

January 2014

Overview: GDP growth in South Asia rose to an estimated 4.6 percent in 2013 from 4.2 percent in 2012 on a market price-calendar year basis. Growth was, however, well below its pre-crisis pace, reflecting a combination of domestic imbalances, weakening investment rates, and a challenging external environment. A cyclical recovery in the second half of 2013 was led by a rapid expansion of regional exports, reflecting a gradual recovery in global demand and currency depreciation in India. India was hit particularly hard by a withdrawal of portfolio capital (resulting in steep depreciation of the rupee) in mid-year, stemming from apprehensions of tapering of United States quantitative easing. Although retail inflation remained high in some countries, normal harvests and lower international commodity prices helped stabilize consumption growth in South Asia. Sri Lanka experienced a significant decline in inflation during the course of 2013. In India, however, despite a negative output gap, consumer price inflation remained elevated at close to 10 percent (y/y) for much of the year. Pakistan also faced inflationary pressures, while inflation picked up towards end of the year in Bangladesh. The growth of remittances to South Asia moderated to an estimated 6.8 percent in 2013 from 9.7 percent in 2012. While India was the largest recipient by size, remittances relative to GDP were more important resource flows for Bangladesh, Nepal, Pakistan, and Sri Lanka in 2013.

Outlook: South Asia's regional GDP growth is projected to improve to 5.7 percent in 2014 in market price terms, and to rise to 6.3 percent in 2015 and 6.7 percent in 2016. A gradual improvement in regional growth over the forecast period will be led mainly by a recovery in global demand and domestic investment, although the latter remains subject to significant downside risks. A projected strengthening of demand in the Euro Area and United States (the two largest trade partners of South Asia) and robust growth in developing-country markets will support regional exports. Despite slowing of US monetary stimulus, a recovery in regional investment is expected to buoy medium-term growth. The projected increase in investment rates and GDP growth, however, will depend critically on ensuring macroeconomic stability (including reducing fiscal deficits and inflation), making sustained progress on policy reforms, and reducing structural and regulatory constraints on production (particularly in the provision of energy and infrastructure). GDP growth in India, measured at factor cost, is projected to rise to over 6 percent in the 2014-15 fiscal year, and then to increase to 6.6 percent in FY2015-16 and to 7.1 percent in FY2016-17. Growth in Pakistan is expected to moderate to 3.4 percent in FY2013-14, as a result of necessary fiscal tightening, but rise to 4.5 percent in the medium term. Relatively stable or declining international commodity prices will contribute to reducing inflationary and current account pressures, and – together with normal harvests and sustained remittance flows – support consumption in the region.

Risks: Risks to the outlook for South Asia's growth are tilted to the downside, on balance. Some upside risks include better-than-anticipated global growth, and lower crude oil prices than projected. Domestic risks are particularly relevant for a sustained revival of investment and for medium-term growth prospects. These main domestic risks concern the ability of South Asian countries to keep current and planned reforms from going off-track and to maintain fiscal discipline. Political uncertainties related to national elections in Afghanistan, Bangladesh and India; entrenchment of inflation expectations (which could reduce space for monetary easing and adversely affect investment); and lack of progress in reducing supply-side constraints may also pose significant risks to the outlook. The tapering of U.S quantitative easing is expected to proceed gradually, but a disorderly adjustment of capital flows could result in currency depreciation pressures and put further stress on the region's corporate and banking sector balance sheets. Prolonged weakness in the Euro Area and geopolitical risks in the Middle East are additional sources of risk.

South Asian policymakers must continue the urgent task of rebuilding domestic and external policy buffers and reducing imbalances to deal with potential intensification of external pressures, as well as accelerate productivity-enhancing reforms and improve their business environment to raise growth rates on a sustained basis. Given already large fiscal and current account deficits, high inflation, and weak reserve positions (or a combination of these) in some South Asian countries, policy makers need to maintain an appropriately tight macroeconomic stance to avoid exacerbating external vulnerabilities and domestic inflationary pressures.

South Asia forecast summary

(annual percent change unless indicated otherwise)

	00-09 ^a	2010	2011	2012	Est. 2013	2014	Forecast 2015	2016
GDP at market prices (2010 US\$)								
Calendar Year Basis^b								
Afghanistan	11.9	8.4	6.1	14.4	3.1	3.5	4.3	5.1
Bangladesh	5.2	6.4	6.5	6.1	5.8	5.9	6.1	6.0
Bhutan	7.7	9.6	9.5	8.3	7.9	8.4	8.6	8.6
India	7.4	9.1	7.0	5.3	4.9	5.8	6.5	7.0
Maldives	6.3	7.1	7.0	3.4	4.3	4.2	4.1	4.1
Nepal	3.4	4.4	4.3	4.1	3.7	4.1	4.8	5.2
Pakistan	4.9	3.1	4.0	4.0	3.5	3.8	4.3	4.5
Sri Lanka	4.4	8.0	8.2	6.4	7.0	7.4	6.5	6.3
Fiscal Year Basis^b								
Bangladesh	5.2	6.1	6.7	6.2	6.0	5.7	6.1	6.0
Bhutan	7.7	9.3	10.0	9.0	7.6	8.1	8.6	8.6
India	7.6	9.3	6.2	5.0	4.8	6.2	6.6	7.1
Nepal	3.4	4.8	3.9	4.6	3.6	3.8	4.4	5.2
Pakistan	4.9	2.6	3.7	4.4	3.6	3.4	4.1	4.5

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.