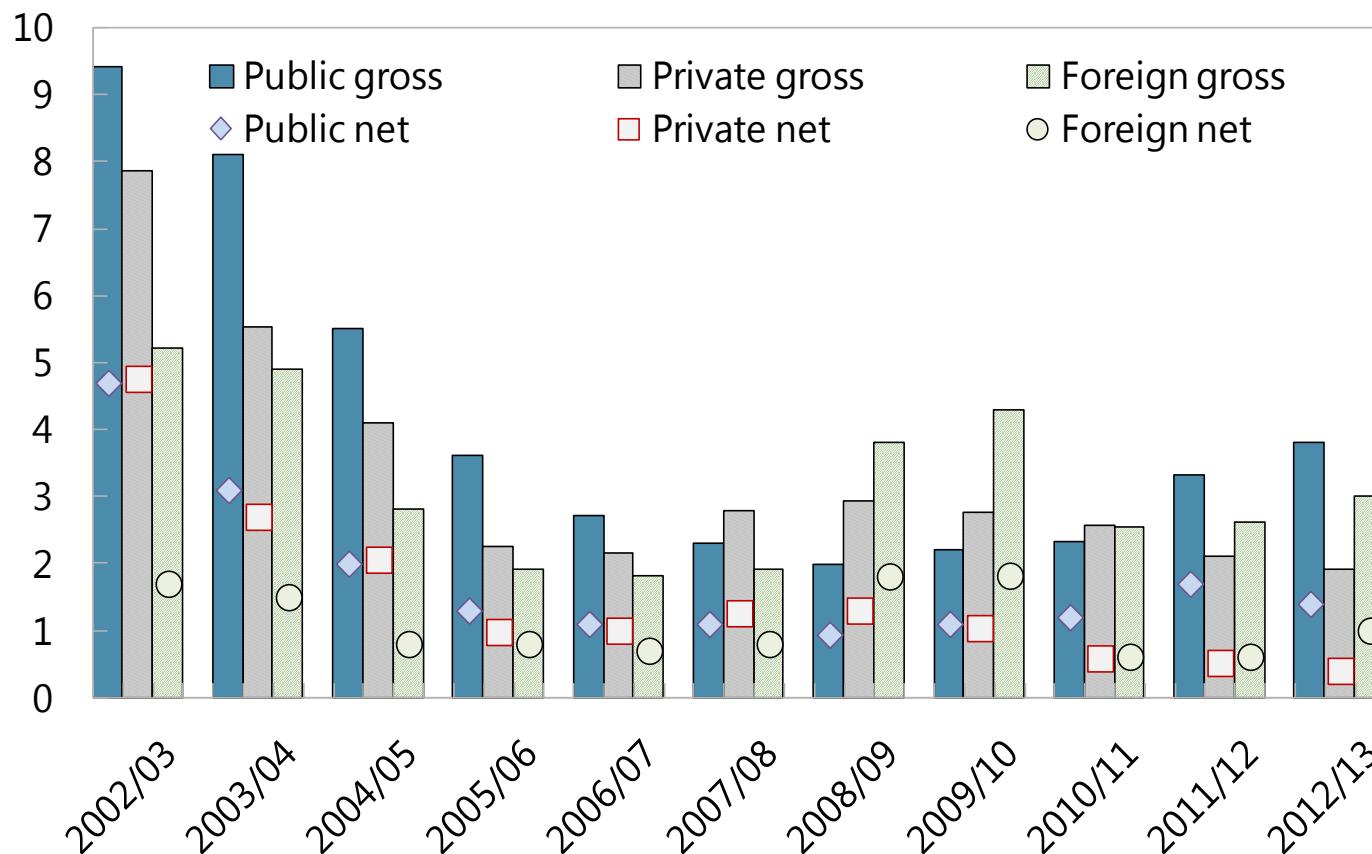


Sources: IMF, Corporate Vulnerability Utility; and IMF staff calculations.

NPAs have been rising in recent years,
but remain at levels well-below the early 2000s

Commercial Banks NPAs

(In percent)

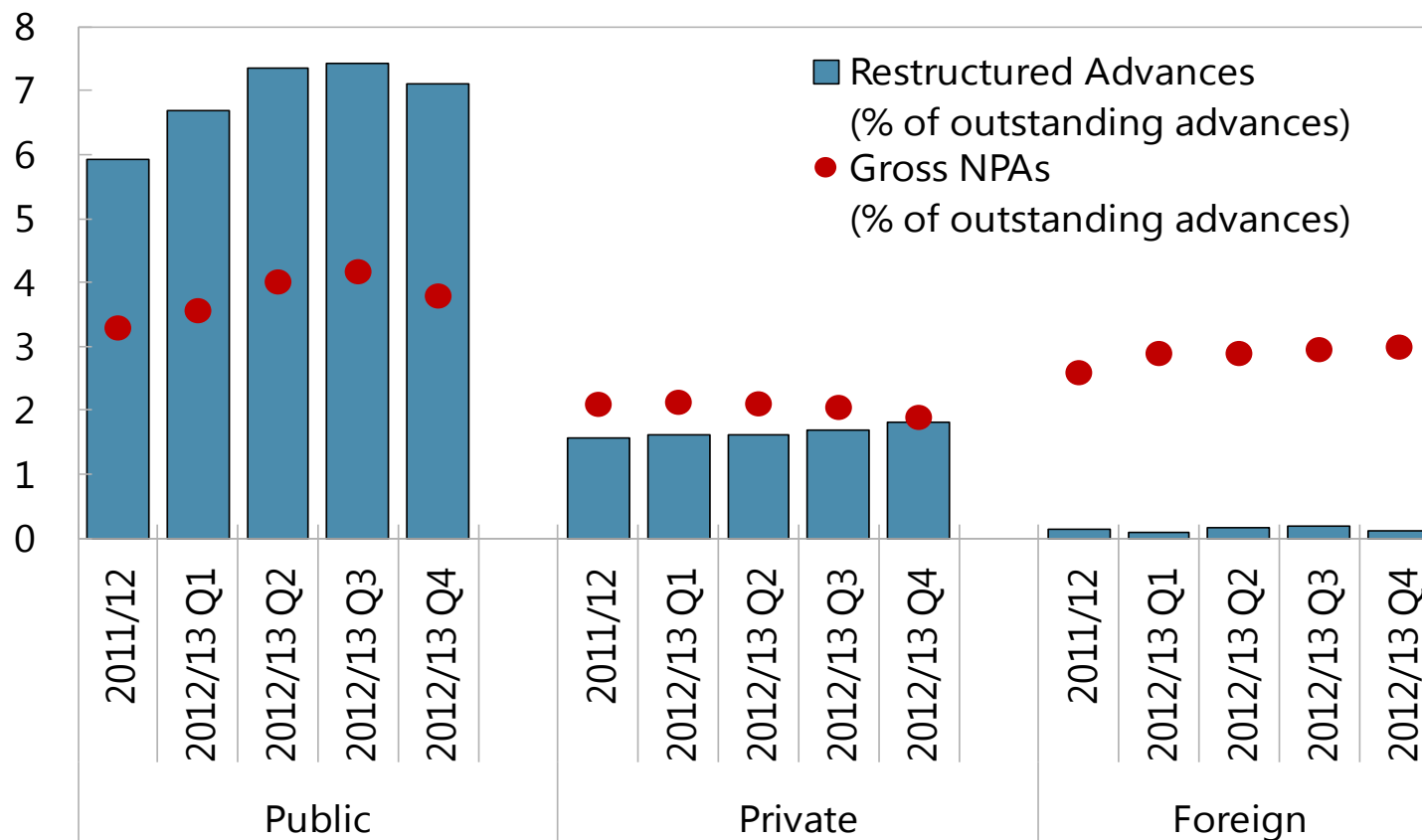


Sources: Reserve Bank of India and IMF staff calculations.

PSU banks have higher NPAs and greater exposure to restructured loans

Commercial Banks: Restructured Advances & NPAs

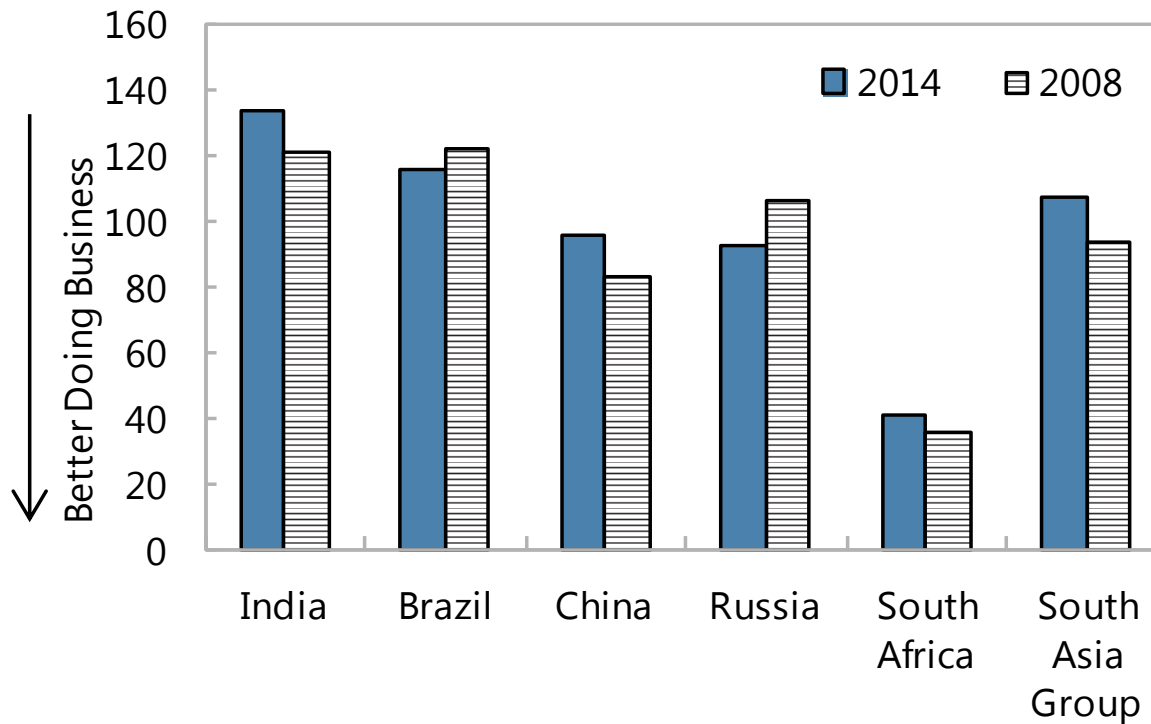
(In percent)



Sources: Reserve Bank of India and IMF staff calculations.

Structural issues

Ease of Doing Business Ranking: BRICS and South Asia



Sources: World Bank, Doing Business Report (2014 and 2008)

Note: South Asia Group includes Bhutan, Maldives, Nepal, Pakistan and Sri Lanka.

Labor market: demographic dividend or demographic bomb?



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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