

**Recent developments:** Regional GDP in **South Asia**, measured at market prices, grew an estimated 4.7 percent in 2013, down from 5.0 percent in 2012. Regional growth in 2013 was 2.6 percentage points below average growth in 2003-12, mainly due to subdued manufacturing performance and a sharp slowing of investment growth in India. Pakistan's growth is estimated to have remained broadly stable notwithstanding fiscal tightening, but remains significantly below the regional average, due in part to energy supply bottlenecks and security uncertainties. India's exports received a boost from steep currency depreciation during the second half of 2013, after the U.S Federal Reserve's "taper talk" in late May 2013. A sharp current account adjustment (from a deficit of nearly 5 percent of GDP in Q2 2013 to 0.2 percent of GDP in Q1 2014) was achieved mainly through efforts to curb imports. In the rest of the region, as demand from high-income countries improved, exports in Bangladesh and Sri Lanka grew rapidly. Bangladesh's export growth, however, slowed in Q1 2014, partly due to the lagged effect of political unrest. Pakistan's exports slowed more sharply, reflecting in part pervasive electricity and natural gas shortages.

Inflation in the first quarter of 2014 was above 7 percent (y/y) in Bangladesh, Pakistan, India and Nepal, reflecting structural capacity constraints and persistence of food inflation. Despite some consolidation, fiscal deficits remain high. India's general government deficit, despite falling, is still more than 2 percentage points of GDP higher than in 2007, indicating that depleted fiscal buffers have yet to be fully restored. In Pakistan, fiscal restraint has reduced the deficit from over 8 percent of GDP in FY2011-12 to an estimated 6 percent of GDP in FY2013-14. However, sustaining fiscal consolidation could prove challenging as revenue mobilization in the region remains weak, while subsidies for fuel, food and fertilizers impose substantial pressure on the expenditure side. Measures to gradually reduce subsidies, and to raise revenues by simplifying the tax system, broadening the tax base, and improving compliance, can help to reduce deficits. Capital flows to the region have grown steadily since the mid-2013 financial turmoil. Growth in remittances slowed in 2013, but remittances continue to provide support to consumption and external balances in most countries in the region.

**Outlook:** Firming global growth and a modest pickup in industrial activity should help lift South Asia's growth to 5.3 percent in 2014. Although growth should improve during the course of 2014, a weak start to the year will weigh on annual growth. Regional growth is projected to rise to 5.9 percent in 2015 and 6.3 percent in 2016 (with most of this acceleration focused on India), supported by a gradual pickup of domestic investment and rising global demand. India's growth is projected at 5.5 percent in FY2014-15, accelerating to 6.3 percent in 2015-16 and 6.6 percent in 2016-17. Medium-term growth in Pakistan and Nepal is projected at about 4 percent, and in Bangladesh at about 6 percent. In Sri Lanka, annual growth is forecast to remain broadly stable at 7.2 percent in 2014, moderating to 6.7 percent by 2016.

The forecasts assume that reforms are undertaken to ease supply-side constraints (particularly in energy and infrastructure), improve productivity, and strengthen the business environment, which would help to raise the region's underlying growth potential. Continued fiscal consolidation would create additional space for private investment, while maintaining a credible monetary policy stance (together with a gradual easing of supply-side constraints) would help to reduce inflation. Regional capital flows are forecast to rebound to \$115 billion in 2014, and then rise broadly in line with GDP (to 4.5 percent of GDP)—below the level of 5.6 percent of GDP in 2012, mainly reflecting tighter international financial conditions.

**Risks:** A key risk to the near-term outlook is weak seasonal monsoon rains, perhaps triggered by El Niño weather conditions. Weaker than average monsoons could reduce regional GDP growth by half a percentage point or more, while stronger El Niño conditions that result in deficient rainfalls or drought can have more significant impacts. Stressed bank loans (including restructured loans in India) exceed 10 percent of loans in Bangladesh, Bhutan, India, and Pakistan. If left unaddressed, these could result in lack of sufficient financing needed for a resumption of the investment cycle. Security uncertainties in Afghanistan and Pakistan and a slow pace of reforms are other risks. External headwinds include escalation of geopolitical tensions in Russia and Ukraine that could cause a disruption in global energy supplies and crude oil prices to spike; a disorderly adjustment of capital flows accompanying monetary policy normalization in the U.S; and a sharp slowing of Chinese growth.

**South Asia forecast summary**

(annual percent change unless indicated otherwise)

	<b>00-09<sup>a</sup></b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>Est. 2013</b>	<b>Forecast</b>		
						<b>2014</b>	<b>2015</b>	<b>2016</b>
<b>GDP at market prices (2010 US\$)</b>								
<b>Calendar Year Basis<sup>b</sup></b>								
<b>Afghanistan</b>	11.9	8.4	6.1	14.4	3.6	3.2	4.2	4.6
<b>Bangladesh</b>	5.2	6.4	6.5	6.1	5.7	5.7	6.1	6.2
<b>Bhutan</b>	8.2	11.7	8.6	4.6	6.5	7.2	7.8	8.0
<b>India</b>	7.4	9.3	7.7	4.8	4.7	5.3	6.1	6.6
<b>Maldives</b>	6.3	7.1	6.5	3.4	3.7	4.5	4.2	4.1
<b>Nepal</b>	3.4	4.1	4.1	4.2	4.0	4.4	4.3	4.3
<b>Pakistan</b>	4.9	2.2	3.1	4.0	4.1	3.8	3.9	4.0
<b>Sri Lanka</b>	4.4	0.0	6.8	6.0	3.5	8.0	8.2	6.3
<b>Fiscal Year Basis<sup>b</sup></b>								
<b>Bangladesh</b>	5.2	6.1	6.7	6.2	6.0	5.4	5.9	6.2
<b>Bhutan</b>	8.2	9.3	10.1	6.5	5.6	6.8	7.6	8.0
<b>India</b>	7.3	8.9	6.7	4.5	4.7	5.5	6.3	6.6
<b>Nepal</b>	3.4	4.8	3.4	4.9	3.6	4.5	4.3	4.3
<b>Pakistan</b>	4.9	2.6	3.6	3.8	3.7	3.7	3.9	4.0

Source: World Bank.

*World Bank forecasts are frequently updated based on new information.*

a. Growth rates over intervals are compound average.

b. Please see regional annex for details on fiscal year reporting.