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ROADMAP FOR FINANCIAL STABILITY*

Interactive Session 1B

Chair: Sanjiv Bajaj

Speakers: Jeronimo Zettelmeyer, Marcel Fratzscher, Ila Patnaik

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Introduction

The global financial system is navigating an era of heightened uncertainty, marked by debt overhangs, inflation persistence, geopolitical fragmentation, and increasingly synchronised monetary tightening. Advanced economies are grappling with elevated debt-to-GDP ratios and sluggish productivity, while emerging markets face volatile capital flows and exchange rate pressures. These evolving dynamics have redefined the contours of financial stability and compelled a rethinking of the institutional, fiscal, and monetary frameworks that underpin macroeconomic resilience.

Against this complex backdrop, India stands out as a case of stability amidst disruption. Through a calibrated mix of fiscal prudence, monetary discipline, and digital transformation, India has managed to sustain robust growth without undermining macro stability. Reforms such as the Fiscal Responsibility and Budget Management (FRBM) Act, the Inflation-targeting framework adopted by the Reserve Bank of India (RBI), the IBC and the rapid expansion of Digital Public Infrastructure (DPI) have collectively strengthened the credibility and adaptability of India's financial ecosystem.

The panel explored how nations can institutionalise financial stability not merely as a safeguard against crises but as a strategic enabler of sustainable growth. The discussion offered a structured blueprint-linking fiscal responsibility, credible monetary frameworks, digital efficiency, and coordinated regulation-to achieve lasting financial resilience.

Main Points

1. Fiscal Resilience

India's fiscal health has improved considerably since the pandemic-induced shock. The fiscal deficit, which expanded to 9.3% of GDP in FY21, is projected to narrow to 4.4% by FY26, signalling credible adherence to the FRBM roadmap. Importantly, this consolidation is not a product of austerity but of structural shifts in expenditure priorities—from revenue-heavy consumption subsidies to productive capital formation.

Over two decades, successive governments have embedded fiscal prudence as a policy norm. The sustained decline in deficits and

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improved quality of spending reflect a deep institutionalisation of responsible fiscal management-an essential anchor for macro stability and investor confidence.

2. Capex-Led Growth

Public investment has emerged as the key lever of fiscal quality. Between FY19 to FY25, Official data show that the central government's capital expenditure rose from 1.6% of GDP in FY19 to a budgeted 3.4% of GDP for FY25, representing a decisive pivot toward long-term productivity and infrastructure creation.

This investment-led fiscal approach crowds in private capital, enhances employment, and multiplies growth effects. As noted during the discussion, fiscal prudence in the Indian context now means "spending better, not less." By targeting high-multiplier sectors, fiscal policy has evolved into a growth enabler rather than a constraint.

3. Digital Transformation of Public Finance

India's digital public finance revolution has redefined state capacity and governance efficiency. The JAM Trinity—Jan Dhan, Aadhaar, and Mobile— combined with Direct Benefit Transfers (DBT), has built a transparent and inclusive fiscal delivery system.

- Since inception, ₹44 lakh crore has been transferred directly into beneficiaries' accounts.
- Reforms have generated ₹3.48 lakh crore in fiscal savings through leakage reduction and verification mechanisms.
- Beneficiaries increased sixteenfold, from 11 crore to 176 crore, spanning 323 active welfare schemes.

The JAM-DBT framework has converted fiscal efficiency into social trust, enabling targeted delivery, financial inclusion, and macro-stability by reducing the quasi-fiscal burden.

4. GST as a Revenue Stabiliser

The Goods and Services Tax (GST), introduced in 2017, represents the most far-reaching fiscal reform in independent India. It has unified fragmented indirect tax structures into a single national market, improving tax buoyancy and compliance.

- Gross GST collections reached ₹22 lakh crore in FY25 and crossed ₹10 lakh crore within the first five months of FY26.
- Average monthly collections rose from ₹0.82 lakh crore (FY18) to ₹2.01 lakh crore (FY26)—a 12% compound annual growth rate (CAGR).

This fiscal transformation has enhanced transparency, reduced distortions, and expanded the revenue base—providing space for growth-oriented expenditure without compromising fiscal discipline.

5. Monetary Credibility

The second pillar of India's macroeconomic framework is a credible and flexible monetary policy regime. The inflation-targeting framework, adopted in 2016, mandates the RBI to maintain inflation around 4% ± 2%. Despite supply shocks and imported inflation, India has remained within this band for 82 of 113 months, demonstrating institutional resilience.

The RBI's response-cutting policy rates during COVID-19 to support recovery, followed by measured tightening post-Ukraine to counter inflation-reflects the agility of a data-driven and counter-cyclical policy approach.

Consistency and clarity in communication have anchored expectations, stabilised long-term yields, and enhanced confidence in the central bank's credibility.

6. Exchange Rate Management

India's exchange rate policy has matured into a pragmatic managed-float regime. The RBI intervenes to smooth volatility, not to fix a level.

- Currency volatility (7.1) remains moderate compared to major economies like Japan (17.3).
- Foreign exchange reserves, exceeding $600 billion, serve as buffers rather than rigid defenses.

This calibrated approach supports external competitiveness, absorbs shocks, and preserves policy autonomy—balancing global exposure with domestic priorities. The rupee's relative stability reflects confidence in India's macroeconomic fundamentals and policy coherence.

7. Global Recognition

India's credibility has been reaffirmed internationally through successive sovereign rating upgrades. In 2025, Rating and Investment Information (R&I) of Japan upgraded India to BBB+ (with Stable outlook), following similar actions by S&P and Morningstar DBRS. These upgrades signify confidence in India's growth trajectory, fiscal consolidation, and monetary prudence, reducing borrowing costs and attracting long-term capital.

8. Financial Resolution and Deposit Insurance (FRDI)

An effective crisis-resolution architecture is vital for sustained stability. The proposed FRDI Bill seeks to create a unified framework for the resolution of financial institutions, ensuring that no single failure undermines systemic confidence.

Key Features:

- Establishment of a Resolution Corporation for banks, NBFCs, and insurers.
- Early intervention mechanisms to detect stress and trigger corrective action.
- A “bail-in” mechanism enabling internal recapitalisation without taxpayer burden.
- Enhanced deposit insurance coverage to safeguard savers and maintain public trust.

The FRDI structure aligns India's financial governance with global standards, improving resilience and accountability across institutions.

9. Digital Finance and Inclusion

India's financial inclusion story has moved from access to empowerment, powered by Digital Public Infrastructure (DPI) such as UPI, Account Aggregator, and Open Network for Digital Commerce (ONDC).

- UPI processes over 12 billion transactions monthly, representing one of the world's largest real-time payment systems.
- The Account Aggregator framework facilitates secure, consent-based data sharing between banks and borrowers, expanding credit access for small enterprises.
- ONDC democratizes e-commerce and digital lending, enabling MSMEs to participate in formal markets.

These innovations have not only deepened financial inclusion but also enhanced monetary transmission, improved credit assessment, and fostered a transparent digital ecosystem.

Context

The panel highlighted that financial stability is a global public good, shaped by interconnected economies and policy spill-overs. The post-pandemic recovery remains asymmetric—while advanced economies face inflationary slowdowns, emerging markets grapple with liquidity constraints and external vulnerabilities.

- The U.S. Federal Reserve's prolonged tightening has triggered capital outflows from emerging markets, increasing debt-servicing burdens.
- Panellists underscored India's strength in institutional coherence—where fiscal, monetary, and regulatory arms work in synchrony, enhancing credibility.

India's macroeconomic success thus stems from policy integration: fiscal consolidation complements monetary prudence, and both are reinforced by digital transparency and institutional depth.

Approaches and Findings

1. Fiscal Approach

India's fiscal strategy prioritises "good expenditure"—investment in infrastructure, human capital, and technology—over populist transfers. Reforms like GST and DBT have expanded fiscal capacity while maintaining discipline. Compliance with FRBM targets anchors investor confidence and lowers borrowing costs.

2. Monetary Policy Approach

The RBI's flexible inflation-targeting model anchors price stability while accommodating growth objectives. Its calibrated adjustments—easing (2020–22), tightening (2022–23), and moderation (2024–25)—reflect balanced pragmatism. Transparent communication has become a cornerstone of monetary credibility.

3. External and Exchange Rate Management

The exchange rate regime has shielded India from sharp capital reversals. Judicious use of reserves ensures stability while maintaining autonomy. This framework enhances competitiveness without inviting speculative volatility.

4. Institutional and Regulatory Reform

The FSDC coordinates oversight across regulators, strengthening systemic risk management. The FRDI Bill will further consolidate early-warning systems and reinforce India's capacity to resolve financial stress effectively.

5. Digital Public Infrastructure (DPI)

Integration of Aadhaar, JAM, UPI, and Account Aggregator frameworks has created an interoperable financial ecosystem. These systems improve transparency, accelerate welfare delivery, and integrate citizens into the formal economy—making inclusion a driver of stability.

6. Global Recognition and Cooperation

India's balanced macroeconomic management offers a model for emerging economies. Expanding cooperation with Europe on sustainable finance, green investment, and fintech regulation will enhance resilience and diversify global partnerships.

Conclusion

India's trajectory from recovery to resilience epitomises how prudent macroeconomic management can coexist with rapid development. Fiscal consolidation, monetary discipline, and digital governance together have transformed India's financial architecture into a durable foundation for growth.

The road ahead demands institutional vigilance and adaptive reform:

- Continue fiscal consolidation with emphasis on capital productivity.
- Deepen bond and institutional investor markets to diversify financial sources.
- Operationalise a Financial Stability Council with cross-regulatory crisis-response powers.
- Implement the FRDI framework for timely and transparent resolution.
- Expand digital inclusion while safeguarding data privacy and cybersecurity.

India's experience offers a credible and replicable model for emerging economies seeking to balance stability with inclusive growth.

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