Policy Frameworks for Economic Resilience: The case of Emerging Markets and India[1]

(Address by Dr. Poonam Gupta, Deputy Governor, Reserve Bank of India - October 29, 2025 - Delivered at the Business Standard BFSI Insight Summit, Mumbai)

It is a pleasure for me to be here at the Business Standard BFSI Insight Summit. I would like to thank the organisers for this opportunity.

2. In my brief comments, I will be reflecting on the observed economic and financial resilience of emerging markets (EMs) in general, and of the Indian economy, in particular. In this context, it may be noted that at the recently concluded Annual Meetings of the IMF, two contradictory themes prevailed: the unprecedented global policy uncertainty; and the surprising resilience of the economies.[2]

3. The global economy has shown remarkable resilience to the shifting trade policies and geopolitical tensions. Global growth has held up better than anticipated earlier. Currently, inflation outlooks are mostly benign across countries (notwithstanding the fact that inflation levels in some advanced economies are somewhat higher than their respective targets). Low inflation has provided the headroom for monetary policies to be eased across jurisdictions. Banking sectors across countries are mostly resilient.[3]

4. IMF has suggested a few factors that are contributing to this resilience.[4] These include improved policy frameworks in EMs; the tariff outcomes being milder than what were anticipated earlier; and very limited retaliation by the partner countries.[5] In other words, the policy making frameworks in EMs are to be credited for their own economic resilience, as well as for the resilience in the global economy. The key questions of

[1] Inputs received from Asish Thomas George, GV Nadhanael, and Somnath Sharma, and comments received from Indranil Bhattacharya, Anupam Prakash, Sunil Kumar, Sangita Misra and Satyashiba Panigrahi are gratefully acknowledged.

[2] We are focusing here more on EMs, not on advanced economies or low-income economies which have their own unique economic features, potentials and challenges.

[3] IMF and other multilateral agencies have also been pointing to the various risks that loom on the horizon. They refer to buoyant equity markets (particularly led by technology stocks) leading to worries that a correction could be in the offing. Central banks of advanced economies are concerned about elevated public debt in their respective economies and worry that there might be a disruptive resolution. The financial landscape has undergone significant change over the years, with non-bank financial intermediaries (NBFIs) now playing a larger role in several markets, including the bond and credit markets. The growing size, complexity, and interconnectedness of these lightly regulated NBFIs in the financial system has raised financial stability concerns.

[4] World Economic Outlook, October 2025.

[5] Adaptability and entrepreneurship of the private sector and supportive financial conditions are the other factors.

interest, therefore, are: What has made this resilience of EMs possible? Is it here to stay? How well has India done on its policy frameworks and economic resilience?

How has the observed economic and financial resilience in EMs been achieved?

5. After completing my Master's in Economics at the Delhi School of Economics and teaching for two years at Delhi University, I joined graduate school in 1993. In my second year, I enrolled in a course on International Finance. The year was 1994 and a balance of payments crisis was unfolding in Mexico, which spread to Argentina and select other Latin American economies, with the risk of far-reaching contagion to many other countries and regions. Despite having witnessed the 1991 crisis at home, I did not have sufficient exposure to the literature on such crises at that time.

6. While taking this course, and subsequently while pursuing my own research in this area, I learnt more systematically about the pitfalls of unsustainable macroeconomic frameworks. These frameworks at that time consisted of: a fixed exchange rate regime which often resulted in appreciation and eroded competitiveness of the real exchange rate and large current account deficits. Premature and rapid liberalisation of the capital account and financial sector, resulting in excessive external borrowing, often in foreign currency (called the Original Sin)[6]. Lax fiscal policy and weak fiscal institutions, which combined with *ad hoc* monetary policy frameworks and limited independence of the central banks resulted in fiscal dominance and pronounced electoral-fiscal cycles, high inflation, and limited policy credibility.[7]

7. It became evident at that time that volatile capital flows, often triggered by external forces, could upend fragile equilibriums characterised by such macroeconomic frameworks. In fact, many more countries, which had such frameworks in place, experienced balance of payment crises in the following years. These included, Thailand, South Korea, Indonesia, Malaysia, and the Philippines during the Asian crisis of 1997-98; Brazil and Russia in 1998; and South Africa and Turkey in 2001.[8] It also became evident that these currency crises could even engulf the banking sector, resulting in "twin crises" with far graver implications.[9]

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[6] Eichengreen, B. J., Hausmann, R., & Panizza, U. (2002). Original sin: the pain, the mystery, and the road to redemption.

[7] I ended up writing two of the three papers in my PhD thesis on Twin Crises--when Balance of Payments and Banking Crises occur simultaneously and feed each other.

[8] These have alternatively been called Currency Crises, Balance of Payments Crises or Sudden Stops.

[9] Kaminsky, Graciela, L., and Carmen M. Reinhart. (1999). "The Twin Crises: The Causes of Banking and Balance-of-Payments Problems." American Economic Review 89 (3): 473–500.

8. In the ensuing years, extensive discussions, introspections, analyses, and research were undertaken within EMs as well as at the multilateral institutions. This culminated in a number of policy reforms undertaken by countries towards sounder macroeconomic management, as they learnt from each other, and were supported by the multilateral institutions.

9. Since early-mid 2000s, EMs have become more cautious in their approach towards the external sector. They have maintained a flexible exchange rate policy (mostly managed floats rather than free floats). They have reduced their liability dollarisation. They have slowed and recalibrated the pace and sequencing of capital account liberalisation. They have built up large foreign exchange reserves to act as a cushion against the adverse impact of external shocks to their balance of payments. In other words, they use their foreign exchange reserves to modulate large fluctuations in the exchange rate, or to meet the demand for foreign exchange emanating from a sudden shock to current account or reversal of capital flows.

10. In addition, they have strengthened their domestic macroeconomic policy frameworks by implementing credible fiscal rules, and have adopted a rule-based framework for monetary policy with inflation targeting or other close alternatives. They have strengthened their banking and financial sectors. Alongside, they have significantly enhanced the independence of their central banks.

11. As a result of these policy efforts, the world for the most part has not witnessed any country-specific or even regional Balance of Payments crises (barring a handful of exceptions) during the last two and a half decades.[10] This resilience has been markedly visible during the last five years when, EMs had to face multiple shocks in succession, such as the COVID-19 pandemic (2020-2021), Russia-Ukraine war (2022) and other geopolitical tensions, surge in inflation resulting in synchronised monetary tightening by Advanced Economy central banks (2022-2023), and the ongoing trade policy and tariff shocks (2025). The fact that EMs, by and large, are able to tide over these shocks with relative macroeconomic stability is a testament to the success of aforementioned policy efforts.

[10] Frontier markets are not similarly insulated, their policy frameworks not having been similarly evolved.

12. This is not to say that the EMs do not face policy challenges anymore. They do. But instead of macroeconomic stability issues, EMs face greater risks to sustained growth, and meaningful employment generation.

13. Their key challenge lies in finding the new sources of growth. In learning to live in a world in which trade as an engine of growth is faltering, and, therefore, domestic sources of growth need to play a larger role.

14. The acceleration in economic growth witnessed across EMs in 2000s was driven by a rapid expansion in global trade. The ratio of world trade to GDP increased from about 41 per cent in 1994 to 61 per cent in 2008.[11] Since the global financial crisis of 2008-09, however, the global trade to GDP ratio has flattened, reducing the avenues for EMs to grow faster by leveraging global demand.

15. More recently, a new threat to global trade has emerged from the increased incidence of protectionism. Apart from reducing the contribution of external demand to growth, these developments also reduce the impact of potential spillover benefits to domestic growth through channels such as technology transfer. Even as some of the trade relations will be rebuilt and others will evolve during the course of time, the years of hyper globalisation are unlikely to return anytime soon.

16. Neither is the manufacturing sector turning out to be a sure way to economic success (the potential of the manufacturing sector seems to have become limited due to the existing large players continuing to be market leaders).

17. Another challenge, especially for those economies where demography is still favourable, is that under employment remains high, gender gaps remain wide, and a large share of workers remain in less productive informal jobs.

18. For some of the EMs, high public debt is also of concern. Many EMs undertook fiscal consolidation after they were hit by the crises in the 1990s. However, after the global financial crisis, public debt has risen steadily, exacerbated further by cascading shocks such as the fiscal stimulus during the pandemic, and higher interest burden of debt servicing from policy tightening. While there is no imminent risk to debt

[11] Source: World Bank. https://data.worldbank.org/indicator/NE.TRD.GNFS.ZS

sustainability in EMs, elevated public debt poses a challenge in financing their developmental goals in the wake of rising interest payments to service this debt.

Where does India stand on the resilience of its policy framework?

19. India's policy frameworks have continued to evolve and are currently among the global best. Its exchange rate, that was pegged until 1991, is increasingly market driven. Its external account has been managed well. There are inherent strengths in its diversified balance of payments. On the current account, the merchandise trade deficit has been balanced by strong services exports and remittances receipts. Oil price is not a dampener that it used to be. All in all, the current account shows resilience and is eminently in a sustainable zone.[12]

20. The capital account too gets a variety of inflows, including FDI inflows that are traditionally known to be stable; and other equity and debt flows, which are traditionally known to be relatively fickle, but have held up well. India has slowly but surely liberalised its capital account, but the external debt as a proportion to GDP has been low and stable. The ratio of external debt to GDP has averaged around 20.5 per cent in the last 10 years (end-March 2015 to end-March 2025); as of end-June 2025, external debt to GDP ratio was 18.9 per cent. Besides keeping the liability dollarisation in check, India's short-term debt level too has remained low. The ratio of Short-term Debt (original maturity) to total debt was 18.1 per cent as of end-June 2025.

21. India has largely adhered to the path of fiscal consolidation, barring periods of significant shocks such as the pandemic. Importantly, the composition of debt, and the improved quality of public spending has rendered public debt safe. Most of the public debt is long term, is denominated in local currency, and is held domestically (a large part of which is held by institutional investors). Furthermore, a favourable growth and interest rate differential has made current level of public debt sustainable.[13]

22. Flexible Inflation Targeting framework for monetary policy, introduced in 2016, was a major structural reform in India. Evidence points towards improved outcomes post adoption of flexible inflation targeting: inflation has become lower and less volatile; inflationary expectations are better anchored; and the transmission of monetary policy

[12] During the last 10 years, the current account deficit (as % of GDP) remained in the range of 0.6 to 2.1 per cent, barring the COVID year (2020-21) where it recorded a surplus of 0.8 per cent.
[13] Another crucial factor is that, of the total debt of the government of India, external debt consists less than 5 per cent, which mitigates the external sector risks (Receipts Budget 2025-26, Government of India).

has become more effective. Inflation targeting has brought in greater transparency to policy making. Frequent communication has helped in anchoring expectations and in building credibility. There is continuous engagement with stakeholders, making monetary policy a two-way consultative process.

23. As a result of the full matrix of policy reforms, India's GDP and per capita income growth rates have accelerated over time; growth has been among the highest globally; and its variability has declined.[14]

24. India's near-term growth outlook is promising too. After growing at a stronger than anticipated rate of 7.8 per cent during Q1:2025-26, various high frequency indicators point towards a robust expansion in Q2:2025-26 as well. In the latest monetary policy statement, growth forecast for FY2025-26 has been revised upwards to 6.8 per cent. Inflation currently is at an eight-year low of 1.5 per cent. As per the latest assessment of the RBI, CPI inflation is projected to be 2.6 per cent for the full year 2025-26, much below the target.

Concluding thoughts

25. Having learnt from the crisis decade of the 1990s, EMs have put in place policy frameworks and decision-making processes that have made them less vulnerable to macroeconomic and financial instability. India has been a frontrunner in implementing these reforms. As a result, while the intensity of external shocks may not have declined, the variability of the macroeconomic outcomes has moderated considerably. This economic resilience has enabled the policy makers to focus on reforms to enhance productivity, facilitate ease of doing business, and improve the quality of financial intermediation. Such collective efforts are surely putting India on the path to graduate from an emerging to an emerged market status in the coming decades (and possibly even in the coming years).

[14] Indian economy grew by an average of 7.8 per cent during the last three years (2022-23 to 2024-25) making it the fastest growing major economy. CPI inflation declined from a peak of 6.7 per cent in 2022-23 to 4.6 per cent in 2024-25. As per the latest available data, CPI inflation was at 1.5 per cent in September 2025.