South Asia Economic Focus Fall 2013

A Wake-Up Call

THE WORLD BANK

1818 H Street NW, Washington DC 20433
Telephone: 202-473-1000; Internet: www.worldbank.org

1 2 3 4 16 15 14 13

ISBN (electronic): 978-1-4648-0118-1
DOI: 10.1596/978-1-4648-0118-1
Cover photo: Dominic Sansoni / World Bank; Cover design: Alejandro Espinosa/Sonideas

South Asia Economic Focus

Fall 2013

A Wake-Up Call

THE WORLD BANK

This report is a product of the Office of the Chief Economist for the South Asia Region. *Its preparation was led by Markus Kitzmuller, with substantive contributions from David Gould, under the oversight of Martin Rama (Chief Economist, South Asia Region). The report benefitted from inputs by country teams in the Poverty Reduction and Economic Management unit (SASEP) as well as Sanket Mohapatra and colleagues in the Development Economics Prospects Group (DECPG) under the supervision of Andrew Burns (Manager, DECPG). Economists providing information for country briefs include Deepak Bhattasali, Daminda Fonseka, Camilo Gomez Osorio, Zahid Hussain, Omar Joya, Faruk Khan, Aurelien Kruse, Chandana Kularatne, Denis Medvedev, Jose Lopez Calix, Kirthisri Rajatha Wijeweera, Saadia Refaqat, Nadeem Rizwan, Smriti Seth, Thirumalai G. Srinivasan, Muhammad Wahid, and Salman Zaidi, under the guidance of Vinaya Swaroop (Sector Manager, Poverty Reduction and Economic Management, South Asia Region) and Ernesto May (Sector Director, Poverty Reduction and Economic management, South Asia Region). Valuable research assistance was provided by Bilgehan Gokcen and Ayesha Raheem, as well as Amir Sadegh Sadeghi, who significantly contributed to the analytical work done for the focus section. Gabriela Aguilar signed responsible for the layout, design and typesetting, and Neelam Chowdhry provided administrative support.*

South Asia as used in this report includes Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.

Table of Contents


Tissues
HAIR

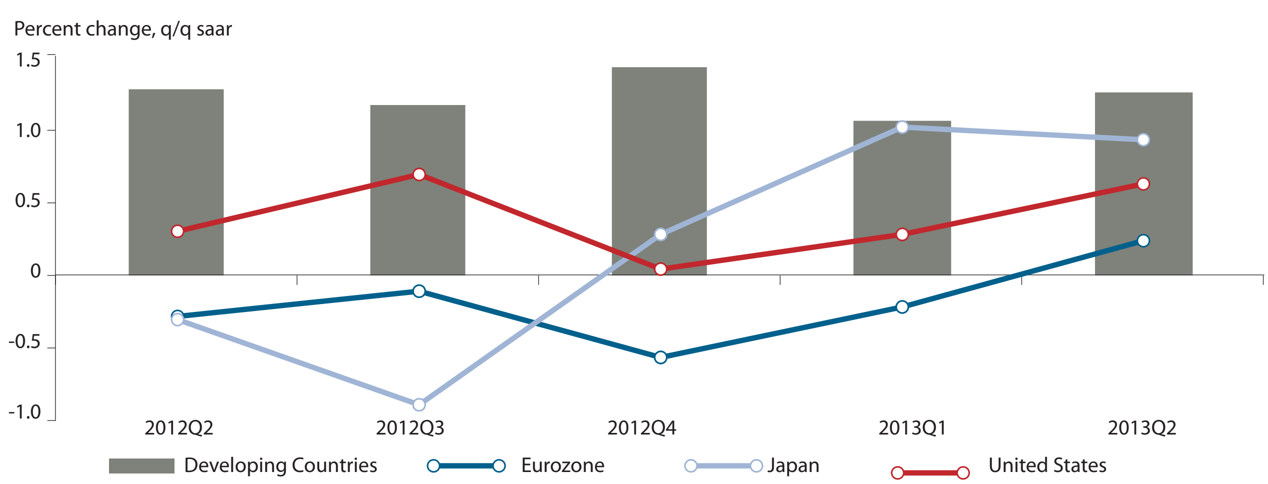
Recent economic developments

Global capital rebalancing has highlighted structural weakness and vulnerability in South Asia, acting as a wake-up call for policy makers. While recent economic developments in advanced countries are encouraging, large parts of the South Asian region continue to slow. Portfolio capital outflows, triggered by the prospect of unwinding Quantitative Easing (QE) tapering in the US, have made current account deficits more difficult to finance across emerging countries. Meanwhile, supply-side constraints and macroeconomic imbalances remain to be tackled in most South Asian countries. But the depreciation of regional currencies offers a great opportunity to kick start exports and growth, and provides the space to re-engage reforms to create a conducive investment climate.

Advanced economies are picking up, while emerging markets are slowing down

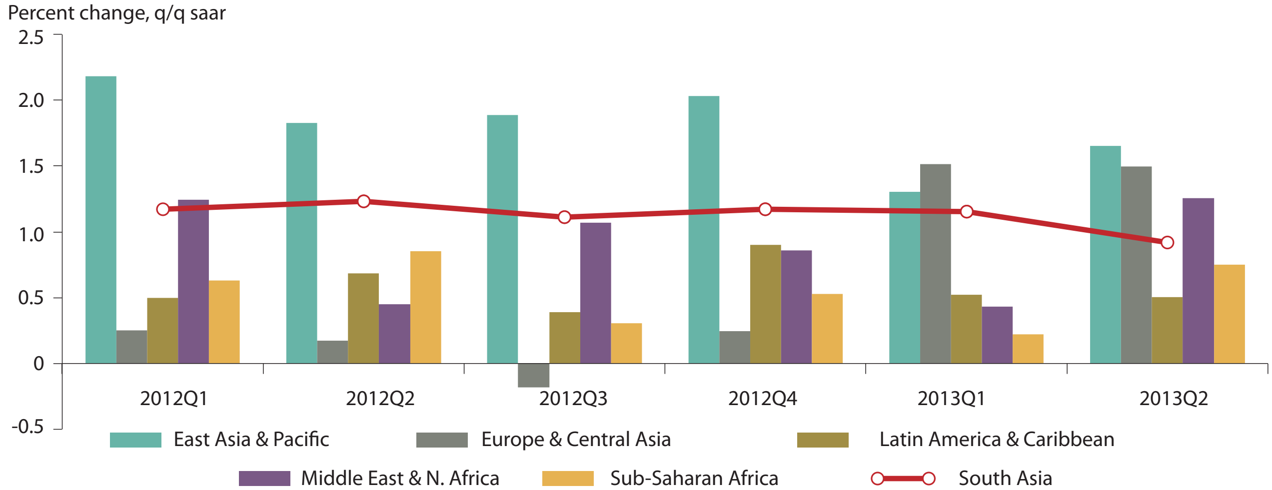
As advanced countries show tentative signs of recovery, developing and emerging market economies continue to exhibit slow and flat growth, particularly in South Asia. Many large developing countries have

FIGURE 1: Real GDP growth suggests a tentative recovery of advanced economies



Source: World Bank DECPG

FIGURE 2: South Asia is not among the fastest-growing developing regions anymore

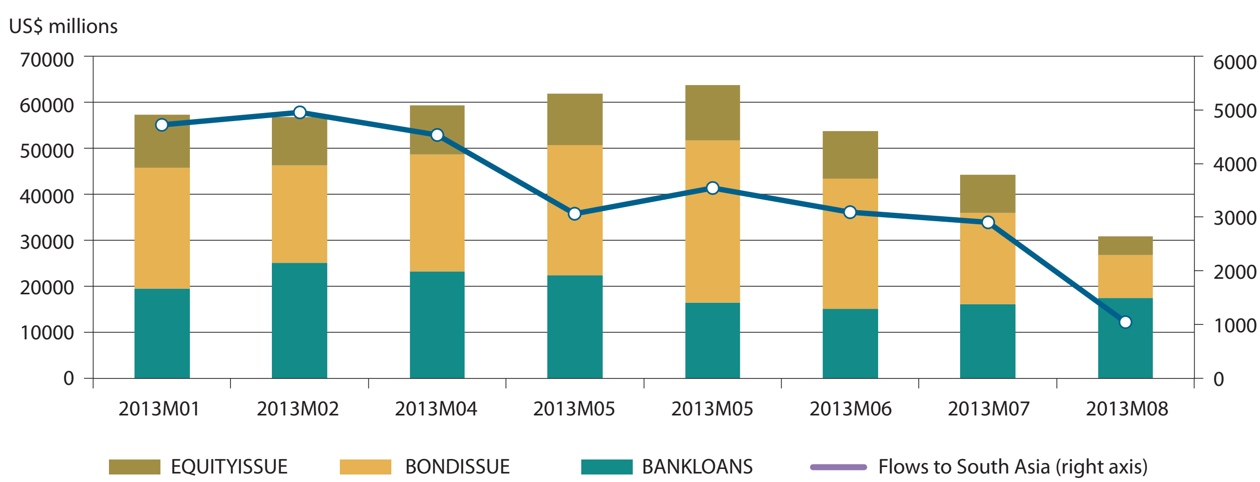


Source: World Bank DECPG

seen economic activity strengthen somewhat in recent months. Europe is beginning to show signs of a tentative recovery and the US economy is exhibiting modest but stable growth, while Japan's exceptionally expansionary monetary policy may finally be moving its economy out of its long deflationary stagnation. Despite recent concerns over the budget impasse in the US, across developed countries, measures of financial market risk have shown a downward trend and asset prices have been increasing.

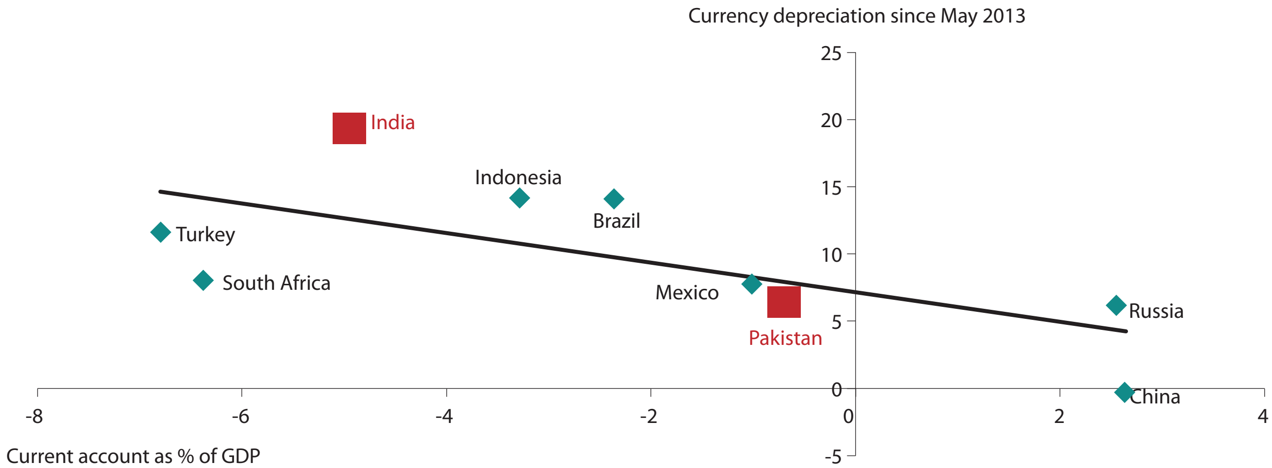
Global portfolio rebalancing has put pressure on emerging markets, particularly those with external and structural weaknesses. With the prospect of interest rates increasing again in advanced economies, developing countries now have to compete more fiercely to attract once plentiful capital inflows. The recent and ongoing international capital portfolio rebalancing has led to depreciating currencies, particularly in those emerging market economies characterized by structural weakness. Capital outflows have also fueled concerns about the sustainability of external financing across developing countries. The postponement of Quantitative Easing (QE) tapering in the US has helped to calm the environment. This offers a window of opportunity to reduce vulnerabilities rooted in over-stretched fiscal balances and structural bottlenecks from inadequate regulation and poor infrastructure.

FIGURE 3: Concerns about Quantitative Easing tapering induced capital to leave developing countries



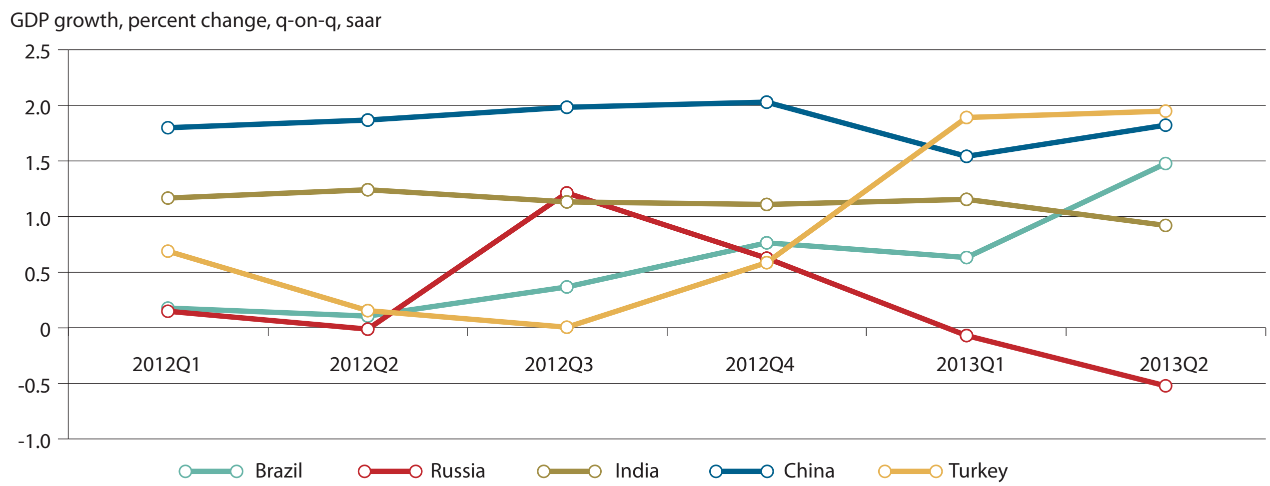
Source: World Bank and Dealogic

FIGURE 4: Currencies adjusted more sharply in countries with larger macroeconomic imbalances



Source: World Bank

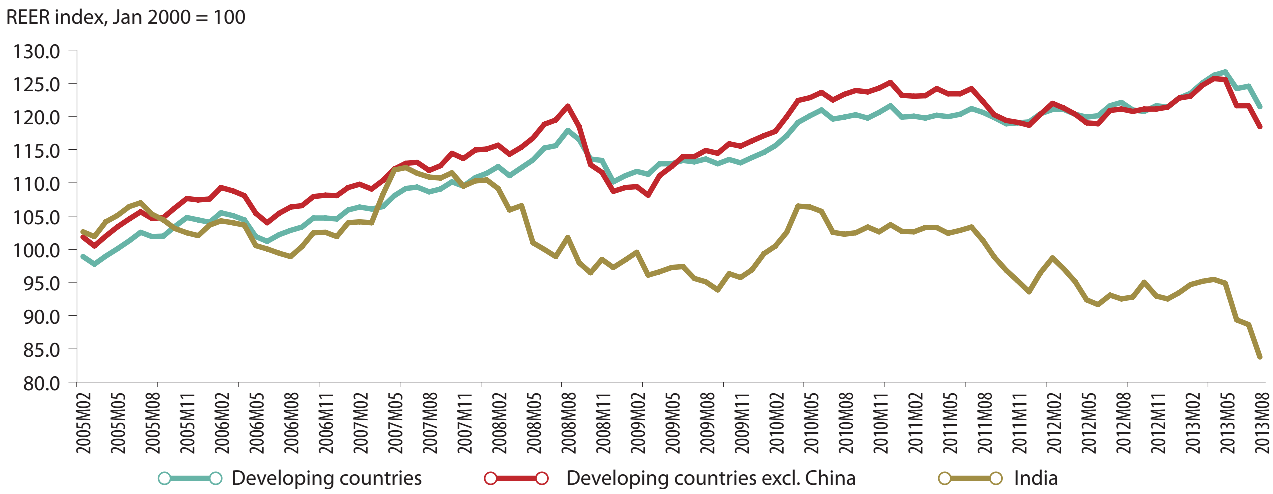
FIGURE 5: India's growth has been declining for several quarters



Sources: World Bank DECPG, IMF International Financial Statistics, JP Morgan

Among emerging economies, India has felt the immediate effects from the QE tapering announcement in May the most. Weak growth and exchange rate depreciation have characterized India for some time; nonetheless, several factors have led to a relative risk re-assessment by investors. A wide current account deficit, at 4.8 percent of GDP for 2012/13 (FY13), that has been financed most recently by volatile portfolio capital flows, has been perceived as a weakness of the economy. Retail price inflation, at 9.6 percent (y-o-y, April-July, 2013), though driven by food and oil price developments, is still unusually high. A relatively large fiscal deficit, at 7 percent of GDP for FY13, continues to constrain fiscal space and leads to greater reliance on monetary policy.

FIGURE 6: **India's real exchange rate has been depreciating for several years**



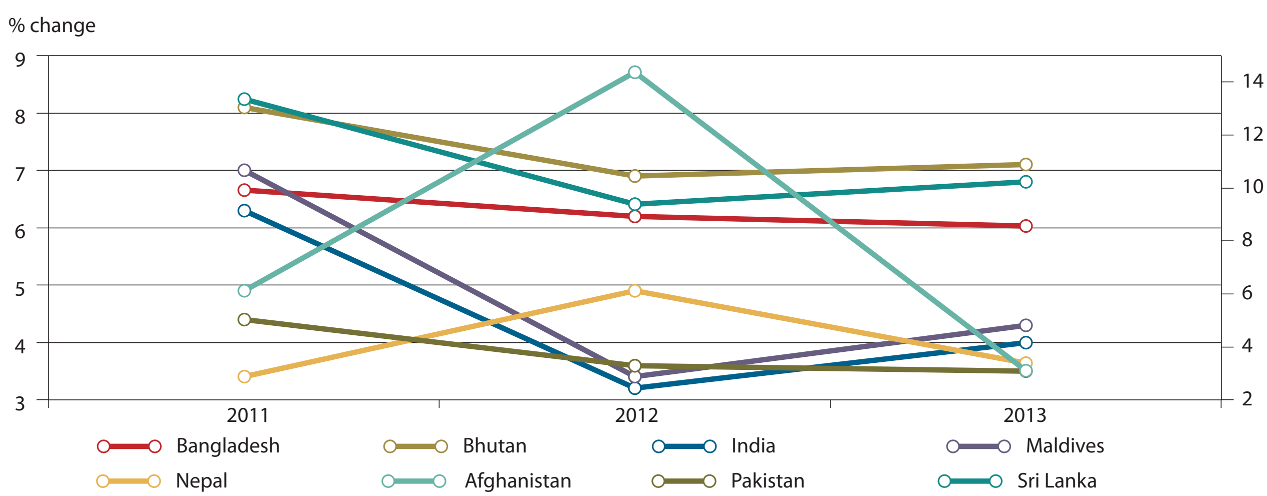
Sources: World Bank DECPG, IMF International Financial Statistics, JP Morgan

Growth across South Asia is slowing down, beyond India

India's slowdown has significant spillover effects to the rest of South Asia, and even more so after the financial crisis of 2008. As shown in this edition's Focus section, there is a clear transmission of the global business cycle to South Asia, but also a significant effect from India on South Asian economies' GDP growth rates. Not only do Indian business cycle movements spill over to other economies in the region: the nature and speed of the pass through has significantly changed in the aftermath of the financial crisis of 2008. This spillover effect adds to the direct effect that other developing countries, the US and other advanced economies have on the region. While India is the country most directly affected by portfolio outflows, the impact is felt across all South Asian economies. And this is so even if each country faces specific idiosyncratic challenges and shocks to economic performance.

Overall, growth in South Asia is expected to moderate in 2013 compared to prior projections. Regional growth has deteriorated in the second and third quarters of 2013, mainly due to supply-side

FIGURE 7: **Real GDP growth remains respectable, but it is on a declining path**

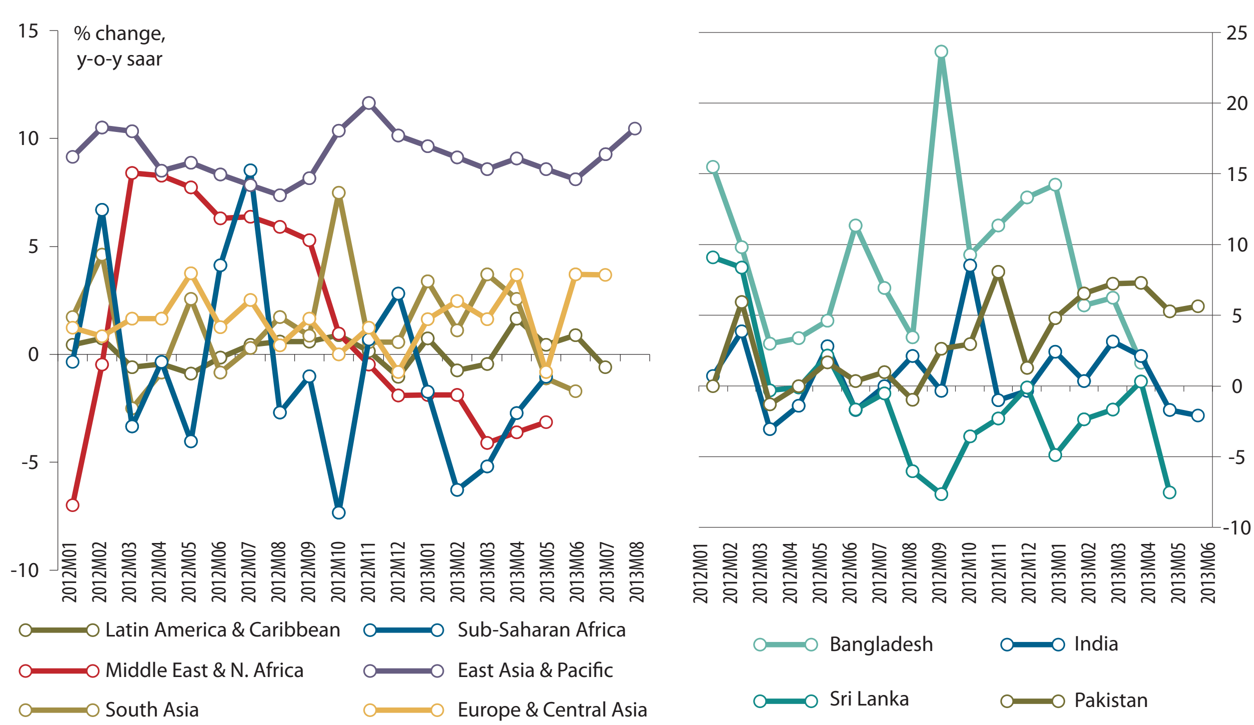


Source: World Bank and National Authorities constraints and weak domestic demand. India, the region's main economy, slowed down significantly to an estimated 3.2 percent real GDP growth at market prices in FY13 from 6.3 percent in the previous fiscal year. Afghanistan sticks out in terms of the size of its slowdown, expecting a 2013 growth rate of just 3.1 percent down from 14.4 percent in an exceptional 2012, mainly driven by increased uncertainty stemming from the political and security transition. Bangladesh's estimated growth for 2013, at 6 percent, is a 0.2 percentage point decrease vis-à-vis 2012, reflecting political uncertainties, supply side constraints and lower private investment. Similarly, real GDP growth is set to fall in Bhutan, to 6.9 percent in 2012/13 down from 8.1 percent, in Nepal, to 3.6 percent in 2013 from 4.9 percent in 2012, as well as in Pakistan, where a marginal 0.1 percentage point decrease to 3.5 percent for 2013 is estimated. Only Maldives and Sri Lanka are expected to see a slight increase in their growth rates.

Industrial Production continues to be lackluster across South Asia. With the exception of Pakistan, all major South Asian economies have seen industrial production (IP) plummet during the second quarter of 2013. Around May, India saw IP growth turn negative, and its recent decline in manufacturing Purchasing Managers' Index is unique among BRICS and advanced economies. Sri Lanka and Bangladesh faced steep declines as well.

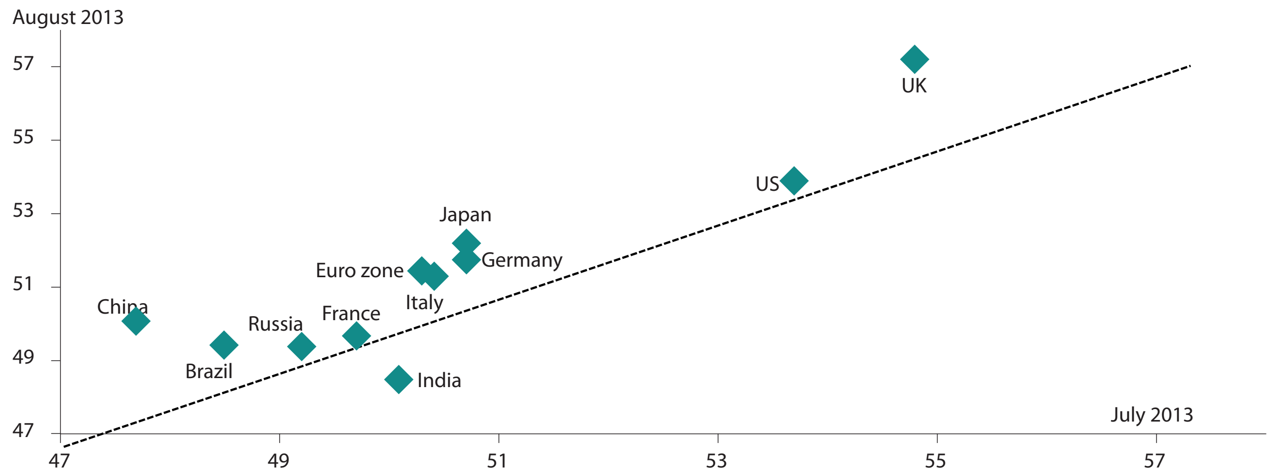
While fundamentals in South Asia have not changed significantly over the last 12 months, exuberance has given way to pessimism, particularly in the case of India. Like other developing regions, South Asia is facing greater turbulence as markets reassess sources of global growth and risks. As capital may become scarcer for developing and emerging markets, those with more pronounced structural weaknesses and higher external exposure will remain more vulnerable. However, short-term capital market turbulence is manageable and the return to sustainable growth in the developed world is a positive development for South Asia. Greater export demand accompanied by relative price advantages offer support to growth over the medium-term. While South Asian countries differ in terms of political, economic, and financing challenges, ensuring macroeconomic stability and removing supply-side constraints remain the best response to ride the turbulent waves of global capital flows.

FIGURE 8: Industrial production remains subdued relative to other regions



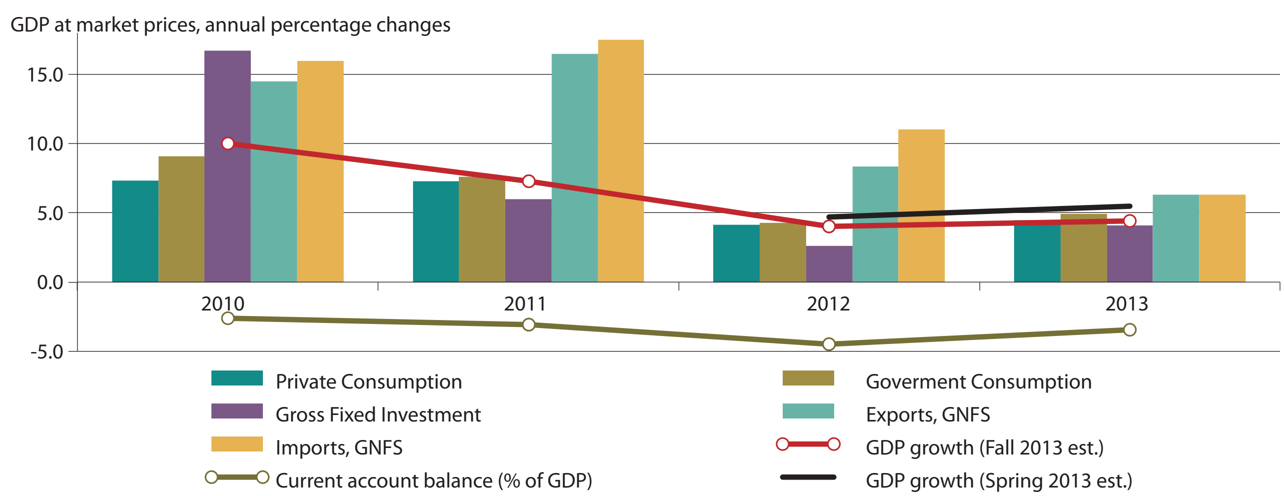
Source: World Bank DECPG

FIGURE 9: In times of increasing confidence around the globe, India's Purchasing Managers' Index is trending down



Source: World Bank

FIGURE 10: Declining exports and investment are at the core of moderating growth

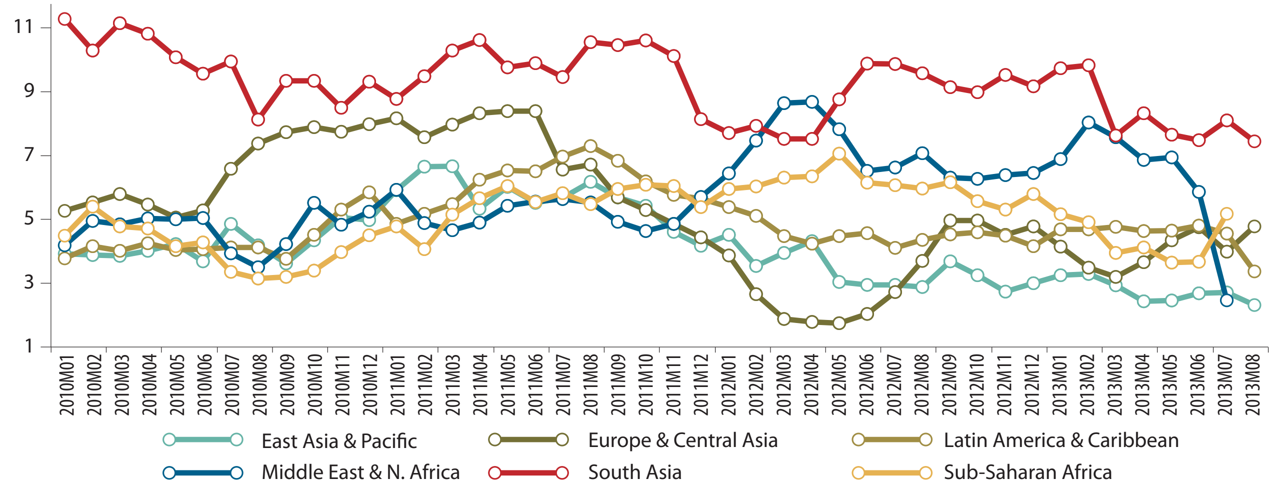


Source: World Bank DECPG

Inflation remains high across most South Asian countries

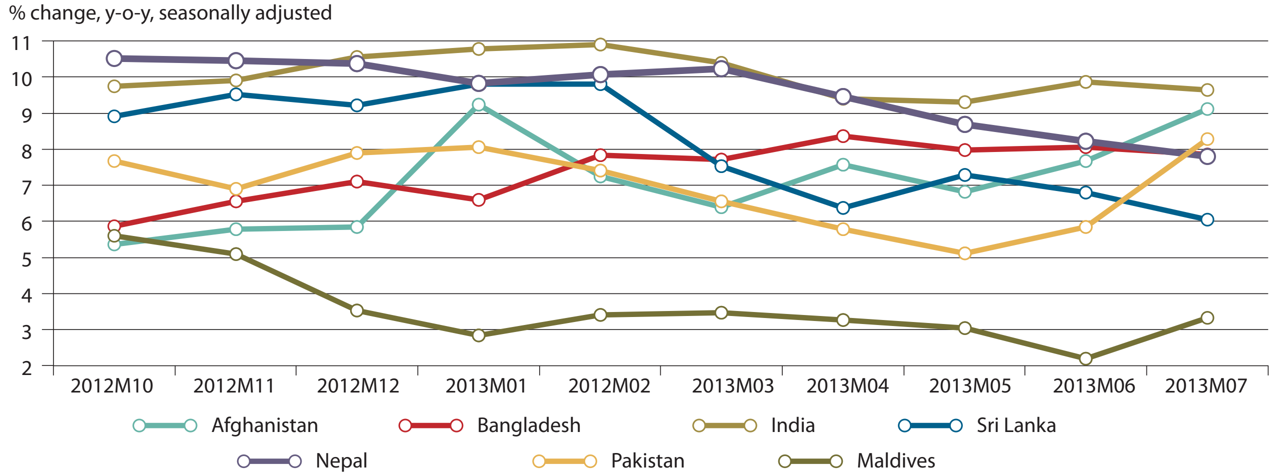
South Asian inflation remains the highest among developing regions and this continues to constrain monetary policy. Core inflation in some countries actually declined and remains within the confidence bands of central banks. But food and commodity price increases drive retail prices, thereby signing responsible for continuously high headline inflation levels. In India, wholesale core inflation decelerated to 2.4 percent y-o-y (April –August 2013) and overall wholesale price inflation came down to 5.3 percent y-o-y. However, over the same period double-digit food and fuel price inflation pushed consumer prices to 9.5 percent. Afghanistan's inflation rate reached 7.7 percent in June 2013. Nepal stood just under 10 percent in FY13, while Bangladesh reached 7.4 percent, up from 5 percent the previous year. Even in countries where inflation declined, it remained at levels which are high by international standards. Bhutan's price increase registered 5.5 percent (y-o-y) during the second quarter of 2013, compared to 8.4 percent in the previous quarter. Pakistan saw its headline inflation decrease to an average 7.4 percent in 2012/13, down from 11 percent in 2011/12. Sri Lanka experienced a decrease to 6.3 percent from 9.8 percent between January and August 2013. Only Maldives maintained moderate average inflation in 2013 at 4.5 percent.

FIGURE 11: **South Asia maintains its top spot for inflation among region**



Source: World Bank

FIGURE 12: **Consumer price inflation remains high in almost all South Asian countries**



Source: World Bank

Fiscal policy space stays constrained

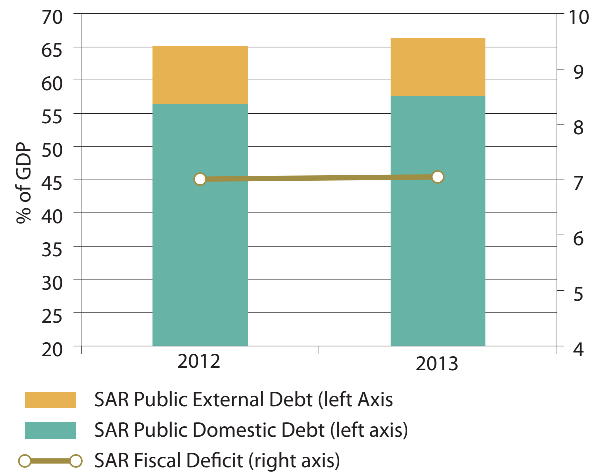
Fiscal deficits and public debt in the region remain large, thereby constraining space for stimulus. The average fiscal deficit across South Asian countries was estimated to be 7.1 percent of GDP in 2013, up from 7 percent. This puts South Asia in the top spot across all regions. The international comparison is slightly more favorable in the case of public indebtedness. Still, general government gross debt reached an average of 66.3 percent of GDP in 2013, up from 62.3 percent in 2012. On the positive side, a large share of that debt is domestic, which reduces the vulnerability of South Asian economies to real exchange rate depreciation.

Across the region, several countries struggle to bring fiscal deficits down. India's general government deficit in 2012/13 is expected to have come down to 7 percent of GDP from 8.1 the previous fiscal year, while the central government deficit stands at 5.1 percent, below the March estimate of 5.4 percent. However, from April to August 2013, this downward trend has come under pressure as the central government deficit has already reached 62.8 percent of the annual ceiling, compared to 51.5 percent in the previous fiscal year.

Similarly, with a fiscal deficit (excluding grants) of 4.3 percent in 2012/13, Bangladesh has done better than in the previous year. However, revenue collection fell short of its target by 0.5 percent of GDP, while the spending pressure from subsidies continues to rise. Revenue shortfalls also caused a deterioration of fiscal balances in other countries. Afghanistan's saw its fiscal revenue decline by 11 percent between the first half of 2012 and the first half of 2013. Pakistan experienced a fiscal deficit of 8 percent in 2012/13, compared to a target of 4.8 percent, partly due to revenues coming in below target. While Sri Lanka reduced its fiscal deficit to 6.4 percent in 2012, revenue mobilization decreased by 4 percent, at a time when a 27 percent increase was expected.

Public debt has similarly resisted reduction. Across countries in the region, public debt remains elevated; in Bhutan and Maldives it is actually increasing. With debt at 86.2 percent of GDP, and little room left for further borrowing, Maldives is at risk of debt distress. In India, the central government's debt marginally increased in 2012/13 to 53 percent of GDP, up from 52.9 in 2011/12, thereby reversing a previous downward trend. This was mainly due to slower growth and lower revenues. Pakistan on the other hand saw its public debt decline to 62.9 percent as of end-June 2013, down from 63.7 percent one year before. But its interest payments continue to be large, at 4 percent of GDP. Bangladesh and Nepal feature the lowest total public debt. In Bangladesh, public debt stands at 41.2 of GDP (down from 42.8 in 2011/12) and in Nepal it is a healthy 30.8 percent (down from 33.6 in 2011/12).

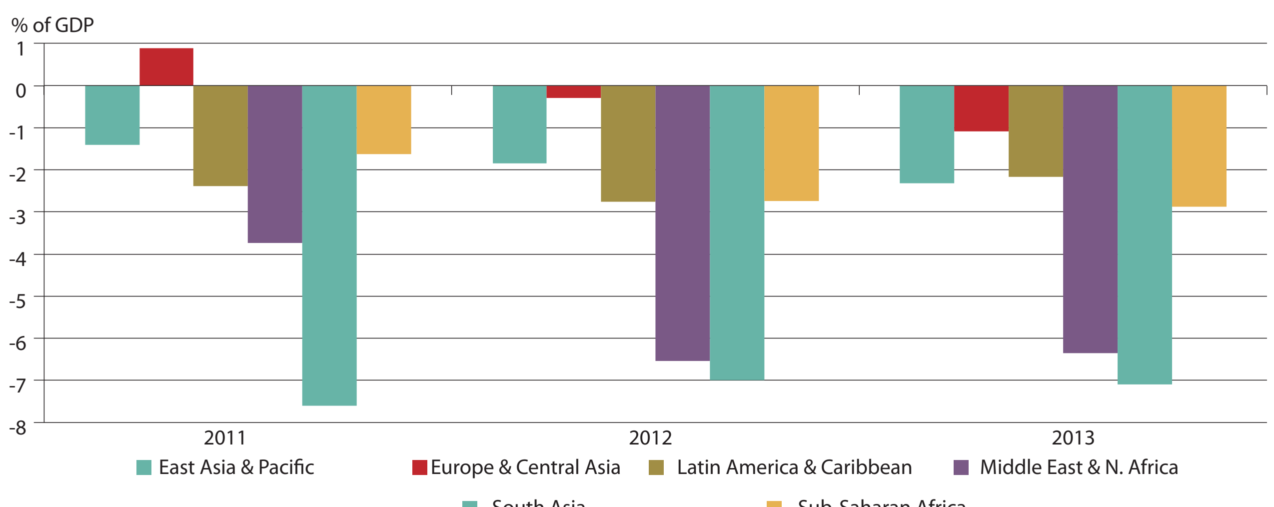
FIGURE 13: South Asia has the largest fiscal deficit of all regions



Source: World Bank Staff Calculations

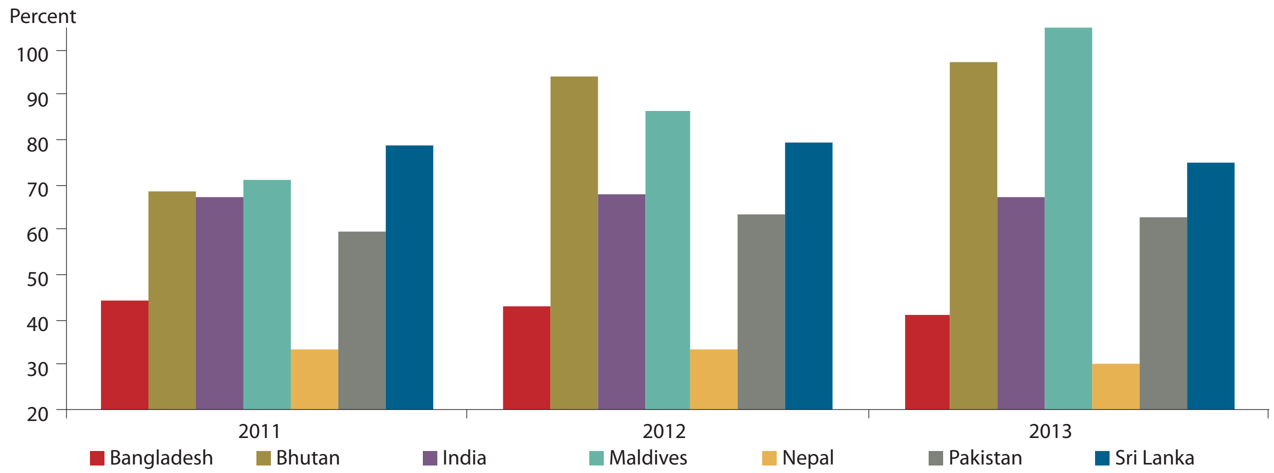
The largest reduction was in Sri Lanka, where public debt declined from 86 percent of GDP in 2009 to 79 percent in 2012.

FIGURE 14: The lion's share of the region's public debt is domestic



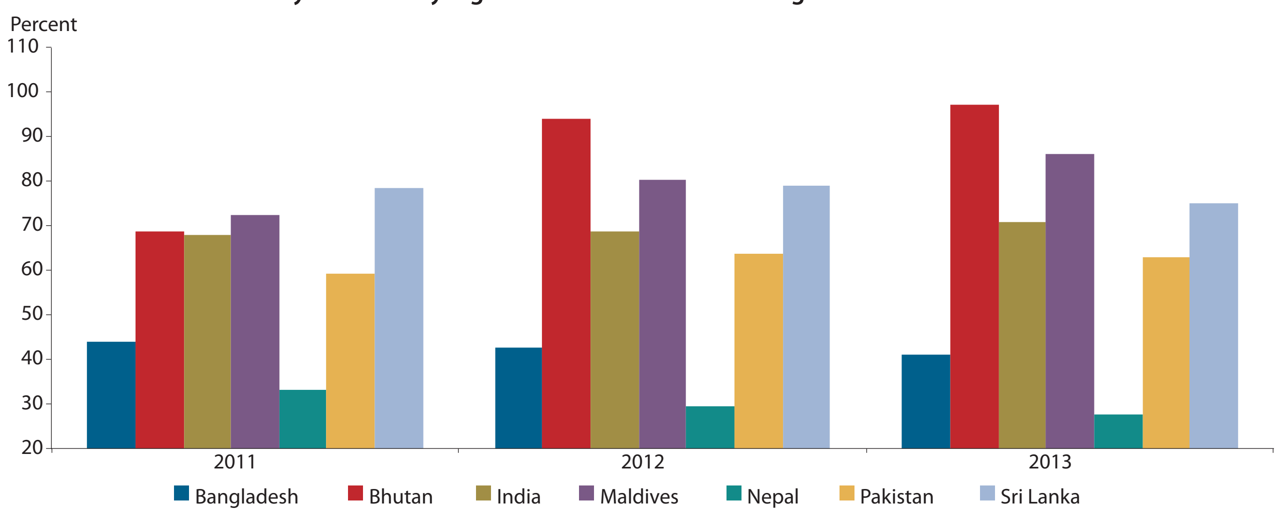
Source: World Banks Global Economic Prospects June 2013

FIGURE 15: Fiscal deficits are sizeable in most South Asian countries



Source: World Bank

FIGURE 16: Public debt stays stubbornly high in most countries in the region



Source: World Bank

The largest current account deficits are not always the most difficult to finance.

Current account deficits are large in most of the region, and some of them are extraordinarily high by international standards. India's current account deficit peaked at 5.2 percent of GDP in the first three quarters of 2012/13, and gave way to a more modest 3.6 percent in the fourth quarter. But the deficit for the fiscal year as a whole was 4.8 percent of GDP, up from 4.2 percent in 2011/12. Sri Lanka's current account deficit is projected at 4 percent of GDP for 2013, up from 6.6 percent in 2012, although the country is grappling with weaker trade performance. On the surface, Pakistan's deficit may not seem a matter of concern, as the country has a rather small and slightly improving current account deficit of 1 percent of GDP in 2012/13, down from 2.1 percent in 2011/12. The most positive notes come from Bangladesh and Nepal. Bangladesh's current account balance managed a solid rebound from a 0.4 percent of GDP deficit in fiscal year 2012 to a positive 1.9 percent in fiscal 2013, mainly fueled by export growth, flattening of imports and strong remittance inflows. Nepal remained in surplus in fiscal year 2013, at 3.3 percent of GDP, mainly thanks to remittances from its large number of migrant workers. On the other hand, Bhutan, Maldives and Afghanistan experience extraordinarily large current account deficits, with the latter two reaching a staggering 28 and 41.5 percent of GDP respectively.

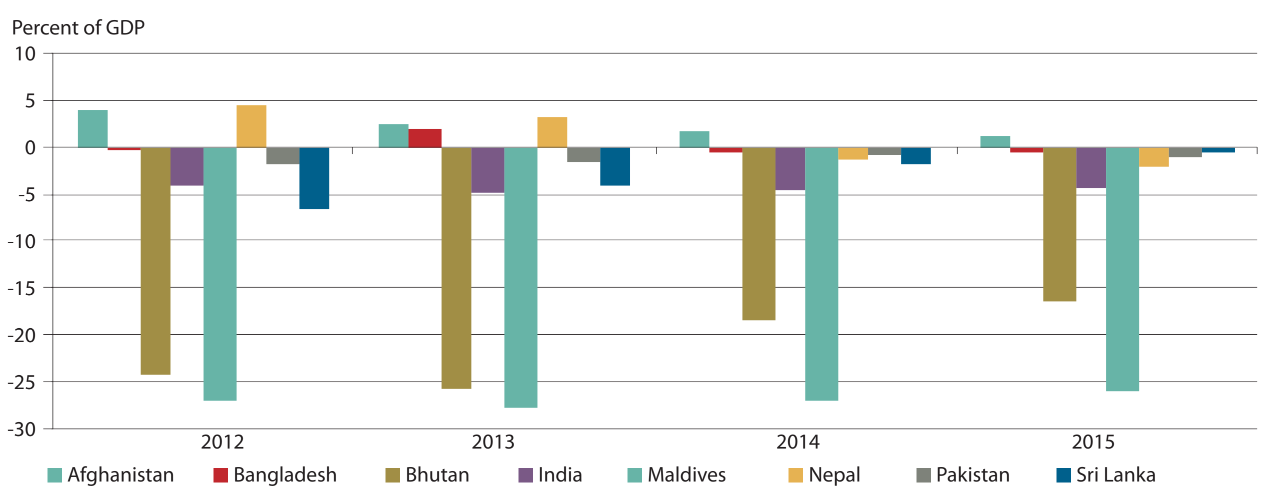
However, the magnitude of current account deficits is not a direct measure of the financing difficulties faced by individual countries. While Afghanistan's deficit is projected at 41.5 percent of GDP for 2013, driven by a widening trade deficit, the country is highly dependent on aid. Factoring in grants puts the balance at a positive 2.5 percent, down from 3.9 percent in 2012. The same applies to Bhutan, which maintained a high and growing current account deficit between 2012 and 2013, but has large reserves and finances its deficit mainly through grants and loans for hydropower development. In Maldives, debt financing continues to put pressure on the country's very low reserves and on its currency, the rufiyaa.

Capital has been leaving South Asia in the months since May 2013. The rebalancing of global portfolios was triggered by global investors reassessing risk and return in emerging markets relative to advanced economies. Overall, regional gross capital inflows declined by 70 percent between May and August, 2013, with bank loans, as well as equity and bond issues all dipping.

Financing current account deficits has become more difficult across South Asia and above all in India, where greater reliance on portfolio inflows increased exposure to sudden changes in investorsentiment. While FDI represented 91 percent of total capital inflows to the region in 2008, by 2012 the share had declined to 31.9 percent, the rest corresponding to more volatile portfolio investments. In India, overall inflows have remained sufficient and actually could increase foreign exchange reserves. But FDI only financed 22.5 percent of the current account deficit in 2012/13, down from 28 percent in 2011/12. In Pakistan FDI slightly increased, from US$ 0.7 billion in 2011/12 to US$ 1.2 billion in 2012/13. But total capital inflows deteriorated to US$ 0.5 billion, down from 1.5 billion the previous year. On the other hand, Bangladesh withstood pressures on its external position through managing constant increases in FDI, this past fiscal year 2013 amounting to growth of 9.2 percent.

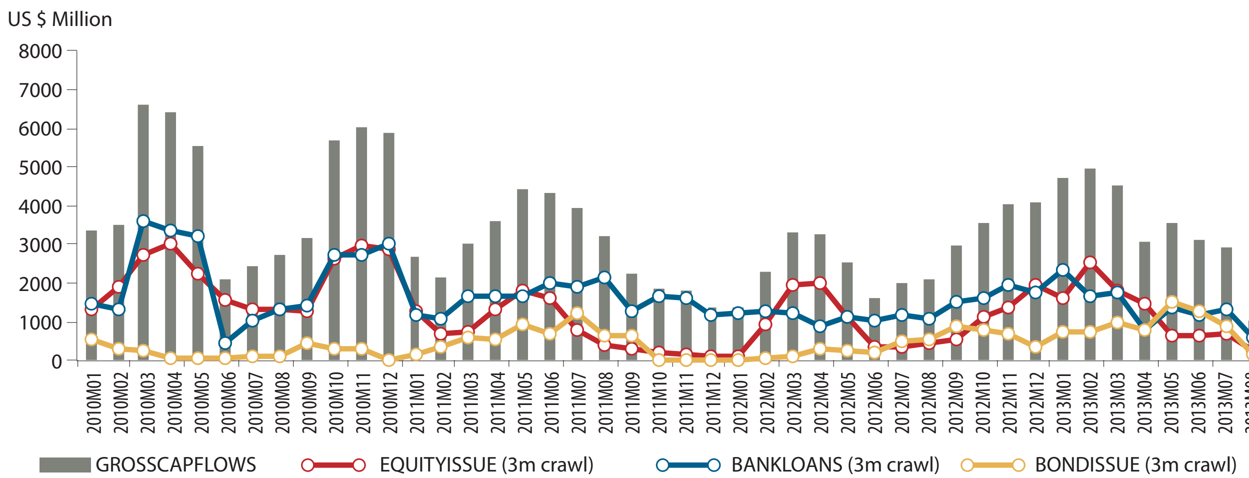
The reversal of capital flows has accelerated a longer-term trend towards real exchange rate depreciation, which in the near term is making the region more competitive. Not all countries in the region were directly affected by the announced QE tapering as India was, but Nepal and Bhutan have their currencies pegged to the rupee so that the consequences were the same. And with business cycle fluctuations in India affecting economic activity in the region, the impact also extended to countries whose currencies are independent from the rupee. Partly due to the substantial currency depreciation, In India exports began to strongly recover, with merchandise exports experiencing double-digit growth rates for the last three months. Afghanistan's exports, though growing more slowly than imports, are up by 76 percent in the first half of 2013, compared to 3 percent in 2012. Bangladesh registered a solid increase in export growth, from 5.9 percent in fiscal year 2012 to 11.2 percent in fiscal year 2013. Nepal, and especially Sri Lanka, are the exceptions to this general trend. Sri Lanka has continued loosing competitiveness relative

FIGURE 17: Large current account deficits are the norm in South Asia



Source: World Bank and IMF

FIGURE 18: There has been a decline in capital inflows in recent months



Source: World Bank DECPG

FIGURE 19: FDI now finances a much smaller share of the current account deficit

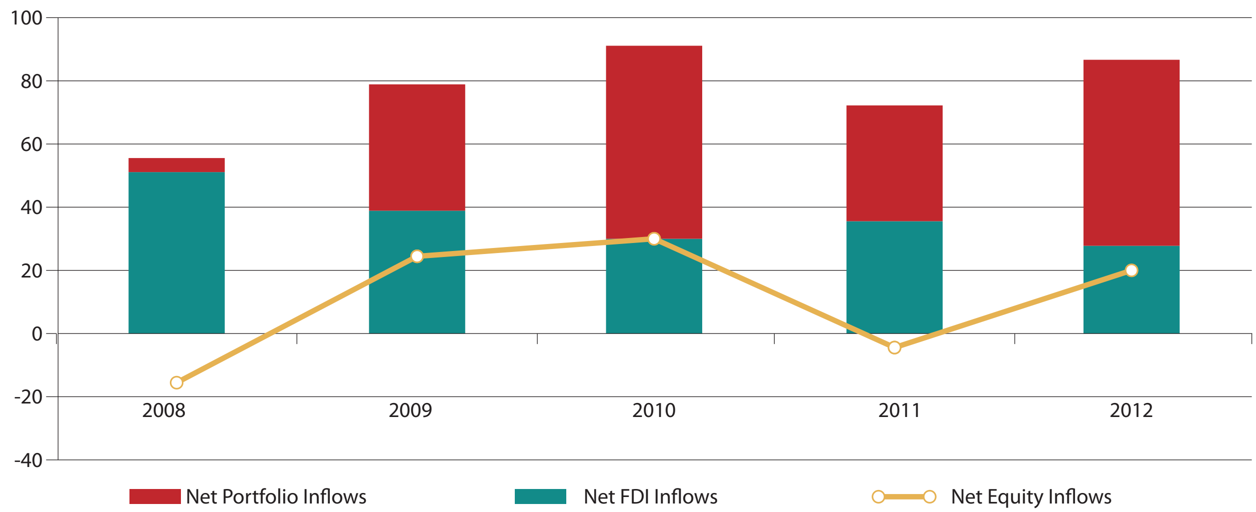
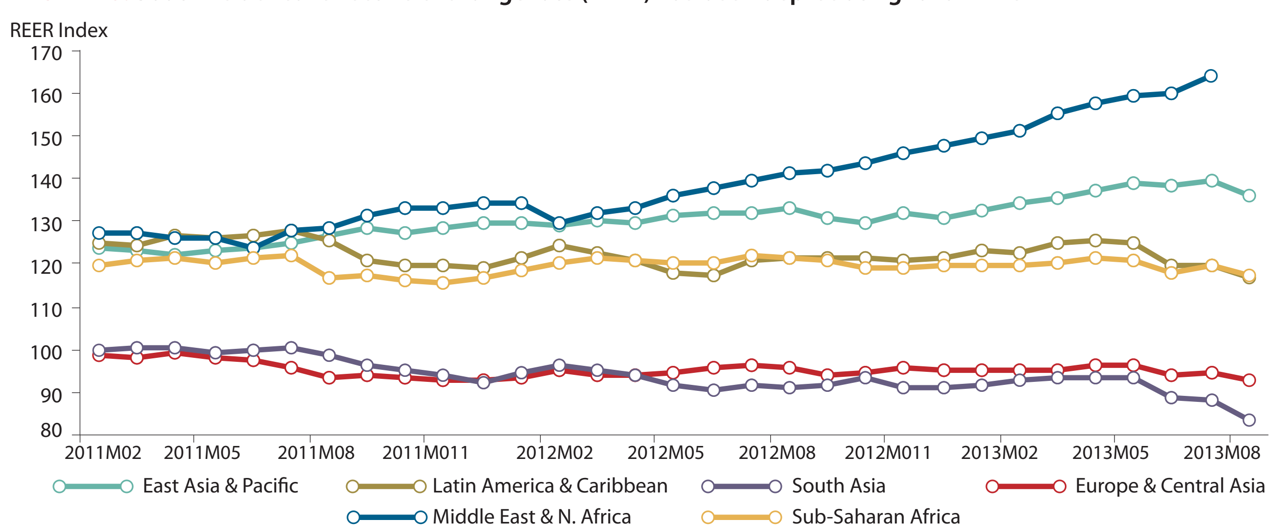
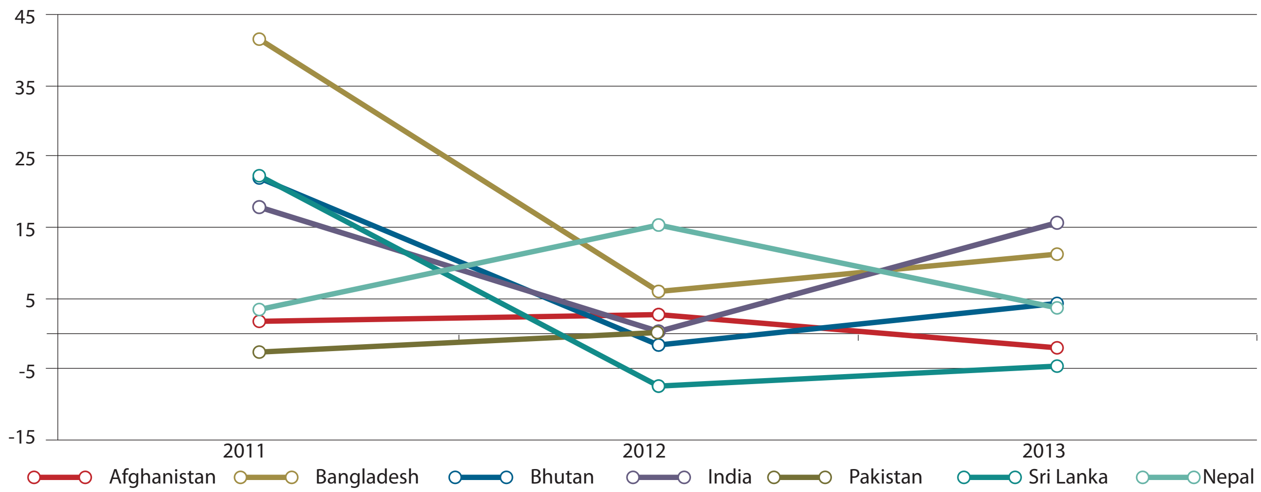


FIGURE 20: South Asia's real effective exchange rate (REER) has been depreciating for a while



Source: World Bank DECPG and ECB

FIGURE 21: Export growth is on its way up across most of South Asia

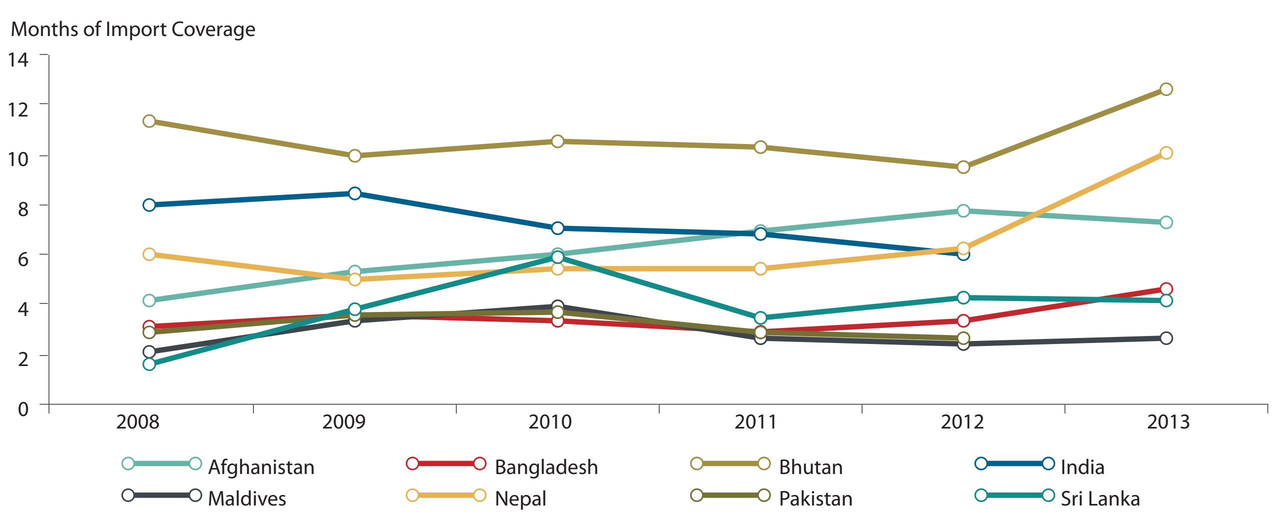


Source: World Bank and National Authorities

to its peers in the region as its currency, the Lankan rupee, appreciated right until May 2013. As a result, exports declined to 13.9 percent of GDP in the first half of 2013, down from 16.4 percent in 2012. In this sense, Sri Lanka has not yet started to benefit from the depreciation of its currency by 4.2 percent since May 2013. Similarly, Nepal experienced a significant slowdown in export growth to 3.6 percent for 2012/13, compared to 15.4 percent in the previous year.

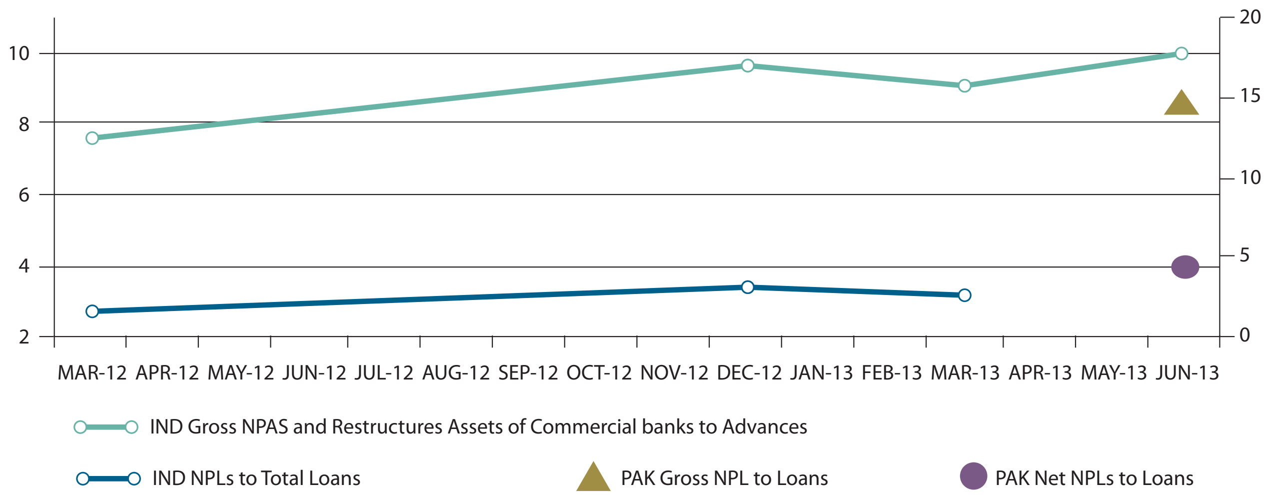
With the exception of Pakistan and Maldives, South Asian countries maintain solid reserve levels. Some of them, notably Bangladesh and Nepal, could even increase reserves in the recent past. India chose to let the rupee float, not risking to drive down its foreign exchange reserves, which were at a comfortable US$245 billion by end September 2013. Afghanistan's reserves plateaued in the first half of 2013 at around US$ 6.9 billion.

FIGURE 22: Foreign exchange reserves are broadly holding ground or even expanding



Source: World Bank, IMF and National Aukthorities

FIGURE 23: Non-performing assets of the banking system remain high in India and Pakistan



Source: Reserve Bank of India and Quarterly Compendium of the Banking Sector, 2013 (Pakistan)

Risks are on the rise but the policy response has been encouraging

Financial and private sector debt constitutes an increasing risk factor in some countries, particularly after the currency depreciation put stress on balance sheets. In India, corporate debt levels increased with the investment boom of recent years. Meanwhile foreign debt exposure, steadily growing over the past five years, strongly picked up more recently due to cheap interest rates on foreign exchange borrowing. Non-government foreign debt accounted for a substantial 16 percent of GDP and 80 percent of total external debt by end March 2013, with around a third due in less than one year. The recent rupee movements particularly affect large corporations, for which 40 to 70 percent of debt is denominated in foreign currency and may not be completely hedged. Bad debt, in turn, creates risks for the banking sector. Warning signs of stress include an increase in non-performing assets (NPAs) and gross non-performing loans (NPLs), from 3.4 percent in March 2013 to 4.4 percent in March 2014. In Pakistan, weak credit quality has translated into risk-averse banking, with NPLs remaining steady at 14.8 percent of total loan portfolio at end of June 2013.

Recent developments haved refocused policy makers' attention on the need to continue the long-term reform agenda—and the market has responded positively to announcements. Measures have been adopted in India to speed up the implementation of major investment projects and to ensure a longer-term supply of coal to newly built power plants. As a result of these announcements, the peak rupee depreciation of around 20 percent since May 2013 has partly been reversed. Also, markets may by now have factored in actual QE tapering – likely to unwind in 2014 – and therefore real effects could be more modest down the road. However, the policy agenda is broad: short-term imbalances, inadequate regulation and structural bottlenecks remain to be tackled.

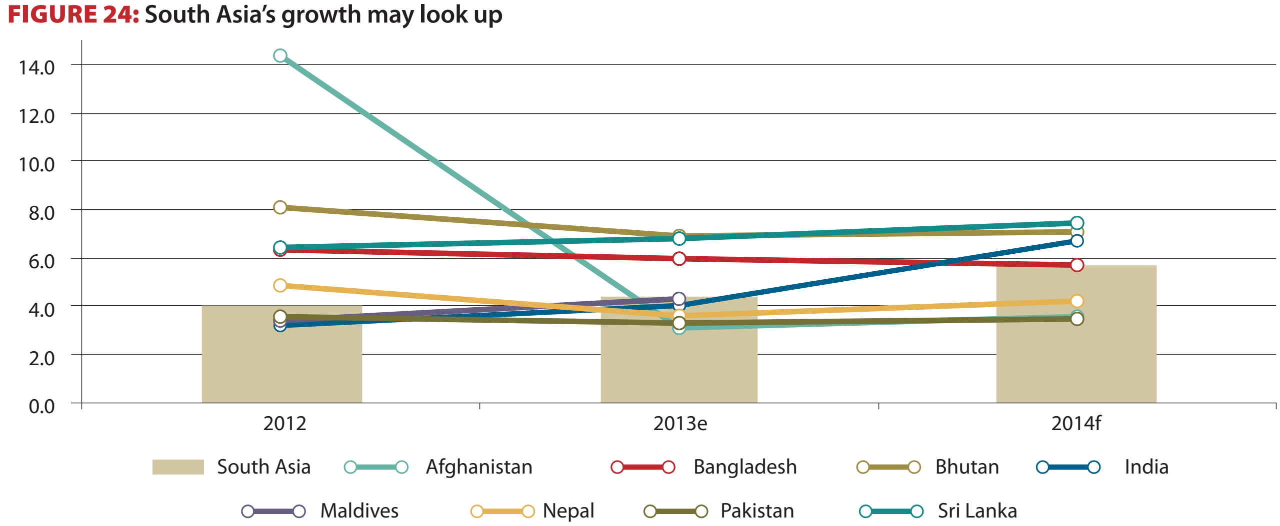
Outlook and policy

While the overall outlook for the region remains positive, serious downside risks continue to exist and any positive development in growth will depend on progress in ensuring macroeconomic stability, strengthening the investment climate, and removing infrastructure bottlenecks.

The overall outlook for South Asia remains cautiously optimistic

Despite the near-term challenges and significant downside risks, South Asia's outlook remains cautiously positive. The main drivers of this expected uptick are exports and investment. Most recent developments point to the direction of increased exports for South Asia, while both domestic and foreign investors continue to cautiously believe in the region's growth potential. However, International capital markets have delivered a loud and clear wake-up call to regional policy makers. A recovery in exports seems possible in light of depreciated currencies and the strengthening of global demand. Furthermore, the expected acceleration of large investment projects , resulting from measures taken in the past few months, is expected to contribute to further growth. In Pakistan, reforms initiated by the new government with the support of a program agreed with the IMF may rekindle investor sentiment. The challenge for South Asian policy makers is to keep a steady hand on the tiller and not get sidelined away from long-term reforms.

FIGURE 24: South Asia's growth may look up



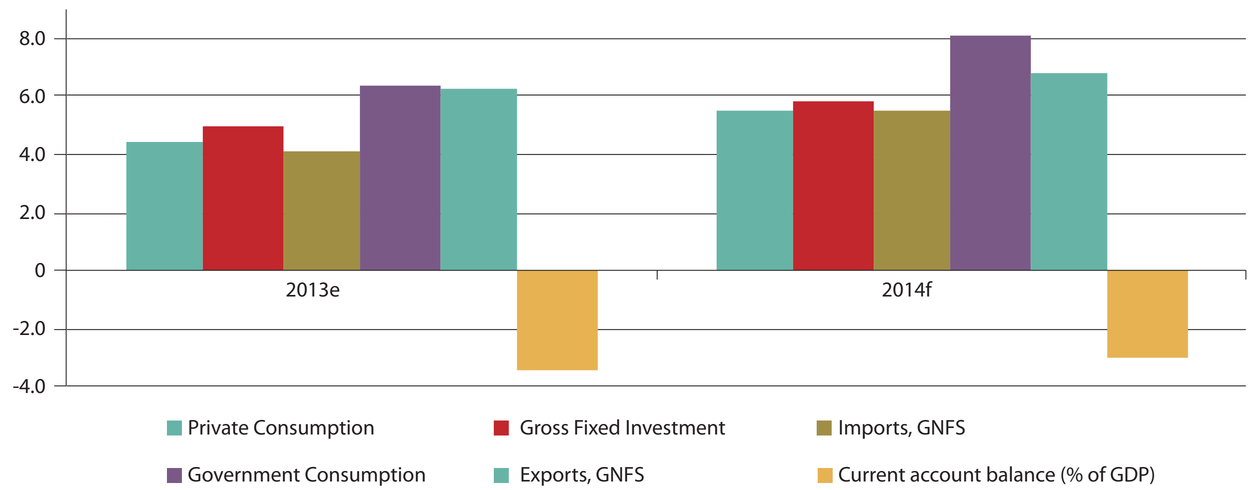
Source: World Bank DECPG (Fall 2013 estimates)

TABLE 1: South Asia's growth forecasts do not match its recent performance but they are encouraging

	Forecasts				
	2010	2011	2012	2013e	2014f
GDP growth	10.0	7.3	4.0	4.4	5.7
Private Consumption	7.3	7.3	4.2	4.5	5.5
Government Consumption	9.1	7.6	4.3	4.9	5.8
Gross Fixed Investment	16.7	6.0	2.6	4.1	5.5
Exports, GNFS	14.5	16.5	8.3	6.3	8.1
Imports, GNFS	16.0	17.5	11.0	6.3	6.8
Statistical Discrepancy (% of GDP)	0.7	2.5	3.3	3.8	3.9
Current account balance (% of GDP)	-2.6	-3.1	-4.5	-3.4	-3.0

Source: World Bank Development Prospects Group
Note: Forecasts are subject to change.

FIGURE 25: The positive outlook in growth will depend on contributions by exports and investment



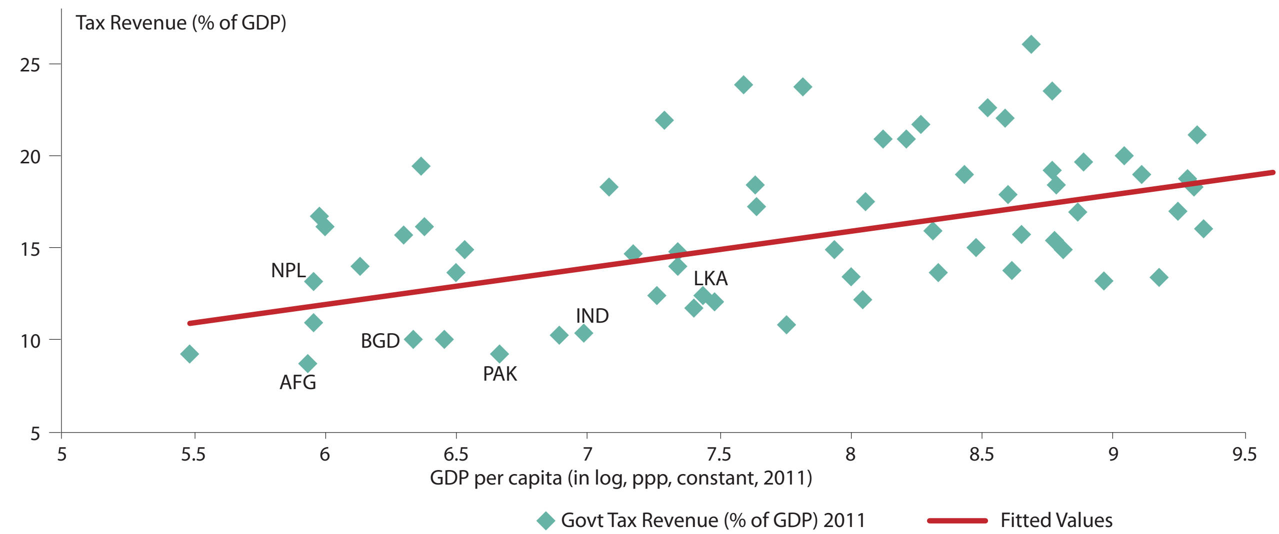
Source: World Bank DECPG (Fall 2013 estimates)

However, significant downside risks need to be closely monitored

Financial sector vulnerabilities and continued weakness in revenue collection will need to be tackled in order to mobilize resources for investment. Particularly some of India's biggest infrastructure companies have a debt coverage of less than one, meaning that their operating profits only cover interest payments. If large investment projects remain stalled, the overleveraged domestic infrastructure sector could face difficulties in the short and middle run. Furthermore, most South Asian countries are operating under tight fiscal conditions, which constraints the mobilization of resources towards much needed infrastructure. Recently, revenue generation has been less than satisfactory in countries such as Pakistan or Afghanistan. More broadly, South Asian economies raise less tax revenue, relative to GDP, than would be expected given their level of economic development. This is the result of frequent tax exemptions, widespread tax avoidance, and rampant tax evasion.

Across the region, a vibrant democratic process can be celebrated, but political transitions have created uncertainty on the policy response to changing global economic conditions. Recent democratic elections in Pakistan have improved the investment climate in the country, but many other countries in the region still face elections over the next 12 months. Heightened uncertainty over their outcome continues to underlie a wait-and-see attitude that restrains investment. Bangladesh remains in a state of political flux and uncertainty, due to protests and conflict between the two major parties. Across the region, the lack of consensus over key policy

FIGURE 26: Tax revenue in South Asia is low when compared to international peers

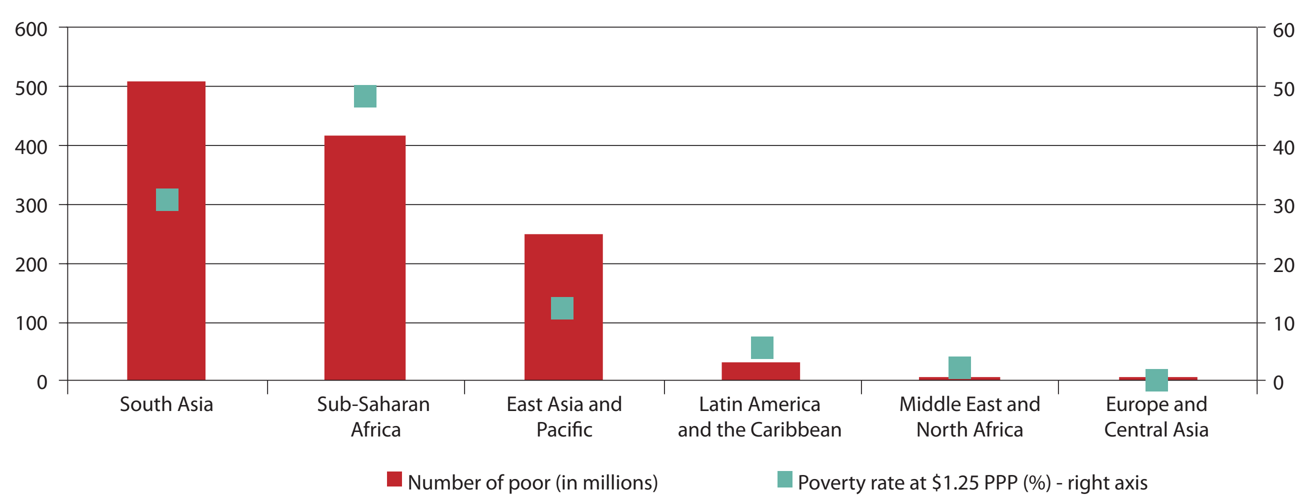


Source: WDI

orientations has become more apparent in the run-up to elections.

Yet macroeconomic stability and rapid economic growth remain top priorities for South Asia to successfully tackle its poverty challenge. While the poverty rate is higher in Sub-Saharan Africa, South Asia is the region with the largest number of poor people. And this is despite the fact that it is becoming a middle-income region. Policies that foster inclusion are necessary to maximize the poverty reduction associated with every percentage point of GDP growth. A focus on lagging regions and on disadvantaged groups is the key in this respect. But even with greater inclusion, meeting global poverty reduction goals will be unlikely if South Asia's economic growth slows down substantially relative to recent years. Three complementary policy areas are central to regaining the growth momentum. South Asian countries need to continue the gradual tightening of their fiscal and monetary policies, to reduce volatility. They also need to improve the quality of their regulations and strengthen governance, to boost investment –domestic and foreign- and support job creation. Last but not least, policy makers in the region must focus on removing infrastructure bottlenecks, especially in relation to energy..

FIGURE 27: South Asia remains at the center of the global poverty reduction challenge



Source: World Bank (2010 data or most recent available(

Focus: Business cycle transmission to and within South Asia

The recent upswing in actual and expected growth in advanced economies has been associated with an unexpected softening in several emerging market economies, particularly in the economies of Brazil, India, and Indonesia. Capital flows to these large developing countries have reversed course and currencies have depreciated significantly over the last five months. This might seem contrary to conventional wisdom, given that improving economic conditions in the US, Europe, and other advanced countries should be associated with better prospects for growth in developing countries if economic linkages are strong.

This may not be such a paradox when considering that higher expected growth in advanced economies will be associated with higher interest rates—as accommodative monetary policy is unwound— and this in turn changes the payoffs to investing in some markets compared to others. Changes in investor sentiment appear to be playing out in recent months as some emerging economies with relatively weaker fundamentals and greater external financing needs have been hit harder than countries with better fundamentals. South Asia is arguably more vulnerable than other regions as its financing needs are relatively large, budgets are strained, and its investment climate has faced significant hurdles. These weaknesses became more evident after the recent talk about QE tapering in the US.

But what has been, and what will likely be, the impact of the uptick in the global business cycle on South Asia? Is acceleration in growth in the US and other advanced economies typically associated with lower growth in South Asia and then a rebound? Do global shocks get transmitted to South Asia through India, or are all South Asian countries impacted jointly? Answering these questions may shed some light on how a global economic recovery may eventually be transmitted to South Asia. Of course, idiosyncratic events in each country are also important, so knowing the typical proportion of cyclical movements of GDP that can be explained by other countries is of interest. While business cycle transmissions between countries may be important, they may only represent a small part of what determines real GDP movements in any one country.

To address these questions, this focus section will examine the relationship between the transmission of economic shocks from India to the rest of South Asia, as well as from the world to South Asia. The intention is not to delve into the precise mechanisms by which economic shocks are transmitted between countries; for example, whether it is through trade, financial flows, remittances, or other factors. The goal is to examine the patterns and timing of the transmission of economic shocks to and within South Asia, and to get a sense of how lasting these connections are.[1] Doing so should help understand better the implications of the acceleration of advanced country growth on India and the rest of South Asia, and also the role of India's slowdown on the rest of South Asia.

1 For a discussion of possible transmission mechanisms, see Ejaz Ghani and Rahul Anand, "How Will Changes In Globalization Impact Growth In South Asia?" World Bank Working Paper #5079, 2009.

The analysis finds that:

- **Controlling for movements in cyclical components of real GDP outside the region, India's cyclical patterns are correlated to, and precede, cyclical growth patterns in the rest of South Asia (Bangladesh, Pakistan, Sri Lanka) and not vice versa.** This suggests that, independent of global business cycle movements, India likely plays an important role in influencing growth across the region. This effect has increased since the 2008 global crisis.

- **The US played a larger role in influencing global cyclical real GDP movements before the global crisis, but since then its independent influence has diminished as all regions are moving together in greater frequency.**

- **While relationships between cyclical movements in real GDP in South Asia and the rest of the world are uncovered, the proportion of regional cyclical movements within the region explained by other regions is quite small, particularly for South Asia excluding India.** This suggests that much of the cyclical real GDP variation in the region is idiosyncratic.

The nature of co-movements in economic activity affecting South Asia changed with the global crisis

Consider the following major economic units: India, South Asia less India SAR-I (which for the purposes of this analysis includes Bangladesh, Pakistan, and Sri Lanka), the US, advanced economies less the US (OECD-US) and the BRICS countries less India (BRCS, which includes Brazil, Russia, China, and South Africa).[2] Consider also the period starting in the first quarter of 2002, indexing the log of quarterly GDP in real terms to 1 in the first quarter of 2005. For all major economic units, and particularly for developing countries, growth was initially quite strong and then peaked in late 2007, before the onset of the global crisis. Not surprisingly, all units experienced a sharp downturn in growth between the fourth quarter of 2008 and the second quarter of 2009, reflecting the onset of the global crisis. The general pattern of growth is roughly similar between advanced economies (US, OECD-US) and developing countries (SAR-I, India, BRCS). While they move at different rates it is difficult to determine, by just eyeballing these trends, whether there is a high co-movement in growth or whether one unit tends to proceed or follow the others, which may provide an indication of the direction from which one region's general shocks are transmitted to other regions.

To better understand how movements in real GDP across units are related, and to extract important quarterly movements in each region's real GDP time-series, a first step is to de-trend the data.[3] De-trending not only allows the data's turning points and variation to become more apparent, but also reduces the likelihood of observing spurious high correlations between the data due to similar trend components. As is well documented in the statistical literature, time-series data that have similar trends will show high correlations even when cyclical movements may differ substantially. This is why the analysis needs to focus on percentage deviations in the real GDP growth of each unit relative to its trend. The availability of data for South Asian countries limits our sample to the period from the first quarter of 2002 to the first quarter of 2013.

Two features of the cyclical components of real GDP are striking. First is the dramatic decline in all series in the third quarter of 2008, corresponding to the global economic crisis which hit the world after the collapse of Lehman Brothers. Second, there is the downturn in India's GDP in the third quarter of 2002, due to the poor monsoon season, and the rebound the following year.

While examining the cyclical components of real GDP is informative, it still is difficult to observe visually any clear pro-cyclical or counter-cyclical co-movements in real GDP between countries, excluding the dramatic downturn at the end of 2008. Digging deeper into the possible relationships requires looking at the simple pair-wise correlations in the

2 Because only annual data for Pakistan and Bangladesh real GDP are available, quarterly series are generated by using the quarterly variation in industrial production, which is then mapped into a quarterly real GDP series using the Denton Method. Due to data availability in Sri Lanka, the analysis begins in 2002Q1 to 2013Q1.

3 This is done using the Hodrick-Prescott (HP) filter with $\lambda=16$. This produces a stationary series, as validated by the Augmented Dickey-Fuller test.

FIGURE F1: The bird's eye view cannot reveal co-movements

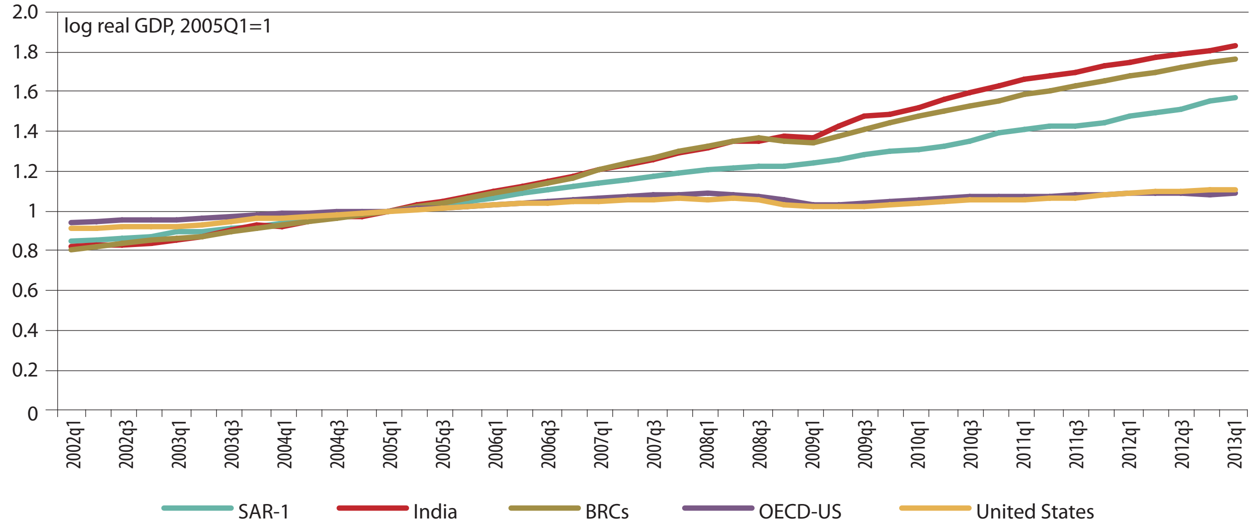


FIGURE F2A: Emerging markets and South Asia were hit hard when the global financial crisis started

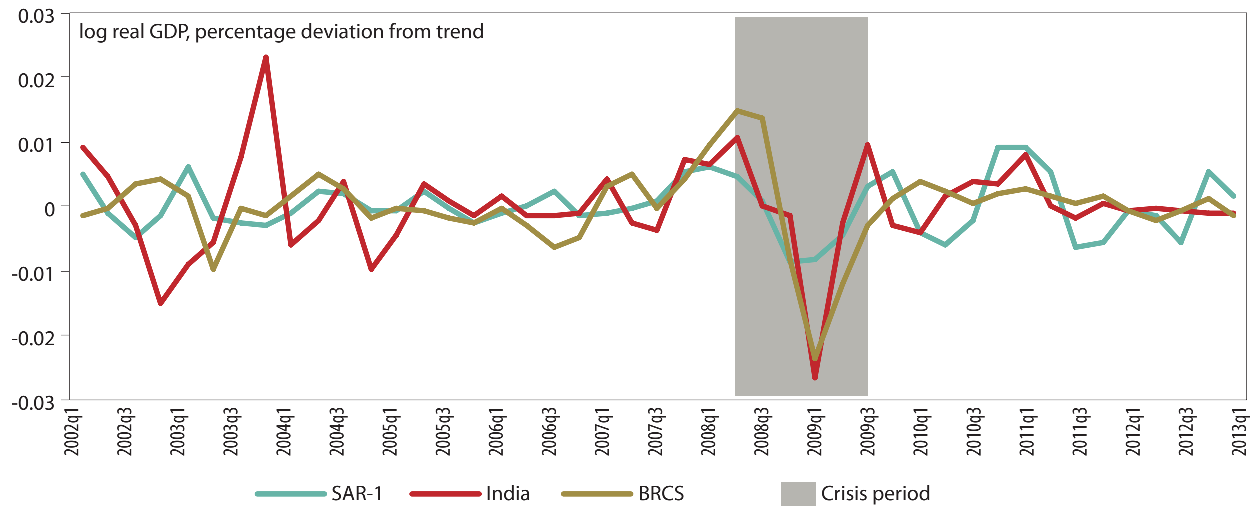


FIGURE F2B: Advanced economies also saw the cyclical component of their real GDP collapse in 2008

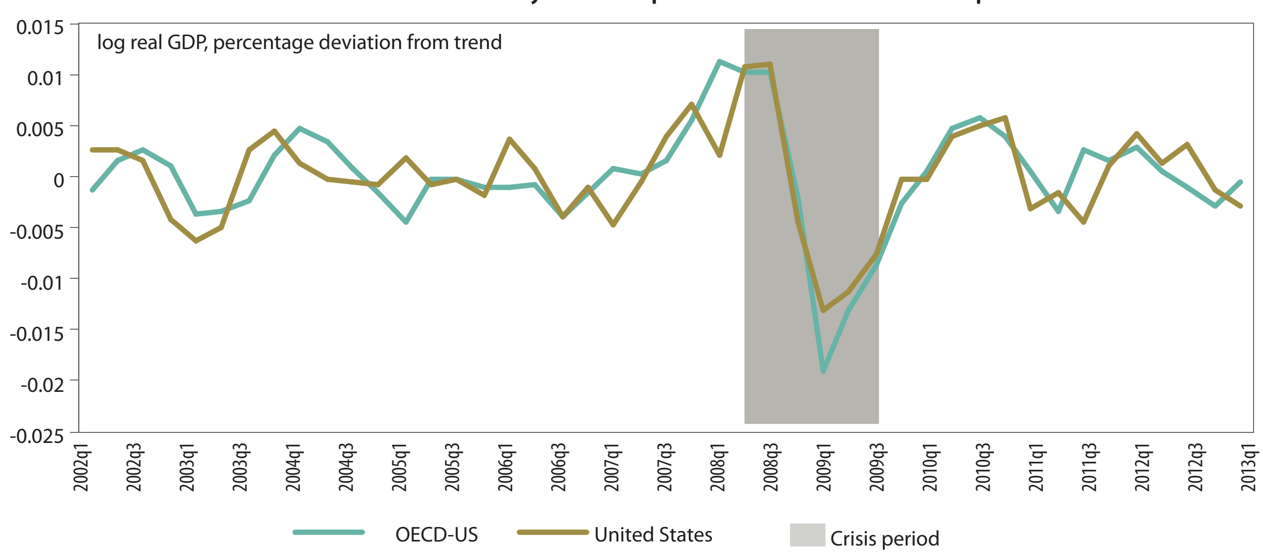


TABLE F1: Cyclical co-movements were strong during the crisis, but not so afterwards

Pre crisis (2002Q1-2008Q1) (#obs 25)

	SAR-I	India	BRCS	OECD-US	USA
SAR-I	1				
India	0.0676	1			
BRCS	0.322	0.0466	1		
OECD-US	0.268	0.275	0.733***	1	
USA	0.0187	0.566***	0.243	0.436**	1

Post crisis (2009Q4-2013Q1) (#obs 14)

	SAR-I	India	BRCS	OECD-US	USA
SAR-I	1				
India	0.399	1			
BRCS	0.173	0.203	1		
OECD-US	-0.368	0.4	0.0859	1	
USA	-0.137	0.197	-0.0412	0.561**	1

Full sample (2002Q1-2013Q1) (#obs 45)

	SAR-I	India	BRCS	OECD	USA
SAR-I	1				
India	0.320**	1			
BRCS	0.438***	0.430***	1		
OECD-US	0.250*	0.460***	0.850***	1	
USA	0.226	0.506***	0.699***	0.799***	1

Crisis (2008Q2-2009Q3) (#obs 6)

	SAR-I	India	BRCS	OECD-US	USA
SAR-I	1				
India	0.767*	1			
BRCS	0.801*	0.761*	1		
OECD-US	0.598	0.65	0.955***	1	
USA	0.638	0.558	0.954***	0.980***	1

Note:
-South Asia region does not include India.
-OECD does not include United States.
-*** p<0.01, ** p<0.05, * p<0.1

cyclical component of the de-trended data. To do this, it is convenient to break the data up into four time periods, 1) the full sample (from the first quarter of 2002 to the first quarter of 2013), 2) the pre-crisis period (until the first quarter of 2008), 3) the crisis period (from the second quarter of 2008 to the third quarter of 2009), and the post crisis period (from the fourth quarter of 2009 onwards).[4]

Examining the simple pair-wise correlations between cyclical components of GDP growth provides some initial insights into the relationship between business cycles in South Asia, India, and the rest of the world. In the pre-crisis period, fluctuations in South Asia excluding India (SAR-I) display relatively low and insignificant correlations with those of other regions. But India has relatively higher correlations—particularly with the US and other advanced countries (OECD-US). At only 7 percent, the correlation is lowest between SAR-I and India. SAR-I has higher correlations with the BRICS excluding India (BRCS, 32 percent) and with other advanced economies (OECD-US, 27 percent), and a relatively small correlation with the US (2 percent). In contrast, India has a relatively low correlation with the other BRICS (5 percent) and a higher correlation with other advanced economies (OECD-US, 28 percent) and especially with the US (56 percent). The low correlation India has with the rest of South Asia seems consistent with the low economic linkages between countries in the region. Paradoxically, India's economy appears to be more closely linked to that of the US than to the rest of South Asia.

Not surprisingly, during the crisis period, all regions show a significant jump in correlations. When the global economy turned downward there was a sharp synchronicity of movements in real GDP. Interestingly, India and the rest of South Asia became much more correlated with each other, and they both became more correlated with the BRCS.

The post-crisis period, 2008-2013, may have stronger relevance for how the recent acceleration in advanced economies may be transmitted to India and the rest of South Asia. During this period the correlation between movements in real GDP across major units falls substantially. This may suggest that the co-movements between economies are being driven by more idiosyncratic factors and less by global events. In other words, the typical transmission mechanisms between countries may have broken down to some degree, at

4 The start and end of the crisis period were determined using the Clemente, Montañés and Reyes test (Clemente, J., Montañés, A., and Reyes, M. (1998), "Testing for a unit root in variables with a double change in the mean", Economics Letters, Vol. 59, pp.175-182), which examines the data to identify structural breaks in the time-series.

least in recent years. There is still a relatively high and statistically significant correlation between the US and other advanced economies (OECD-US, 56 percent) and also, quite interestingly, between India and the rest of South Asia (SAR-I, 40 percent). However, the latter is not statistically significant at the 10 percent level.

Global cyclical movements do get transmitted to India and the rest of South Asia

Two key questions are how do cyclical movements in global real GDP get transmitted to India and the rest of South Asia, and how do cyclical movements get transmitted within South Asia itself. While simple correlations are indicative, they do not give a clear sense of the impact over time, nor do they account for the indirect impact of cyclical movements through third countries. For example, a high correlation in business fluctuations between India and the rest of South Asia could be jointly driven by the US and other advanced economies, and not independently by co-movements with each other. Moreover, correlations do not make it possible to determine the direction of the impact; for instance, whether changes in real GDP in the US precede changes in India's GDP, or vice versa.

As a means to answer these questions, a vector autoregressive (VAR) analysis is conducted. A VAR analysis helps to determine the impact of changes of the cyclical component of one unit's real GDP on another unit, taking into account the dynamic interdependencies among multiple units over time.[5] The results can be summarized by showing the impact of a one standard deviation change in the cyclical component of log real GDP on various units in the pre-crisis and full sample periods, over eight quarters. In the terminology of VAR analysis, this is called an impulse response. Confidence intervals of two standard deviations around the path of the estimated impact are also shown. The post-crisis period is not shown due to the lack of sufficient data to estimate the model.

What stands out the most from these analyses is the different pattern that a positive change in the cyclical component of real GDP in advanced economies has on India and the rest of South Asia, compared to a positive change in the cyclical components of real GDP in BRCS countries. A cyclical growth impulse from the US or other advanced economies tends to be associated with a one- to two- quarter initial increase in cyclical real GDP in India and the rest of South Asia. This positive response is followed by a decline and a reversion to the steady state trend. Reversion to the steady state is a much slower process in the pre-crisis period than in the full-sample. In contrast, an impulse from the BRCS countries tends to be associated with an initial decline and then an increase, as real GDP reverts to its steady state trend. This process also appears to have accelerated in more recent years. One possible explanation for this behavior is that BRCS may act more like competitors with South Asia than the advanced countries, so cyclical growth acceleration in these countries may be associated with a decline in South Asia as economic activity initially shifts away from the region. Overall, however, the statistical significance of these patterns is quite low, particularly for South Asia excluding India, as indicated by the wide confidence intervals.

The relationship between India and the rest of South Asia is quite interesting. The response of South Asia excluding India to a positive cyclical change coming from India is similar to its response to a change coming from the BRCS. There is an initial downturn and then upturn as the cyclical component returns to the steady-state trend. This indicates a possible substitution effect—a positive growth shock to India may initially take away growth from the rest of South Asia. In contrast, a positive cyclical change coming from the rest of South Asia has an initial positive impact on India, indicating that the rest of South Asia may complement India's growth prospects, as least in the near term.

5 All variables in a VAR are treated symmetrically in a structural sense, even if the estimated quantitative response coefficients will not in general be the same. Each variable (the cyclical log of real GDP in one unit) has an equation explaining its evolution based on its own lags and the lags of the other units' cyclical log of real GDP. The VAR used in this analysis incorporates two own lags and two lags of the other units' real GDP. Only two lags were chosen due to the relatively short time series, especially in the pre- and post-crisis time periods.

FIGURE F3: Pre-crisis: India and rest of South Asia initially respond positively to positive shocks in advanced economies

Response to one standard deviation changes in the cyclical component

South Asia less India response to: India's response to:

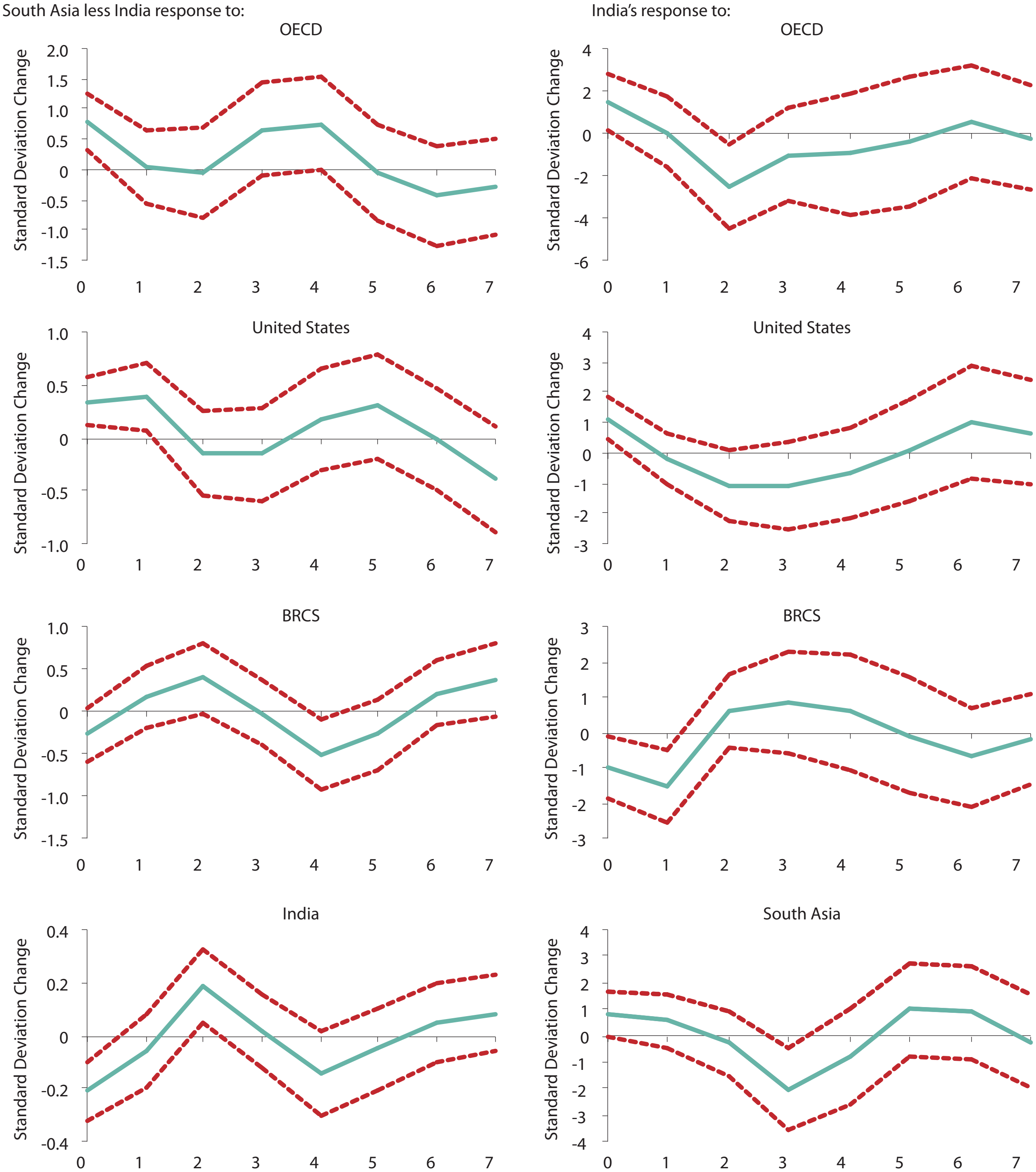


FIGURE F4: Full Sample: In recent years, India's cyclical upturns have become more of a benefit to the rest of South Asia

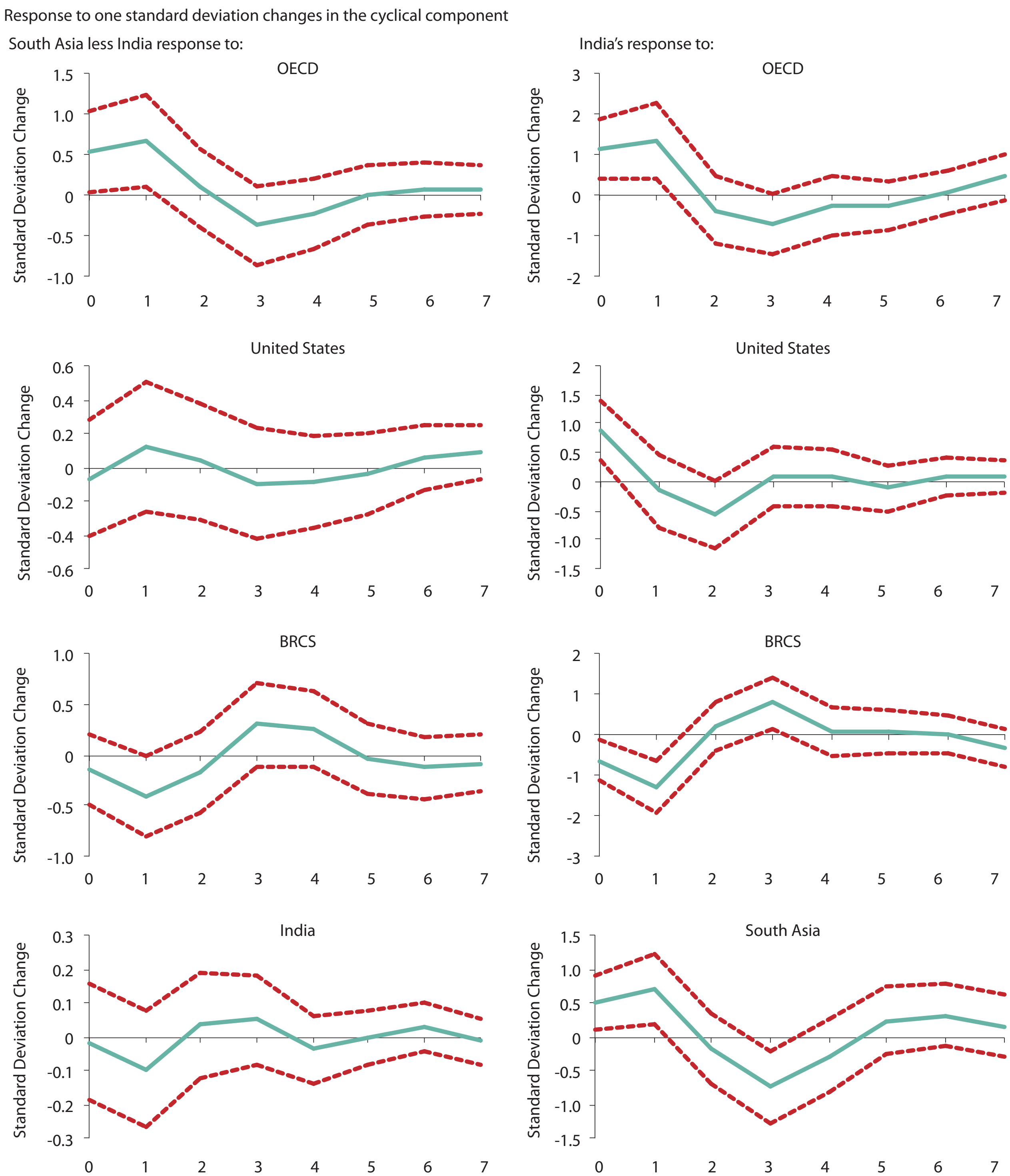


TABLE F2: India stays important for the rest of South Asia

(Temporal Precedence in Cyclical Real GDP)

Pre crisis period (2002Q1-2008Q1)

South Asia	0.253405 → -0.30726** ←	India
South Asia	0.048731 → -0.14376 ←	BRCS
South Asia	0.28173* → 0.680422* ←	OECD
South Asia	0.083588 → 0.354911* ←	United States
India	-0.29054* → -2.47017** ←	BRCS
India	-0.01563 → 1.954893 ←	OECD
India	0.163867 → 0.63499** ←	United States
BRCS	-0.30804 → 1.432267** ←	OECD
BRCS	0.040999 → 0.036295 ←	United States
OECD	0.189488 → 0.107577** ←	United States

Post crisis (2009Q4-2013Q1

South Asia	0.493468 → 3.636643** ←	India
South Asia	-0.21615** → 0.353468** ←	BRCS
South Asia	-0.66713** → -2.06934** ←	OECD
South Asia	-1.37113** → 1.851602** ←	United States
India	0.472048** → -0.31093* ←	BRCS
India	-0.54645** → 0.479699** ←	OECD
India	-0.8482** → 0.391596** ←	United States
BRCS	2.768388** → 0.050662 ←	OECD
BRCS	2.662996** → 0.442245** ←	United States
OECD	0.70047** → 0.121819 ç	United States

Fluctuations in India affect the rest of South Asia, albeit modestly, but not the other way around

While it is not possible to determine definitive causality in the relationship between economic shocks flowing from one economic unit to another, it is possible to observe whether cyclical shocks from one country or region tend to precede or follow shocks from another country or region. Showing temporal precedence can be indicative of causality, even if it does not confirm it. In statistical analysis, so-called Granger Causality is a means to provide some suggestive evidence how economic shocks transfer from one major economic unit to another. The direction of these pairwise relationships in cyclical components can be summarized by an arrow reporting the sum of the estimated coefficients on the lagged variables.[6] Relationships that are significant in one direction and not the other are considered to indicate clear temporal precedence and are highlighted in blue.

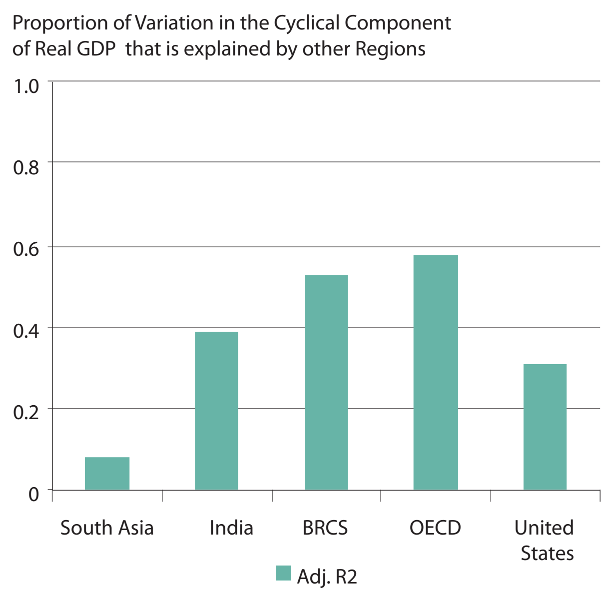
This analysis shows that India has clear directional impact on the rest of South Asia, but not vice versa. In the pre-crisis period, the relationship was negative, indicating possible competition with the rest of the region, while in more recent post-crisis years the relationship became much stronger and positive. This may indicate growing complementary economic relationships in the region, although they remain relatively modest compared to other regions.

In the pre-crisis period, the US has had a clear positive directional impact on India and the rest of South Asia; however, in the post-crisis period the direction of the relationship is not clear and goes in both directions. In the pre-crisis period the US also had a positive directional impact on other advanced economies and the BRCS. However, in the post-crisis period the direction of impact reversed vis-à-vis advanced economies and became ambiguous vis-à-vis the BRCS. In general, in the post-crisis period the direction of impact is less clear and there appears to be more bi-directional co-movements between countries and regions. The exception are co-movements between India and the rest of South Asia, and between the US and other advanced countries.

6 Two lags of the independent variables are used due to the small sample size in the post-crisis period.

One important question is how much overall variation in cyclical movements in each economic unit is explained by other countries and regions, and is not idiosyncratic. An answer to this question is provided by the proportion of variation in each unit's cyclical real GDP that is explained by two lags of all the other regions for the full sample (the so-called adjusted R-squared)[7]. For South Asia excluding India, the total variation explained by other major economic units is only 7.9 percent. For the US it is 30.4 percent, for India it is 39.2 percent, for the BRCS 52.3 percent, and for other advanced economies 57.3 percent. The comparison suggests that in South Asia's case, most of the variation in cyclical real GDP is idiosyncratic and not related to other major economic units.

FIGURE F5: India, the rest of South Asia, and the US are largely subject to idiosyncratic shocks



7 The Adjusted R-squared is estimated applying Ordinary Least Squares to an equation with the cyclical fluctuation of the major unit of interest as the independent variable and two lags of all the business cycle fluctuations of all other major units as the explanatory variables.

South Asia Country Briefs

In alphabetical order:

AFGHANISTAN

BANGLADESH

BHUTAN

INDIA

MALDIVES

NEPAL

PAKISTAN

SRI LANKA

Afghanistan

Recent Economic Developments

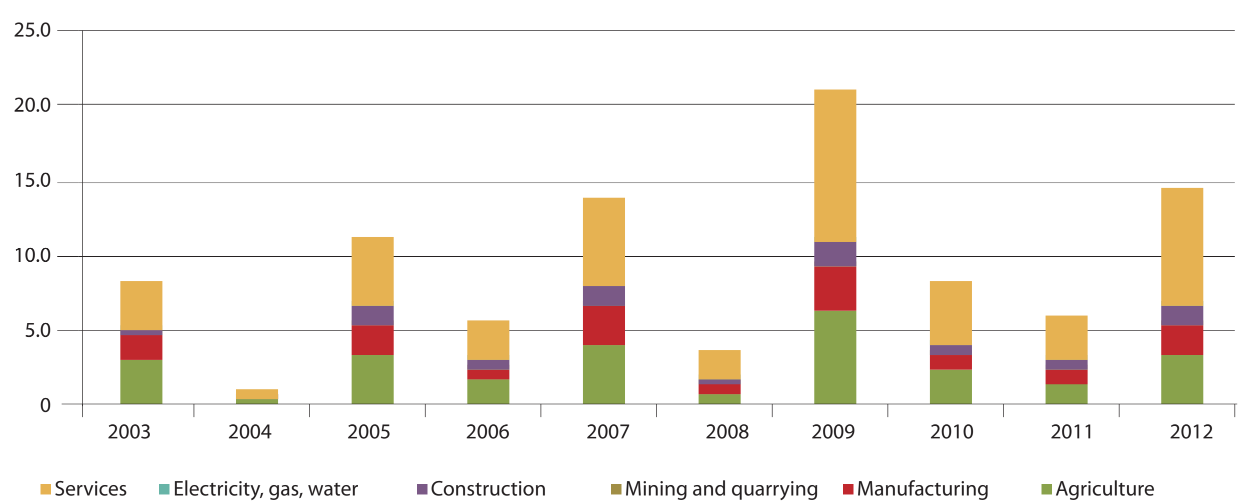
Economic growth slowed considerably in 2013 from a strong showing in 2012, amid uncertainty over the political and security transition in Afghanistan. GDP growth is projected to reach 3.1 percent this year and 3.5 percent in 2014, from an outstanding 14.4 percent in 2012 that was driven by a bumper harvest and pre-transition surge in services. Agriculture this year is expected to contribute flat or slightly negative growth, while investment has slowed as well. Overall growth is slated to pick up again in 2015, assuming a smooth political and security transition.

Presidential elections are scheduled for April 2014, which seems likely to complicate uncertainty over whether the new government will be sufficiently cohesive to make coherent policy decisions.

Fiscal performance of the current government, meanwhile, has weakened, leading to declining revenues that could potentially derail Afghanistan's smooth passage toward self-reliance. Revenues amounted to Afs 48 billion in the first six months of 2013, down 11 percent in nominal terms from Afs 54 billion in the first six months of 2012. The decline in revenue collection was due to leakages and weakness in administration, particularly in customs, and the economic slowdown. As the political uncertainty invites greater rent-seeking behavior and undermines enforcement, revenues are expected to remain low, at about 10-10.5 percent of GDP during 2013-14. To preserve fiscal sustainability, a concerted effort will be required on the part of the authorities to improve revenue mobilization by strengthening tax and customs administration and expediting the introduction and implementation of the planned value-added tax. Afghanistan faces considerable expenditure needs in the areas of security, infrastructure development, service delivery, and operations and maintenance. Meeting these needs will also require significant donor assistance for the foreseeable future.

In the midst of these transition-related uncertainties and underperformance, Afghanistan's leaders will need to stay focused on the country's medium-term structural reform goals. These include: (i) safeguarding sustainability by mobilizing revenue and securing grant assistance; (ii) supporting inclusive and job-creating post-transition growth by unlocking the potential of the agriculture and natural resource sectors and by tapping the potential of regional integration; (iii) raising the low levels of human capital and skills; and (iv) continuing to strengthen institutions and governance.

Services remain a large component of GDP Growth



Outlook and Policy

Political stability, security, and certainty, or their absence, are the primary factors that will determine the economic performance of Afghanistan in the medium term. Continued violence, economic crime, and systemic corruption also have undermined progress in Afghanistan's governance and state-building agenda. Much will depend, therefore, on Afghanistan's success in achieving peace, stability and reconciliation

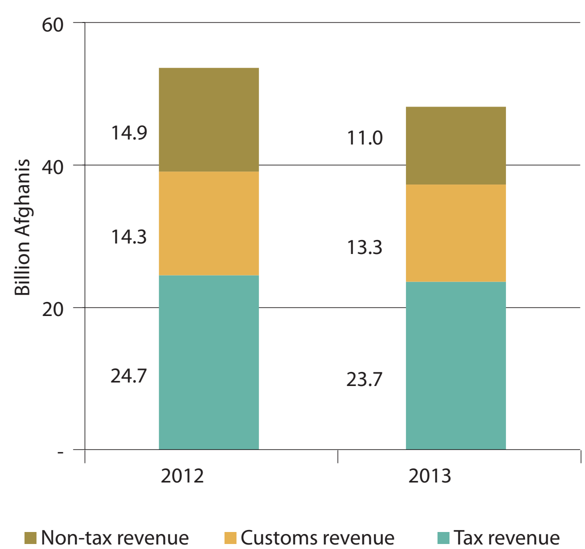
In the medium term, post-transition growth is projected at about 5 percent per year during 201516. This is less than the average annual growth of 9.4 percent during 2003-12 that was fueled by the surge in international aid and security spending.

Agriculture and extractive industries are most likely to drive growth. Agriculture accounts for about a quarter of GDP and is linked closely to other parts of the economy, such as food and beverages, which account for almost all of manufacturing, and parts of transport and retail. Afghanistan has the potential to build on this foundation by reviving its historical position as an important exporter of fruits, nuts, vegetables, and other higher value-added products. This will require investments in irrigation and extension services to improve capacity, as well as efforts to build and improve downstream agro-processing activities. The extractive industry, which currently accounts for a very small share of GDP, has significant potential in light of Afghanistan's deposits of copper, iron ore, and hydrocarbons. However, the timeline for natural resources to contribute meaningfully to Afghanistan's prosperity has become less certain in light of recent developments in the sector. Unlocking this potential will require progress on the legislative framework as well as the ability to secure financing for the necessary infrastructure.

The current fiscal revenue outlook is subpar and likely to delay Afghanistan's progress to self-reliance, so the authorities need to improve revenues. In light of the recent weak revenue performance, domestic revenues are projected at 10.1 percent of GDP in 2013, rising to 12.6 percent by 2016. Weak revenue performance in 2013-14 is projected to result from a number of factors including the slowdown in economic activity, changes in the structure of imports, but perhaps more importantly, from high leakages and weaknesses in administration, particularly in customs. In light of recent developments, the increase in revenues to 12.6 percent of GDP by 2016 will require a concerted effort on the part of the Afghan authorities to (i) reduce leakages and strengthen customs administration; and (ii) expedite the introduction and implementation of the planned value-added tax (VAT).

Budget expenditures are expected to continue to rise from about 24 percent of GDP in 2012 to about 30 percent of GDP by 2016. The increase in budget expenditures is largely a result of more spending moving on budget from previously being undertaken directly by donors. Afghanistan has considerable public expenditure needs in the areas of security, service delivery, building essential infrastructure, and operations and maintenance. These needs are likely to remain substantial for the foreseeable future.

Cumulative Revenues, H1 2012 & 2013



Donors have committed to cover the budget financing gap, but the funds are contingent upon the Afghan government making sufficient progress under the Tokyo Mutual Accountability Framework (TMAF) that calls for improved domestic revenues. The framework commits the Afghan government to increasing revenues to 15 percent of GDP by 2016 and 19 percent of GDP by 2025. Given current projections, it could achieve this only by developing the mining sector, fostering private sector development, broadening the tax base and reducing the leakages at customs. The current decline in revenue therefore poses risks not only to long-term fiscal sustainability but also to the achievement of TMAF targets.

Bangladesh

Recent Economic Developments

GDP growth in FY13 decelerated for the second successive year, to 6 percent. Disruptions caused by political and labor strife, deepening tensions over the impending political transition, and inadequate improvements in the provision of power, gas, and infrastructure were key factors in the slowdown. These served to weaken investor and consumer confidence, prompting real private investment to fall by 1.2 percent and private consumption to grow moderately at around 5 percent, well below the historic 9 percent average growth rate. Robust increases in exports and remittance helped maintain GDP growth above the average 5 percent growth for developing countries in 2013. Growth declined in both agriculture and services while industry rose slightly.

Annual average inflation declined to 6.8 percent in FY13, from 8.7 percent in FY12, due mainly to declines in both food and non-food prices internationally. Increased production, declining demand from large importers, and increasing food stocks in international markets exerted downward pressures on international prices. The conduct of monetary policy improved remarkably in FY13, which helped reduce non-food price increases. As year-on-year inflation was still high in August, at 7.4 percent, the Bangladesh Bank's (BB) decision to stay the course on monetary discipline in FY14, despite the forthcoming elections, was a bold and timely step.

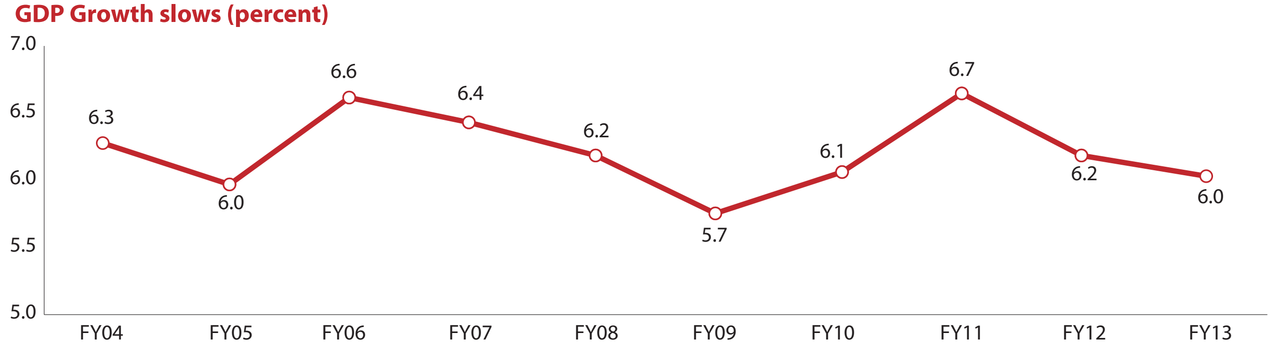
The external trade deficit decreased significantly, due mainly to an increase in export growth from FY12 and flat import payments. The surplus in current and financial accounts also improved remarkably. As a result, foreign exchange reserves continued to set historic records. The current reserve level, at 4.9 months of imports, is adequate but not excessive. Bangladesh Bank interventions helped keep the interbank average nominal exchange rate stable, but the premium on the curb market rate has been increasing since April, 2013. This apparent divergence in the behavior of the formal and informal market exchange rates is attributable to a rise in demand for informal market dollars, perhaps due to capital flight.

The banking system remains under stress and capital market activities have been weak. Several financial scams and resultant loan defaults in the state-owned commercial banks (SCBs) moved them into positions of insolvency, which requires, and has begun to receive, urgent attention. Capital market activities remained generally weak throughout FY13. Low investor confidence persisted, and securities traded narrowly in both volume and price.

Fiscal policy is on track, but a host of domestic challenges remain. The conduct of fiscal policy in FY13 has been broadly in line with the original budget. The overall fiscal deficit (excluding grants), at 4.3 percent of GDP, has been below the budget target of 5 percent. The FY14 budget targets a modest deficit of 4.6 percent of GDP and a domestic financing target of 2.9 percent, as the authorities face numerous domestic challenges. These range from increasing road traffic congestion, and shortages of power, water, and gas to the need for higher welfare spending to protect the poor and vulnerable.

Structural reform has progressed slowly. The IMF's Extended Credit Facility (ECF) is on track, strengthening macroeconomic conditions and structural policies. The new VAT law is being implemented; the

GDP Growth slows (percent)



Source: Bangladesh Bureau of Statistics

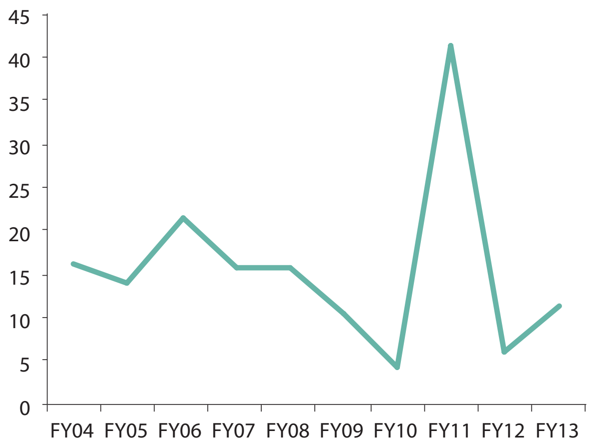
National Board of Revenue has introduced an online tax registration system; amendments to the Banking Companies Act have been passed, and progress is being made in identifying critical weaknesses in the state-owned commercial banks in a step toward strengthening their governance and financial positions; the FY14 budget introduced revenue reforms such as increasing the corporate-profit tax rate on cigarette manufacturing companies and reducing the nominal protection rate to 28.1 percent in FY14 from 28.9 percent in FY13.

A succession of devastating factory accidents in the past 11 months, topped by the Rana Plaza building collapse in April that killed more than 1,100 workers, have revived concerns over labor standards, wages, and compliance with safety regulations, and threaten the future growth of Bangladesh's most important export industry, ready-made garments. The government has pledged to work with the International Labor Organization to improve worker safety in the country. At the same time, supply-side bottlenecks have to be addressed. Ongoing political uncertainty, frequent general strikes and associated hostilities, have added to the existing negative pressure caused by longstanding energy and infrastructure deficits that continue to dampen the investment climate.

Outlook and Policy

Bangladesh's near- and medium-term macroeconomic outlook hinges on internal stability and structural reforms. The outlook is subject to several vulnerabilities – further growth slowdown due to internal strife, the prospect of resurgent inflation due to intensified supply disruptions and wage-push factors, slowing of exports and remittances, fiscal expansion due to increased recurrent expenditures in response to political pressures, and failure of financial intermediation. Overall, the Bangladesh economy is moving into a more volatile phase. The risks stemming from the impending political transition have grown significantly, while new risks and challenges have gained prominence. Notable among the latter is the damaged image of Bangladesh's only manufacturing mega-success story – garment manufacture.

Export Growth moderates (percent)



Source : Export Promotion Bureau

Revamping the garment industry in the wake of the deadly factory accidents will be crucial to Bangladesh's future economic growth. The crisis within the garment industry has placed the country's vital foreign currency generator at a historic crossroads. The sector could become a US$36-42 billion revenue-earner by 2020 if it can prevent a recurrence of the horrors seen in the Tazreens Fashions and Rana Plaza disasters and improve workers' employment conditions. But continued neglect of workers' rights and safety would prompt international buyers to cut their reliance on Bangladesh, or even abandon the country altogether. The United States' removal of Bangladesh products from its Generalized System of Preferences (GSP) might not hurt unduly, but if the EU were to suspend its GSP benefits, the country could lose 4.1 percent, or even as much as 8.1 percent of total exports.

The impact of the Indian rupee depreciation is uncertain. The rupee had depreciated to about 62 per dollar in mid-September from 53.7 in early May. Similar large depreciations have occurred in Indonesian and Turkish currencies as well. Since these countries compete with Bangladesh in the export markets, such large depreciations are likely to toughen competition for Bangladesh. The impact will depend on the permanence of the currency depreciation, the impact of the policy response in these countries, the feedback effects on their inflation rates, and the impact on the cost of intermediate input and raw material imports to Bangladesh. But a weaker Indian currency is not all bad news for Bangladesh; since the country sources more than one-third of its imported cotton and cotton fabrics in India, the weaker rupee makes these imports far cheaper, which in turn reduces the production costs of Bangladesh's garment exports, thereby muting the loss of competitiveness.

Overall, the Bangladesh economy is moving into a more uncertain phase. The risks stemming from the impending political transition have enhanced significantly while new risks and challenges have gained prominence.

Bhutan

Recent Economic Developments

Bhutan's growth remains strong, averaging over 8 percent annually, though it is estimated to have moderated to 6.9 percent in 2012/13 due to the rupee shortage and statutory measures that restricted credit. Hydropower contributes about one-third of GDP and one-fifth of economic growth, including direct and spillover activities.

The construction of ongoing and pipeline hydropower projects will remain the major drivers of growth, with the industry sector projected to grow at 6.2 percent through 2014. Growth in the service sector has come from an increase in domestic demand and tourism, particularly new investments in hotels and restaurants, the finance sector, and transport and communications.

The overheating episode which started in 2011 has ended, though its effects linger. Rapid private-sector credit growth has been severely dampened by a credit crunch caused by the government's emergency halt to personal loans as a temporary measure to curb the demand for rupees.

The 2013/14 budget projects a higher budget deficit of 3.7 percent combined with an off-budget stimulus plan of around 4 percent of GDP executed through the banking system. The deficit was ramped up by a sharp drop in project-tied grants from India.

Inflation, which had fallen from last year, was up again, to 5.5 percent (y-o-y) in Q2 2013 from 8.4 percent in Q1, due mostly to pass-through from higher fuel prices imported from India.

Bhutan remains dependent on donor funding to finance capital expenditures. The FY 2013 fiscal position is expected to produce a moderate deficit of 0.9 percent of GDP, down from the previously estimated 1.6 percent. Tax collection slightly over-performed, particularly corporate tax and excise duties -- though tax revenues overall were lower this year by India refunding only one year of excise duty as opposed to the customary two-year's duty. Current expenditures remained below the fiscal anchor of staying within the domestic revenue envelope (a constitutional requirement), while capital spending increased commensurately with additional donor grant financing.

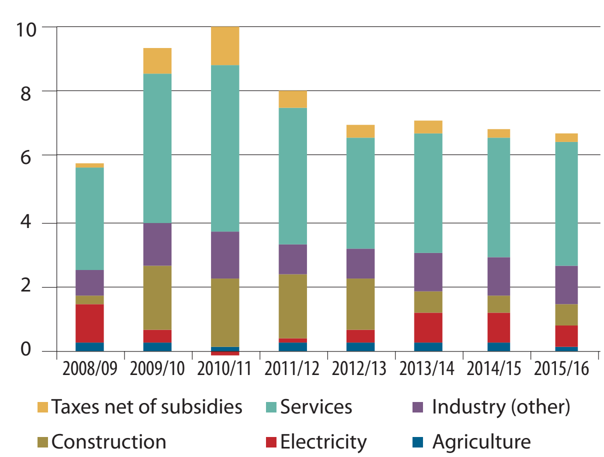
Bhutan has relatively high debt, but the risks of debt distress are mitigated because public debt is concentrated in the commercially-viable hydropower projects, which are virtually guaranteed revenues from electricity exports to India.

Outlook and Policy

The economic outlook is favorable if risks are managed well. In the medium term, GDP growth is expected to average 6.9 percent, driven by investment in hydropower projects and expansion of the service sector. The fiscal stimulus package could boost growth. India's growth slowdown and the rupee depreciation have the potential to adversely affect Bhutan's growth through financing uncertainties and by reducing Indian tourist arrivals.

Long-term development challenges remain. Economic volatility is a natural risk, with more than half of government revenues coming from grants and electricity sales to India. Revenues are subject, therefore, to the timing of hydropower developments coming on-stream, seasonality of power generation, and timely receipt of grants. The absence of scale economies in most industries, limited access to finance, skill mismatch of the labor force, and under-provision of infrastructure constrain the development of a vibrant private sector. With its thinly-spread population and high transport costs, Bhutan would benefit from urban agglomeration with careful city management. Located in a region subject to natural disasters, Bhutan would also benefit from prioritizing the development of robust plans for proactive risk management.

GDP Growth by Sector



India

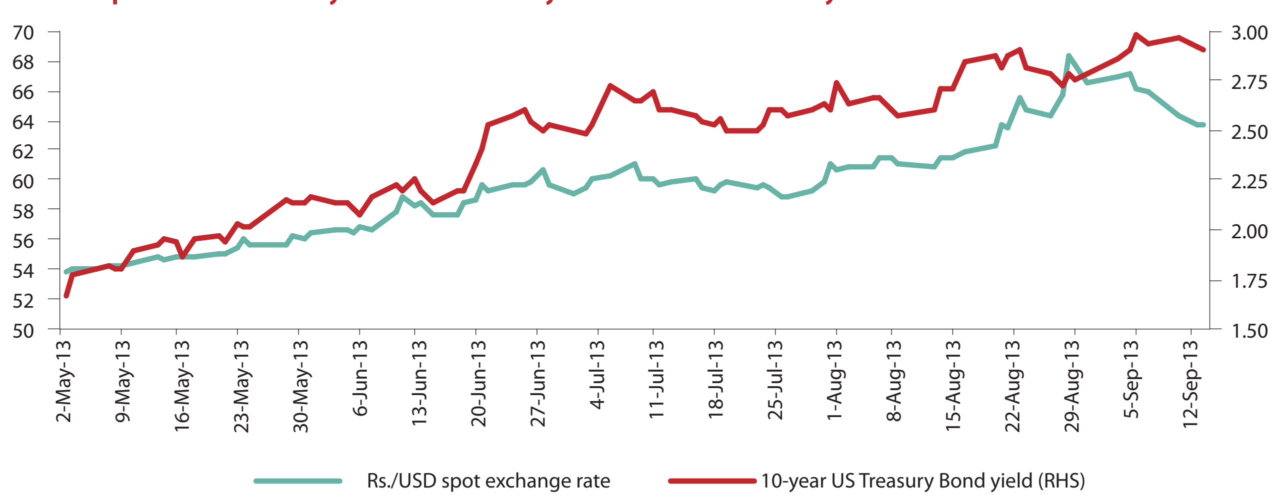
Recent Economic Developments

Recent market turmoil – while driven mainly by external factors – has magnified India's macroeconomic vulnerabilities. India was just one of a large number of emerging market economies whose currency and capital account were adversely affected by a large outflow of portfolio investment this summer. While these portfolio flows have been driven largely by investor fears of a shift in the US monetary policy, countries with greater macroeconomic vulnerabilities have come under greater scrutiny. India's below-potential GDP growth, due to continued slowdown in investment, high current account deficit with growing structural vulnerabilities, rising food and fuel prices, and an improving but still elevated fiscal deficit, have added to investor fears about the economy's ability to cope well with external shocks. As global investors withdrew US$15 billion of portfolio investment from Indian markets in June-August, the rupee fell by 18 percent vis-à-vis the US$ during this period before recovering more than a third of its losses in September.

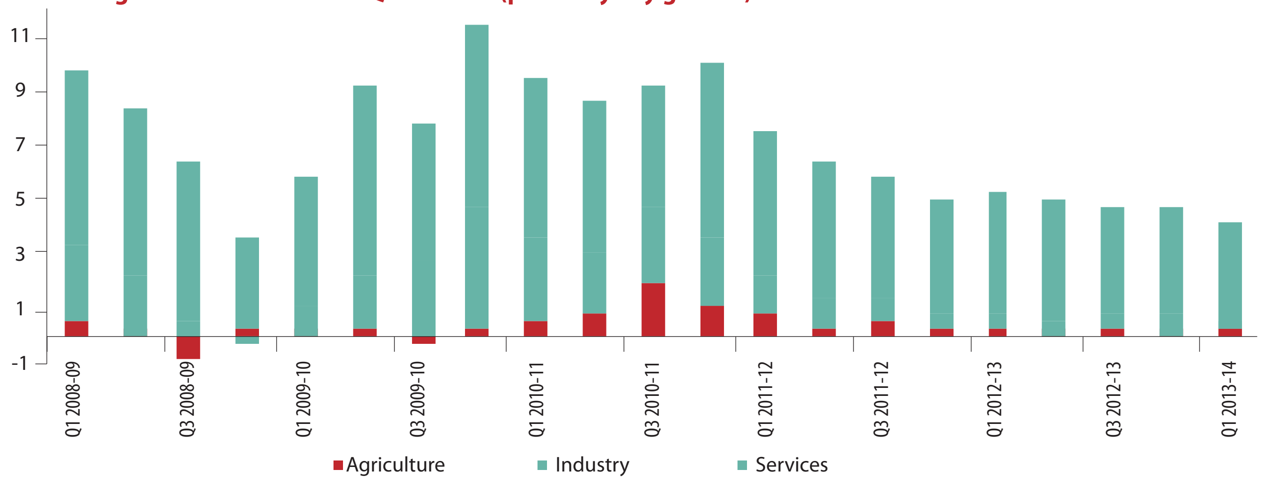
Economic growth decelerated to 4.4 percent in the first quarter of the current fiscal year. Growth in real GDP at factor cost came in below 5 percent for the third quarter in a row, slowing from 4.8 percent in Q4 FY2013. On a seasonally adjusted annual (saar) basis, GDP growth fell to a seventeen-quarter low of 4.2 percent, its worst performance since the onset of the global financial crisis in FY2009. Output in mining continued to contract, while growth in manufacturing – which had already shrunk by 0.1 percent saar in the previous quarter – fell sharply by -9.4 percent saar. On the other hand, growth in services strengthened somewhat to 8.0 percent saar (due largely to a larger contribution from the public sector), and growth in agriculture more than doubled to 3.7 percent saar due to a favorable monsoon. Reflecting weakness in the manufacturing sector, investment contracted by 1.2 percent y-o-y in Q1 FY2014 after registering single-digit growth during the previous three quarters. Business confidence, as captured by the HSBC Composite Purchasing Managers' Index which surveys private manufacturing and service firms, has fallen to 46.1 in September, marking the worst outturn in over four years and a third consecutive month below the contraction threshold of 50. Consumer confidence was also affected, with consumption growth falling to below 2.0 percent saar for the first time since FY2004.

Acceleration in food and fuel price growth offset the decline in core inflation. Core inflation decelerated to 2.4 percent y-o-y for the fiscal year-to-date, marking a major deceleration from an average price growth of 4.9 percent during FY2013 and placing core inflation well within the Reserve Bank of India (RBI) comfort level of 4 percent. On other hand, food price growth ticked up in June to 10.3 percent y-o-y due to higher vegetable and cereals prices. Growth in fuel prices has also accelerated with gradual deregulation of diesel

Indian rupee mirrored closely the movement of yields on 10Y US Treasury bonds

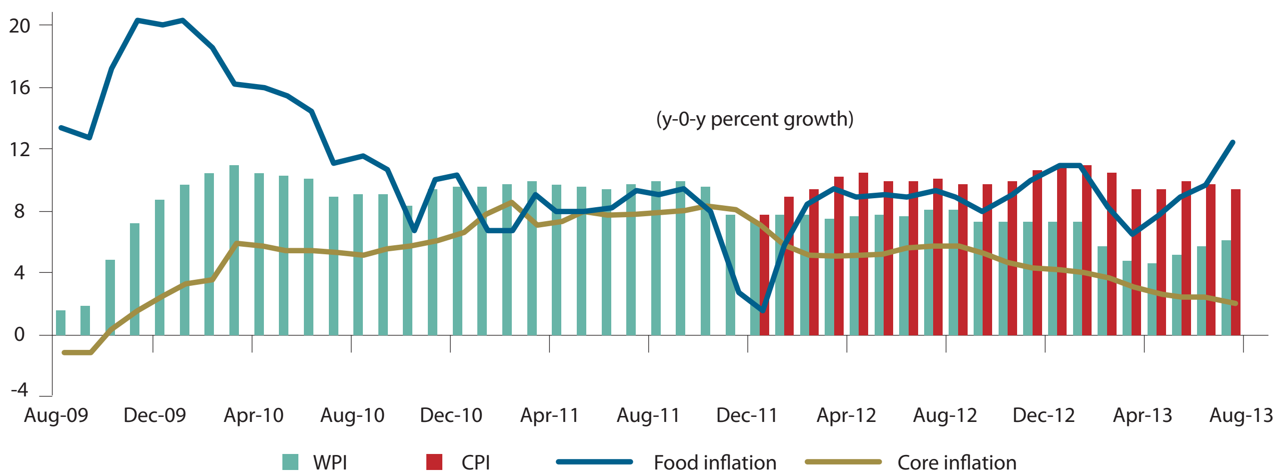


Economic growth decelerated in Q1 FY2014 (percent y-o-y growth)



Source: Central Statistics Office and World Bank Staff estimates

Headline inflation remained subdued

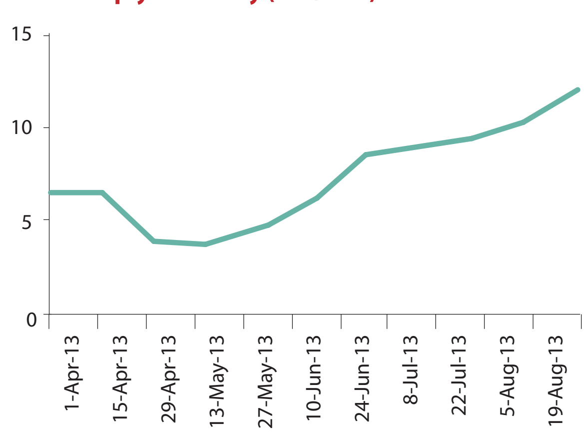


Source: Ministry of Commerce and Central Statistics Office

prices and mark-to-market petrol prices which have been affected by the depreciation in the rupee. As a result, growth in consumer prices – where food and fuel account for nearly 60 percent of the entire basket – remained elevated at 9.5 percent in the current fiscal year (although down from an average of 10.2 percent in FY2013).

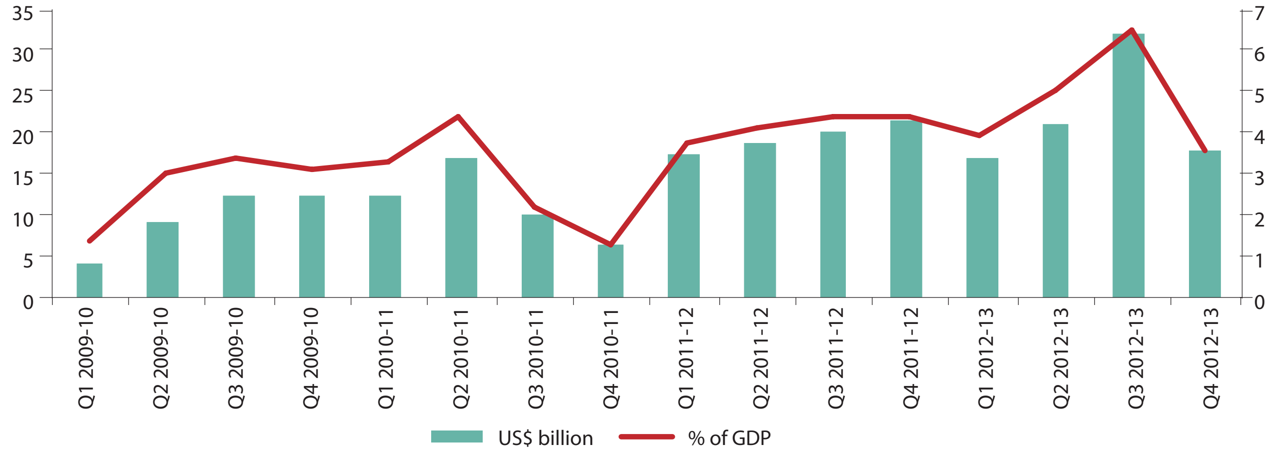
Vulnerabilities in the corporate sector are on the rise. While corporate debt levels have risen, earnings and profitability remained under pressure, pushing up debt coverage ratios. These vulnerabilities were transmitted to the banking sector, with a concomitant increase in non-performing assets, particularly among public sector banks. The banking system remains robust overall, although stress levels are elevated, meriting close attention.

Diesel under-recoveries rose sharply after May (INR/litre)



Source: Ministry of petroleum and natural gas

Current account deficit improved in Q4 FY2013



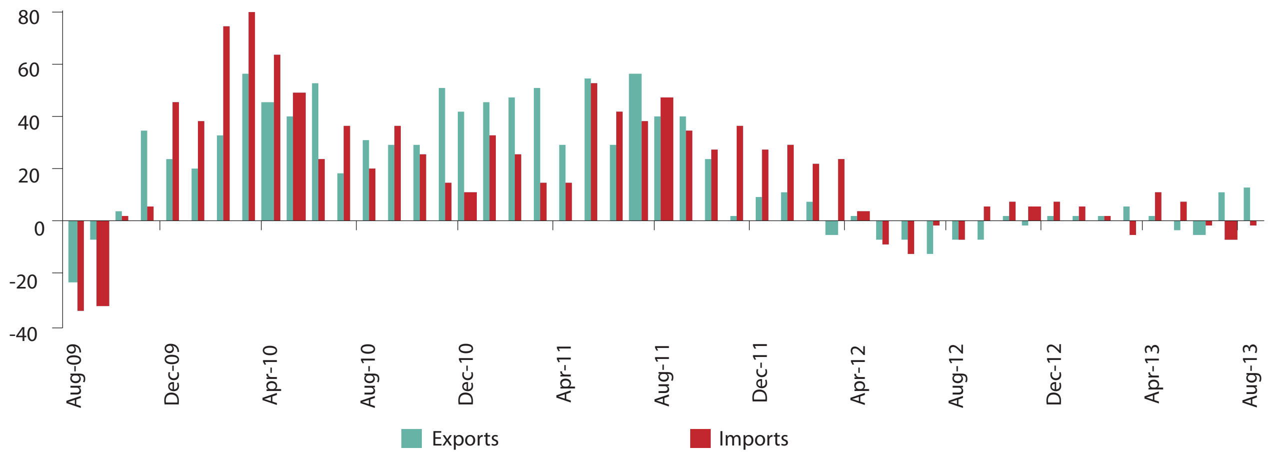
Source: Reserve Bank of India

The central government's FY2013 fiscal deficit came in better than expected, but fiscal pressures have increased this year. Revised data show that the central government's fiscal deficit in FY2013 reached 4.9 percent of GDP –well below last October's target of 5.3 percent and better than the 5.2 percent estimate in March – due to lower current expenditures and higher non-tax revenue. However, the central government incurred a fiscal deficit of 3 percent of GDP during the first four months of FY2014, equivalent to 62.8 percent of its fiscal deficit target for the year. A significant portion of the shortfall can be attributed to lower tax collection due to a slower pace of economic activity: the central government collected just 16.4 percent of its total budgeted tax revenue between April and July 2013, compared with 18.5 percent of budget estimates over the same period last year. In addition, rising under-recoveries on diesel – the difference between international fuel prices and costs of production that arise due to regulated domestic fuel prices – have erased the gains achieved under the diesel price reform earlier this year and threaten to push the central government's subsidy bill above last year's outturn of 2.5 percent of GDP.

After reaching a record high in Q3 FY2013, the current account deficit improved in the fourth quarter. The current account balance has gone through a major shift in the past decade, deteriorating from a surplus of 0.2 percent of GDP in the five years before the global crisis (FY2003-2007) to an average deficit of 2.6 percent of GDP during FY2008-2012, and reaching consecutive record highs of 4.2 and 4.8 percent of GDP in FY2012 and FY2013. Most of the deterioration in FY2013, however, took place during the first three quarters when the current account deficit rose to 5.2 percent of GDP. As merchandise exports strengthened in Q4 FY2013, the current account deficit improved to 3.6 percent of GDP. Strong portfolio inflows – which rose from 0.9 to 1.5 percent of GDP during the fiscal year – played an increasingly important role in financing the deficit while external commercial borrowing (ECB) remained stable at 0.5 percent of GDP. Even with a 10 percent y-o-y decrease in FDI (in US$), total capital inflows rose by nearly 32 percent, comfortably financing the current account deficit and adding almost US$4 billion to the stock of international reserves.

The growing trade deficit has been responsible for the majority of the widening in the current gap, but export performance improved recently. The merchandise trade deficit rose to 10.6 percent of GDP in FY2013 from 10.2 percent in the previous year as merchandise exports (in US$) fell by 1.1 percent y-o-y while imports increased by 0.5 percent. The slowdown in mining – a decline in iron ore exports and a concomitant increase in imports of coal over the past two years – exacerbated the widening of the trade deficit while appetite for gold remained high as declines in international prices have somewhat offset the impacts of the depreciating rupee and higher import duties. More recently, however, the rupee's depreciation helped improve export competitiveness and close the merchandise trade gap. Merchandise exports (in US$) grew at an eighteen month high of 12.3 percent y-o-y in July and August while imports, which already fell by 0.4 percent in June, contracted further by 3.6 percent y-o-y in July-August. Industrial output also rebounded strongly by 2.6 percent y-o-y in July (58.1 percent saar), led by a 3.0 percent y-o-y increase in manufacturing and particularly 15.6 percent y-o-y growth in the production of capital goods.

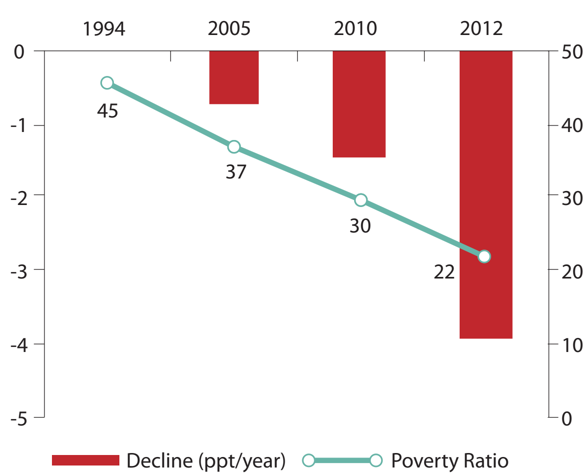
Export growth accelerated with rupee depreciation (y-o-y percent growth)



Source: Ministry of Commerce and Industry v

The decline in poverty has accelerated, although vulnerability remains high. Between 2005 and 2012, India lifted 137 million people out of poverty and reduced the poverty headcount (at the national poverty line) to 22 percent of the population. The pace of poverty reduction has been accelerating over the years, and a much larger fraction of the decline is taking place in low-income states. On the other hand, inequality continues to rise – albeit at a decelerating rate – and more than half of India's population remains vulnerable, living close to the poverty line.

Poverty Decline Accelerated



Outlook and Policy

The reform momentum has picked up in the last year with authorities putting forth a number of important reform initiatives. These reforms include a major expansion of social protection coverage with the passage of the National Food Security Act, a new Land Acquisition Bill that replaced more than 100-year-old legislation, a new Pension Bill that allows foreigners to invest in Indian pension fund companies, a Banking Bill that allows for new banking licenses, a Companies Bill that replaces sixty-year old legislation and increases transparency and corporate accountability and FDI-facilitating reforms in a number of sectors. Together with new policy announcements by the new RBI Governor and a 10-point action plan to accelerate growth by the Finance Minister, these developments send a strong signal about a recovery in reform momentum.

The economy is expected to expand by 4.7 percent in the current fiscal year. The pace of economic activity in FY2014 will be restrained by a weak outturn during the first quarter; furthermore, two consecutive months (July-August) of negative business sentiment and higher interest rates indicate a modest recovery in Q2 FY2014 despite a strong rebound in manufacturing output in July. However, as financial markets stabilize, exporters continue to take advantage of improvements in external competitiveness following the depreciation bout in the rupee, recovery in the manufacturing sector continues, and delayed investment projects begin to come on stream, activity is expected to pick up strongly in the last six months of the fiscal year, rising above 6.0 percent saar in Q4 FY2014. The recovery will also be supported by a pick-up in agricultural activity due to heavy and early monsoon rains which – while damaging some crops like coffee – have resulted in higher summer planting of rice, corn, barley, cotton, and soybeans. This is expected to result in a bumper summer crop as well as improved agricultural output in winter due to higher soil moisture levels.

The macroeconomic environment is expected to improve further and growth is expected to accelerate gradually in the medium term. The baseline scenario is conditional on further improvements in the macroeconomic framework, benign global conditions, and continued efforts by the authorities to strengthen the business environment and improve fiscal sustainability. Under these assumptions, the pace of economic activity is expected to improve further to 6.2 percent in FY2015. The acceleration in growth is unlikely to create inflationary pressures as several years of growth below potential have opened a positive output gap, and inflation is expected to decelerate to 5.3 percent and 5.2 percent in FY2014 and FY2015. The pick-up in exports bodes well for closing of the current account gap, but the merchandise trade deficit is likely to remain elevated in the short- and medium-term as fuel imports, which tend to be relatively less sensitive to price changes, account for more than one-third of the total import basket. In addition, the acceleration of growth in the second half of FY2014 and FY2015 is likely to require higher imports of capital goods. Under these assumptions, the current account deficit is expected to decline to 4.1 percent of GDP in FY2014 and 3.7 percent of GDP in FY2015. Financing of the gap is expected to come in roughly equal parts from FDI and institutional flows in FY2014, with a growing contribution from FDI in FY2015.

The depreciation in the rupee is unlikely to have major adverse effects and provides an opportunity to accelerate growth through further progress on the reform agenda. Adverse impacts of the depreciation on investment growth are likely to be offset by gains in export performance due to improved external competitiveness. Even with new pressure on fiscal balances, external and domestic financing needs are likely to be financed without much difficulty as real interest rates are close to zero and government short-term debt is around 1 percent of GDP. Although external short-term debt at residual maturity is relatively high at 9 percent of GDP (44 percent of total external debt), short-term sovereign external debt is just 0.3 percent of GDP and the vast majority of the remainder is accounted for by deposits by Indians abroad (which have a reasonable likelihood of being rolled over) and short-term trade credits (which are implicitly hedged, to an extent). Increases in inflation are likely to be limited by a small share of imported food in the overall consumption basket and the diesel pricing mechanism which limits increases to Rs.0.50 per liter per month. While rising prices will put some pressure on household budgets, real income losses – particularly in the rural areas – could well be offset by a favorable monsoon. The greatest risks are in the corporate and banking sector, where depreciation has exacerbated pressures from falling profitability and rising non-performing assets. Overall, however, the situation is likely to be manageable and instead offers the authorities a window of opportunity for measures to strengthen the business environment, attract more FDI, and increase productivity. These measures could include steps to reinforce the financial sector via capitalization and broader banking/financial sector reforms, simplify the regulatory environment for firms, and strengthen fiscal balances through continued fiscal discipline and the adoption of GST. Further steps in the above directions by the authorities could bode well for stronger growth in the medium and long-term.

Maldives

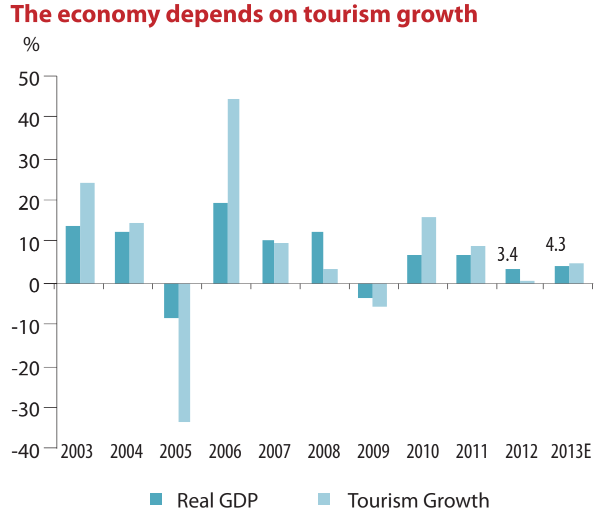
Recent Economic Developments

The economic position has become dependent on resolution of its volatile and fluid political situation. The second round of the Presidential election has been postponed after the first round has been disputed in September. The *majlis* (parliamentary) election is scheduled for the second quarter of 2014, and lack of political consensus is expected to slow reforms.

After two years of 7 percent annual growth, real GDP growth slowed to 3.4 percent in 2012 and is expected to remain modest in 2013. Tourism demand is slowly picking up, and the growing Chinese tourist segment will continue to compensate for lower arrivals from Europe – so long as it is not derailed by political unrest. Strong tourism will also have a positive spill-over to the non-tourism sectors, such as construction, communications, and fisheries, which will remain dynamic with a positive contribution to the economy.

Maldives is spending beyond its means, and financing the large budget deficit risks harming the real economy. Deficit financing will be challenging for the remainder of 2013. The government has opted for financing in ways that could pose macro risks: reliance on short-term commercial borrowing from the banks, private sector, and high-net-worth individuals at high interest rates; increased monetization of the deficit; and growing payment arrears.

The economy depends on tourism growth



Loose fiscal policy has led to a significant accumulation of debt and the country is under risk of debt distress. Arrears, at close to 6 percent of GDP, have become a significant fiscal burden. The balance of payments is under stress reflected by critically low external reserves. Reserves have unexpectedly held up, even after settlement of significant external debt commitments in early 2013. They will continue to be under pressure from public spending, demand for imports, other currency needs, and a risk that settlement of the terminated airport concession and arbitration process could lead to a significant payment requirement.

Outlook and Policy

Growth is expected to remain at or a little over 4 percent in 2013, contingent on tourism maintaining its growth trend.

With a growing fiscal deficit financing will be challenging during 2013. The government already has encountered serious cash flow problems that are likely to worsen in the fourth quarter. This would mean continued ad-hoc, expensive financing of the budget and the accumulation of more arrears. Debt is expected to continue to accumulate to over 91 percent of GDP by 2014.

The new government will need to seek rapid measures to curtail expenditures and raise revenues. Better targeting of the main subsidy schemes – particularly the electricity subsidy and the universal health insurance scheme – should be a priority, while postponing capital expenditure beyond 2014 may also be viable. In the medium term the government may look to address structural pressures on public finances: the size of the civil service and associated high costs of pay and allowances. The recently-established pay commission needs to be supported with a targeted program to rationalize the public sector and its payroll. Furthermore, limiting the direct budget transfers to SOEs would require containing operational loses and contingent liabilities. Consolidation of tax measures – raising tax rates (particularly GST) and rationalizing the import-duty regime may help to close the gap.

Nepal

Recent Economic Developments

Nepal's economic development depends chiefly upon political developments. Political uncertainty continues to hamper growth-oriented fiscal policies while the private sector has adopted a wait-and-see position. Over the short term, the scheduled elections – if they are held and achieve a degree of consensus – will be a major test. Over the medium term, increased political stability should be followed by structural reforms to tackle enduring sources of fragility, including financial sector consolidation, public financial management reform, governance improvements, and a strategy to address the gradual erosion of Nepal's external trade competitiveness.

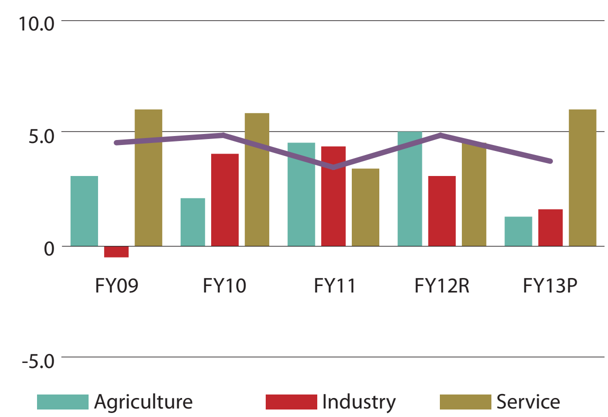
Political instability has clouded the outlook in FY13. The delayed adoption of a full budget in FY13 has depressed growth, while agricultural activity has suffered from a weak monsoon. Overall economic growth is estimated to have dipped to 3.6 percent, with average inflation just under the double-digit mark.

However, Nepal's underlying fundamentals remain healthy. Despite a large – and growing – trade imbalance, the current account remained in surplus, thanks to the countervailing impact of remittances, which have continued to grow robustly (albeit at a slower pace than in past years). On the fiscal side, the combined effect of low spending and continued revenue growth has allowed the government to draw down its overall stock of debt.

A critical source of weakness in past years, the financial sector, has rebuilt strength. All key indicators of financial sector health – credit default rate, exposure to real estate, non-performing loans (NPLs) – have registered improvements, on the back of resolute policy interventions by the Nepal Rastra Bank (NRB) and accommodative monetary policy. Further consolidation is needed, however, with key policy actions still pending or in progress, and the possible need to adopt a tighter monetary stance in coming months.

Industrial output performed marginally better than the last two years, as structural bottlenecks were compounded by weak public demand and political uncertainty. Industrial growth in FY13 was a lackluster 1.6 percent, down sharply from 4.3 percent and 3.0 percent in FY11 and FY12. Manufacturing activity growth slowed to 1.8 percent (from 3.6 percent the previous year) as unresolved structural bottlenecks were compounded by political uncertainty. While construction activity picked up in FY13 (1.6 percent vs. 0.2 percent growth in FY12) after the real estate bubble burst, it remained constrained by delays in budget execution, low levels of public spending on capital projects, restrictions on bank lending to the real estate sector, and investor nervousness over possible changes to administered prices.

Growth is expected to slow due to weak agriculture and industrial production

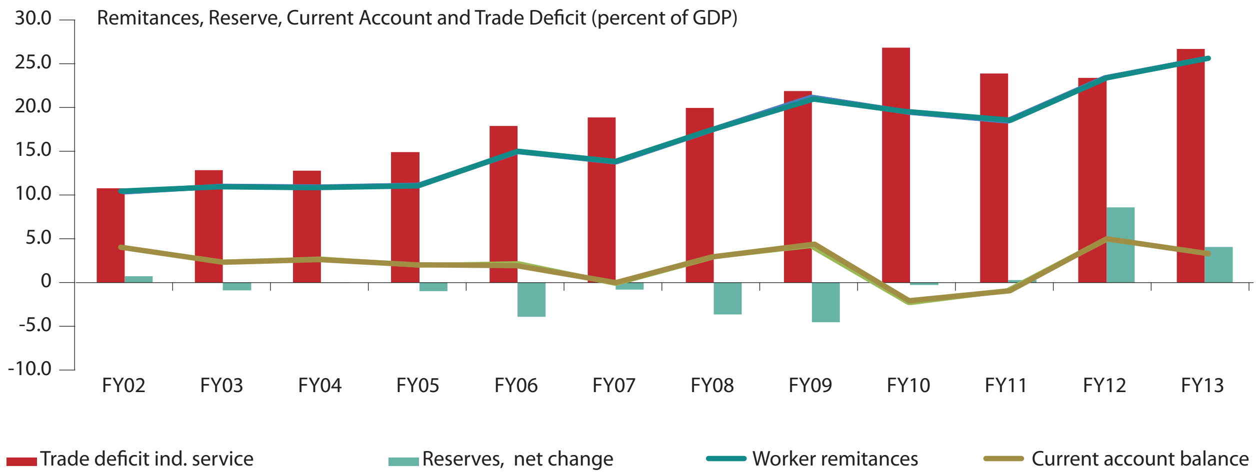


Source: CBS

The services sector, which accounts for an ever-growing share of total value added, was an outlier with a healthy 6.0 percent increase over the 4.5 percent and 3.4 percent of the preceding years. Within the sector, wholesale & retail trade (+9.5 percent), hotels & restaurants (+6.8 percent), transport, storage & communications (+6.7 percent), and financial intermediation (+6.6 percent) saw considerable growth in FY13, whereas it was more muted in the remaining sub-sectors, real estate and public/community services. Services growth has been unaffected by the deceleration in remittance growth in FY13, possibly because of lag effects.

Inflation rose to 9.9 percent in FY13, reversing a trend of steady decrease since FY09. The rise was well above the NRB's initial target of 7.5 percent (and mid-term revised targets of 9.5 percent). It remained near or above 10 percent until mid-March this year and moderated only in the last four months of the fiscal year because of seasonal trends, similar movements in Indian prices, and the ability of firms to mobilize inventories.

Trade deficit largely offset remittances



"Cost-push" factors kept prices high in FY13: a disappointing harvest prompted a surge in imported food (volumes of rice and vegetables from India grew by 98 percent and 76 percent); food prices rose by 9.7 percent, from 7.6 percent in FY12; and non-food prices also increased to 10 percent from 9 percent the year before. Structural factors – supply side rigidities – were the main drivers: higher fuel and gas prices that raised transport costs, and the onset of the rupee's depreciation against major convertible currencies, that drove up costs of imported goods, and domestic production via imported inputs and raw materials.

Nepal's trade balance continued to deteriorate, to a record 27.1 percent, in FY13, with adverse developments in both exports and imports. Export growth decelerated to a mere 3.6 percent, from 15.4 percent in FY12, while imports growth rose to 20.6 percent compared to 16.5 percent the previous year.

Outlook and Policy

Whether and how well Nepal manages the political transition process will be a major determinant of economic progress going forward. There is considerable uncertainty still surrounding the elections scheduled for November 19 – whether they will be delayed and how consensual the outcome will be. If elections are held successfully, public and private investment are expected to pick up.

Important initiatives to improve the governance environment have been taken, which could be broadened. In past months the government has tried to address major bottlenecks to public expenditures and private sector development. These include de facto streamlining of the budget preparation/adoption process, which could be further institutionalized, high profile anti-corruption initiatives (as part of a broader effort to strengthen PFM), and the establishment of the Investment Board Nepal, which appears poised to approve transformational projects in coming months.

For FY14, the baseline scenario is a gradual return to trend with higher growth and sustainable fiscal expansion. If elections are held on time and the result achieves broad consensus, macroeconomic projections point to a gradual return to trend with economic growth returning to 4-4.5 percent and inflation remaining in single digits. The government of Nepal has ample scope to increase spending, while maintaining overall fiscal sustainability targets, an opportunity that ought to be put to good use by boosting capital spending.

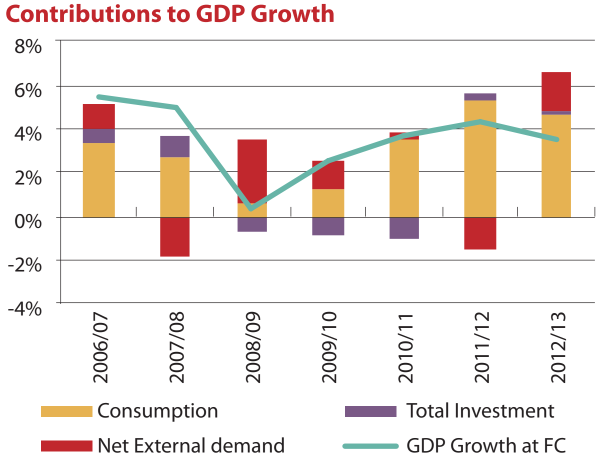
While important psychologically, and for specific sectors of the economy, the Nepalese rupee's depreciation is not expected to hold back growth or threaten macroeconomic stability. Nepal has important buffers against currency shocks, most notably strong remittance inflows. That said, specific sectors of the economy will be affected adversely. Of particular concern are (i) the financial health of major SOEs, and (ii) possible inflationary pressures, which will need to be managed proactively. While a revision of the peg with India may eventually be warranted, Nepali policy makers that determined that this is not the time – when markets are unstable – to move impulsively; instead, such a major policy shift should be based on clear policy objectives and in-depth analysis of likely economic outcomes, including the long term impact on Nepal's trade competitiveness.

Pakistan

Recent Economic Developments

Pakistan's economy remains stuck in a low-investment, low-growth trap. Real GDP growth fell to a modest 3.6 percent in 2012/13, from 4.4 percent the previous year, bringing the average for the last five years to 3 percent. The tepid performance has slowed poverty reduction and undermined progress in social services such as education. The 2012/13 slowdown was due in part to a marked fall in private investment (to 10.3 percent of GDP), the lowest level in two decades. Energy bottlenecks and security concerns are also major contributors to the slump. Inflation dropped markedly to single digits (7.4 percent in 2012/13) due to improved food supply, reduced demand, and lower inflationary expectations. However, pressure on prices from monetary expansion might push inflation back into double digits.

Contributions to GDP Growth



** Data on constant prices of 2005/06.*

Source: Pakistan Economic Survey

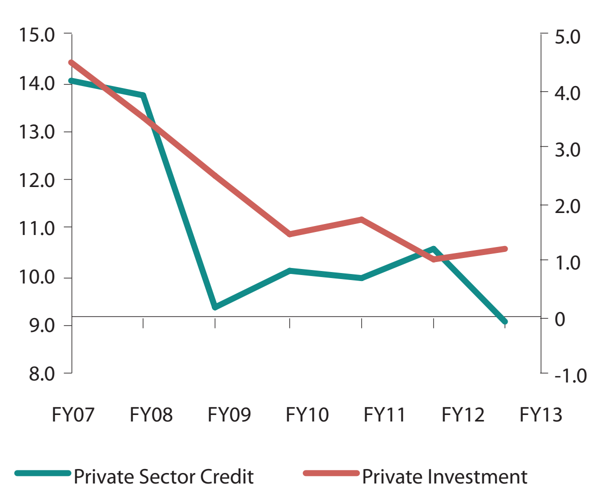
Private-sector investment continued its long, slow decline of recent years, while consumption growth was driven by strong workers' remittance inflows and higher fiscal spending. The drop in private-sector investment stemmed largely from a shortage of bank credit to the private sector, which fell to -0.1 percent of GDP in 2012/13.

On the supply side, growth continued to be dominated by the services sector, even as the sector decelerated to 3.7 percent in 2012/13. Services accounted for 60 percent of economic growth, with agriculture and industries contributing 20 percent each. Weakening profits in telecoms and transport and a slowdown in general government services overshadowed the improved performance of the wholesale & retail trade and finance & insurance sub-sectors. The latter reflected he higher volume of commercial bank financing of the fiscal deficit and strong growth in State Bank of Pakistan (SBP) profits.

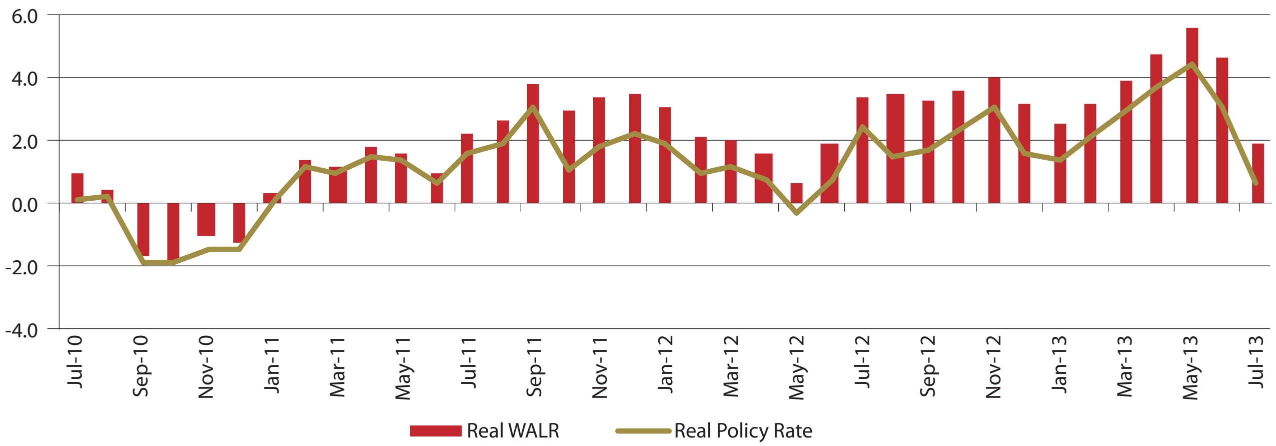
Agricultural sector growth of 3.3 percent in 2012/13 was characterized by large differences between the expected and actual outputs of various crops. Kharif crops (particularly cotton and rice) were hit by heavy rains and localized flooding. Sugarcane production in Sindh rose because farmers had opted to sow a more resilient variety. Wheat, the staple crop of Pakistan, responded quite well to better water availability, moderate temperatures, and a higher off-take of fertilizer. The sector was further supported by a steady performance of the livestock sub-sector, and strong performance of minor crops.

Industrial sector growth was boosted to 3.5 percent by the large-scale manufacturing (LSM), mining, and quarrying sub-sectors. The LSM recovery was broad-based as industries that account for about 80 percent of manufacturing's value added showed positive results. Negative results, however, continued to flow from the consumer durables industries, especially automobiles and electronics, reflecting bearish consumer sentiment.

Private Sector Credit and Investment (% of GDP)



Real Policy and Weighted Average Lending Rates



**Real rates calculated using YoY inflation*

Source: State Bank of Pakistan Data and WB Staff

A large increase in the fiscal deficit was due in part to a shortfall in budgeted revenue. Revenue collection, at Rs 1,936 billion, was Rs 445 billion (or 1.9 percent of GDP) below the target set in the 2012 budget. The shortfall was caused by sub-par collection of GST and direct taxes. And despite greater-than-budgeted disbursements from the Coalition Support Fund (CSF) – i.e., reimbursements of the cost of the "war on terror" by the US administration – non-tax revenue fell short of the target by 0.8 percent of GDP, mainly because revenue expected from the auction of 3-G telecoms licenses failed to materialize for the third year in succession. Overall, consolidated revenue collection was 1.7 percent below the budget target, even counting revenue collected by the provinces.

The falloff in headline inflation, coupled with the low level of private investment, prompted the SBP to reduce the policy rate by a cumulative 300 bps during 2012/13. However, despite nominal easing, the real policy rate remained positive. Nonetheless, as y-o-y inflation rose from 5.1 percent in May 2013 to 8.5 percent in August 2013, the SBP raised the policy rate by 50 bps in September 2013.

Public debt remained above the 60 percent threshold set in the Fiscal Responsibility and Debt Limitation Act. Nevertheless, compared with last year's level (63.8 percent of GDP), the debt declined marginally to 62.9 percent of GDP. This resulted from the growth in nominal GDP and the virtual absence of additional foreign debt creating inflows during the year. External debt stood at US$59.6 billion at the end of 2012/13, decreasing by a historic US$5.9 billion over the previous year. Net flows were negative across most external debt categories, especially IMF financing. However, significant government borrowing increased domestic debt stock from 38 percent of GDP in 2011/12 to 41.5 percent in 2012/13.

Broad money creation was expansionary, growing by 15.9 percent y-o-y in 2012/13. A large increase in the financing requirements of the fiscal deficit raised net domestic assets of the banking system by 21.1 percent (y-o-y) during 2012/13. Not only did the government resort to inflationary borrowing from the central bank (Rs 507 billion), it also borrowed heavily from scheduled commercial banks (Rs 940 billion), for net budgetary borrowing from the banking system of Rs 1,447 billion (38 percent growth y-o-y).

Outlook and Policy

Pakistan is facing many crises at the same time: terrorism, economic problems, and energy shortages. In this very difficult context, the country has elected a new government with a large majority. This has raised hopes that the new administration will be able to tackle the implementation of a comprehensive reform agenda necessary to help the country avoid a balance of payments crisis and regain strong and sustained growth rates.

The administration has moved swiftly to confront the country's economic woes, requesting a US$6.6 billion loan under an Extended Fund Facility (EFF), which the IMF approved in early September. Within the EFF, the government set out a bold program of stabilization and structural reforms for the next three years aimed at reducing the risk of a crisis in the short term and regaining and sustaining high and inclusive growth in the medium term. As its initial steps, the government pledges to focus on fiscal consolidation and strengthening the external situation. A well-implemented reform program will restore a framework for effective budget support from the World Bank and, possibly, other donors which could address structural reforms in areas such as the power sector, business climate, SOEs, trade liberalization, and strengthening of the safety-net system.

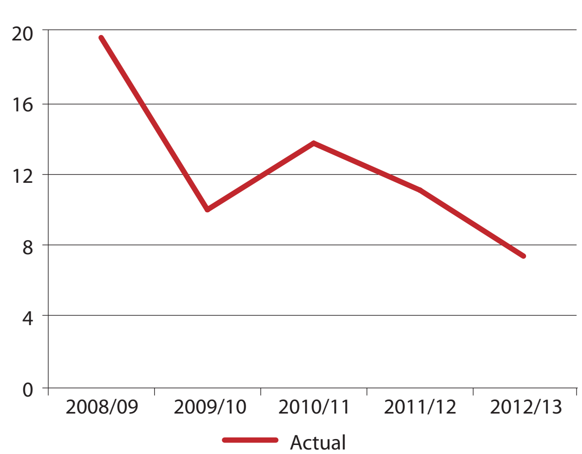
Pakistan's weak external position remains the most pressing short-term economic challenge. While the current account deficit remained small due to a marginal improvement in export growth, deceleration in imports associated with the economic slowdown and inflows of workers' remittance, falling financial inflows, and substantial debt amortization payments have resulted in a marked drawdown of foreign reserves. In terms of import coverage, reserves declined from about 2.7 months by June 2012 to 1.5 months by June 2013 (1.2 months in September 2013).

Pakistan's unsustainable fiscal imbalances compound the current crisis and need urgent attention. The consolidated fiscal deficit exceeded by a sizeable margin the budgeted target, to return to 8 percent of GDP. Significant shortfalls in revenue and a sharp overrun in energy subsidies worsened the already-large fiscal deficit. Moreover, restricted external financing, domestic bank borrowing, and direct financing from the State Bank of Pakistan rose, reducing the availability of private-sector credit.

Pakistan will not be able to recover without major structural reforms, especially in tax administration and the energy sector. The Federal Board of revenue, responsible for collecting taxes, has tried to register tax evaders, remove zero ratings for domestic sales of selected export products, and raise excise duties on tobacco, but with little success, as the tax ratio fell to 9.6 percent of GDP. On the energy front, the government balked again at increasing power tariffs and, as a result, expenditures on the tariff differential subsidy reached Rs 349 billion – 1.5 percent of GDP. Meanwhile, the financial losses of state-owned enterprises (SOEs) continue to bleed the budget.

A cautious estimate would put GDP growth for 2013/14 at the same level as last year. Fiscal adjustment might have a contractionary effect on the economy, as fiscal consolidation may fall disproportionately on public investment. However, all economic sectors have shown significant resilience in the past year, agriculture and large-scale manufacturing growth remains positive and should benefit from the government's commitment to effectively address the energy bottlenecks and reduce security concerns, while reducing SOE losses and improving the services they deliver. Fiscal consolidation may also enhance general investor perceptions about the economy and government performance. Indeed, if reforms are adopted and implemented promptly, this would also contribute to keeping inflation low, thereby improving the investment climate.

Average Headline CPI Inflation



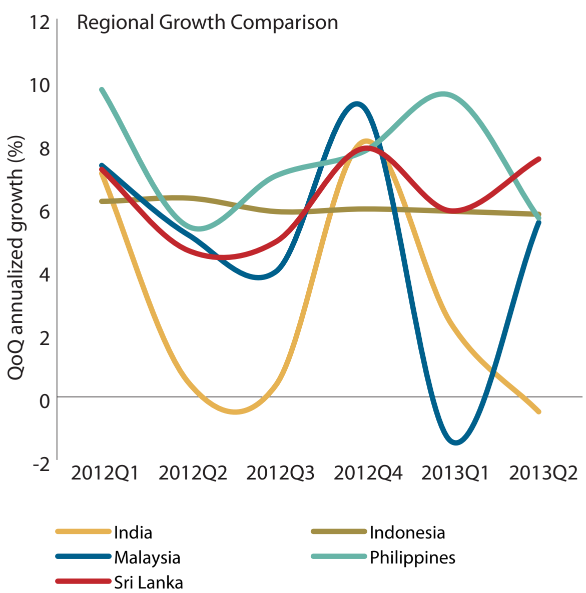
Source: Federal Bureau of Statistics

Sri Lanka

Recent Economic Developments

Sri Lankan GDP grew by 6.8 percent in the second quarter of 2013, on the back of expansion in both services and industry despite slowing in agriculture. The rate was broadly consistent with the average 6.4 percent annual growth rate of the past ten years, characterizing a country that has weathered the uncertainties of the global economic environment. Growth also has been inclusive, with poverty rates declining dramatically to 9 percent in 2010 from 22 percent in 2002.

Sri Lanka growing relatively well



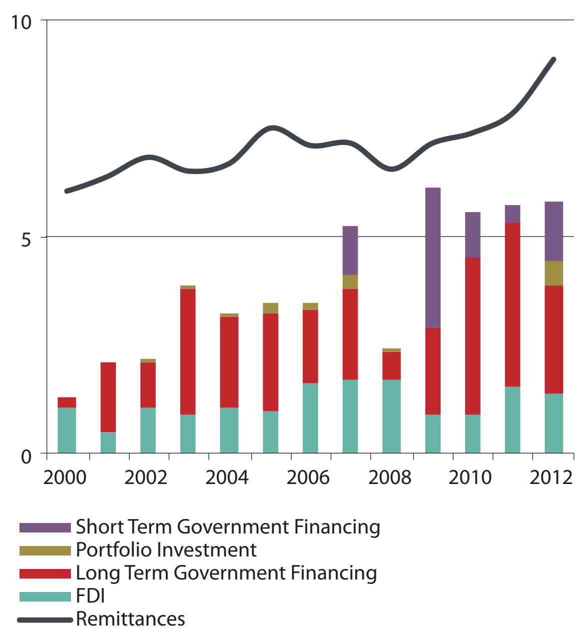
Headline inflation continued to fall, along with food prices, while a tighter monetary policy environment in 2012 was responsible for a drop in core inflation.

Monetary policy became expansionary in 2013 to stimulate growth by reducing policy rates and the statutory reserve ratio, and eliminating the credit ceiling. Responding to these changes, private sector credit is beginning to pick up.

Although the management of fiscal spending has been strengthened progressively over the past few years, the fiscal balance deteriorated considerably in the first four months of 2013 due to low revenue collection. The higher deficit is being financed through increased domestic bank borrowing.

The country has been financing the current account deficit through external debt. From 2000-2012, short- and long-term external debt has been the main driver of capital inflows to Sri Lanka, accounting for an average 70 percent of such funding. Of this, long-term debt accounts for 80 percent of total sovereign external debt. High external debt could expose a country to numerous risks, including exchange rate risk. Therefore there is need to promote non-debt-creating capital inflows, particularly FDI, to fund the current account deficit.

Portfolio debt flows increasing (% of GDP)



In the first half of 2013, the exports-to-GDP ratio continued its downward trend. Yet, owing to a steeper decline in the import bill, the trade deficit narrowed. Buoyant worker remittance and tourism receipts further reduced the pressure on the balance of payments. However, the external sector remained vulnerable to sudden capital outflows.

FDI in Sri Lanka has increased but remains relatively low compared to other middle-income countries. In 2012, FDI in Sri Lanka reached 2 percent of GDP, US$1.3 billion lower than the government's target of US$2 billion for that year (although, 69 percent of total FDI (US$6.2 billion) over the past 35 years has accrued since 2006, indicating a clear upward trend). Much of the recent foreign investment into Sri Lanka went into the manufacturing sector (23 percent), telecoms (18 percent), and port development (15 percent). In September, the Board of Investment began allowing would-be investors to make online applications, thereby streamlining the application process. The country hopes to attract US$2.1 billion in FDI this year.

Outlook and Policy

GDP growth is expected to average 6.8 percent in 2013, with acceleration through the second half of the year and into 2014, when the rate should normalize at about 7.4 percent. Growth will be led by strong performances of construction and services, with wholesale and retail trades benefiting from rising consumption buoyed by the more accommodative monetary policy stance and increasing remittance inflows. Positive agricultural production growth may boost consumption further.

Three salient macroeconomic challenges face the Sri Lankan economy:

1. **Raising the domestic savings rate to support rising investment;**
2. **Increasing exports in order to generate jobs; and**
3. **Improving FDI rather than external debt to cover the external payments deficit and add to reserves.**

Risks to the outlook include increased fiscal stress due to anemic tax revenue growth, state-owned enterprises incurring acute and persistent losses, a declining export-to-GDP ratio adversely affecting the trade balance, and further nominal depreciation of the currency due to capital flight.

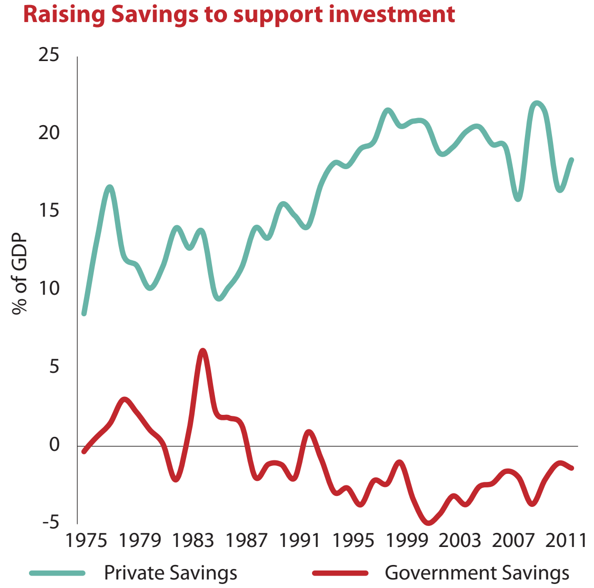
Rising losses by SOEs are adversely affecting private-sector credit growth and, therefore, investment and GDP growth. The government may have to transfer additional resources to improve the balance sheets of these SOEs, which could also raise administered prices to cover their costs. The latter could have an adverse inflationary impact reducing overall consumption expenditure and affecting export competitiveness negatively.

Given that the growth in the two key export sectors, i.e., tea and apparel, remain stagnant, there is a risk that there will be a continued decline in the exports-to-GDP ratio. There needs to be a new thrust towards diversification of both product and export markets to ensure that the trade balance remains manageable.

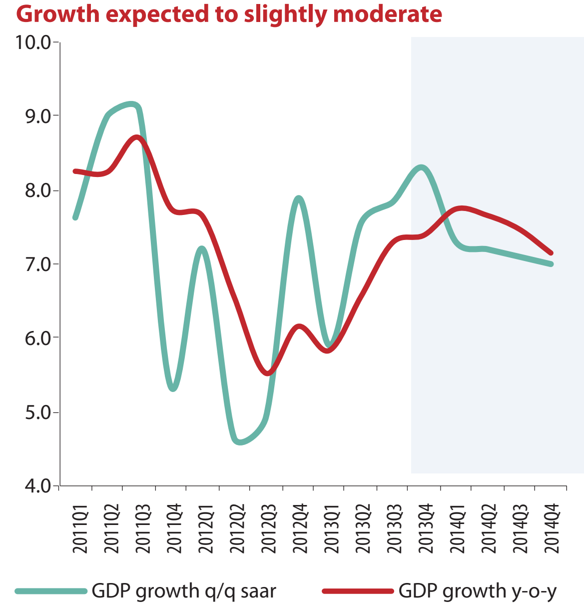
Continued depreciation of the Indian rupee may have adverse effects on FDI inflows and tourist arrivals from India together with a decline in Sri Lanka's exports to that country, its biggest trading partner and source of tourism revenues. Further deprecation of the Indian rupee would likely fuel imports from India which, *ceteris paribus,* could undermine Sri Lanka's trade balance.

External factors could be influential: the US Fed's future decisions on tapering its stimulus program will improve or limit Sri Lanka's economic prospects, as would growth levels in China and the euro zone, and the performance of Japan's fiscal stimulus.

Raising Savings to support investment



Growth expected to slightly moderate



South Asia at a Glance

			AFG (1)	BGD (5)	BTN (8)	IND (10)	MDV (15)	NPL (18)	PAK (22)	LKA (28)	SAR (32)
OUTPUT and PRICES	Real GDP Growth	2010	8.4	6.1	10.0	10.5 (11)	7.1	4.8	3.7	8.0	10
		2011	6.1	6.7	8.1 (prov)	6.3	7.0	3.4	4.4	8.2	7.2
		2012	14.4	6.2	6.9 (e)	3.2 (e)	3.4	4.9	3.6	6.4	4.7
		Q4	..	..	..	4.8	..	..	..	6.3	4.8
		2013	3.1 (p)	6.0 (e)	7.1 (p)	4(p)	4.3 (e)	3.6 (p)	3.5 (p)	6.8 (f)	5.5 (f)
		Q1	..	..	..	4.4	..	..	..	6.0	4.8
		Q2	..	..	..	4.4	..	..	..	6.8	4.4
	Inflation (y-o-y)	2010	7.7	6.8	5.7	10.4	6.2	9.5	13.7	6.2	10.0
		2011	10.2	10.9	8.9	8.4	11.3	9.6	11.0	6.7	9.6
		2012	6.4	8.7	9.1	10.4	10.9	8.3	7.4	7.5	9.4
		2013	7.1 (p)	6.8 (p)	7.6	7.74 (f)	6	9.9 (e)	6.0 (p)	5.9 (f)	6.04 (f)
		May	6.8	8.0	8.4 (Q1)	9.3	3.0	8.7	5.1	7.3	6.9
		June	7.7	8.1	5.5 (Q2)	9.9	2.2	8.2	5.8	6.8	7.0
		July	9.1	7.8	..	9.6	3.3	7.8	8.3	6.0	7.4
		August		7.4					8.5		
	Core Inflation	2010	9.8 (2)	4.8	..	5.0	..	5.8	9.3	7 (29)	..
		2011	14.6	6.8	..	7.3	..	6.4	9.9	6.9	..
		2012	6.6	11.5	..	5.4	..	10.7	10.6	5.8	..
		2013	6.8 (p)	7.5 (6)	..	4.9	..	9.9 (19)	9.8 (23)	4.3 (H1)	..
		May	6.2	..	..	2.5 (12)	..	..	..	..	..
		June	6.9	..	..	2.2	..	..	..	..	..
		July	8.2	..	..	2.3	..	..	..	..	..
	Food Inflation	2010	-1.4	10.1	10 (Q4)	14.2	12.4	15.1	..	6.9	11.4
		2011	12.1	12.8	9 (Q4)	7.9	12.0	14.7	11	9.0	11.4
		2012	4.6	7.5	12 (Q4)	8.1	-8.0	7.6	9	5.0	4.9
		2013	..	7.8	..	9.3	-2.0	9.7	8	12.0	..
		May	5.2	8.1	..	10.7	5.3	7.8	..	3.5	6.8
		June	7.0	8.3	..	10.3	3.8	8.4	..	3.3	7.1
		July	9.7	8.1	..	11.1	7.9	8.8	..	2.7	8.1

			AFG (1)	BGD (5)	BTN (8)	IND (10)	MDV (15)	NPL (18)	PAK (22)	LKA (28)	SAR (32)
BALANCE of PAYMENTS	Current Account (% of GDP)	2010	2.8 (3)	3.7	-21.5 (prov)	-2.8	-9.2	-2.4	-2.2	-2.2	-2.6
		2011	3.1	0.8	-19.3 (p)	-2.7	-21.4	-1.0	-2.1	-7.8	-3.1
		2012	3.9	-0.4	-19.4 (p)	-4.18 (e)	-27.1	4.8	-1.0	-6.5	-4.5
		Q4	..	..	..	3.6	..	..	..	..	..
		2013	2.5 (p)	1.9 (p)	-29.7 (p)	-4.78 (p)	-27.9 (e)	3.3 (e)	-1.7 (e)	-3.9 (p)	-3.7 (f)
	Trade Balance (% of GDP)	2010	-45.9	-5.2	-7.9	-7.5	15.1 (e)(16)	-26.2	-0.5	-9.7	-5
		2011	-42	-6.9	-31	-8.8	3 (e)	-25.8	-8	-16.5	-6
		2012	-41.9	-7.8	-32.3	-10.9	-3.1 (e)	-24.3	-7.4 (p)	-15.9	..
		2013	-41.6 (e)	-5 (p)	-28.3	..	-6 (p)	-27.1	..	-13.3 (p)	..
	Import Growth	2010	5.1	5.5	36.9 (e)	28.8	-6.5	10.2	4.7	34.5	16.0
		2011	2.7	41.8	39.4 (e)	24.2	24.0	3.4	12.8	50.0	17.8
		2012	11.2	9.9	-3.3 (e)	1.1 (e)	20.4	16.5	-1.6	-5.8	8.6
		2013	..	0.8	2.4 (p)	7.8 (p)	..	20.6	6 (e)	11 (e)	5.8 (f)
		May	..	..	..	7.0	1.9	..	..	..	..
		June	..	..	..	-0.4	6.7	..	..	..	..
		July	..	7.9	..	-6.2	8.3	..	..	..	..
	Export Growth	2010	4.7	4.1	7.1 (e)	37.5	-18.6	..	7.0	17.1	14.0
		2011	1.8	41.5	21.8 (e)	17.9	55.1	..	-2.6	22.4	16.7
		2012	2.7	5.9	-1.6 (e)	0.3 (e)	22.6	15.4	0.2	-7.4	4.5
		2013	-2 (e)	11.2	4.2 (p)	15.7 (p)	..	3.6 (p)	..	7 (e)	5.9 (f)
		May	..	..	..	-3.3	-7.9	..	..	..	..
		June	..	..	..	-4.6	-8.5	..	..	..	..
		July	..	23.9 14.6 (Jul-Aug)	..	11.6	-7.2	..	..	..	..
	Remittances (US$ billion)	2010	..	10.9 (7)	-0.1	54 (13)	-0.2	3.5 (20)	9.7 (24)	4.2 (30)	82 (33)
		2011	..	12.1	-0.1	63	-0.2	4.2	13.2	5.2	97
		2012	..	13.7 (e)	..	69.8 (e)	..	5.1 (e)	13.9	6.3 (e)	109 (e)
			AFG (1)	BGD (5)	BTN (8)	IND (10)	MDV (15)	NPL (18)	PAK (22)	LKA (28)	SAR (32)

			AFG (1)	BGD (5)	BTN (8)	IND (10)	MDV (15)	NPL (18)	PAK (22)	LKA (28)	SAR (32)
GOVERNMENT FINANCES and MACRO POLICIES	Fiscal Deficit (% of GDP)	2010	0.9 (4)	-3.7	1.6	-7.6	-15.7	-0.8	-5.9 (25)	-8	-8.7
		2011	-1.2	-4.0	-1.1	-8.1	-11.3	-1.0	-8.4	-6.9	-7.6
		2012	-0.8	-4.1	-0.9	-7.0 (e)	-13.4	1.9	-7.7	-6.4	-9 (e)
		Q4	..	..	..	..	..	..	-8	..	..
		2013	-0.6 (p)	-4.3	-3.7 (b)	-7.3 (p)	-11.0 (e)	-0.8	-5.5 (p)	-5.8 (p)	-8.3 (f)
	Public Debt to GDP (%)	2010	13.8	42.9	54 (e)	67.9	65.7	35.4	61.6 (26)	81.9	..
		2011	13.2	44.2	68.8	67.9	72.4	33.4	59.4	78.5	..
		2012	11 (e)	42.8	94 (r)	68.7 (f)	80.4	29.6	63.8	79.1	..
		Q4	..	..	..	..	..	..	62.9	..	..
		2013	..	41.3 (p)	97.2 (b)	70.8 (p)	86.2 (f)	27.8 (e)	62.9	75.0 (p)	..
	Reserves in Months of Import	2010	6.7	3.4	10.5	7.1	3.9	5.4	3.7	5.9	7
		2011	6.9	3.9	25.4 (prov)	6.8 (14)	2.7	5.8	2.9	3.5	..
		2012	7.7	3.3	27.8 (p)	6.6	2.4	7.2	..	4.3	..
		H1	..	..	..	..	..	..	2.7 (June)	..	..
		2013	7.3 (p)	4.6	23 (p)	..	2.6 (e)	7.6 (e)	..	4.2 (p)	..
		H1	..	4.1 (December)	11 (June)	6.58 (Feb)	2.4 (Jan)		1.5 (June	..	..
		H2	..	3.7 (Jul-Aug)	..	..	2.6 (Jul)	10.1 (Jul)	1.2 (Sept)	..	..
	REER	2010	114.4	108.3	97.4 (9)	99.3	124.5 (17)	54.1 (21)	71.9 (27)	81.9 (31)	99.8
		2011	126.2	108.9	98.6 (p)	96.8	135.0	46.0	66.8	57.34	97.9
		2012	127	105.2	..	90.7	120.3	40.3	52.9	47.8	92.7
		2013	..	111.6 (p)	..	88.5	..	..	..	..	90.6
		Q1	127.3	..	..	..	95.7	47.1	42.3	40.8	..

			AFG (1)	BGD (5)	BTN (8)	IND (10)	MDV (15)	NPL (18)	PAK (22)	LKA (28)	SAR (32)
CONSUMPTION and INVESTMENT	Consumption (% of GDP)	2010	120	80	66.3 (e)	72.5	..	88	90	66	..
		2011	120	81	64.1 (e)	72.8	..	91	92	70	..
		2012	..	81	63.2 (e)	77 (p)	..	80	..	69 (e)	..
		2013	..	81	60.7 (p)	75.5 (p)	..	88	..	..	..
	Investment (% of GDP)	2010	27	24.4	51.6 (e)	31.7	..	32.5	16	28	28
		2011	25	25.2	59.4 (e)	30.6	..	32.8	12.5	30	27
		2012	..	26.5	61.8 (e)	30.5 (p)	..	..	11	28 (e)	..
		2013	..	26.8	65 (p)	31.3 (p)	..	..	..	..	..
	FDI (US$ billion)	2010	..	0.9	0.1	9.4	0. 22 (e)	0.1	1.6	0.9	30.4
		2011	..	0.8	0.37 (prov)	22.1	0. 28 (e)	0.1	0.7	1.5	35.7
		2012	..	1.2	0.1 (p)	19.8 (e)	0.16 (e)	0.1	1.2	1.4	29.7 (e)
		Q4		..	..	2.1	..	..	..	..	..
		2013	..	1.3	0.01 (p)	20 (p)	0.22 (p)	..	..	2.1 (p)	36.9 (e)
		Q1	..	..	..	5.7	..	..	..		..
	Portfolio Investment (US$ billion)	2010	..	-0.12	..	28.2	..	0.0	0.3	-0.46	29.9
		2011	..	-0.03	..	16.6	..	0.0	-0.14	-0.29	-4.8
		2012	..	0.24	..	26.7 (e)	..	0.0	0.03	0.5	11.5 (e)
		Q4				9.8					
		2013	..	0.29	..	22 (p)	..	..	..	..	16.4 (f)
		Q1				11.3					

Notes

b	Budgeted
e	Estimate
f	Forecast
p	Projections
prov	Provisional
r	Revised
	Afghanistan
1	These numbers are for calendar year unless otherwise mentioned
2	Core inflation (exc. Fuel and cereal, %)
3	Including grants
4	Including grants
	Bangladesh
5	These numbers are for fiscal year unless otherwise mentioned. For example; for 2012 numbers, 2012-2013 values are used.
6	(Avg of Jan-Feb)
7	Remittances numbers are taken from GEP 2013 Jan report and they are calendar year numbers (US$ billions)
	Bhutan
8	These numbers are for fiscal year unless otherwise mentioned. For example; for 2010 numbers, 2010-2011 values are used.
9	WB Staff Calculations
	India
10	These numbers are for fiscal year unless otherwise mentioned. For example; for 2012 numbers, 2012-2013 values are used.
11	Real GDP Growth (at market prices)
12	WPI Core Inflation
13	Remittances numbers are taken from GEP 2013 Jan report and they are calendar year numbers (US$ billions)
14	Calendar year for 2011 and 2012
	Maldives
15	These numbers are for calendar year unless otherwise mentioned.
16	WB Staff Calculations
17	WB Staff Calculations

Nepal

18 These numbers are for fiscal year unless otherwise mentioned. For example; for 2012 numbers, 2012-2013 values are used.

19 (Avg of Jan-Feb)

20 Remittances numbers are taken from GEP 2013 Jan report and they are calendar year numbers (US$ billions)

21 WB Staff Calculations

Pakistan

22 These numbers are for fiscal year unless otherwise mentioned. For example; for 2012 numbers, 2012-2013 values are used.

23 (Avg of Jan-Feb)

24 Remittances numbers are taken from GEP 2013 Jan report and they are calendar year numbers (US$ billions)

25 Including grants

26 Data is end of the year for 2010-2013

27 WB Staff Calculations

Sri Lanka

28 These numbers are for calendar year unless otherwise mentioned.

29 (Avg of Jan-Feb for 2010-2012)

Remittances numbers are taken from GEP 2013 Jan report and they are calendar
30 year values which is same as the fiscal year (US$ billions)

31 WB Staff Calculations

SAR

32 These numbers are for calendar year unless otherwise mentioned.

33 Remittances numbers are taken from GEP 2013 Jan report and they are calendar year numbers (US$ billions)

THE WORLD BANK

1818 H Street, N.W.
Washington, DC 20433