



# **Economic Outlook for India and Nepal in Global Context**

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## Global Setting

- Gradual upturn in growth outlook as tail risks recedes

## Asia Outlook

- Resilience and growth pick-up as capital inflow returns
- Risks and policy challenges

## India & Nepal Outlook

- Growth to recover but only moderately. Domestic reforms are the key concerns

# Global Setting

## Main Messages

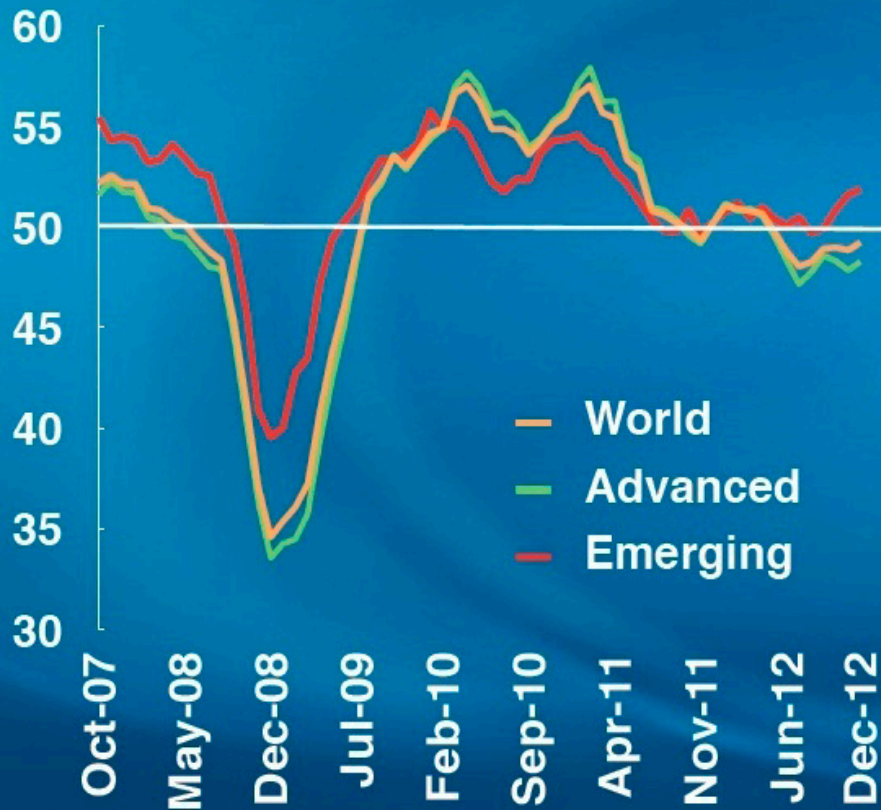
- Global recovery expected later this year—acute risks diminished
- Yet downside risks remain significant
- So policy action needed to secure recovery

# World Economy: Tail risks receding...

Global

## Global Manufacturing PMI

(Index; >50 = expansion; SA)



## Selected Europe: Sovereign CDS Spreads

(In basis points; 5-year senior debt)



Source: IMF, Global Data Source.

Sources: Thomson Reuters Datastream; and Haver Analytics.

# Global outlook remains subdued

Global

## Growth Projections (Year-on-year percent change)



## Real GDP Growth (Year-on-year percent change)

	2012	2013
World	3.2	3.5
Advanced economies	1.3	1.4
Emerging economies	5.1	5.5



Source: IMF, World Economic Outlook.

Source: IMF, World Economic Outlook.



# IMF global GDP forecasts recently marked down

## WEO Real GDP Growth Projections

(percent change from a year earlier)



	World	U.S.	Euro Area	Japan	Brazil	Russia	India	China
<b>2012</b>								
(Jan 2013)	3.2	2.3	-0.4	2.0	1.0	3.6	4.5	7.8
(Oct 2012)	3.3	2.2	-0.4	2.2	1.5	3.7	4.9	7.8
(Jul 2012)	3.5	2.0	-0.3	2.4	2.5	4.0	6.1	8.0
<b>2013</b>								
(Jan 2013)	3.5	2.0	-0.2	1.2	3.5	3.7	5.9	8.2
(Oct 2012)	3.6	2.1	0.2	1.2	4.0	3.8	6.0	8.2
(Jul 2012)	3.9	2.3	0.7	1.5	4.6	3.9	6.5	8.5

# Asia Outlook

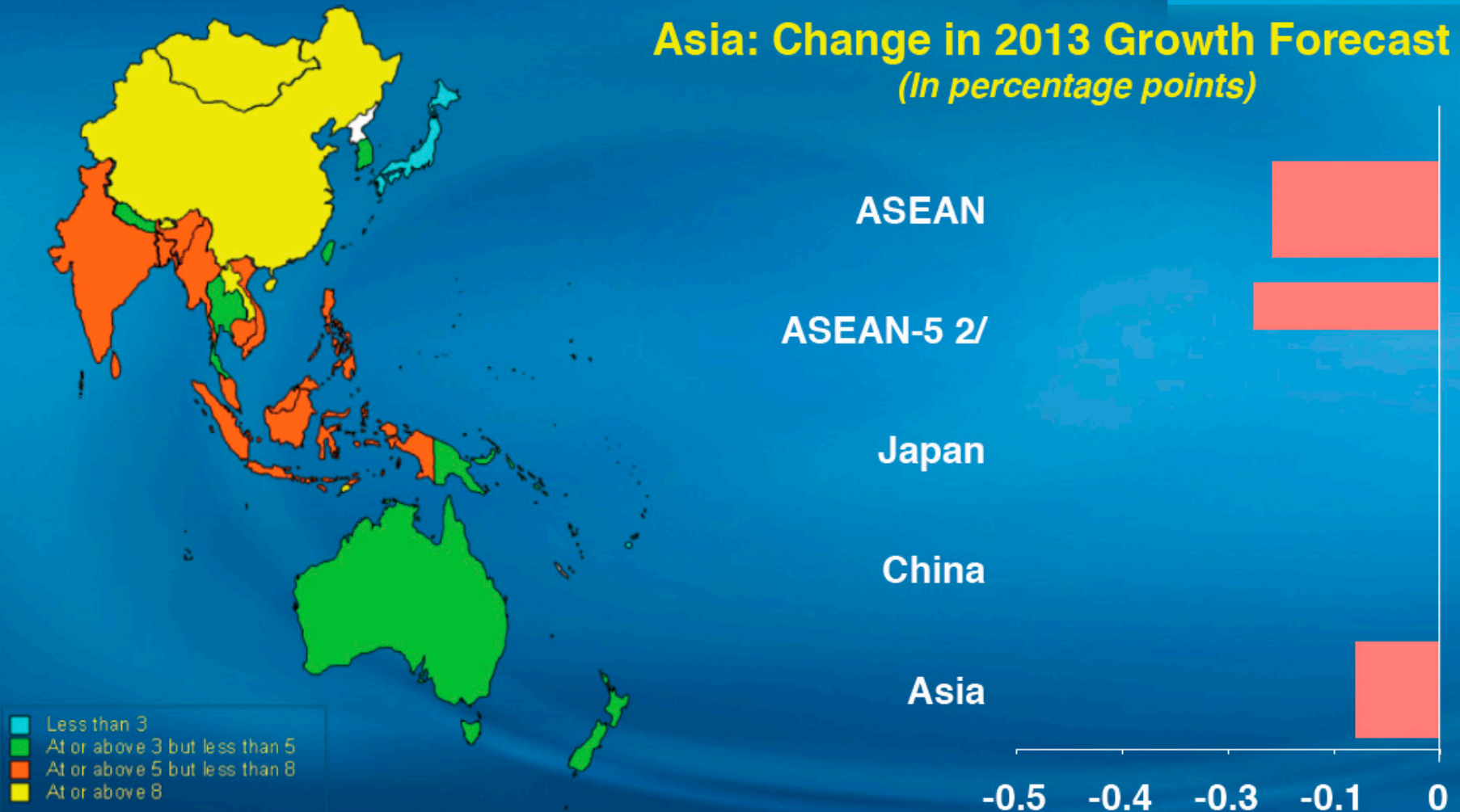
## Main Messages

- Asia is still global growth leader
- Recovery of demand for most countries, leading to capital inflows
- Most countries have some fiscal space, but not India or Japan
- Try to avoid “middle income trap”

# Asia remains global growth leader, but some downward revisions to forecasts.

Outlook and Risks

## Asia: Change in 2013 Growth Forecast 1/ (In percentage points)



■ Less than 3  
■ At or above 3 but less than 5  
■ At or above 5 but less than 8  
■ At or above 8

Source: IMF, World Economic Outlook.  
 1/ Compared with October 2012 WEO projections.  
 2/ ASEAN-5 includes Indonesia, Malaysia, the Philippines, Singapore, and Thailand.

Source: IMF, World Economic Outlook.





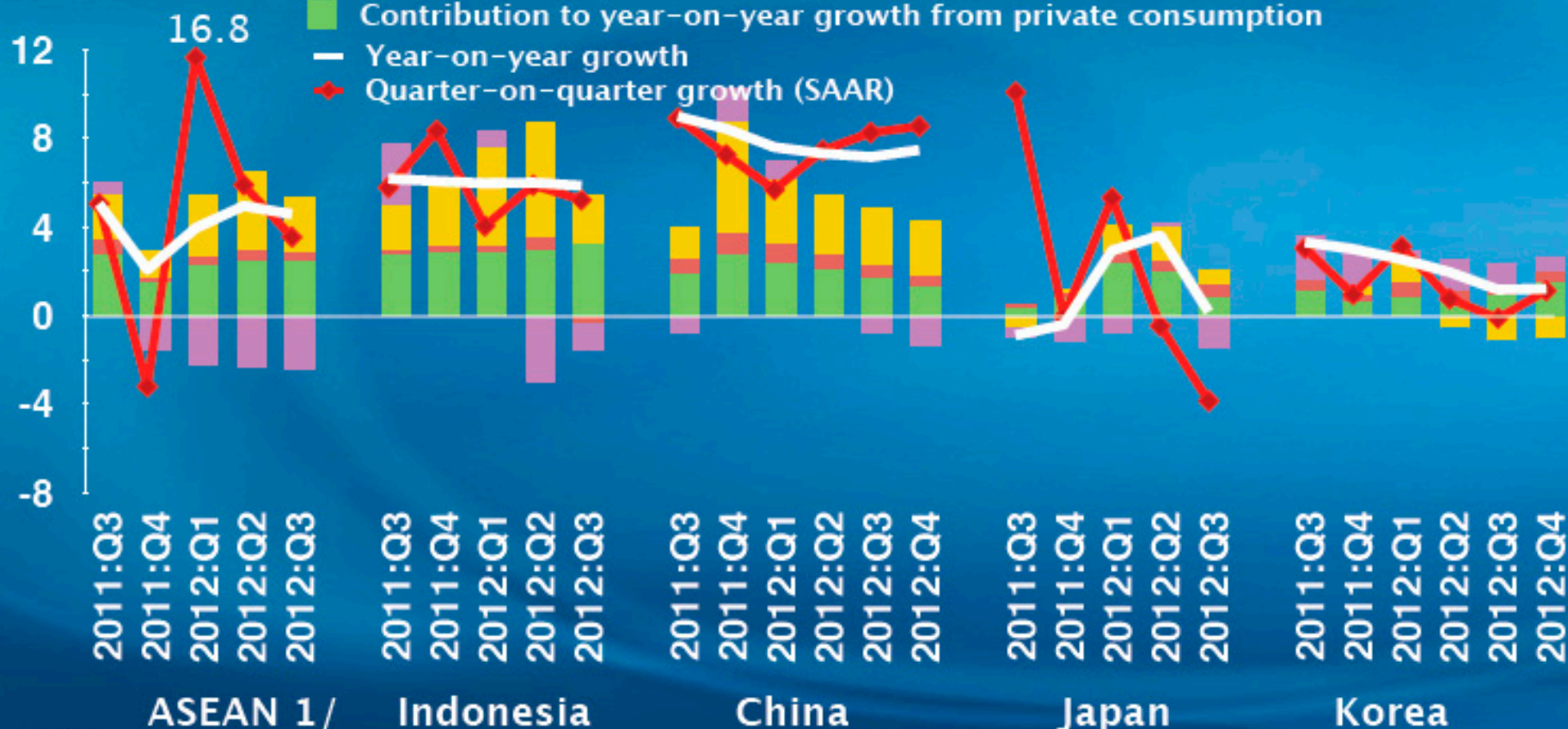
# Growth has stabilized across the region... Except in Japan

## Asia: Changes in Real GDP at Market Prices

Asia

(In percent)

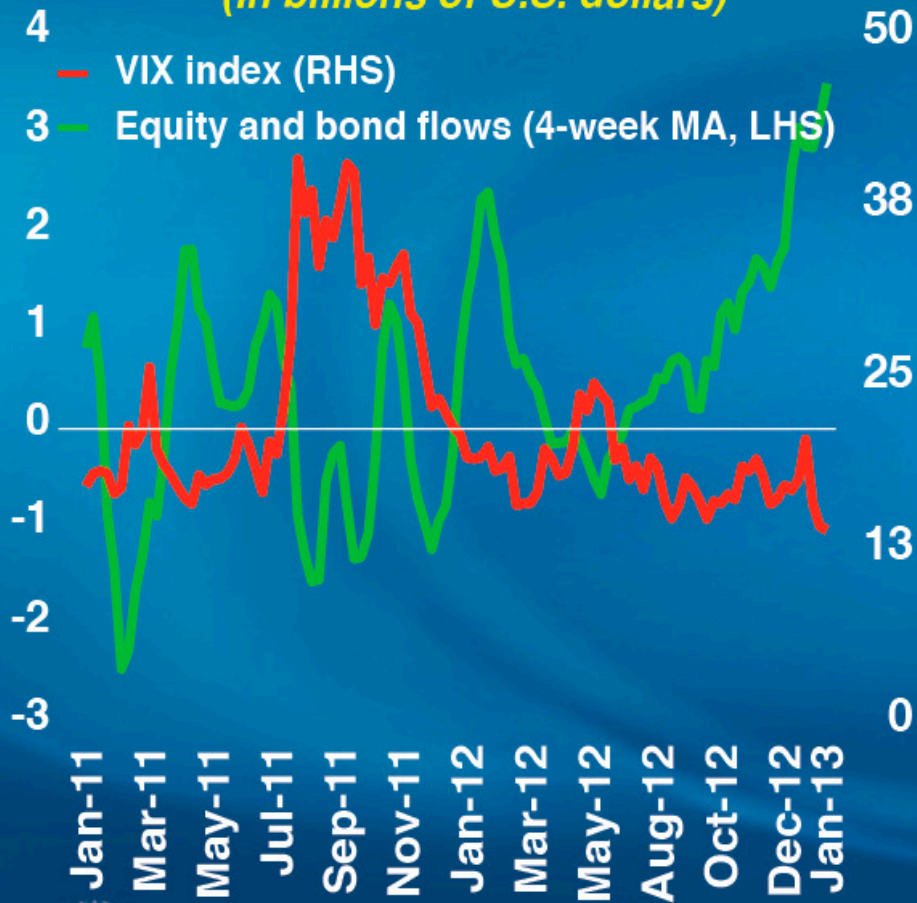
- Contribution to year-on-year growth from net exports
- Contribution to year-on-year growth from investment
- Contribution to year-on-year growth from public consumption
- Contribution to year-on-year growth from private consumption
- Year-on-year growth
- ◆ Quarter-on-quarter growth (SAAR)



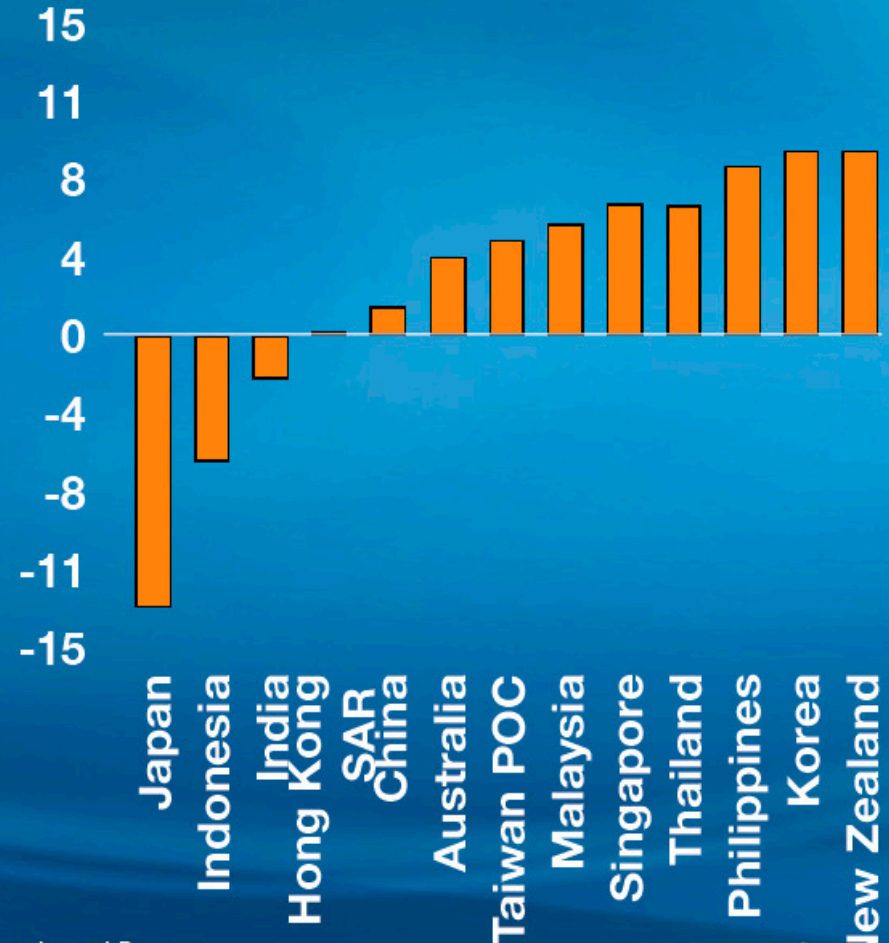
Sources: CEIC Data Co.Ltd; Haver Analytics; and IMF staff calculations.  
1/ Includes Indonesia, Malaysia, the Philippines, Singapore, and Thailand.

# Portfolio inflows have clearly picked up, resulting in currency appreciation in many EMs.

**Emerging Asia: Equity and Bond Funds Net Flows**  
(In billions of U.S. dollars)



**Changes in Bilateral Exchange Rates**  
(Percentage change in US\$ to national currency)

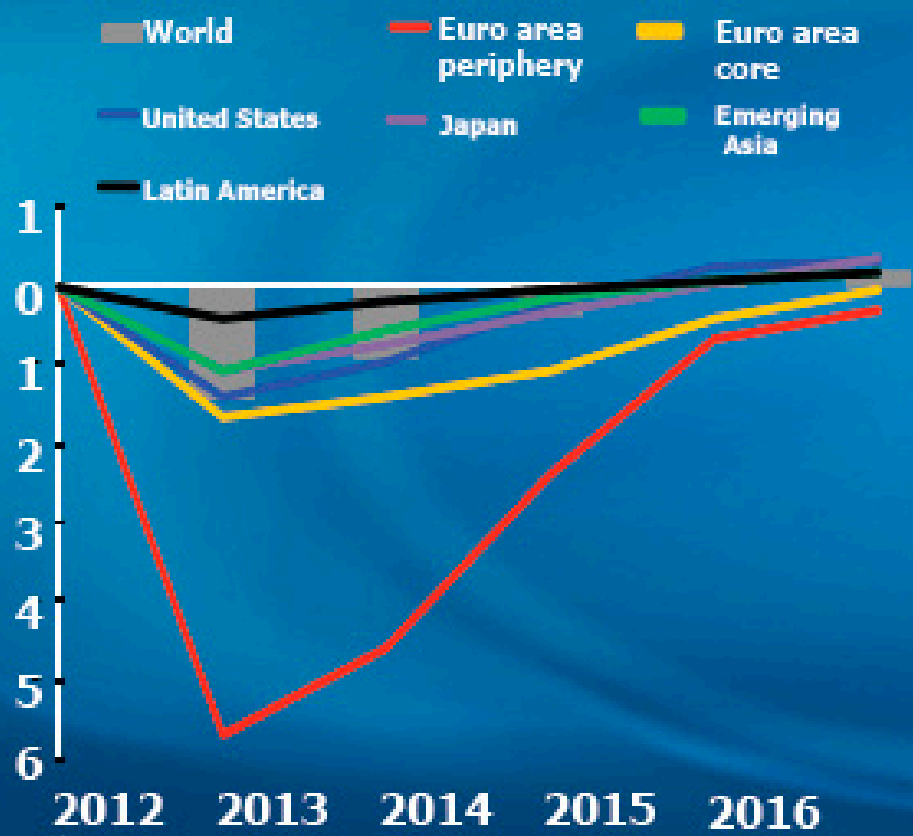


Sources: EPFR Global accessed through Haver Analytics; and Bloomberg LP.

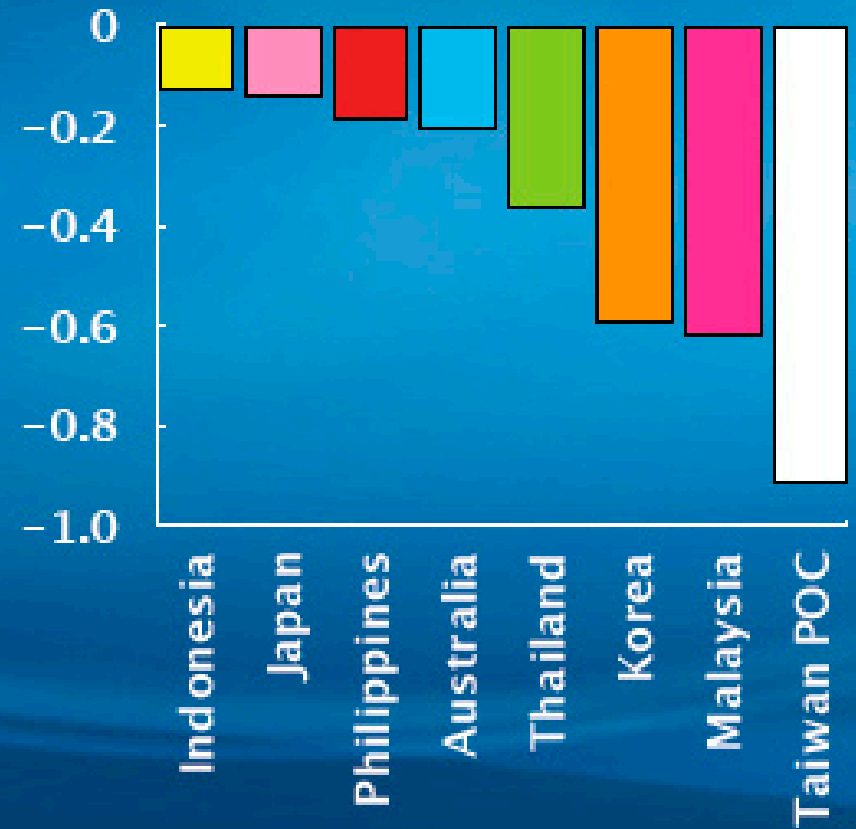
# Major downside risks: Escalation of the Euro area crisis and renewed China slowdown...

Near-term Challenges

## Euro Area Downside Scenario (GDP growth; percentage deviation from baseline)



## China Investment Slowdown (1 pct point): Impact on Growth (in percentage points)

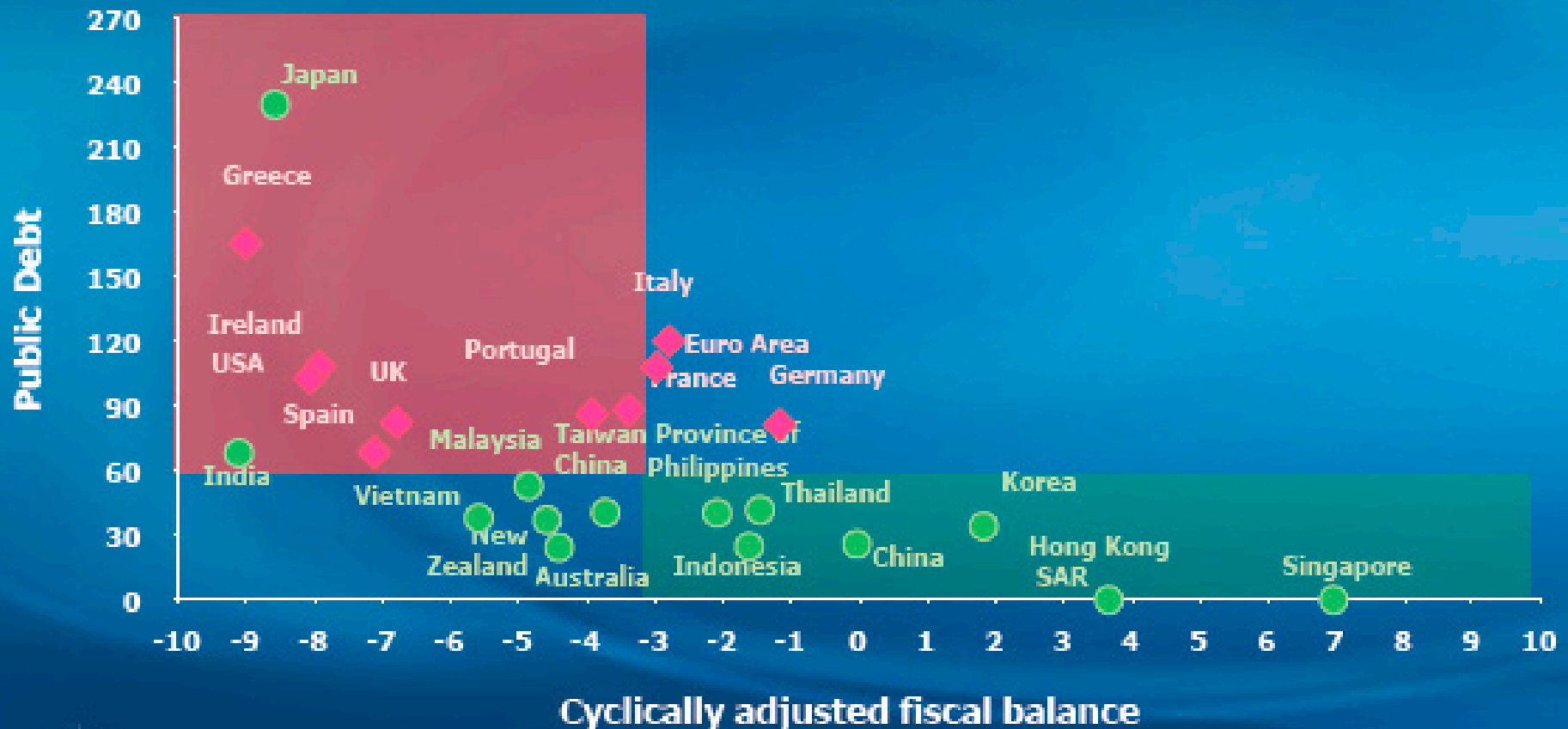


Source: IMF staff estimates.

# Fiscal Policy: Need to maintain fiscal space, but room to cushion new external shocks

Near-term Challenges

## Cyclically Adjusted Fiscal Balance versus Public Debt (In percent of GDP, 2011)

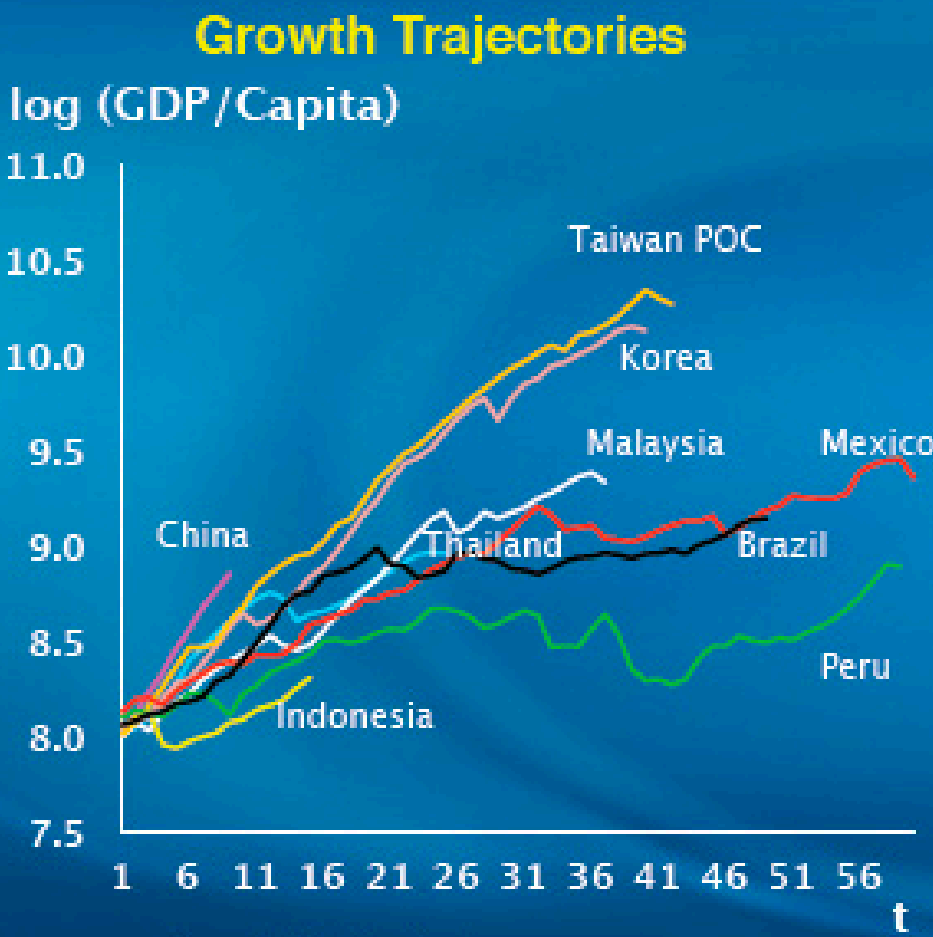


Source: IMF, World Economic Outlook.



# Broader challenges: Avoiding middle-income trap, and achieving inclusive growth.

Medium Term Challenges



Source: IMF staff estimates.  
 Note: t=0 is defined as the year when the GDP/capita for a particular country reached US\$ 3000 in PPP terms.

Sources: World Bank, World Development Indicators, PovCal database; OECD; IMF staff calculations.





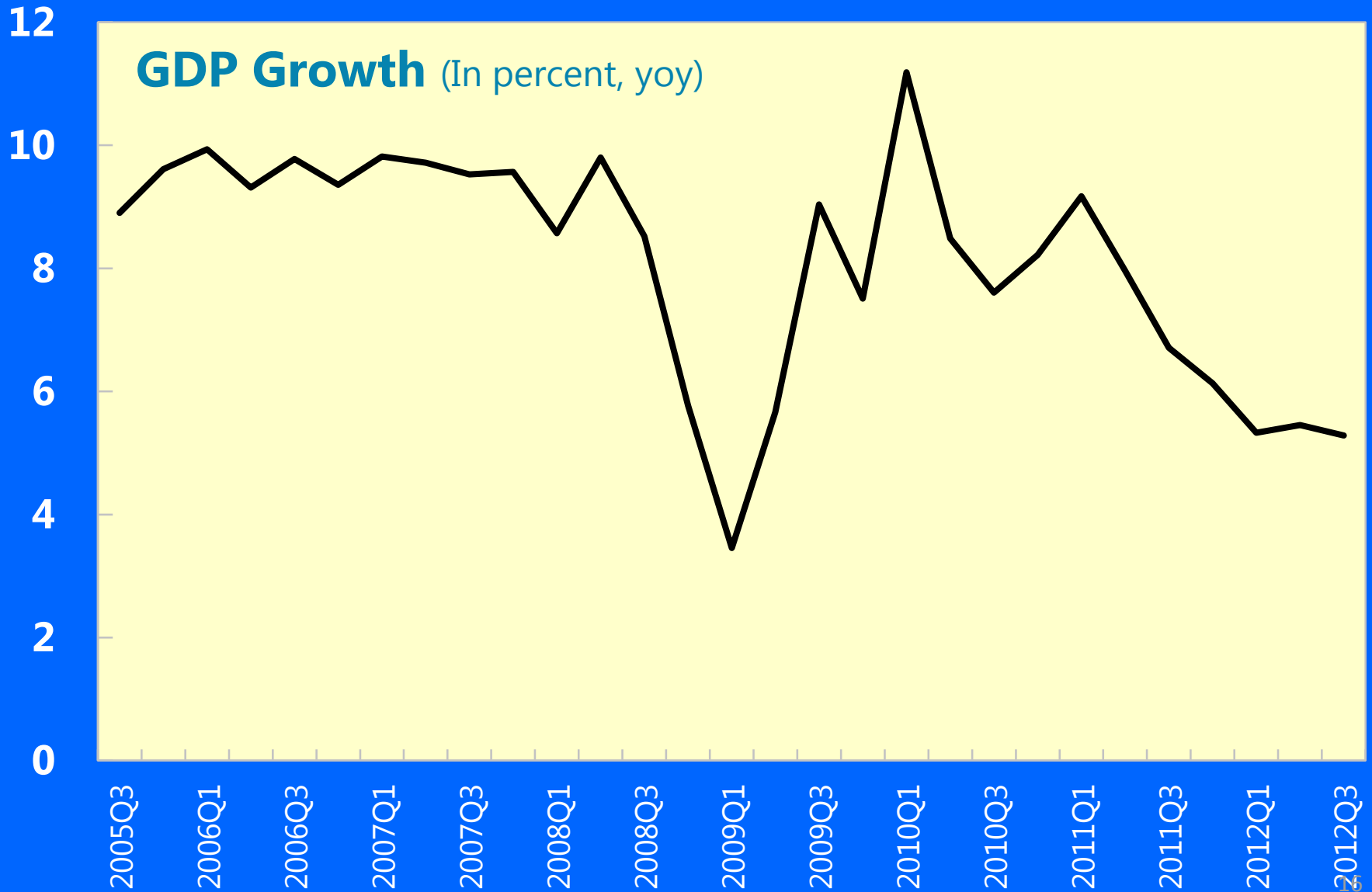
# India Outlook

# *India's economy to witness subdued growth in 2013...*

## Growth Outlook

- **The growth slowdown has become generalized and has led to large downward revisions in projections.**

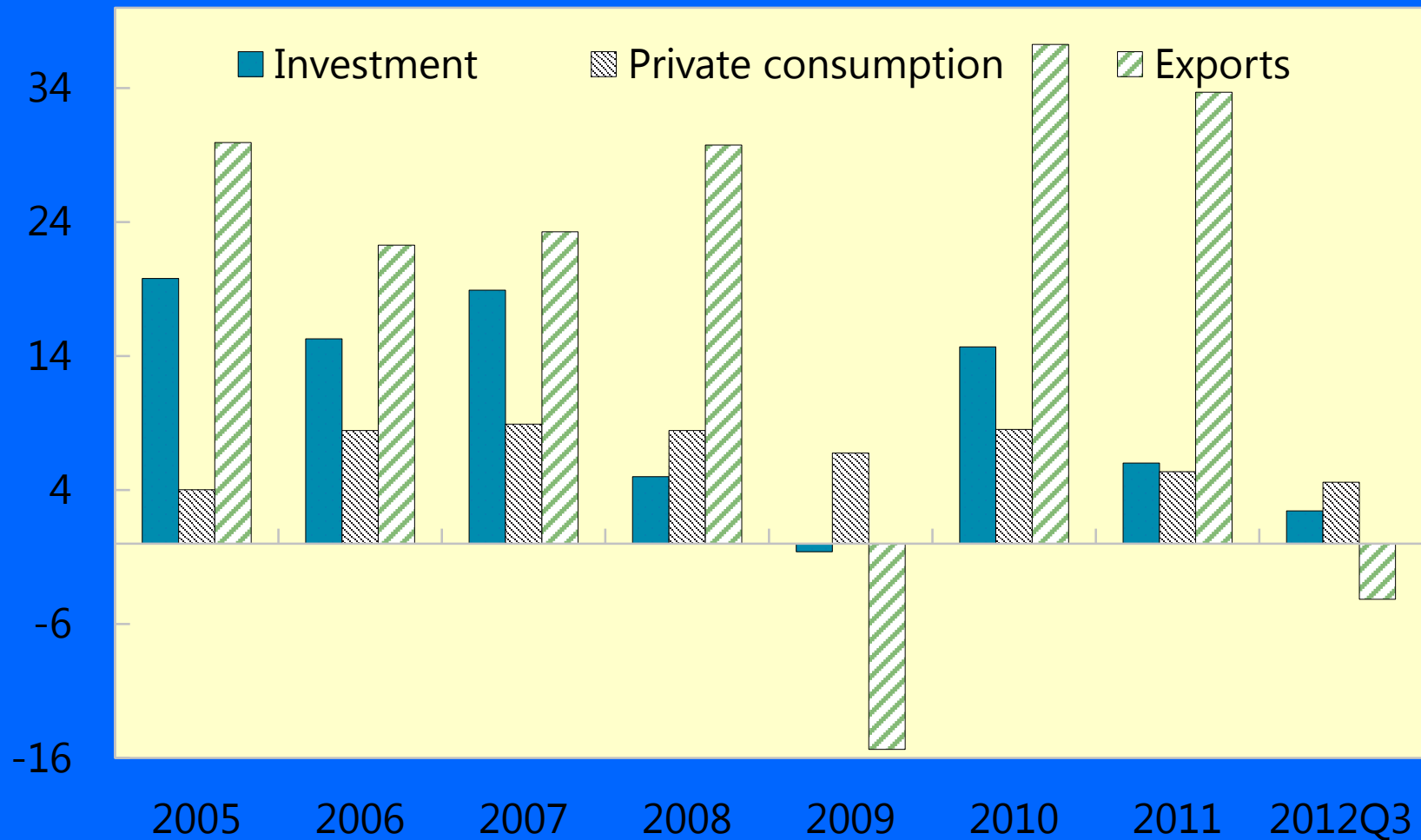
# *India's growth has decelerated sharply over the past year and half*



*What started as an investment slump has become a generalized slowdown.*

## Demand Components of GDP

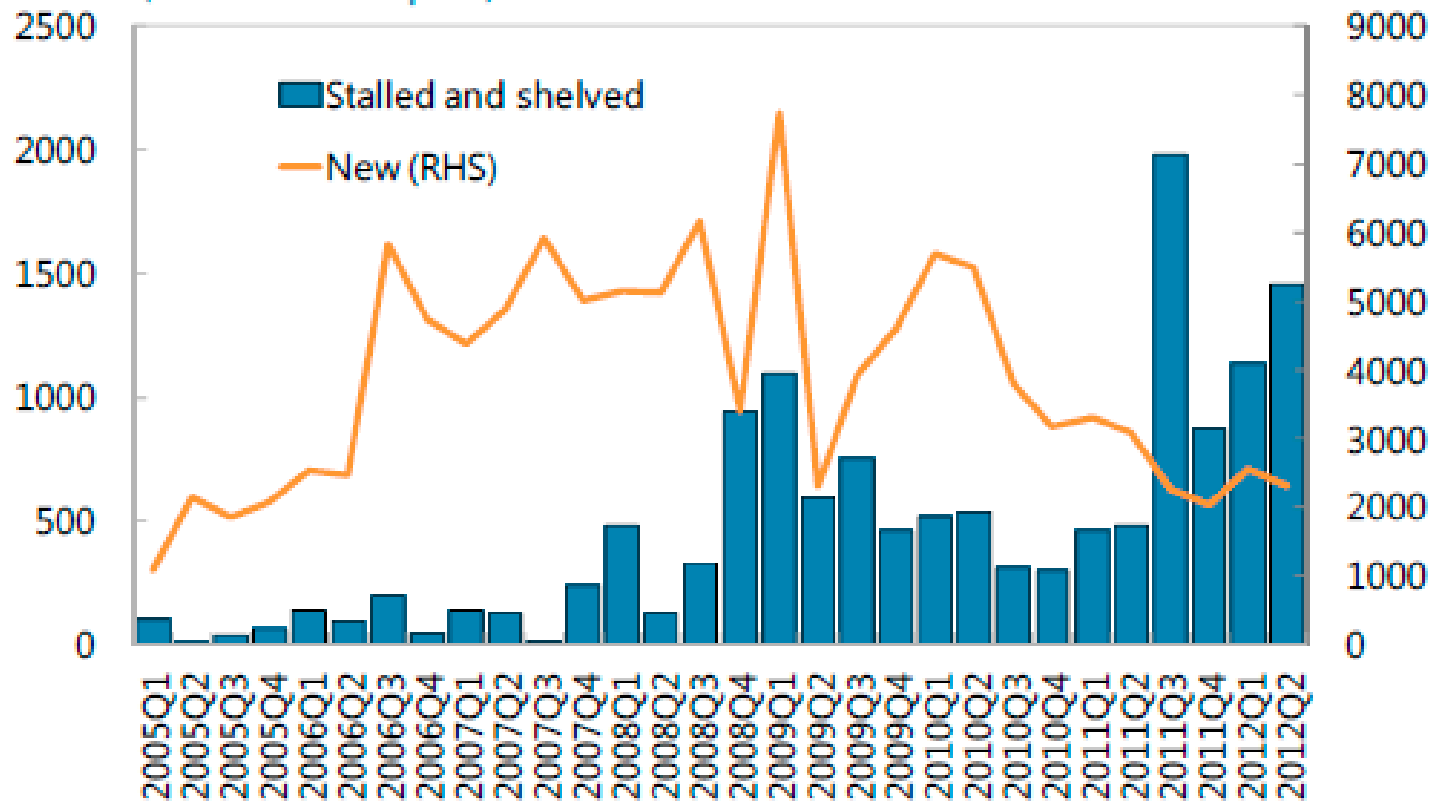
(In percent, yoy)



# *New investment project are sharply down and many projects are stalled or being shelved*

## Investment

(In billions of Rupees)



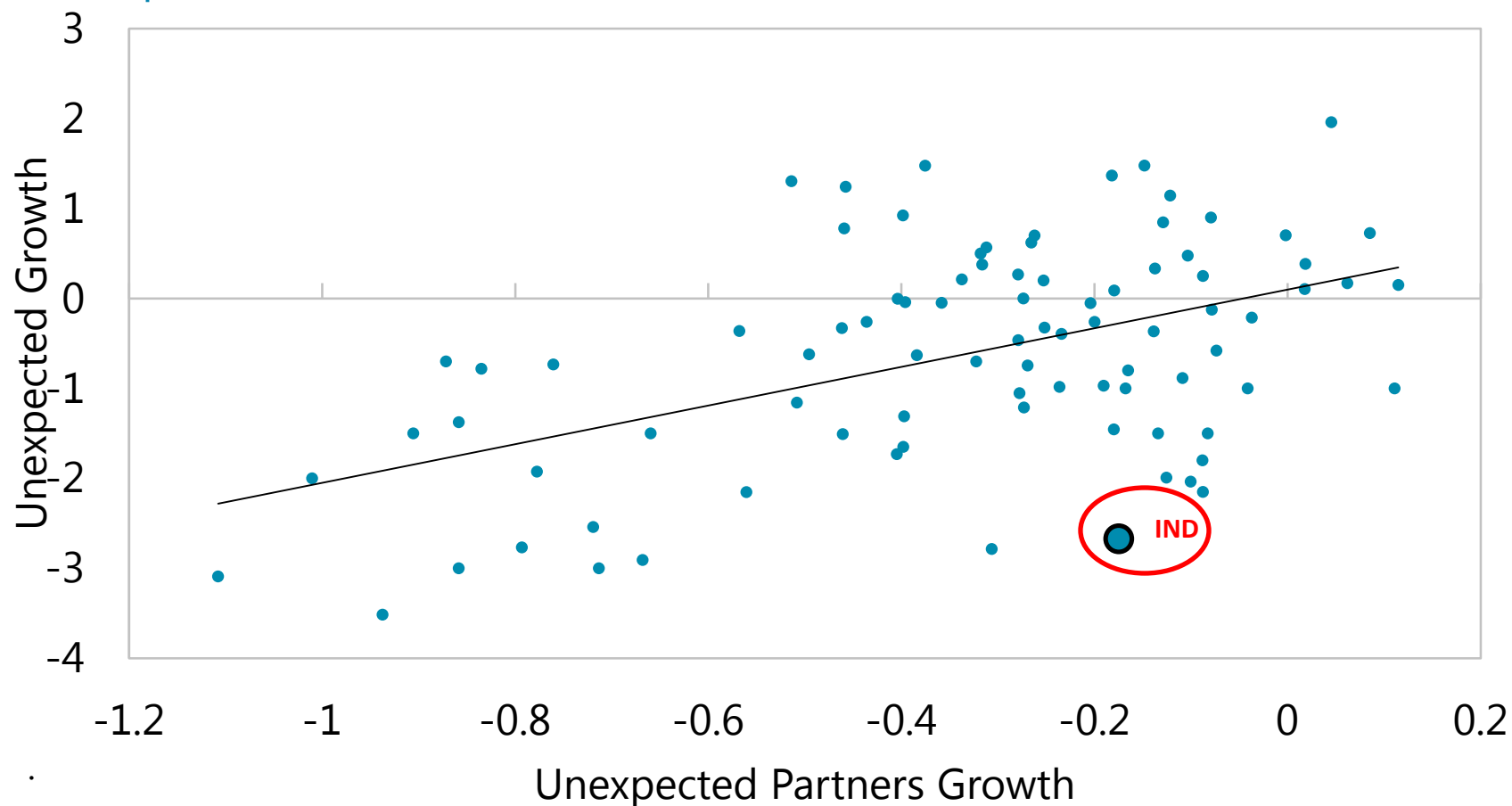
Source: CMIE.



***GDP growth has slowed more than external factors can explain.***

## **The 2012 Slowdown: More than External Spillover**

(In percent)



# *Inflation to remain elevated ...*

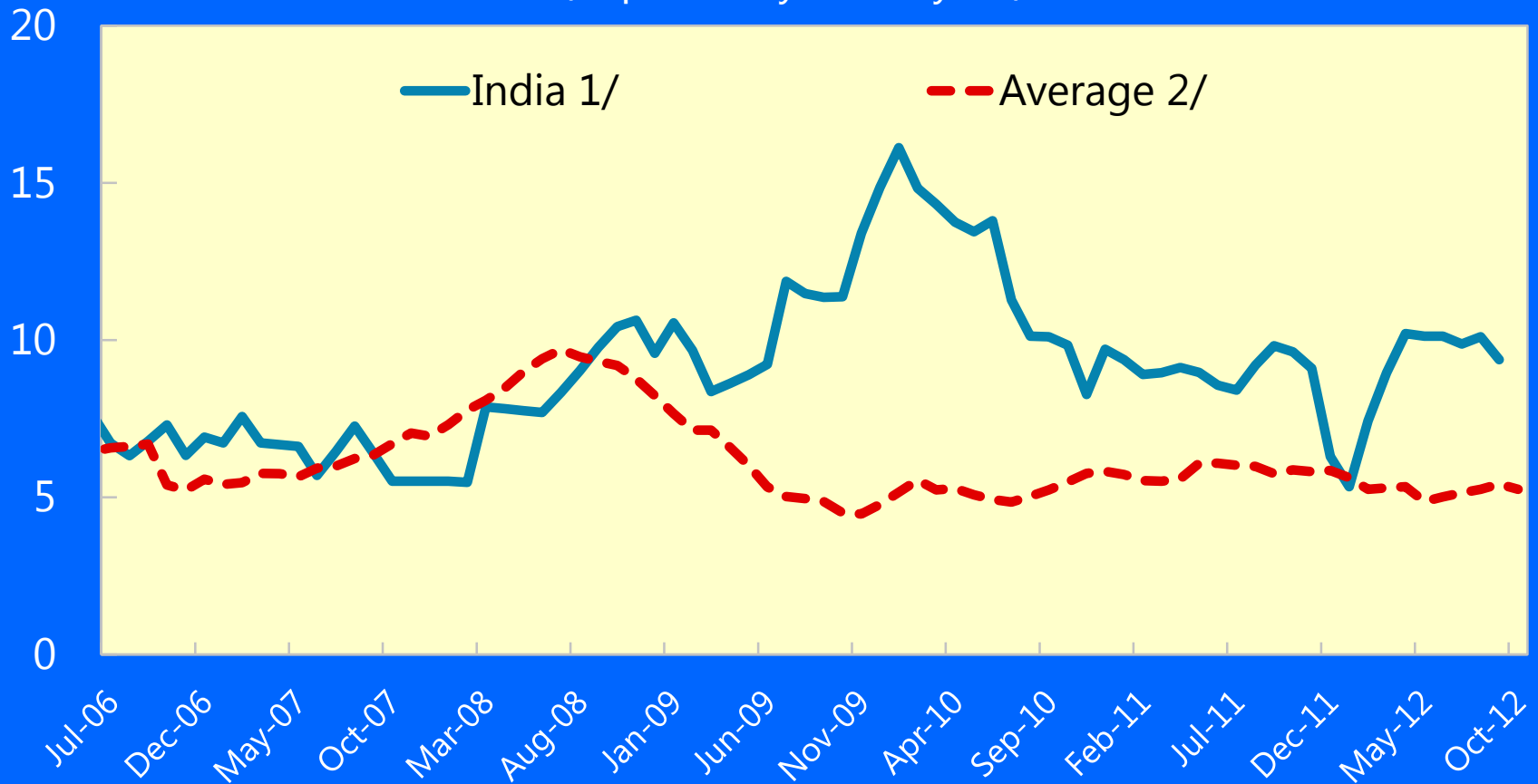
## Inflation Outlook

- **Inflation pressures have moderated, but remain substantial**

# *Inflation remains well above the average of other emerging market economies*

## **Inflation**

(In percent year on year)



Sources: Haver Analytics and staff calculations

1/CPI Industrial Workers

2/ Brazil, Russia, China, South Africa, Indonesia, Turkey, Mexico

# *Banking sector is under some stress...*

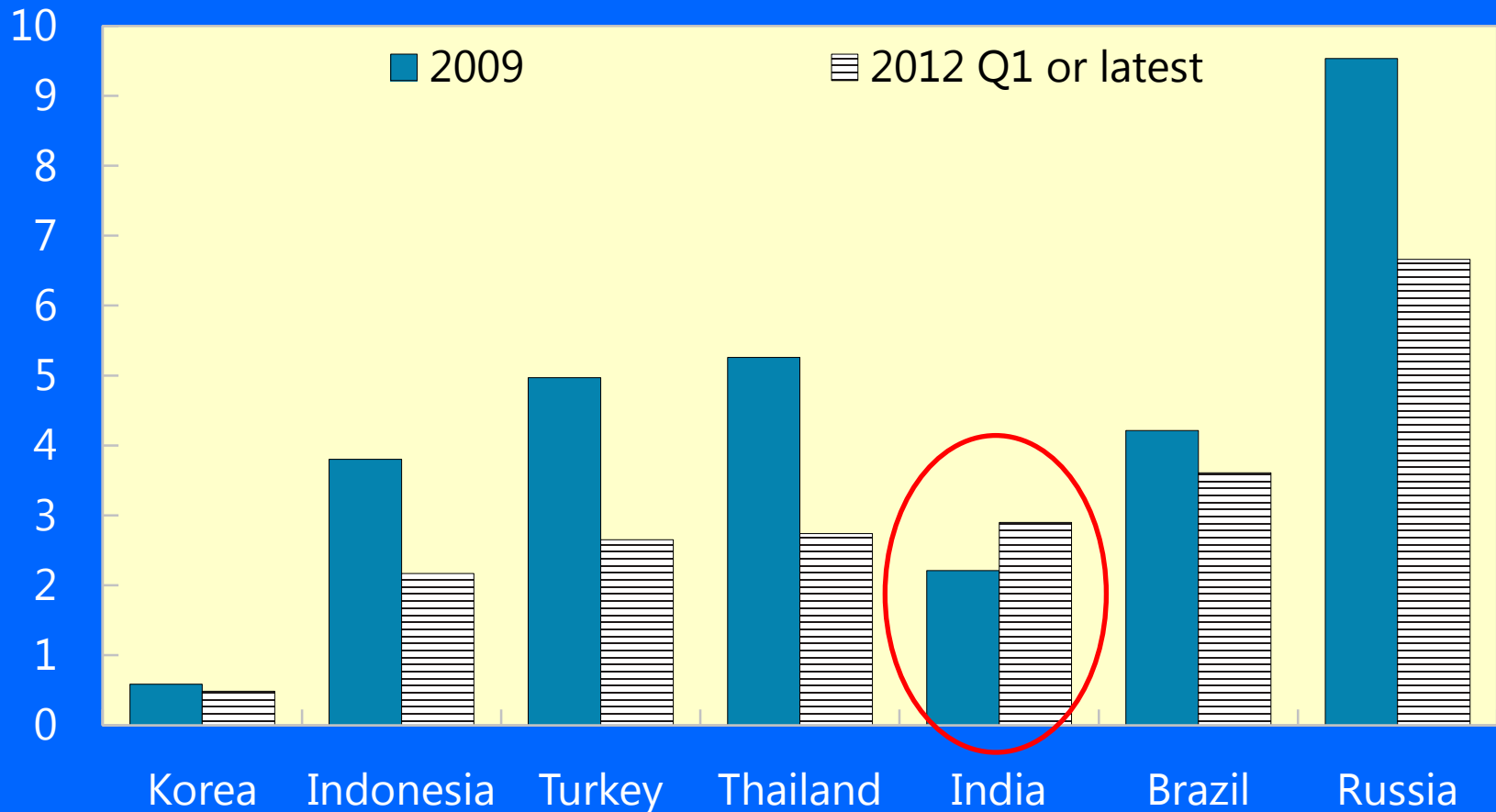
## Banking Sector Outlook

- **The banking system has seen a significant deterioration in asset quality, with public banks underperforming private banks.**

*... resulting in a deterioration of asset quality*

## Non Performing Loans

(In percent to total gross loans)



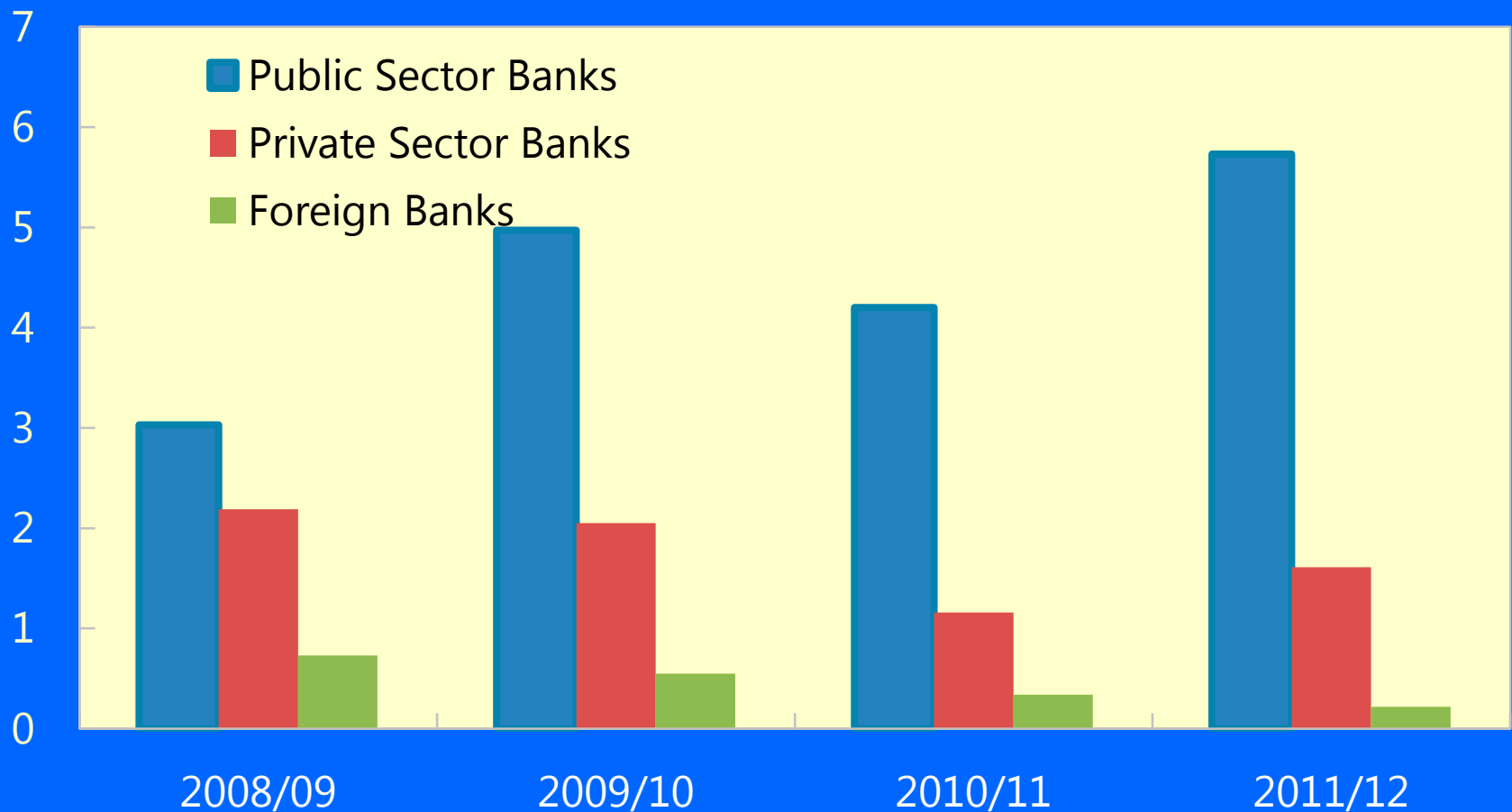
Sources: IMF, Financial Soundness Indicators; Country authorities; and CEIC Data Company.



# *Restructured loans have risen sharply, especially in PSU banks*

## Outstanding Restructured Advances

(In percent of gross advances)



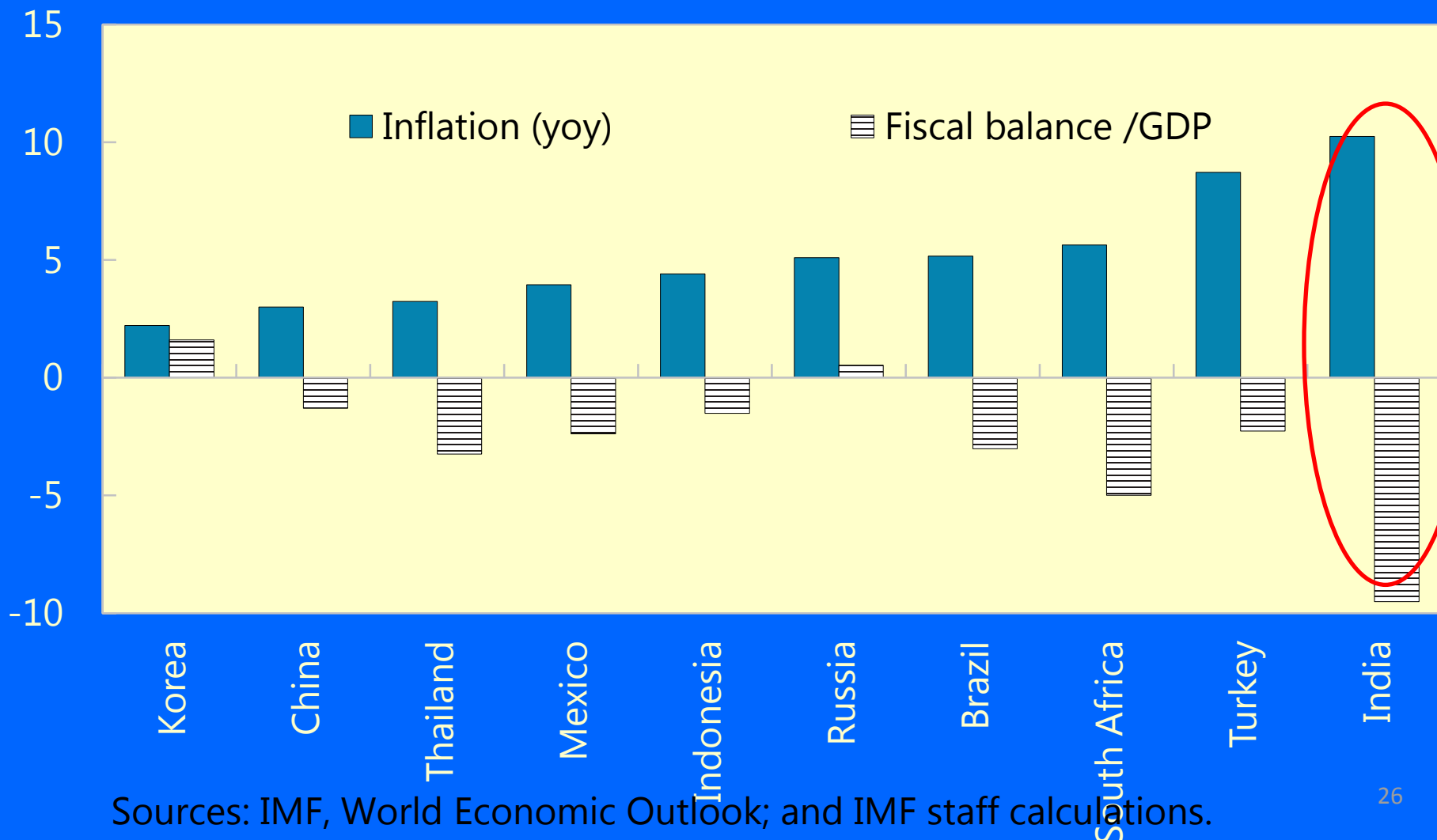
*Fiscal space to remain limited over near term...*

Fiscal  
Sector  
Outlook

- **The post-crisis fiscal consolidation came to a halt, but may now be picking up**

# India's fiscal deficits are large compared to other EMs

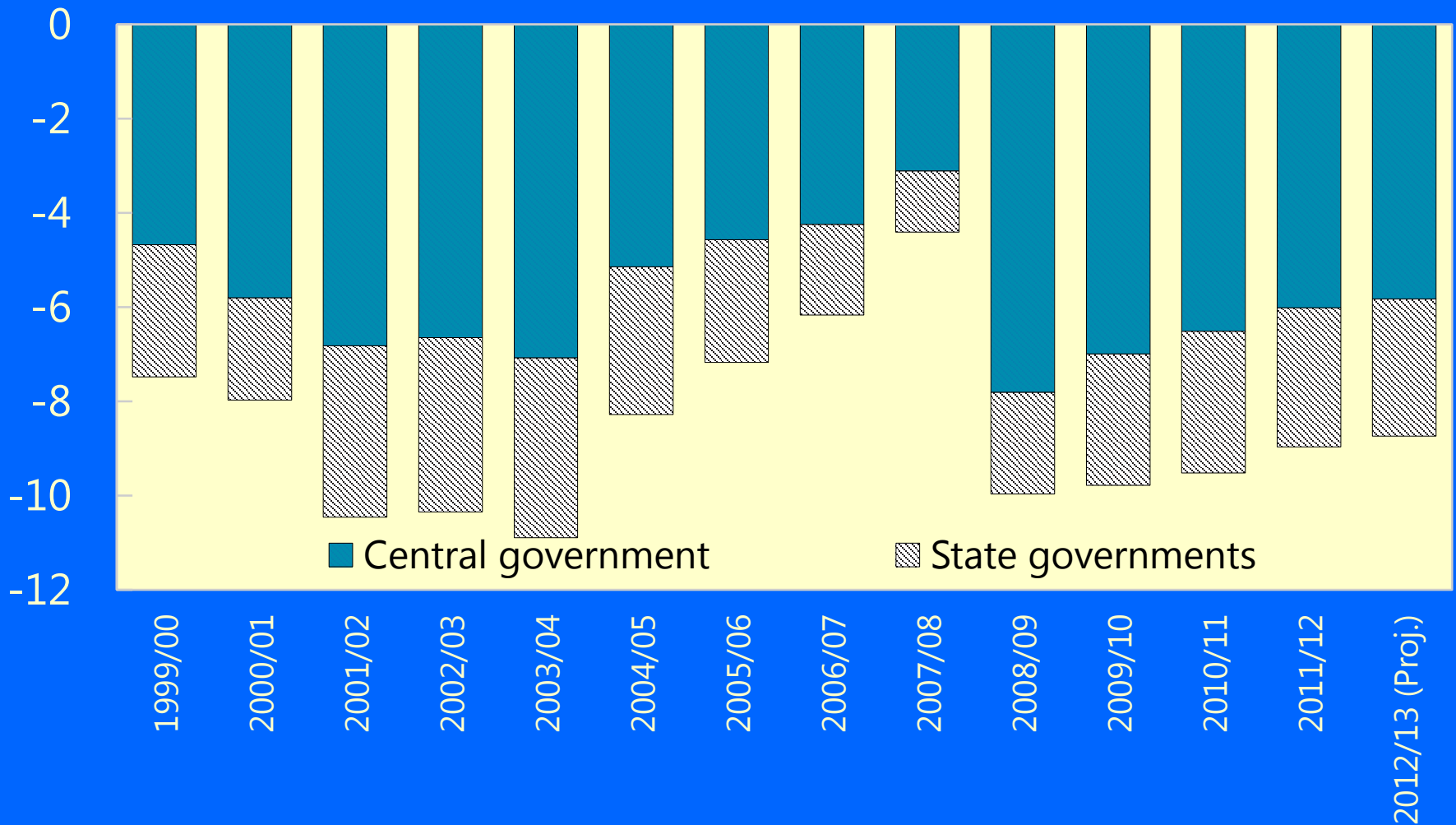
## Inflation and Fiscal Balance, 2012 (In percent)



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

*The budget deficit has been falling only slowly since the global financial crisis.*

## Government Balance (In percent of GDP) 1/

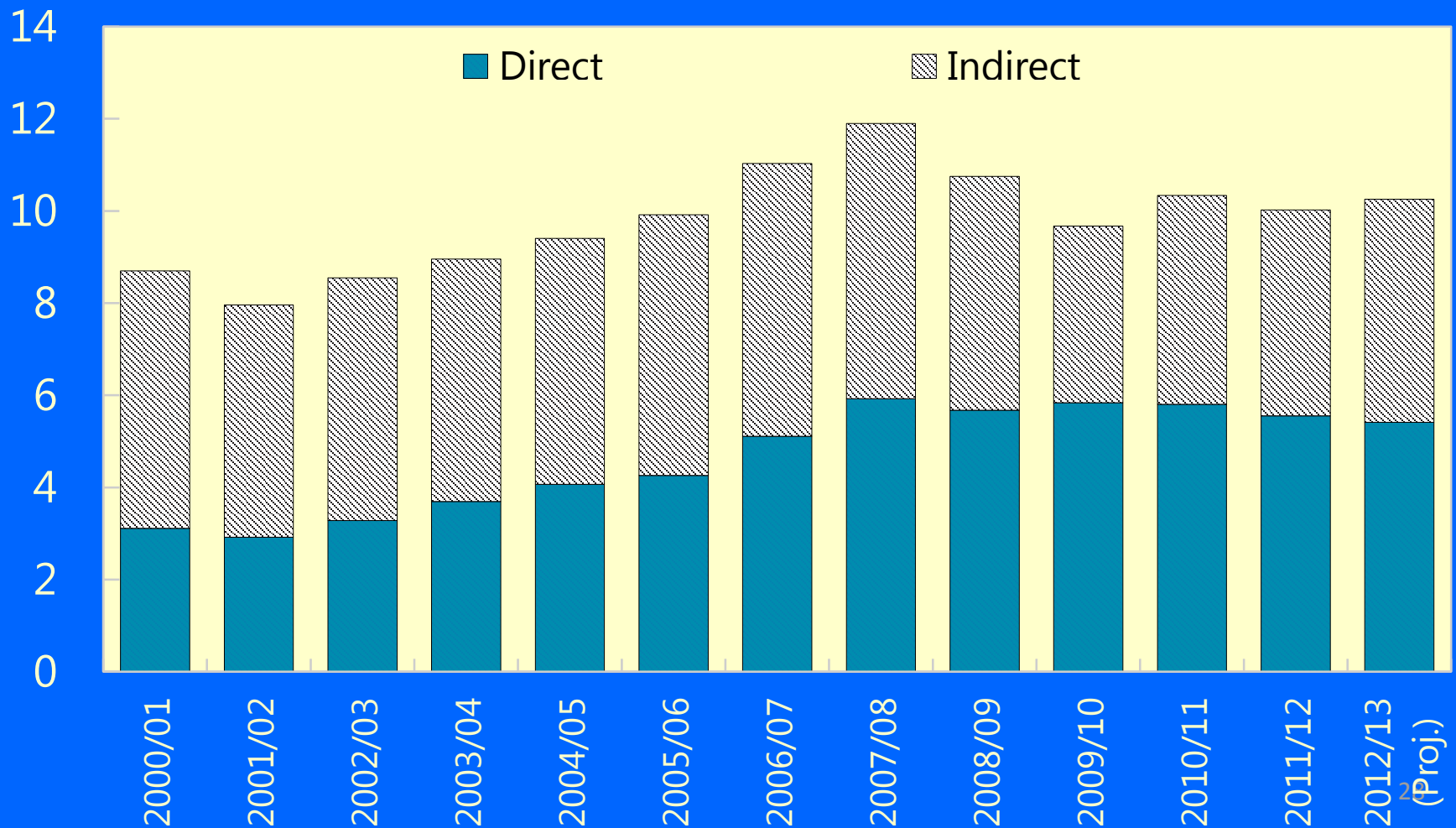


1/ Includes subsidy-related bond issuance.

*Tax revenue remains below levels reached before the global financial crisis.*

## Central Government Revenue

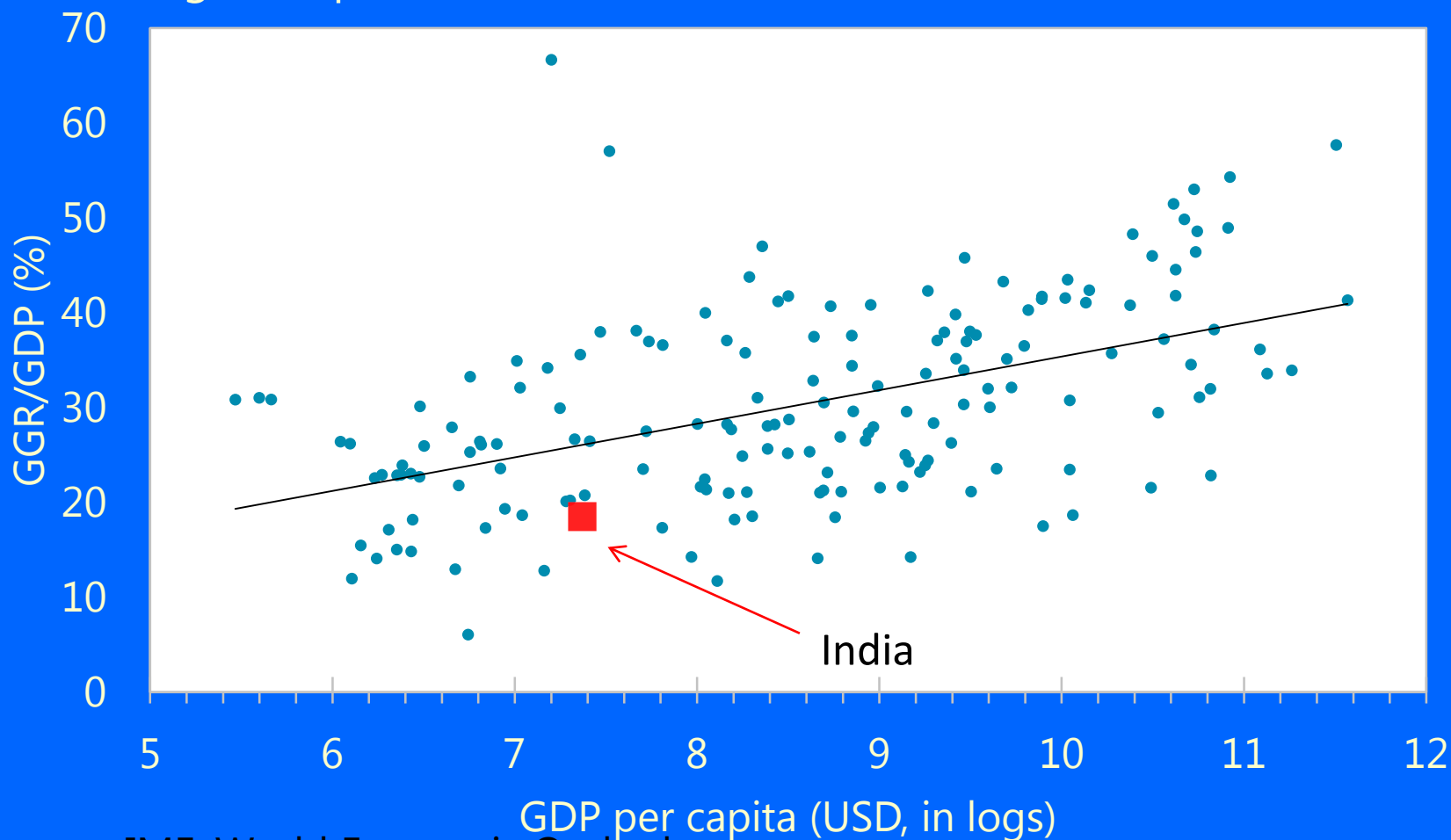
(In percent of GDP)



# Cross-country comparison: India's fiscal revenue is on the low side

## General Government Revenue and GDP per capita, 2012

(excluding oil exporters and microstates)



# *External vulnerability has increased...*

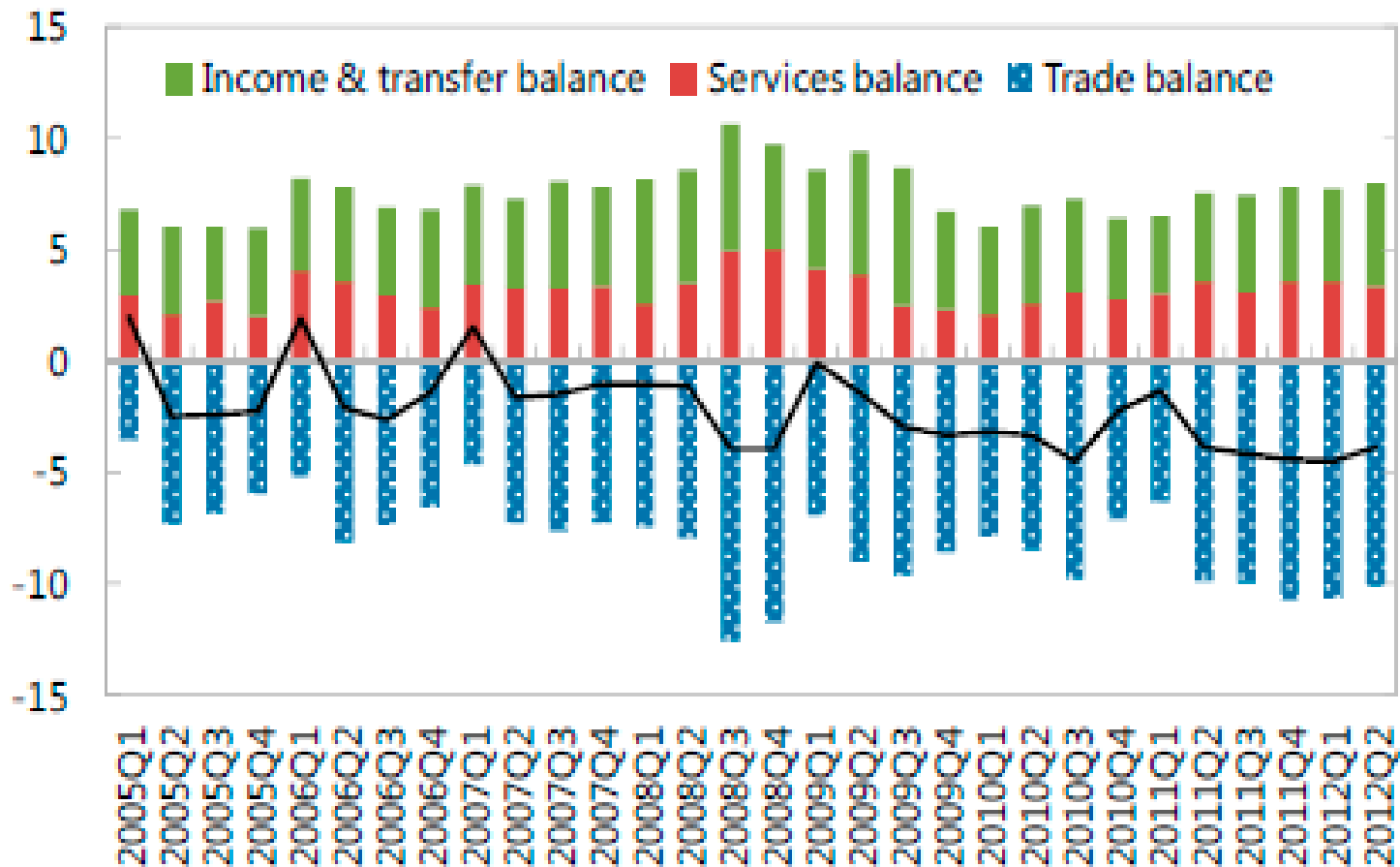
## External Sector Outlook

- **The current account deficit widened on the back of a rising trade deficit**

# The current account deficit has widened, but remains manageable

## Current Account Balance

(In percent of GDP)

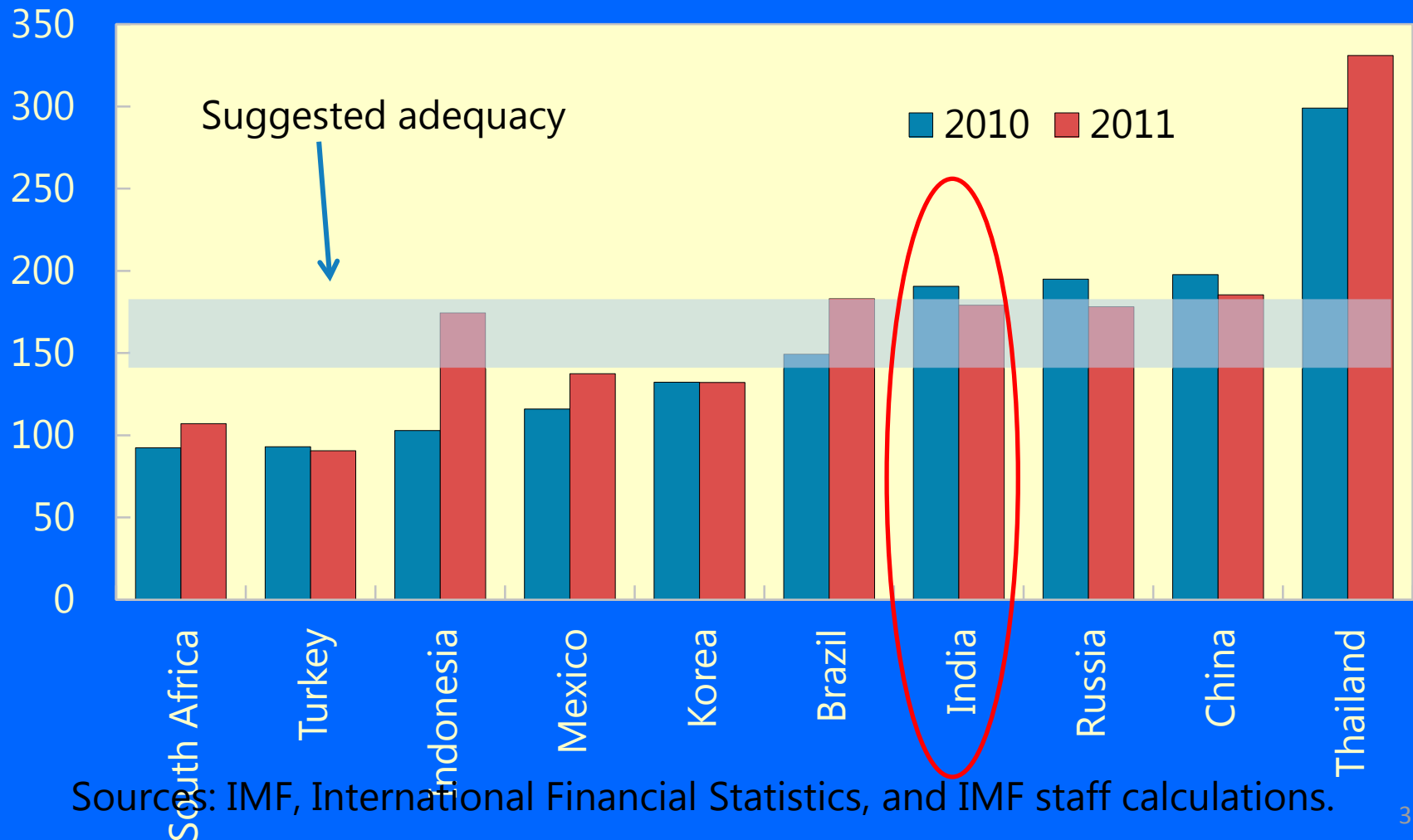




# Although RBI's reserve coverage is adequate...

## Estimated Reserve Adequacy

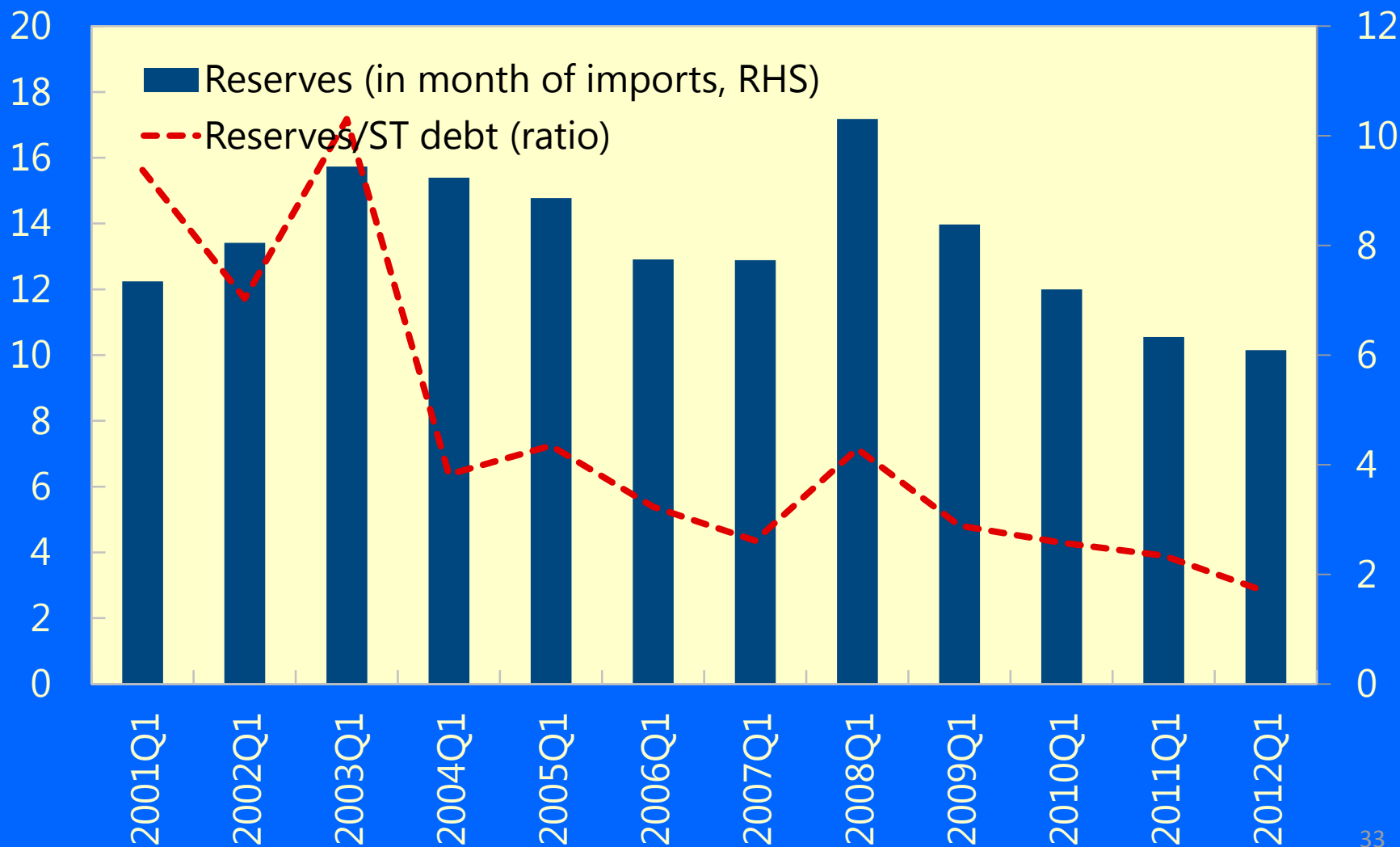
(Official reserves as a percent of IMF country-specific metric)



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

*...it has deteriorated somewhat in recent years*

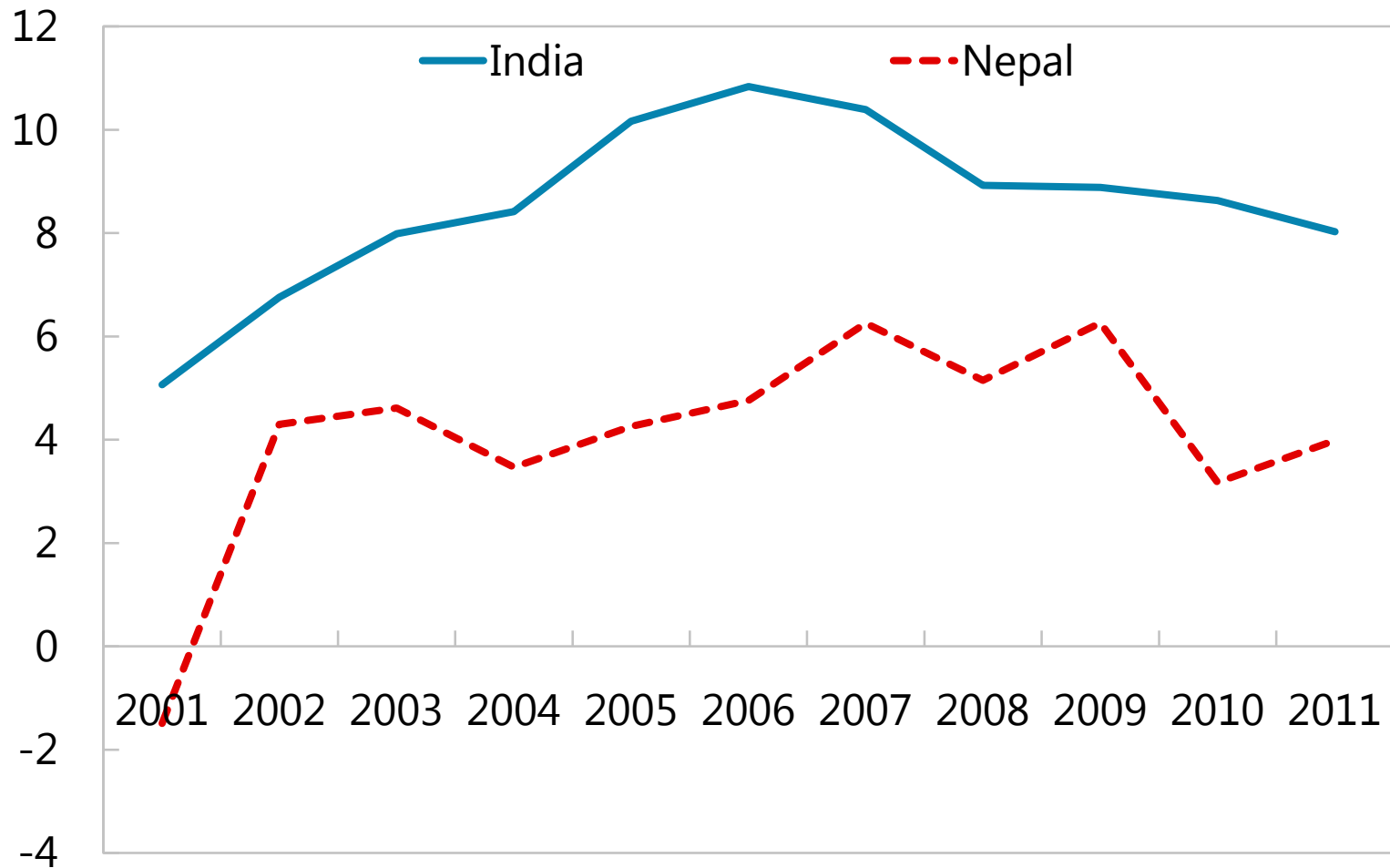
## India: Reserve Coverage



# Nepal Outlook

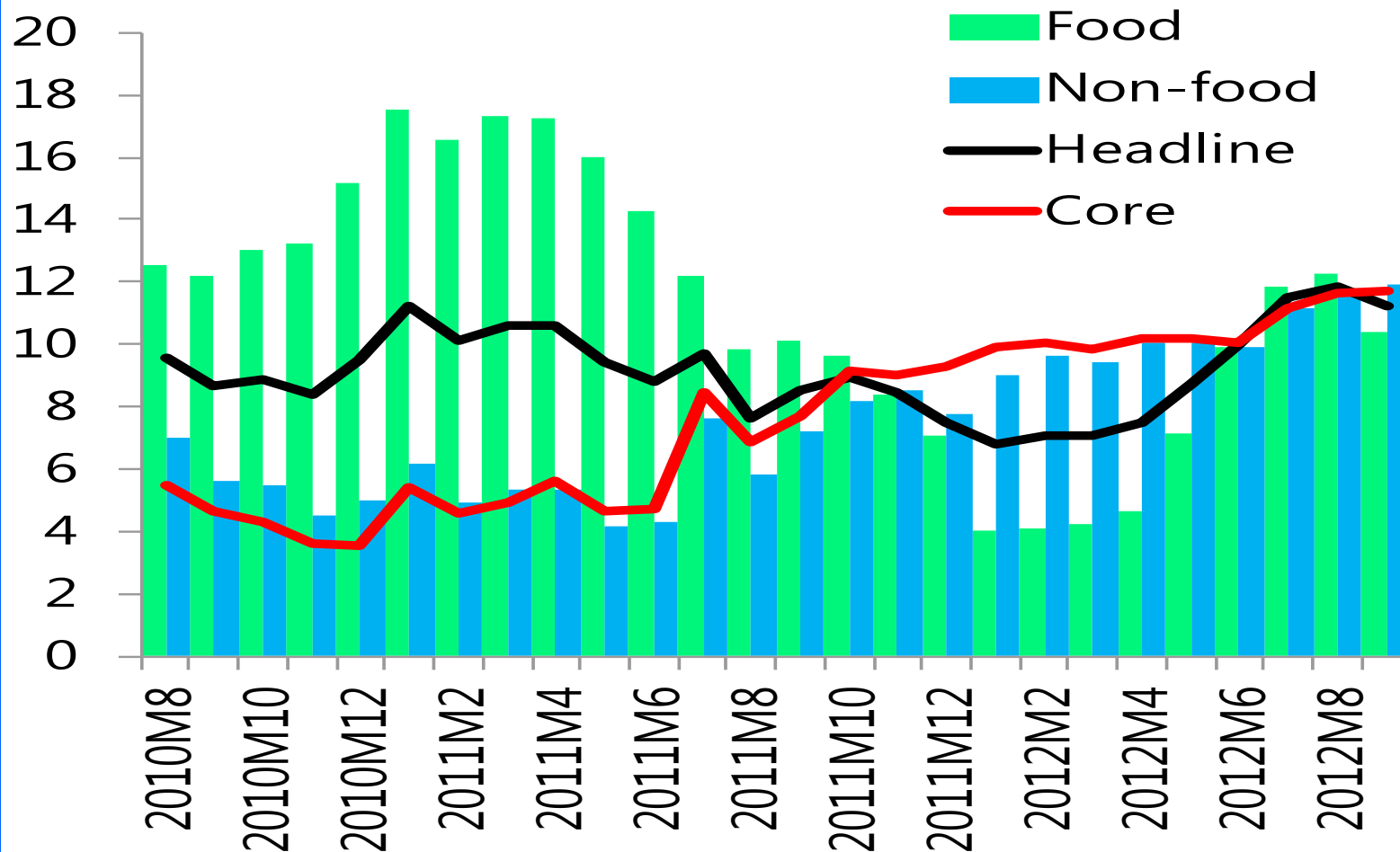
# Growth is linked to (but below) that in India

**India and Nepal: Nonagricultural GDP Growth**  
(in percent)



# But inflation remains a concern

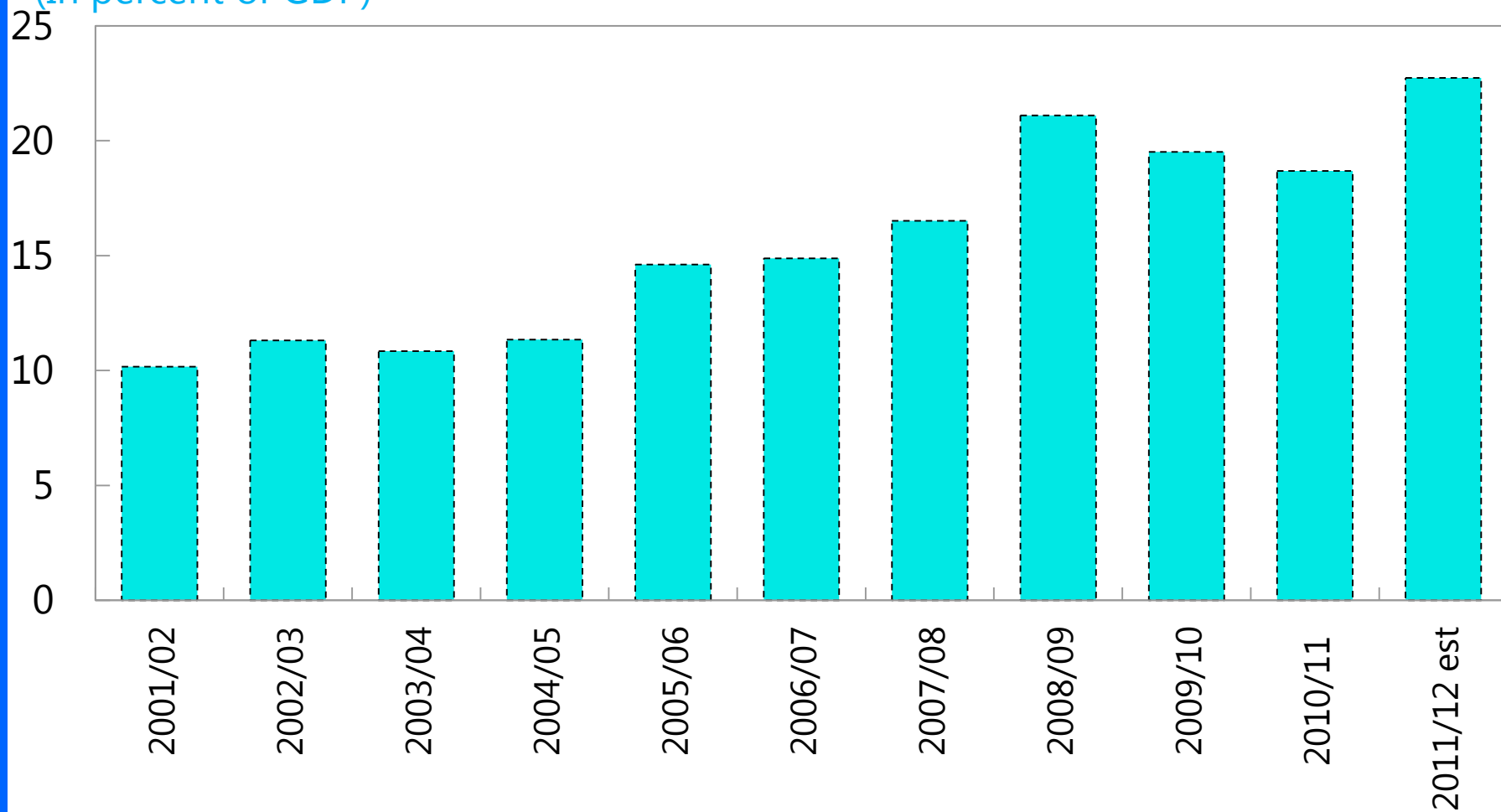
## Inflation (Year-on-year percent change)



# Remittances—export of labor—bolster the BoP

## Remittances

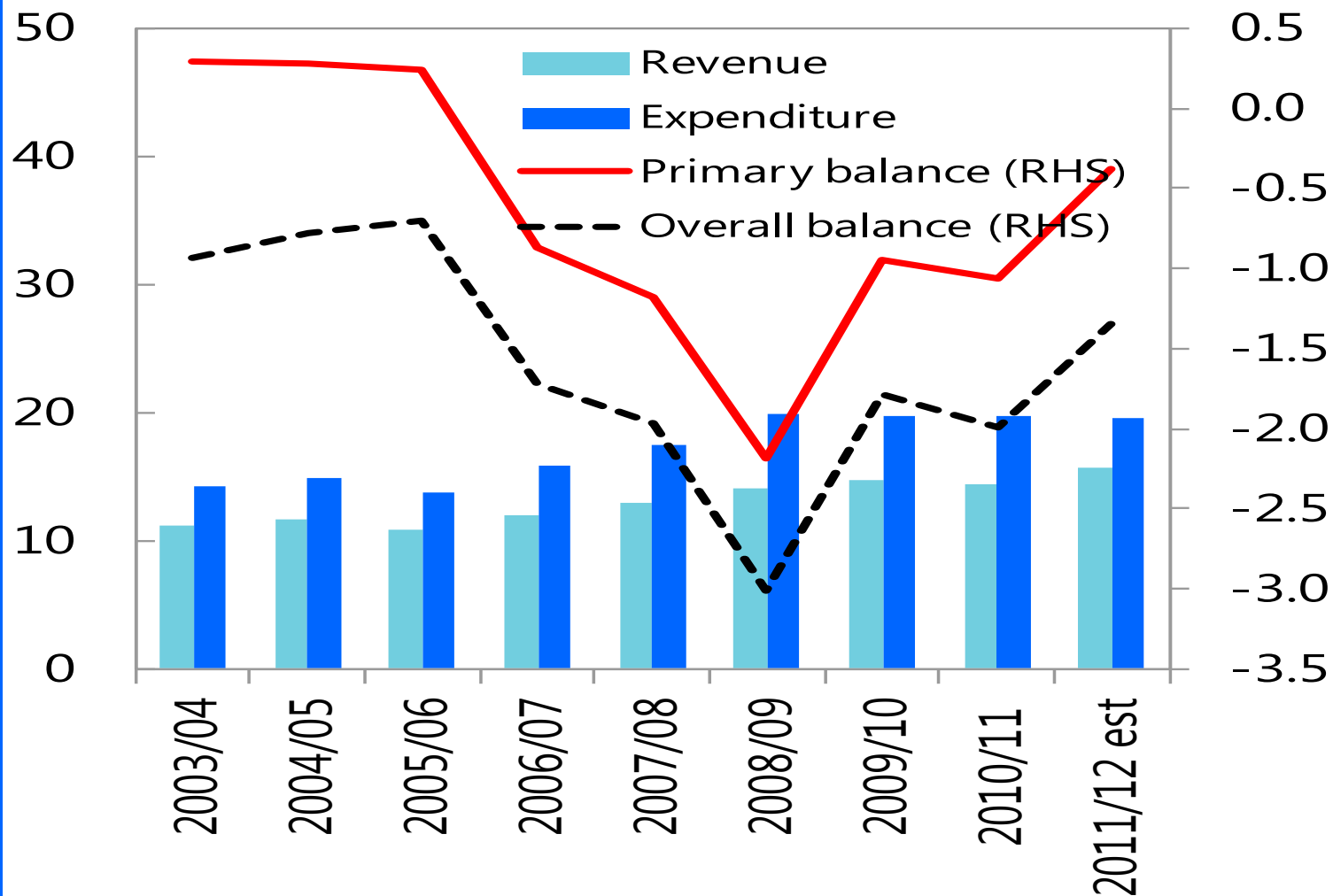
(In percent of GDP)



# Fiscal deficit “over-performance” is a problem

## Revenue and Expenditure

(In percent of GDP)



# Outlook for Nepal

- **GDP growth is likely to decline further**
  - Agriculture (poor monsoon)
  - Global economic uncertainty
  - Fiscal “cliff” is a drag on growth
- **Inflation to remain elevated**
  - Spillover from India
- **Current account to weaken**
  - Outflow of workers is slowing, so remittances could fall
  - Imports seem to be recovering



# Policy Messages for Nepal

- Need proper full-year budget (avoid “fiscal cliff”)
- Structural reforms needed:
  - Mounting quasi-fiscal liabilities (NOC)
  - Weak capital spending (will need to catch up)
  - Interest rate differential with India and rising inflation limit monetary policy
  - Strengthen business climate to promote investment
- Addressing financial sector vulnerability is key
  - Strengthen Anti-Money Laundering (AML) regime

Thank you



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