

HIGHLIGHTS

- Developing Asia's prospects remain largely in line with forecasts in *Asian Development Outlook 2016*, despite disappointing growth in the United States and a surprise Brexit vote outcome that chilled already tepid recovery in the euro area. This *Supplement* expects the region to expand by 5.6% in 2016—0.1 percentage points less than earlier forecast—and 5.7% in 2017.
- The People's Republic of China is on track to meet forecast growth of 6.5% in 2016 and 6.3% in 2017. East Asia is seen to expand by 5.7% this year and 5.6% in 2017 notwithstanding softness in Taipei, China and Hong Kong, China.
- Similarly, India has shrugged off global headwinds and is expected to grow by 7.4% in 2016 and 7.8% next year. South Asia as a whole will be the region's fastest growing subregion.
- First quarter 2016 growth in the major Southeast Asian economies also met projections except that Viet Nam fell short as bad weather dragged on agriculture. In aggregate, the subregion is forecast to expand by 4.5% in 2016, picking up to 4.8% in 2017.
- With fiscal pressures from continued low oil prices more acute than anticipated, the growth forecast for Central Asia is adjusted down by 0.4 percentage points to 1.7% in 2016, but the pace is still expected to pick up next year. The Pacific as a whole should meet forecasts as tourism boosts some economies and lagging disaster-recovery spending holds back others.
- Oil prices may have picked up somewhat more strongly than forecast, but local factors are having a bigger impact on average regional inflation. In particular, higher food prices in the People's Republic of China boost regional inflation forecasts by 0.3 percentage points, to 2.8% in 2016 and 3.0% in 2017.

ASIA'S GROWTH PROSPECTS UNDIMMED BY BREXIT VOTE

Growth outlook

Developing Asia's growth outlook this year is revised slightly down from that published in March in *Asian Development Outlook 2016 (ADO 2016)*. Growth in Central Asia is weaker than predicted, while expansion in the Pacific is now expected to be a touch higher. Forecasts are unchanged for East, South, and Southeast Asia. In aggregate, the region's gross domestic product (GDP) is now forecast to grow by 5.6% in 2016. The growth projection of 5.7% for 2017 is maintained (Table 1).

The combined growth forecast for the major industrial economies—the United States (US), the euro area, and Japan—is trimmed from *ADO 2016* projections. Surprisingly soft growth in the US and heightened uncertainty in the euro area following the British vote to leave the European Union prompted revisions to the 2016 and 2017 forecasts (Box 1). While the Brexit vote has affected developing Asia's currency and stock markets, its impact on the real economy in the short term is expected to be small (Box 2).

East Asia

East Asia is on track to meet expectations in *ADO 2016*. The growth outlook for the subregion is maintained at 5.7% in 2016 and 5.6% in 2017. In the People's Republic of China (PRC), slight moderation of GDP growth—to 6.7% in the first half of 2016 from 6.9% in 2015—is expected to continue over the forecast period amid weakening investment growth and anemic exports. Weaker-than-expected private investment was only partly compensated by stronger

The Asian Development Bank Regional Economic Outlook Task Force led the preparation of the revised outlook for this *Asian Development Outlook 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.

2 ASIAN DEVELOPMENT OUTLOOK SUPPLEMENT

government-led infrastructure investment and a credit-driven recovery in real estate sales and investment, which appears to have peaked in May 2016. Consumption has remained relatively robust, but its growth is also moderating, as expected, as wage and income growth slow. To meet its growth target of at least 6.5% in 2016, the government will continue to provide fiscal and monetary stimulus, though less than in the first 4 months of 2016, to contain asset bubbles and the asset quality problems that have been building on the balance sheets of banks and other financial institutions. This *Supplement* therefore maintains the growth projections in *ADO 2016*. The economy is expected to grow by 6.5% in 2016. The curbing of excess industrial capacity will drag GDP growth down to 6.3% in 2017 unless bolder structural reform unlocks growth potential in other parts of the economy such as the service sector.

Elsewhere in East Asia, growth forecasts for Taipei,China and Hong Kong, China are scaled back from those in *ADO 2016*. In Hong Kong, China, GDP was up by just 0.8% year on year in the first quarter of 2016, a considerable slowdown from 1.9% expansion in the fourth quarter of 2015. Prolonged weakness in the external sector and recent asset market corrections continued to batter local sentiment. Domestic demand weakened in the first quarter. This and the continued slowdown in inbound tourism dragged down retail sales, which saw their largest year-on-year decline since the Asian financial crisis in 1997. Capital spending contracted further, mainly reflecting the large fall in machinery and equipment acquisition as business confidence weakened. With disappointing private consumption, growth in 2016 is revised down from 2.1% to 1.5%, before a slight pickup to 2.0% in 2017.

The export-driven economy of Taipei,China contracted by 0.7% in the first quarter of 2016 as demand for its goods remained sluggish. Capital and inventory investment also contracted in response to greater political uncertainty. Robust private and government consumption could not offset the slowdown in trade and investment. The latest indicators from the second quarter confirm that economic activity continues to be weak. As immediate recovery looks unlikely, the growth forecast for Taipei,China is downgraded from 1.6% to 1.1% in 2016 and from 1.8% to 1.6% in 2017.

Supported by robust expansion in construction and total consumption, the Republic of Korea grew by 2.8% year on year in the first quarter of 2016. The recent economic performance has been broadly in line with expectations, with domestic demand sustaining growth. Both consumption and construction are expected to support economic expansion and offset the effects of soft external demand. Meanwhile, investment will continue to be hard hit by uncertain external and domestic environments. As there is no clear trend of marked improvement in domestic demand, and as the slowdown in global trade continues, the growth forecast for 2016 is unchanged at 2.6%. The forecast for next year is likewise kept at 2.8%, the improvement spurred by expected strengthening in the global economy.

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

	2015	2016		2017	
		ADO 2016	ADOS	ADO 2016	ADOS
Developing Asia	5.9	5.7	5.6	5.7	5.7
Central Asia	3.0	2.1	1.7	2.8	2.7
Kazakhstan	1.2	0.7	0.4	1.0	1.0
East Asia	6.0	5.7	5.7	5.6	5.6
China, People's Rep. of	6.9	6.5	6.5	6.3	6.3
Hong Kong, China	2.4	2.1	1.5	2.2	2.0
Korea, Rep. of	2.6	2.6	2.6	2.8	2.8
Taipei,China	0.7	1.6	1.1	1.8	1.6
South Asia	7.0	6.9	6.9	7.3	7.3
India	7.6	7.4	7.4	7.8	7.8
Southeast Asia	4.4	4.5	4.5	4.8	4.8
Indonesia	4.8	5.2	5.2	5.5	5.5
Malaysia	5.0	4.2	4.2	4.4	4.4
Philippines	5.9	6.0	6.0	6.1	6.1
Singapore	2.0	2.0	2.0	2.2	2.2
Thailand	2.8	3.0	3.0	3.5	3.5
Viet Nam	6.7	6.7	6.3	6.5	6.5
The Pacific	7.1	3.8	3.9	3.1	3.0

ADO = Asian Development Outlook, ADOS = ADO Supplement.

Note: **Developing Asia** refers to the 45 members of the Asian Development Bank listed below. **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. 2016. *Asian Development Outlook 2016*; Asian Development Bank. 2016. *Pacific Economic Monitor*, July; Asian Development Bank estimates.

South Asia

The economic outlook for South Asia remains strong, with growth on track to meet *ADO 2016* projections of 6.9% in 2016 and 7.3% in 2017. In Bangladesh and Pakistan, initial government estimates of GDP growth in FY2016 (ended 30 June 2016) beat *ADO* forecasts, but this was balanced somewhat by slower growth in Nepal. Industry growth in Bangladesh in FY2016 was higher than expected in line with a strong garment sector. Services growth also boosted the economy, supported by higher wages in the public sector. However, the recent terror attack in Dhaka could affect investor confidence and undermine growth.

In Pakistan, further improvements in energy supply, higher infrastructure investment, and a better security environment will push up GDP in both 2016 and 2017. In contrast, the slowing pace of earthquake reconstruction has dampened Nepal's prospects.

Box 1 Outlook for the major industrial economies

The growth outlook for the major industrial economies—the US, the euro area, and Japan—is revised down from *ADO 2016* projections. Disappointing results in the US and heightened uncertainty in the euro area following the United Kingdom vote to exit the European Union are weighing down the outlook. Together, these economies are forecast to grow by 1.5% in 2016 and 1.7% in 2017.

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

Area	2015	2016		2017	
	Actual	ADO 2016	ADOS	ADO 2016	ADOS
Major industrial economies	1.8	1.8	1.5	1.9	1.7
United States	2.4	2.3	1.9	2.5	2.5
Euro area	1.6	1.5	1.3	1.6	1.1
Japan	0.6	0.6	0.5	0.5	0.8

ADO = Asian Development Outlook, ADOS = ADO Supplement.

Note: Average growth rates are weighed by gross national income, Atlas method, in current US dollars.

Sources: Asian Development Bank. 2016. *Asian Development Outlook 2016*; Asian Development Bank estimates.

US economic activity had an unimpressive start to 2016 as first quarter GDP grew by a seasonally adjusted annualized rate (saar) of only 1.1%, below most market expectations. Consumption remains the pillar of growth, followed by government outlays. Net exports also contributed to growth after 2 quarters of decline. Industrial activity and business investment remain weak as readings of industrial production and purchasing managers' indexes suggest slower expansion in production. Consumer confidence rebounded at the end of the second quarter, suggesting an anticipated acceleration in consumption growth as retail sales reached a 2-year high in May. The unemployment rate inched up to 4.9% in June from 4.7% a month earlier—this despite the greatest gain in nonfarm jobs since November 2015. The relatively stable and strong dollar helped keep headline inflation low, but core inflation breached 2% in January and has since stayed above that mark. However, the US Federal Reserve delayed monetary policy tightening in response to the mixed June labor market report and to uncertainty caused by the Brexit vote. Weaker-than-expected first quarter growth prompts a downward revision to the outlook for 2016 to 1.9% from 2.3% in *ADO 2016*. The 2017 growth forecast is kept at 2.5%.

The euro area expanded by a saar of 2.2% in the first quarter of 2016, driven by robust domestic demand strengthened by low oil prices, ultra-loose monetary policy, and labor market recovery. However, recent data have cast a shadow over the momentum: While the purchasing managers' index suggest steady output growth in June, industrial production contracted again in May after rebounding in April. Economic sentiment hit

a pothole in June as well, weakening for the first time since March. These developments—together with rising oil prices and a weak external sector—point to a feeble second quarter. Prices remain subdued in light of muted global producer prices. The Brexit vote further tilted risk to the downside as highly unsettled financial markets hit regional wealth and investment. Direct effects via the trade channel could be fairly benign—at least before 2018—depending on the size of a British demand shock this year and next. The European Central Bank will likely expand and extend its asset purchase program to stem the fallout, while some transitory leniency in meeting European Union fiscal rules is also possible. As heightened uncertainty will weigh on domestic demand, the GDP growth forecast for 2016 is downgraded to 1.3% from 1.5% in *ADO 2016*. Concerns clouding Britain's actual exit, on top of a fragile global economy and jittery financial markets, is seen to limit growth to 1.1% in 2017.

Following contraction in the last quarter of 2015, Japan avoided a technical recession in the first quarter of 2016 and expanded by a saar of 1.9%. Higher wages and the boost to personal spending from the additional working day in February helped private consumption recover. Government consumption and trade also contributed to growth. These developments were partly offset, however, by falling private investment. Industrial production rose in April, and firms' projections point to further small gains in June. On 30 May 2016, the government announced that it would delay the value-added tax rate rise from April 2017 to October 2019, lowering the prospect of a spike in private consumption toward the end of 2016 as consumers front-load their spending and a balancing collapse in mid-2017. While the likely impact on growth from the postponement of consumption is debatable, delaying it will impose a fiscal squeeze at least in the near term. Meanwhile, financial market volatility following the Brexit vote and the consequent abrupt appreciation of the yen will add further strain. Japan is expected to grow by 0.5% this year and 0.8% in 2017—slightly faster in 2017 than previously forecast with the postponement of the value-added tax hike.

In Australia, strong growth in commodity and service exports helped the economy achieve remarkable 1.1% growth in the first quarter of 2016, the fastest pace in 4 years. Fixed investment continued to be the soft spot in the economy as resource extractors further scaled back capital expenditure. Business confidence remains robust. The Reserve Bank of Australia forecasts the economy to grow by 2.5%–3.5% in both 2016 and 2017. In New Zealand, GDP growth fell in the first quarter to 0.7% from the 0.9% in the fourth quarter of 2015. The softness stemmed from weak mining, manufacturing, and wholesale trade. Yet, with solid domestic demand seen to support growth in the rest of the year, the Reserve Bank of New Zealand foresees the economy expanding by 2.4% in 2016 and 3.2% in 2017.

Box 2 Brexit's economic impact on developing Asia

The United Kingdom (UK) voted on 23 June 2016 to leave the European Union (EU), sparking negative reactions on global financial markets. Sterling immediately fell to a value not seen since the mid-1980s (box figure), and stock markets also fell. But the immediate damage from the unexpected outcome does not appear to be catastrophic. Critically, unlike the global financial crisis, Brexit does not reflect fundamental weakness in the global financial system.

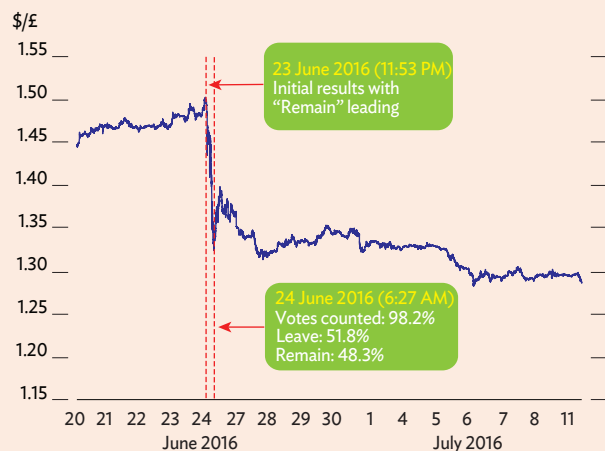
While Brexit has often been cited as a potential risk to global growth, its economic costs are widely foreseen borne primarily by the UK. Indeed, many analysts predict that post-Brexit political and economic uncertainty could push the UK into recession. Various institutions estimate the GDP losses for the UK economy to range from 0.1% to 4.0% in 2016 and 2017. Estimates of the long-run impact on the UK GDP vary more widely, from a drop of 9.7% to a gain of 4.0%.

Brexit will affect EU growth as well by changing the dynamics of trade, investment, and financial sector relationships between the EU and the UK. But the impact on the EU is likely to be much smaller than on the UK. EU merchandise exports to the UK accounted for only 6.4% of all EU merchandise exports in 2015. Bundling in lesser factors, this *Supplement* predicts the euro area will see economic growth at 1.3% in 2016 and 1.1% in 2017, 0.2 and 0.5 percentage points lower than the respective *ADO 2016* projections in March.

It is still far too early to judge how Brexit will affect growth in developing Asia, as this will depend very much on how the future relationship between the UK and the EU evolves, and on other economic and political developments that result. Certainly, the sooner the uncertainty arising from the Brexit vote is resolved, the smaller its economic impact, both globally and in Asia. As things stand, the short-term economic impact of Brexit on developing Asia is expected to be small.

The region's merchandise exports to the UK accounted for only 2.2% of the total in 2015. As such, a slowdown in the UK is unlikely to significantly affect, through the trade channel, Asian growth on average, though the impact could be bigger on some economies in South and Southeast Asia that are more dependent on the UK market. Developing Asia's exports to the EU are higher, accounting for 13.3% in 2015 on average, with some economies shipping more than 40% of their total

Box figure Sterling against the US dollar



Note: Time in British summer time (GMT+1).

Source: Bloomberg (accessed 11 July 2016).

exports to the EU. But, as mentioned above, the short term impact of Brexit on EU growth is likely to be limited.

In addition to trade, financial spillover such as capital flow reversals can affect developing Asia. While Asian currencies fell on 24 June 2016 as investors sought safety, the fall was nowhere near as large as the plunge in sterling. The region's markets rallied and recovered a few days later in tandem with global markets. Furthermore, developing Asia has become more resilient to external shocks thanks to sound macroeconomic policy, stronger financial systems, and large buffers in the form of foreign exchange reserves. The financial spillover so far is manageable.

However, if Brexit-induced uncertainty on global financial markets and economies turns out to persist and grow, Brexit's impact on Asia could be greater through the channels of trade, investment, capital flows, exchange rates, and consumer and business confidence. Brexit is a timely reminder of the need for developing Asia to continue its efforts to strengthen resilience against external shocks through sound macroeconomic management and structural reform.

Economic growth in India gained momentum in the final quarter of FY2015 (ended 30 March 2016) and pushed full-year growth to 7.6% in line with the *ADO 2016* estimate. Brisk consumer spending propelled India's economic growth to its highest in 5 years. As measured by the purchasing managers' index, manufacturing steadily inched up over the first quarter of FY2016, reaching 51.7 in June as new orders proliferated. However, actual industrial production suffered a small contraction, dragged down by a larger contraction in manufacturing output. After a weak start, the monsoon picked up in mid-June and overcame the early rain deficit by the first week of July. The improved monsoon encouraged

more planting of rice, pulses, and sugarcane into July. There are some signs of an uptick in rural demand in anticipation of good monsoon and a rural-oriented government budget. Reforms like the passage of the Bankruptcy Code, which creates time-bound processes for resolving corporate insolvency, and the easing of rules governing foreign direct investment are likely to facilitate business. Growth forecasts are maintained at 7.4% for 2016 and 7.8% for 2017.

Southeast Asia

The growth outlook for Southeast Asia remains at 4.5% in 2016 and 4.8% in 2017, as outcomes in the first half of the

year were as projected in March for all economies except Viet Nam. Private consumption aided by lower inflation provided strong support to most economies in the region in 2016 and is projected to pick up in 2017. Lackluster export performance amid weak global demand is limiting growth potential in most countries. The more open economies will remain susceptible to external risks such as a greater-than-expected slowdown in PRC, weaker growth in the major industrial economies, and sharply lower oil prices.

The Indonesian economy grew by 4.9% in the first quarter of 2016, supported by strong private consumption and investment. Low inflationary pressures from stable administrative prices for motor fuel, liquefied petroleum gas, and electricity supported private consumption, as did a stable rupiah. Meanwhile, government consumption grew by 2.9% in line with historically low spending in the first quarter. Private consumption is expected to pick up slightly in response to moderate inflation, a relatively stable rupiah, and an April cut in energy prices. Household spending will enjoy additional boosts from the announced 50% increase in the threshold for liability to personal income tax in 2016 and a 14th monthly salary payment for civil servants. Consumer confidence was up in the first 4 months of the year, but other high-frequency consumption indicators remain mixed. These factors will help achieve the growth forecasts in *ADO 2016* of 5.2% for 2016 and 5.5% for 2017. Support will come from gradually improving domestic demand, including accelerated government capital spending.

In Malaysia, GDP expanded by 4.2% in the first quarter of 2016, lower than the 5.7% expansion recorded during the same period last year and reflecting mainly sluggish external demand and cautious private sector spending. Gross fixed capital formation slowed on lower investment in the upstream mining sector and lower government spending, but change in stocks turned positive, lifting overall investment. Industrial production recovered, increasing by 3.0% in April as mining and electricity improved. Despite the rebound in consumer sentiment and the minimum wage increase expected by mid-2016, private consumption is expected to remain under pressure from elevated inflation and slowing employment growth. Private investment is also expected to remain relatively subdued as housing approvals and nonresidential loan applications slowed in the first quarter. Cautious business sentiment and lower commodity prices are also expected to weigh on investment in the upstream mining sector. As envisaged in *ADO 2016*, a broad economic slowdown is expected to continue through 2016. This *Supplement* maintains the growth forecast at 4.2% in 2016, picking up to 4.4% in 2017.

The Philippine economy recorded growth at 6.9% in the first quarter of 2016, which was 1.9 percentage points higher than in the same period in 2015. Election-related spending ahead of the May 2016 national elections helped drive the upbeat economic performance. Pre-election spending helped boost investment, household consumption, and government expenditure. Strong growth in industry and

services also fueled this impressive economic performance. Robust domestic consumption catalyzed construction and manufacturing. Private construction continued to grow, while public infrastructure spending strongly rebounded, rising by 39.9% in the first quarter. Growth is expected to slow in the rest of 2016 as the effect of the pre-election spending wanes and global economic uncertainty persists. In addition, remittances experienced slow growth at 3.0% in January–April, down from 8.6% in the same period of 2015. GDP growth is forecast at 6.0% in 2016 and 6.1% in 2017, as in *ADO 2016*.

Singapore's economy grew by 1.8% in the first quarter of 2016, supported by growth in wholesale and retail trade, finance and insurance, and construction. Construction recorded the strongest performance, expanding by 6.2% on support from public sector construction and building by private industry. Manufacturing contracted by 1.0%, but this improved on the previous quarter thanks to a surge in pharmaceuticals and expansion in electronics. Despite the weak global economic outlook early this year, domestic-oriented sectors have remained supportive of growth, and the economy as a whole is likely to experience modest growth throughout 2016. The expansion of construction and improvement in manufacturing will counterbalance moderation in services, particularly in finance and in transportation and storage. The GDP growth forecasts are thus maintained at 2.0% for 2016 and 2.2% for 2017.

The Thai economy expanded by 3.2% in the first quarter of 2016, supported by government investment and exports of services. Private investment also started to expand after a decline last year. Recently released indicators show, however, that economic activity remains feeble. In April, manufacturing production growth decelerated to 1.5% from 2.2% in March. Exports fell by 8.0% from the same month in 2015. With high household debt, wages rising only slowly, and the effects of stimulus measures fading, private consumption is expected to expand only slowly in the rest of 2016. The *ADO 2016* growth projection for 2016 is therefore maintained at 3.0%. Growth in 2017 is forecast at 3.5% as a better economic climate and higher commodity prices help consumption to expand and as private investment recovers.

In Viet Nam, GDP growth in the first half of 2016 came in at 5.5%, significantly lower than projected and steeply down from the 6.3% registered in the same period last year. Agriculture shrank by an estimated 0.2% as adverse weather deepened into a severe drought in the Central region and the Central Highlands. Other parts of the economy remained relatively strong, with services recording higher growth than in 2015, coming in at 6.1%, while industry and construction grew by 6.7%. Foreign direct investment continues to hit record highs. However, the growth forecast for 2016 is downgraded to 6.3% as the unexpected weakness in agriculture will likely keep the economy from achieving 6.7% growth as envisaged in *ADO 2016*. GDP growth in 2017 is still expected at 6.5%.

6 ASIAN DEVELOPMENT OUTLOOK SUPPLEMENT

Central Asia

Low global commodity prices, in particular for oil and natural gas, and the ongoing recession in the Russian Federation have dampened the growth outlook for Central Asia.

Growth in the subregion's energy exporters—Azerbaijan, Kazakhstan, Turkmenistan, and Uzbekistan—is suffering from a decline in public investment as lower revenues from hydrocarbon exports necessitate fiscal consolidation. The energy importers—Armenia, Georgia, the Kyrgyz Republic, and Tajikistan—are witnessing, together with Uzbekistan, weak domestic consumption hampered by lower remittances, in particular from the Russian Federation. While agriculture supported growth in the first 5 months of 2016, industry and trade remained sluggish under weak demand. The aggregate growth projection for Central Asia in 2016 is revised down to 1.7%, from the 2.1% projected in *ADO 2016*, reflecting weaker-than-expected performance in the subregion's major energy exporters so far in 2016, as well as lagging recovery in the Russian Federation. The growth forecast for 2017 is adjusted downward by 0.1 percentage points to 2.7%.

Kazakhstan, Central Asia's largest economy, has seen its currency appreciate in 2016 in tandem with modest recovery in global oil prices. By the end of June, the tenge stood at T339 to the dollar, after having hit a low of T385 on 21 January 2016. In the first quarter of 2016, Kazakhstan's GDP contracted by 0.1% year on year, mostly because of recession in industry as demand weakened both domestically and externally. Services—normally a driver of growth—contracted by 0.5% in the first quarter of 2016, suffering from weak private consumption after the exchange rate band was abandoned. Additional fiscal stimulus and a stabilizing tenge exchange rate as global energy prices recover are expected to help domestic demand pick up in the second half of 2016 and through 2017. Given the weak economic performance in 2016 to date, the growth forecast for 2016 is revised down to 0.4% from the 0.7% projected in the *ADO 2016*. The forecast for 2017 is unchanged at 1.0%.

The Pacific

Economic growth in the Pacific is expected to moderate to 3.9% in 2016. This is down from 7.1% last year but a 0.1 percentage point upgrade from the *ADO 2016* projection. Consistency in the growth forecast at the subregional level masks divergent outlooks for some individual economies in light of recent developments. Unexpectedly strong tourism helped push output growth above projections in the Cook Islands and Samoa during FY2016 (ended 30 June 2016). In Vanuatu, the implementation of major infrastructure projects (including previously delayed post-cyclone reconstruction) and broader economic recovery prompt an upward revision to the country's 2016 growth projection. Conversely, the growth outlook for Fiji is cut further, as the full extent of economic damage and losses caused by Cyclone Winston in February is taken into account. Prospects for the Solomon Islands economy are also more muted as stimulus from planned fiscal expansion is seen to provide less benefit

for economic activity than previously anticipated. This is reflected in reduced estimates of GDP growth in 2015. The outlook for Tuvalu is also downgraded, but this largely reflects base effects from surprisingly strong growth in 2015. Most of these in-country trends are seen to persist into next year. The opposing trends in individual economies are projected to support subregional average growth at 3.0% in 2017, about the same as projected in *ADO 2016*.

Inflation outlook

Rising commodity prices are putting upward pressure on inflation in the region, though the rates of consumer price increases remain low for most economies. Inflation forecasts for developing Asia are revised to 2.8% in 2016 and 3.0% in 2017, up by 0.3 percentage points each year (Table 2).

After dropping to \$26/barrel on 20 January 2016, oil prices rebounded to more than \$40/barrel in April. They have consistently been above \$40 since 8 April (on 8 June climbing past the \$50/barrel mark) and are currently trading within a narrow band of \$46–\$50/barrel. Several factors put upward pressure on crude oil prices: rising oil demand, ongoing declines in the US rig count and crude oil production, and worsening oil supply outages. In addition, the onset of the summer driving season in North America has supported prices. On the other hand, the recent strengthening of the US dollar and the failure on 2 June of the Organization of the Petroleum Exporting Countries to agree on a production ceiling have hampered further upside gains. Futures markets still signal a modest recovery in prices over the next 2 years. The Brent crude oil price is forecast to average \$43/barrel in 2016 and \$50/barrel in 2017.

The World Bank food price index averaged 98.9 points in June 2016, 8.9% higher than in June 2015. This was the second consecutive month of year-on-year price increases after more than 3 years of declines. Further, the June increase marked the fifth consecutive month that the food price index rose. However, food prices still languish 25.8% below their August 2012 peak. According to the latest *Food Outlook* report from the Food and Agriculture Organization of the United Nations, global food commodity markets are broadly stable, supported by adequate supply, and the prospects for market supply remain favorable for 2016 and 2017. The food price index is forecast to contract by 1.0% in 2016 and rise by only a modest 2.0% in 2017.

East Asia inflation projections are revised up for 2016 and 2017 as higher prices are now expected in the PRC, Mongolia, and Taipei, China. In the PRC, consumer price inflation averaged 2.1% in January–June 2016. While weaker demand is containing price pressures, the stabilization of global commodity prices and a strong cyclical increase of domestic food prices have been pushing up consumer price inflation and moderating producer price deflation faster than expected. Inflation forecasts are therefore revised up

to 2.2% from 1.7% for 2016 and to 2.4% from 2.0% for 2017. Significant loosening of monetary policy is pushing prices up in Mongolia. In Taipei, China, inflation in the first 5 months of 2016 showed strong increases, especially in February and March, driven by sharp increases for fruits and vegetables. With further easing of monetary policy possible, as well as pressure to stimulate the economy, higher inflation is now anticipated, at 1.3% in 2016 and 1.5% in 2017.

The South Asia inflation forecast of 5.2% for 2016 is in line with the projection in *ADO 2016*. Most 2017 inflation projections for individual economies remain current—excepting Bangladesh and Bhutan, which can now expect lower inflation thanks to domestic factors such as ample food supply and slow private sector credit growth, and still low global fuel and commodity prices. Despite this, the subregional inflation forecast remains at 5.7% for 2017. In India, inflation in May 2016 was 5.8%, slightly higher than the 5.5% recorded in April 2016. The pickup in inflation was driven entirely by food prices, while fuel inflation eased marginally and core inflation remained largely unchanged.

Inflation in Southeast Asia is now seen at 2.2% in 2016, which is lower than original forecast of 2.6%. The forecast for 2017 is revised from 2.9% to 3.0%. The unexpected reduction in fuel prices in Indonesia will likely slash inflation from 6.4% in 2015 to 3.9% in 2016. Inflation is seen accelerating slightly in 2017 as both growth and energy prices firm up. Inflation in the Philippines is expected at 1.8% in 2016, a downward revision from 2.3% in *ADO 2016*. The adjustment is in line with a lower-than-expected result in the first 5 months as the impact of El Niño on food prices was less severe than anticipated. Rice imports augmented domestic supplies, helping to ease price pressures. The inflation forecast for 2017 is revised slightly up to 2.8% in anticipation of higher gains in oil prices. The forecast for Brunei Darussalam has deflation moderating slightly in 2016 as economic growth picks up, but subsidies and price controls will continue to keep inflation low. In Singapore, deflation is projected to persist through 2016 but reverse in 2017. The inflation forecast for Thailand in 2016 is revised downward in light of relatively low oil and commodity prices and the slow pace of economic growth. Inflation in the Lao People's Democratic Republic is expected to pick up at a slower pace as global oil prices increase only moderately, as does the growth of bank credit in the economy.

In Central Asia, although inflation has been lower than expected during the first 5 months of 2016 in Armenia, Georgia, and the Kyrgyz Republic, an increase in the inflation projection for Kazakhstan in 2016 is pushing up the aggregate inflation forecast to 11.0% from the 10.8% projected in *ADO 2016*. In Kazakhstan, average inflation in the first half of the year stood at 15.9%. As there has been an upward trend in

Table 2 Inflation (%)

	2015	2016		2017	
		ADO 2016	ADOS	ADO 2016	ADOS
Developing Asia	2.1	2.5	2.8	2.7	3.0
Central Asia	6.2	10.8	11.0	5.9	5.7
Kazakhstan	6.6	12.6	13.5	4.6	4.6
East Asia	1.3	1.6	2.1	2.0	2.3
China, People's Rep. of	1.4	1.7	2.2	2.0	2.4
Hong Kong, China	3.0	2.5	2.4	2.7	2.5
Korea, Rep. of	0.7	1.4	1.2	2.0	2.0
Taipei, China	-0.3	0.7	1.3	1.2	1.5
South Asia	4.9	5.2	5.2	5.7	5.7
India	4.9	5.4	5.4	5.8	5.8
Southeast Asia	2.7	2.6	2.2	2.9	3.0
Indonesia	6.4	4.5	3.9	4.2	4.3
Malaysia	2.1	2.7	2.7	2.5	2.5
Philippines	1.4	2.3	1.8	2.7	2.8
Singapore	-0.5	-0.6	-0.8	0.4	0.4
Thailand	-0.9	0.6	0.4	2.0	2.0
Viet Nam	0.6	3.0	3.0	4.0	4.0
The Pacific	3.4	4.5	4.4	4.7	4.7

ADO = Asian Development Outlook, ADOS = ADO Supplement.

Note: **Developing Asia** refers to the 45 members of the Asian Development Bank listed below. **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. 2016. *Asian Development Outlook 2016*; Asian Development Bank. 2016. *Pacific Economic Monitor*, July; Asian Development Bank estimates.

inflation since the beginning of 2016, particularly for nonfood items, the inflation forecast for the year is revised to 13.5% from 12.6%. Inflation in the subregion is forecast to slow in 2017 to 5.7%, slightly below the 5.9% projected in *ADO 2016*. This anticipates waning pass-through of local currency depreciation to consumer prices, particularly in Kazakhstan.

Inflation in the Pacific is projected at 4.4% for 2016, down from the 4.5% forecast in *ADO 2016* in light of lower-than-expected price increases so far this year. In 2017, subregional inflation is still expected to rise to 4.7%, as in *ADO 2016*, in light of a projected modest recovery in international food and fuel prices.

Asian Development Outlook Supplement

Asian Development Outlook is the main economic forecasting product from ADB. It is published each April with an *Update* published in September and brief *Supplements* published in July and December.

Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to half of the world's extreme poor. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.

The views expressed in this publication are those of the authors and do not necessarily reflect the views and policies of ADB or its Board of Governors or the governments they represent. ADB encourages printing or copying information exclusively for personal and noncommercial use with proper acknowledgment of ADB. Users are restricted from reselling, redistributing, or creating derivative works for commercial purposes without the express, written consent of ADB.

Asian Development Bank
6 ADB Avenue, Mandaluyong City
1550 Metro Manila, Philippines
www.adb.org; openaccess.adb.org

In this publication, "\$" refers to US dollars.



Creative Commons Attribution 3.0 IGO license (CC BY 3.0 IGO)

© 2016 ADB. The CC license does not apply to non-ADB copyright materials in this publication.