

## HIGHLIGHTS

- With the United States contracting in the first quarter and some underperformance within Asia and the Pacific, growth forecasts for developing Asia are adjusted down from those published in *Asian Development Outlook 2015*. This *Supplement* envisages aggregate growth in the region at 6.1% in 2015 and 6.2% in 2016.
- As growth in the People's Republic of China was slower than expected in the first half of the year, projections for the region's largest economy are revised down to 7.0% in 2015 and 6.8% in 2016. The weaker external environment means East Asia as a whole is now expected to grow by a slower 6.2% in both 2015 and 2016.
- India's growth forecasts remain at 7.8% for this fiscal year and 8.2% for next, supported by a healthy monsoon and new investment—and assuming concrete progress on reform. South Asia will grow by 7.3% in 2015, as a strong outturn in Bangladesh outweighs a disaster-induced slowdown in Nepal, and by 7.6% in 2016.
- The growth outlook in Southeast Asia is trimmed to 4.6% in 2015 because outcomes in the first half of the year in Indonesia, Singapore, and Thailand disappointed expectations. Subregional growth will likely accelerate next year to 5.1%.
- Low international food and fuel prices are containing inflation this year. Developing Asia's inflation forecast is revised down slightly to 2.4% in 2015 but retained at 3.0% in 2016.

GROWTH PROSPECTS SOFTEN  
FOR DEVELOPING ASIA

## Growth outlook

Growth projections for developing Asia are revised down from those published in *Asian Development Outlook (ADO) 2015* in March, as slower-than-expected recovery in the United States (US) and moderating growth in the People's Republic of China (PRC) weigh on the region's prospects. The region is now projected to grow at 6.1% in 2015 and 6.2% in 2016, downgrades of 0.2 and 0.1 percentage points from *ADO 2015* forecasts. By subregion, growth projections are revised down for East and Southeast Asia for both years, unchanged for Central Asia and the Pacific for 2015 but for 2016 slightly downgraded for Central Asia and upgraded for the Pacific, and for South Asia upgraded for 2015 and retained for 2016 (Table 1).

The collective growth outlook for the major industrial economies is trimmed from *ADO 2015* projections. The unexpected contraction in output in the US prompted revisions in the growth forecasts for 2015 and 2016 (Box 1).

Brent crude oil prices had been picking up from their lows at the beginning of 2015 to average \$62 per barrel in June. The average in the year to date is \$58 per barrel, still more than 40% below the average in the whole of 2014. Meanwhile, multiple factors exert downward pressure on prices and worsen daily price volatility. Demand factors are uncertain recovery in the euro area pending a resolution of the Greek debt crisis and the impact on commodities of unexpectedly slow growth in the PRC. Supply factors are continuing expansion of global oil output and the nuclear deal with Iran. This *Supplement* maintains the *ADO 2015* forecast of \$65 per barrel for Brent crude on average in 2015 but revises down the projection for 2016 from \$75 to \$70. Favorable cropping conditions are pushing food prices down further, with food prices deflating by 16% in the first half of 2015 from the same period a year earlier. This *Supplement* anticipates food prices dropping by 11% in 2015, a much steeper decline than the 6% drop previously forecast, before steadying in 2016.

ADB's Regional Economic Outlook Task Force led the preparation of the revised outlook for this *ADO Supplement*. The Task Force is chaired by the Economic Research and Regional Cooperation Department and includes representatives from the Central and West Asia Department, East Asia Department, Pacific Department, South Asia Department, and Southeast Asia Department.

Table 1 Gross domestic product growth, developing Asia (%)

	2014	2015		2016	
		ADO 2015	ADOS	ADO 2015	ADOS
<b>Developing Asia</b>	<b>6.3</b>	<b>6.3</b>	<b>6.1</b>	<b>6.3</b>	<b>6.2</b>
<b>Central Asia</b>	<b>5.1</b>	<b>3.5</b>	<b>3.5</b>	<b>4.5</b>	<b>4.2</b>
Kazakhstan	4.3	1.9	1.9	3.8	3.2
<b>East Asia</b>	<b>6.6</b>	<b>6.5</b>	<b>6.2</b>	<b>6.3</b>	<b>6.2</b>
China, People's Rep. of	7.4	7.2	7.0	7.0	6.8
Hong Kong, China	2.5	2.8	2.6	2.9	2.9
Korea, Rep. of	3.3	3.5	3.0	3.7	3.5
Taipei, China	3.8	3.7	3.4	3.6	3.6
<b>South Asia</b>	<b>6.8</b>	<b>7.2</b>	<b>7.3</b>	<b>7.6</b>	<b>7.6</b>
India	7.3	7.8	7.8	8.2	8.2
<b>Southeast Asia</b>	<b>4.4</b>	<b>4.9</b>	<b>4.6</b>	<b>5.3</b>	<b>5.1</b>
Indonesia	5.0	5.5	5.0	6.0	5.6
Malaysia	6.0	4.7	4.7	5.0	5.0
Philippines	6.1	6.4	6.4	6.3	6.3
Singapore	2.9	3.0	2.8	3.4	3.4
Thailand	0.9	3.6	3.2	4.1	4.1
Viet Nam	6.0	6.1	6.1	6.2	6.2
<b>The Pacific</b>	<b>6.3</b>	<b>9.9</b>	<b>9.9</b>	<b>4.8</b>	<b>5.0</b>

ADO=Asian Development Outlook, ADOS=ADO Supplement.

Note: **Developing Asia** refers to 45 members of the Asian Development Bank. **Central Asia** comprises Armenia, Azerbaijan, Georgia, Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan. **East Asia** comprises the People's Republic of China; Hong Kong, China; the Republic of Korea; Mongolia; and Taipei, China. **South Asia** comprises Afghanistan, Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan, and Sri Lanka. **Southeast Asia** comprises Brunei Darussalam, Cambodia, Indonesia, the Lao People's Democratic Republic, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Viet Nam. **The Pacific** comprises the Cook Islands, Fiji, Kiribati, the Marshall Islands, the Federated States of Micronesia, Nauru, Palau, Papua New Guinea, Samoa, Solomon Islands, Timor-Leste, Tonga, Tuvalu, and Vanuatu.

Sources: Asian Development Bank. 2015. *Asian Development Outlook 2015*; Asian Development Bank. 2015. *Pacific Economic Monitor*, July; ADB estimates.

### East Asia

The outlook for East Asia remains subdued, necessitating downgrades to the 2015 and 2016 growth projections. The subregion is now expected to grow at 6.2% in both years, 0.3 and 0.1 percentage points lower than envisaged in *ADO 2015*. This reflects lower-than-expected growth outcomes in the PRC; Hong Kong, China; the Republic of Korea; and Taipei, China.

The PRC economy expanded by 7.0% in the first half of 2015, a more moderate start to the year than anticipated in *ADO 2015*. Consumption growth eased somewhat but remained robust, supported by strong income growth. Net exports contributed less to growth than expected because recovery in the major industrial economies disappointed. Investment growth continued to decelerate year over year as real estate investment was held back by a large inventory overhang, as was investment in manufacturing by weaker sales growth and excess capacity in some industries. Demand

for credit thus ebbed further despite monetary easing. Although the authorities relaxed some controls on local governments' off-budget financing to avoid a fiscal crunch and support infrastructure growth, important progress has been made toward strengthening local government finances by improving the enabling environment for local government bond issuance and public-private partnership. The financial sector, which contributed disproportionately to growth over the past 3 quarters, should contribute less after the recent stock market correction. The drop in stock prices is unlikely to have much impact on consumption or investment growth. Government efforts to stem the sell-off jar with its goal of allowing market forces to prevail but are consistent with the priority attached to stability. External demand should strengthen somewhat over the forecast period, but a strong exchange rate vis-à-vis the euro and yen will limit gains for the PRC. Although these broader trends are expected to continue over the forecast period, the authorities are likely to pursue only limited countercyclical measures in light of healthy labor markets. Accordingly, the growth forecast for the PRC in 2015 is revised down to 7.0% from 7.2% in *ADO 2015*, and to 6.8% from 7.0% in 2016.

Elsewhere in East Asia, 2015 growth projections for Hong Kong, China; the Republic of Korea; and Taipei, China have been scaled back from those in *ADO 2015*. In Hong Kong, China, the forecast is trimmed by 0.2 percentage points to 2.6% as recent indicators show moderating economic performance. In the first quarter of 2015, gross domestic product (GDP) grew by 2.1%, down from 2.4% in the previous quarter as demand from advanced markets was sluggish and visitor arrivals from the PRC declined. In the Republic of Korea, preliminary estimates for the first quarter of 2015 show continued deceleration in GDP expansion to 2.5%, the slowest in 2 years. Recent data point to persistent weakness in the next quarter, with the HSBC Manufacturing Purchasing Managers' Index dropping to a 21-month low in May and exports contracting in June for a sixth straight month. On account of the lackluster performance in exports and the likely economic impact of Middle East respiratory syndrome, GDP growth forecasts are revised down from 3.5% to 3.0% for 2015 and from 3.7% to 3.5% for 2016. Growing at 3.4%, the economy of Taipei, China also moderated in the first quarter of 2015 owing to modest export growth and declines in investments and government consumption. With export orders growing at only 0.7% from January to April, compared with 4.3% a year earlier, sluggish external sector performance is likely to persist. Given uncertainty in the global economy—and particularly in the PRC, the economy's top trading partner—the forecast for GDP growth in 2015 is revised down to 3.4% from 3.7% in *ADO 2015*. The forecast for 2016 remains unchanged at 3.6%.

### South Asia

The economic outlook for South Asia is for stronger growth in the subregion as a whole in 2015 than forecast in *ADO 2015*, now bumped up slightly to 7.3% from 7.2%. The

### Box 1 Outlook for the major industrial economies

The growth outlook for the major industrial economies—the US, the euro area, and Japan—is downgraded from the *ADO 2015* projection of 2.2% to 1.6% for 2015 and from 2.4% to 2.3% for 2016. The weather-related downturn in the first quarter of 2015 in the US weighs on an otherwise robust recovery there. The outlook for the euro area is maintained pending clarity on the situation in Greece. Forecasts for Japan are also maintained despite a relatively strong first quarter because second quarter indicators have been less positive.

Gross domestic product growth in the major industrial economies (%)

Area	2014	2015		2016	
	Actual	ADO 2015	ADOS	ADO 2015	ADOS
Major industrial economies	1.6	2.2	1.6	2.4	2.3
United States	2.4	3.2	2.2	3.0	2.9
Euro area	0.9	1.1	1.1	1.4	1.4
Japan	-0.1	1.1	1.1	1.7	1.7

ADO=Asian Development Outlook, ADOS=ADO Supplement.

Note: Average growth rates are weighed by gross national income, Atlas method.

Sources: Asian Development Bank. 2015. *Asian Development Outlook 2015*; ADB estimates.

The strong recovery projected for the US this year is tempered by gross domestic product (GDP) contraction in the first quarter. The final official GDP growth figure for the quarter had the US economy contracting by a seasonally adjusted annualized rate (saar) of 0.2%. The drop is seen as temporary, reflecting production disrupted by unseasonably harsh winter weather and trade disrupted by a ports dispute on the West Coast. Growth is thought to have revived in the second quarter, but its strength going forward remains uncertain as a high US dollar may continue to hamper export performance. Unemployment fell to 5.3% in June in tandem with improved consumer confidence and manufacturing performance. Poor results in the first quarter may prompt the US Federal Reserve to delay any interest rate increase, and the rise is expected to be gradual and moderate as inflation remains subdued. The growth outlook is now lower than in *ADO 2015*, with GDP in 2015 projected to grow by 2.2% instead of 3.2%. Assuming no extreme weather to interfere with economic activity in the first quarter of next year, growth momentum is expected to return in 2016, with GDP growing at 2.9%.

The euro area strengthened in the first quarter of 2015, growing by a surprisingly strong saar of 1.5% and with positive growth recorded in the four large economies of France, Germany, Italy, and Spain. While private consumption was the main driver of growth in the region, the recovery appears to be broad based, as investment and government consumption

also contributed positively. Indicators show real economic activity improving further in the second quarter. Industrial production increased by 0.1% in April (weak but still a rebound from contraction in March), and the composite purchasing managers' index climbed to 53.4 in June, the highest value in 4 years. Retail trade rose in April and May on the back of strong consumer confidence, low inflation, and falling unemployment (11.1% in May), which suggests that consumer spending will continue to drive growth in the second quarter. A weak euro possibly boosted merchandise exports, which increased by 8.7% in April, up from 4.8% in the first quarter. The combination of low oil prices, monetary easing, a weak currency, and low inflation supported euro area growth in the first 2 quarters, but the recovery may lose momentum as some of these factors fade. Further, while an agreement to provide additional support to Greece is being finalized as this *Supplement* goes to press, the euro area debt crisis will take time to resolve and may still hamper growth in the second half of the year. On balance, the *ADO 2015* forecasts of 1.1% growth in 2015 and 1.4% in 2016 are maintained.

Japan's GDP grew by a saar of 3.9% in the first quarter this year, slightly outpacing the expectations underlying *ADO 2015* forecasts. This acceleration was supported by private domestic demand for consumption and investment. Higher corporate profits fueled growth in business investment by 11.0% in the first quarter, following 3 quarters of anemic growth last year. External demand subtracted 0.7 percentage points from growth, as exports remained sluggish in May despite the weaker yen. The baseline scenario for 2015 is unchanged, but a correction in production is expected following inventory accumulation in the first quarter. For 2016, the baseline assumption is that private consumption of durable goods and housing investment will pick up somewhat in anticipation of the value-added tax hike from 8% to 10% planned for April 2017. All in all, Japan is forecast to post 1.1% growth in 2015 picking up to 1.7% in 2016, as envisaged in *ADO 2015*.

Australia's economy grew by a saar of 3.8% in the first quarter of 2015, double the 1.9% recorded in the fourth quarter of 2014. The acceleration is driven mainly by inventory buildup and a sharp increase in export growth. In June, Australia signed a free trade agreement with the PRC that will help bolster investment in Australia's deteriorating mining and resources sectors and support its external sector through increased exports. The Reserve Bank of Australia forecasts the economy expanding at between 1.75% and 2.75% in 2015 and between 2.50% and 3.50% in 2016. New Zealand's economy grew at a saar of 0.6% in the first quarter of 2015, the slowest growth rate in 3 years as agriculture and mining languished. Recently released data suggest that the economy continues to lose steam, as both business and consumer confidence significantly dropped in May. The Central Bank of New Zealand anticipates GDP expanding by 3.3% in 2015 and 3.2% in 2016.

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projection for 2016 remains at 7.6%. By individual economy, however, projected growth rate changes are mixed, with much stronger growth estimated for Bangladesh in FY2015 (ended 30 June 2015) but slower growth for the Maldives and earthquake-struck Nepal.

Recent data revisions from India show that GDP grew by 7.3% in FY2014 (ended 31 March 2015), slightly slower than the 7.4% reported in *ADO 2015*. The underlying indicators suggest that India is on track to achieve the *ADO 2015* forecast of growth at 7.8% in FY2015. A healthy monsoon extending to early July has seen summer crop sowing increase by 57.6% over last year and is expected to boost growth in agriculture. The number of new investment projects announced has continued to increase for the fourth consecutive quarter during the quarter ending June 2015, indicating brighter investment sentiment. Improvements in indirect tax collection in the first quarter of FY2015 similarly point to some recovery in manufacturing. The index of industrial production rose at an average rate of 3.2% during January–May 2015, double the 1.6% growth registered in the same period of 2014. The pace is expected to accelerate to 8.2% in FY2016, driven by continued service sector growth and the removal of procedural bottlenecks that have hampered investment. On the other hand, risks to growth prospects could emerge from further delay in passing some legislation crucial to easing land acquisition for industry and to implementing a uniform goods and services tax.

Developments in other South Asian economies have been mixed. The latest official estimates for economic growth in Bangladesh in FY2015 see growth coming in at 6.5% for the year, outperforming the 6.1% recorded in FY2014 and projected in *ADO 2015* for FY2015. These developments come on the back of stronger performance by industries serving the domestic market, supported in turn by healthy remittance inflows. Investment growth also contributed, with public investment rising strongly. Forecasts for Afghanistan, Bhutan, Pakistan, and Sri Lanka are retained as each economy stays its course. However, political factors present some downside risks to forecasts in the subregion, as a political transition in Sri Lanka causes private investors to take a wait-and-see approach to new investment, and political risk persists in Afghanistan and Pakistan. The forecasts for the Maldives is downgraded for 2015 and upgraded for 2016 because an expected surge in infrastructure investment has been pushed back a year. Finally in Nepal, the catastrophic earthquake in April caused widespread destruction in the capital and to other infrastructure, severely disrupting economic activity and substantially hobbling growth prospects. While the timing of the earthquake in the last months of FY2014 left growth outcomes decent in that fiscal year, forecasts for growth are revised down to 3.0% from 4.6% in FY2015 and to 4.5% from 5.1% in FY2016 (Box 2).

### Box 2 Macroeconomic impacts of the Nepal earthquake

As a part of its postdisaster needs assessment, the Central Bureau of Statistics released preliminary estimates of the macroeconomic impact of the April earthquake, arrived at in cooperation with the National Planning Commission, Asian Development Bank, and World Bank. GDP growth in FY2015 (ended 15 July 2015) is estimated to be 1.6 percentage points slower than the 4.6% forecast that *ADO 2015* made before the quake. Although the disaster struck Nepal in the tenth month of FY2015, the impact on GDP growth seems to have been sizable, especially in the service sector, which accounts for about half of GDP. The sector is expected to grow by 3.9%, compared with 6.0% projected for the no-earthquake scenario. The subsectors worst affected are wholesale and retail trade; tourism (including air transport, hotels, and restaurants); education; and real estate renting and business activities.

The earthquake's impact has been the most severe in the rural central and western administrative regions. As the Kathmandu Valley, Nepal's demand center, is also heavily affected, the quake and its aftershocks have slowed production throughout the country. The government estimates that recovery will take from 5 to 6 years.

### Southeast Asia

The 2015 and 2016 growth forecasts for some Southeast Asian economies have been trimmed, resulting in small downward revisions for the subregion as a whole. Southeast Asia's aggregate GDP is projected to grow by 4.6% in 2015, down by 0.3 percentage points from forecasts in *ADO 2015*, and 5.1% in 2016, down by 0.2.

Indonesia, the largest economy in the subregion, saw GDP growth decelerate further to 4.7% in the first quarter of 2015. The decline was sharper than anticipated mainly because budget approval was unusually late and significant bureaucracy changes across ministries diminished the contribution of government consumption. Private consumption remained robust despite being slightly affected by higher inflation following a domestic fuel price increase in November 2014. Recovery in investment was also weaker than projected. The contribution of net exports turned slightly positive as oil imports moderated significantly. Although the government has implemented a number of reforms—including a fuel subsidy cut, improvements to land acquisition regulations, and the introduction of one-stop services to simplify the procurement of investment licenses—their positive impacts will take time to materialize. Growth is expected to recover in the second half of the year, supported by government infrastructure spending and gradual recovery in net exports. Rupiah depreciation should boost exports. The growth projection for 2015 is revised down to 5.0% for

several reasons: a lower projection for the government's contribution reflecting delay in executing the budget and tax returns below target, only gradual realization of benefits to investment from economic reform, and delayed export recovery as commodity prices continue to fall and growth languishes in trading partners. Exports and investment should begin to recover soon enough to bring economic growth to 5.6% in 2016.

Malaysia's GDP grew by 5.6% year on year in the first quarter, underpinned mainly by private demand spurred by such one-off factors as flood relief early in the year and the frontloading of household spending prior to the implementation of the goods and services tax. This anticipates growth in 2015 buffeted by the fall in prices for energy and other commodities. However, government revenue streams are gradually diversifying away from oil as planned fiscal reforms remain on track. Growth forecasts are therefore maintained at 4.7% for 2015 and 5.0% for 2016.

GDP growth in the Philippines eased to 5.2% in the first quarter, the slowest pace in over 3 years, on sluggish exports and weak government spending. Net exports were a drag as import growth, driven by buoyant domestic demand, outpaced a modest rise in exports. Sluggish government expenditure is attributed to slow budget disbursement and caution exercised by agencies following Supreme Court rulings in November 2013 and July 2014 that found some public funds unconstitutional. Private investment and household consumption remain strong, however, supporting the maintenance of GDP growth forecasts of 6.4% for 2015 and 6.3% for 2016. Election-related spending is expected to boost domestic demand through May 2016, when elections will be held. Risks to the outlook include weaker-than-expected recovery in the major industrial economies and continued slow public spending despite government measures taken to improve budget execution.

An early estimate of GDP revealed that Singapore's economy grew by 1.7% in the second quarter of 2015, down from 2.8% growth in the first quarter. The slowdown primarily reflected 4.0% contraction in manufacturing as biomedical production and transport engineering suffered output declines. Growth also moderated in services, notably wholesale and retail trade and business services. Sector-specific factors such as low oil prices could weigh down growth in some sectors, and tourism-related industries may face headwinds from lackluster visitor arrivals for the rest of the year. Consequently, the GDP growth forecast for 2015 is revised down from 3.0% to 2.8%.

The Thai economy expanded at a disappointing rate of 3.0% year on year in the first quarter of 2015, caused in part by damage to agriculture from drought. Although the economy is on the path of recovery, expansion in private consumption has been gradual, and merchandise exports have contracted. Tourism has been the bright spot, contributing to a 1.0% expansion in exports of goods and services over the same period in 2014. Total investment accelerated by 10.7%, led by government investment. On

top of the drought, low commodity prices hit agricultural production hard. Reduced rural incomes combined with high household debt will slow recovery in private consumption in 2015. Weak first quarter growth, continued deterioration in the consumer confidence index, and the contraction of merchandise exports in the first 5 months of 2015 help guide the revision of the GDP growth forecast for 2015 down to 3.2% from 3.6% in *ADO 2015*. The growth projection for 2016 remains at 4.1% as government investment recovers and catalyzes private investment.

Growth forecasts for Viet Nam remain unchanged at 6.1% in 2015 and 6.2% in 2016. The economy expanded by 6.0% year on year in the first quarter of 2015. Government revenue collection leapt by 15.9% in that quarter, reflecting improving business sales and buoyed consumer confidence. The HSBC Manufacturing Purchasing Managers' Index rose to 54.8 in May, well above the 50.0 that signals expansion and the strongest reading since 2011. While bank reform remains slow and many nonperforming loans go unresolved, demand for consumer credit is driving a recovery in bank lending. Credit growth rose to 16% year on year by the end of the first quarter, up from 12% a year earlier. The trade deficit widened to \$1.2 billion in the first half of the year as rising growth and consumer spending prompted a surge in import demand. The emergence of a trade deficit and efforts to preserve a stable exchange rate are together putting pressure on foreign exchange reserves, which stood at the end of 2014 at \$34 billion, or 2.6 months of import cover.

### Central Asia

Lower global commodity prices and recession in the Russian Federation have dampened economic performance in Central Asia. Growth in the region's energy exporters—Azerbaijan, Kazakhstan, Turkmenistan, and Uzbekistan—is dragged down by low oil and gas prices and consequently lower export revenues. The energy importers—Armenia, Georgia, the Kyrgyz Republic, and Tajikistan—face, along with Uzbekistan, domestic consumption weakened by lower remittances. Growth factors are mixed. While agriculture, mining, and services performed well in the first quarter of 2015, as did construction associated with public investment programs, trade and export-oriented manufacturing remain stymied by weak external demand. The aggregate growth projection for Central Asia is maintained as projected in *ADO 2015* at 3.5% for 2015 but revised slightly down for 2016 to 4.2% from 4.5%. Revised projections for 2016 reflect unexpectedly weak performance in the subregion's energy exporters and, given the prolonged recession in the Russian Federation, low external demand.

Kazakhstan, Central Asia's largest economy, posted 2.2% growth in the first quarter of 2015. Despite low hydrocarbon prices and spillover from recession in the Russian Federation, unemployment and domestic consumption have remained stable thanks to mild growth in agriculture and construction, coupled with a modest 3.9% increase in fixed capital investments and the rollout of government programs. In the

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first quarter of 2015, the trade deficit deteriorated to 2.0% of GDP, reflecting a significant 5 percentage point decline in merchandise exports. The *ADO 2015* growth forecast of 1.9% for Kazakhstan in 2015 is maintained in light of low global commodity prices, ongoing recession in the Russian Federation, and weak business performance. A slower recovery prompts a downward revision of the 2016 growth forecast from 3.8% to 3.2%.

### The Pacific

This year is expected to be a strong one for the Pacific, as about half of its 14 developing member economies are expected to accelerate growth relative to last year. Average growth across the Pacific is projected to reach 9.9% in 2015, as envisaged in *ADO 2015*. The largest factor behind the Pacific's strong growth this year is the first full year of liquefied natural gas exports from Papua New Guinea (PNG), the subregion's dominant economy. Although low international gas prices are dampening growth expectations this year in PNG, gas exports are still expected to cause a spike in growth domestically and statistically across the subregion. Meanwhile, rapidly rising tourist arrivals brighten Palau's near-term economic prospects but also raise concerns about environmental sustainability and carrying capacity at the country's main tourist attractions. Growth in the Pacific is projected to halve to 5.0% in 2016, largely a base effect following this year's growth spurt from PNG gas exports. Meanwhile, severe weather dampens the 2015 growth outlook for the Federated States of Micronesia (FSM) and Vanuatu. Typhoon Maysak hit the FSM at the end of March, wiping out as much as 90% of food crops and destroying hundreds of homes in the states of Chuuk and Yap. The contraction in agricultural output is expected to be offset by reconstruction, but no numeric growth projection for the FSM economy is possible this year. Vanuatu, which was hit earlier by Cyclone Pam, appears to be headed for slight economic contraction in 2015. This reflects mainly a projected decline in tourist arrivals because of the time required to reconstruct and rehabilitate damaged facilities and infrastructure.

### Inflation outlook

Low oil prices and declining food prices continue to exert downward pressure on inflation in the region. The forecast for inflation in developing Asia is revised slightly down to 2.4% from 2.6% for 2015 but retained at 3.0% for 2016 (Table 2).

The inflation forecast for East Asia in 2015 is revised down from 1.7% to 1.4%, as inflation forecasts for the PRC, the Republic of Korea, Mongolia, and Taipei, China are downgraded from the rates projected in *ADO 2015*. In the PRC, falling commodity prices, decelerating credit growth, and weaker demand reduced average headline inflation to 1.3% year on year in the first half of 2015 and core inflation to 1.5%. Price reform for public goods and rebounding

Table 2 Inflation (%)

	2014	2015		2016	
		ADO 2015	ADOS	ADO 2015	ADOS
<b>Developing Asia</b>	<b>3.0</b>	<b>2.6</b>	<b>2.4</b>	<b>3.0</b>	<b>3.0</b>
<b>Central Asia</b>	<b>5.7</b>	<b>6.7</b>	<b>6.7</b>	<b>6.6</b>	<b>6.6</b>
Kazakhstan	6.7	6.0	6.0	6.2	6.2
<b>East Asia</b>	<b>1.9</b>	<b>1.7</b>	<b>1.4</b>	<b>2.2</b>	<b>2.2</b>
China, People's Rep. of	2.0	1.8	1.5	2.3	2.2
Hong Kong, China	4.4	3.3	3.3	3.4	3.4
Korea, Rep. of	1.3	1.3	0.8	2.1	2.0
Taipei, China	1.2	0.5	0.2	1.0	1.0
<b>South Asia</b>	<b>6.2</b>	<b>5.1</b>	<b>5.0</b>	<b>5.6</b>	<b>5.6</b>
India	5.9	5.0	5.0	5.5	5.5
<b>Southeast Asia</b>	<b>4.1</b>	<b>3.1</b>	<b>3.4</b>	<b>3.1</b>	<b>3.4</b>
Indonesia	6.4	5.5	6.4	4.0	4.9
Malaysia	3.1	3.2	3.3	2.9	3.0
Philippines	4.1	2.8	2.8	3.3	3.3
Singapore	1.0	0.2	0.2	1.5	1.5
Thailand	1.9	0.2	-0.4	2.0	1.8
Viet Nam	4.1	2.5	2.5	4.0	4.0
<b>The Pacific</b>	<b>3.6</b>	<b>5.0</b>	<b>4.7</b>	<b>4.1</b>	<b>4.0</b>

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Note: **Developing Asia** refers to 45 members of the Asian Development Bank. **Central Asia** comprises Armenia, Azerbaijan, Georgia, Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan. **East Asia** comprises the People's Republic of China; Hong Kong, China; the Republic of Korea; Mongolia; and Taipei, China. **South Asia** comprises Afghanistan, Bangladesh, Bhutan, India, the Maldives, Nepal, Pakistan, and Sri Lanka. **Southeast Asia** comprises Brunei Darussalam, Cambodia, Indonesia, the Lao People's Democratic Republic, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Viet Nam. **The Pacific** comprises the Cook Islands, Fiji, Kiribati, the Marshall Islands, the Federated States of Micronesia, Nauru, Palau, Papua New Guinea, Samoa, Solomon Islands, Timor-Leste, Tonga, Tuvalu, and Vanuatu.

Sources: Asian Development Bank. 2015. *Asian Development Outlook 2015*; Asian Development Bank. 2015. *Pacific Economic Monitor*, July; ADB estimates.

commodity prices will push inflation up somewhat in late 2015 and 2016. The producer price index fell by 4.6% year on year but should return to positive territory over the forecast period, driven by rising commodity prices. In the Republic of Korea, inflation during the first half averaged 0.5% and is likely to pick up during the remaining months of 2015, but not at the pace anticipated earlier as recovery in domestic demand will likely be slow. In Mongolia, monetary policy tightening and slowdowns affecting activities other than mining are keeping inflation lower than anticipated in *ADO 2015*. Taipei, China saw inflation enter negative territory in the first half of 2015, reaching -0.6%, as prices declined for fuels and lubricants, as well as for utilities. This prompts a downward revision to the 2015 inflation forecast from 0.5% to 0.2%.

In South Asia, inflationary pressures remain subdued as economic slack and low global food and commodity prices contain price pressures except in Nepal, where disrupted economic output and goods supply force up inflation

forecasts. In India, inflation remains low, suggesting that the recent uptick in activity has not yet been enough to take up the slack persisting in the Indian economy for many years. Muted hikes in rural wages and minimum support prices and a healthy monsoon would help rein in food inflation, while low crude oil prices globally bode well for fuel inflation as diesel and gasoline prices have both been deregulated.

Southeast Asia is the only subregion with higher 2015 and 2016 inflation projections, revised from 3.1% to 3.4% for both years. Upward revisions for Indonesia and Malaysia outweigh the downward revision for Thailand. In Indonesia, inflation is now expected to reach 6.4% in 2015 and 4.9% in 2016, almost a point higher than the *ADO 2015* projections of 5.5% and 4.0%, reflecting significant additional increases in administered prices. In Malaysia, the depreciating ringgit is seen to apply upward pressure on prices to the forecast horizon. Bucking the trend, headline inflation in Thailand fell by 0.8% in the first half of 2015 from a year earlier, largely as energy prices declined. The fall in prices for 6 consecutive months meets the technical definition of deflation. As domestic consumption is slow to recover and global oil and commodity prices remain low, deflation is projected to persist for the whole of 2015, with inflation returning in 2016.

Inflation has been contained in Central Asia thanks to effective price controls enacted across the region after currency devaluations in 2014 and early 2015. Aggregate inflation projections for Central Asia remain stable, as in *ADO 2015*, at 6.7% in 2015 and 6.6% in 2016. Aside from stability in most subregional economies, lower inflation expected in Georgia in 2015 offsets upward revisions for the Kyrgyz Republic and Tajikistan. In Kazakhstan, consumer prices increased by an average of 5.3% in the first half of 2015, driven mainly by increases for food and services. Committed to keeping inflation in the 6%–8% range, the government has set price ceilings for essential items such as food and fuel and has frozen utility tariffs. Strict price controls are envisaged keeping inflation stable as projected in *ADO 2015* at 6.0% in 2015 and 6.2% in 2016.

Inflation in the Pacific is projected to accelerate from 3.6% in 2014 to 4.7% in 2015, before moderating to 4.0% in 2016. The 2015 and 2016 inflation projections are slightly lower than those reported in *ADO 2015*, as soft international commodity prices kept inflation outcomes lower than expected early this year. The rise and fall of the revised inflation projections are consistent with expected trends in economic activity.

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