

**“India and the International Financial System: An Economic Policy Outlook”:**  
**A Discussion with Dr. Arvind Virmani**

December 3, 2009

On Monday 22nd February, Dr. Arvind Virmani, Executive Director of the IMF presented his research and personal views on India’s position in the global economic order.

**The Future Global Economic Order**

Dr. Virmani began by forecasting a significant change in the global order, caused by the economic rise of China and India. According to him by 2050, a tripolar world comprising of the US, China and India would emerge. Dr. Virmani’s power projections were based on his calculations of the relative economic strength of each country. His latest forecasts estimated that India’s GDP would equal that of the US’s in 2035 in PPP terms, while China would catch up to the US in 10 years. However, he cautioned that the exact timing was subject to change, given the uncertainty of world events.

**The Current Global Economic Order**

At present however, he stated that the global economic order was in a period of confusion. The US retained its monopoly power, but was surrounded by a competitive fringe of emerging economies. In his view, in the next 20 years this so called congestion would ‘break out’ leading to a more polarized world, with a clearer economic order. This transformation is what we needed to be aware of, given its impact on the rules relating to the governance of global institutions.

**The Three Economic Shocks and the US**

Dr. Virmani outlined three economic shocks, which occurred in the last 10 years and strongly influenced his current economic power projections, namely the boom-and-bust of oil prices (Russia’s economic revival), the global financial crises and the large UN 2005 revision of data on GDP-PPP. He expected that as a result of these shocks, the US’s economic power would contract in the future. In particular the financial crisis would enlarge the US’s already massive fiscal deficit, hurting its economy. In addition, he argued the US’s status as a democracy would constrain the amount of power it could wield, as it would be expected to act responsibly.

**India, China and Post Financial Crisis World**

According to Dr. Virmani, the post financial crisis global economy would be characterized by lower GDP growth and trade for some time to come. However, in comparison India would be less affected by the slowdown due to its export neutral nature. He notes that reforms in India were enacted deliberately slowly to maintain this export neutrality, which India has benefitted from this as its recovery process demonstrates.

On the other hand China’s strong export orientation model, or what he liked to refer to as the ‘Chinese export machine’ had hurt growth in recent times. Consequently, he forecasted the difference in ‘relative’ growth rate between China and India narrowing considerably in the next 10-15 years. However, Dr. Virmani expressed an appreciation for China’s overall economic policies. For example, he found bringing in public sector control and spending and using Foreign Direct Investment to stimulate entrepreneurial activities, extremely beneficial. Dr. Virmani also

predicted that the other two BRIC countries, Russia and Brazil would continue to grow because of consistently high oil and gas prices and rich a natural resource endowment respectively.

### **Securing India's Future in the Global Economic Order**

Dr. Virmani strongly felt that India must participate in the 'changing of the rules' at the global level. This would help it secure more power, which he defined as a 'relative concept' that was embedded in the influence an entity had in the governance of institutions. He acknowledged that at present India had a 'weak bargaining position' in the world, which is why it could realistically only focus on pushing for reform as opposed to circumventing or dictating to global organizations. Other strategies he advocated to secure power included becoming an integral part of the global terror strategy and participating more fully in the new technology regime.

Dr. Virmani highlighted that another major challenge, critical for securing power for India would be sustaining growth. When questioned about how India should go about doing this, he responded by stating that it would require embracing economic reforms that would adjust to shocks. He cautioned that there would be many barriers to implementing a fresh set of reforms, given India's strong history of coalition politics and infrastructure constraints. However with respect to governance he saw positive signs with recent developments in Bihar and the change in the leadership of the Home Ministry.

### **Conclusion**

In his closing remarks he emphasized that while another crisis may call for more adjustments in his forecasts, the underlying trend or the 'big picture,' was robust and clear: China and India were catching up to the US at a relatively fast pace and the US needed to be mindful of this trend.