



EADS Regional Trends Report on South Asia

September 2014

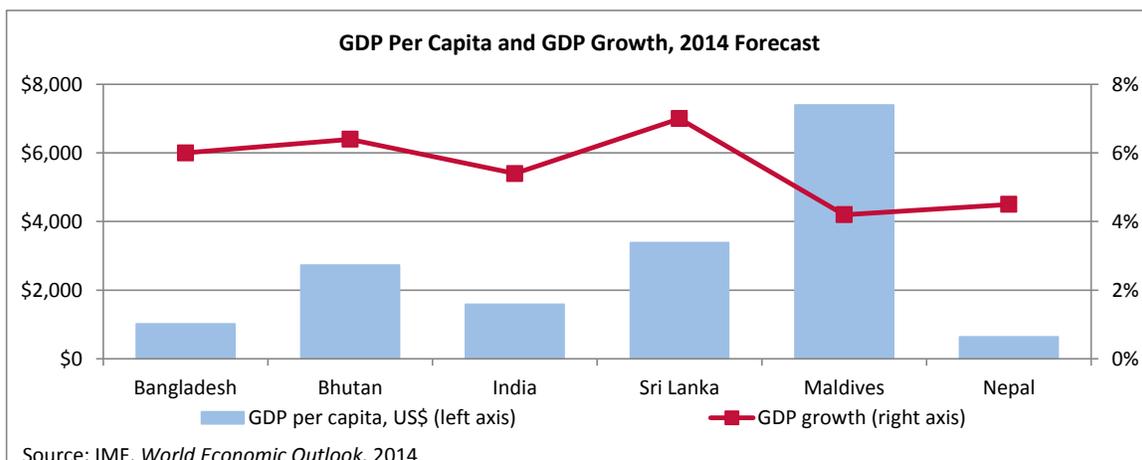
The South Asia region has faced several elections and transitions in recent months, with May's elections in India, the region's largest country and economy, ushering in Narendra Modi of the Bharatiya Janata Party (BJP) on a platform of economic prosperity and reform. The region also saw general elections in Bangladesh, Constituent Assembly elections in Nepal, presidential elections in the Maldives, provincial council elections in Sri Lanka, and National Assembly elections in Bhutan in the past year. Political uncertainty contributed in part to relatively slow growth in South Asia in 2013, while a poor business environment in many countries further slowed growth.

This Trends Report focuses on South Asian countries that received \$2 million or more of USAID-assistance in 2012 and are not defined as high-income by the World Bank, referred to as USAID-assisted countries; only USAID-assisted countries are included in regional and world averages. In South Asia, Bhutan and the Maldives did not receive \$2 million in USAID-assistance and are not strongly emphasized in the report. Although Afghanistan and Pakistan are considered part of South Asia and are included in regional averages, the Afghanistan and Pakistan Trends Report addresses them in greater depth, and they are only occasionally discussed in this report.

Economic Growth: Modest Quickening This Year, Higher Growth Rates Ahead

According to the World Economic Outlook (WEO) from the International Monetary Fund (IMF), average GDP growth for USAID-assisted countries in South Asia is projected to rise to 4.9 percent in 2014, up from 4.7 percent in 2013. Growth is forecast to rise slowly but steadily from 5.4 percent in 2015 to hit 6.0 percent in 2019, still not matching 2012's growth of 6.7 percent. Growth rates for individual countries in 2014 range from a high of 7.0 percent in Sri Lanka to a low of 3.1 percent in Pakistan. Sri Lanka's higher growth is driven by domestic demand, higher exports, and increased tourism in 2013. Tourist arrivals increased 16.4 percent in 2013, and hotel and restaurant sector showed 22.3 percent year-on-year growth. In 2014, the economy is expected to improve due to a better external environment, growing domestic consumption, and new investments.

India is forecast to have 5.4 percent GDP growth in 2014, which is higher than average for the region, but lower than its growth in the mid- and late-2000s. From 2015 through 2019, growth is forecast to be between 6.4 and 6.8 percent. India's economy has been sluggish due to deceleration in industry growth, services growth below 7 percent, continued weakness in advanced economies, and low consumption. Fiscal austerity, high inflation, and a weak currency will continue to discourage consumption. It remains to be seen if the change of leadership will improve the country's economy.

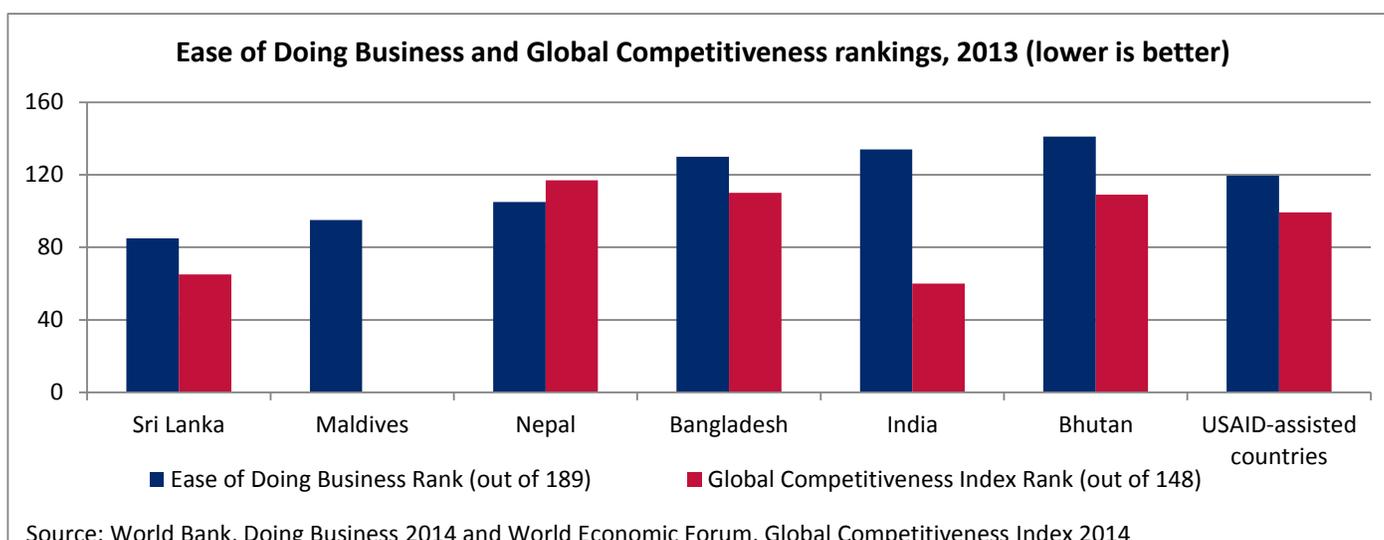


The IMF expects Bangladesh to also grow above the regional average, with growth of 6.0 percent in 2014 and 7.0 percent in 2019. Economic growth in Bangladesh depends in part on the political situation; unrest before the elections in January 2014 adversely impacted growth in 2013. Remittances from Saudi Arabia and the United Arab Emirates have fallen due to a crackdown on foreign workers and non-issuance of new permits to Bangladeshis. Growth was also slowed by lower export expansion, and Bangladesh’s poor business environment, including inadequate infrastructure, which hurts its growth potential. The Asian Development Bank (ADB) believes that infrastructure investment will be needed for any major boost in Bangladesh’s future growth rate.

Nepal and the Maldives are forecast to have slower growth, with neither country rising above five percent in the IMF’s projections. Nepal, the poorest country in South Asia, had slow growth in 2013 due to a drop in agriculture and a delayed budget. Growth is forecast to pick up slightly in 2014 thanks to a completed budget and political stability post-election, assuming a good Southwest monsoon (an annual seasonal wind with high precipitation). The Maldives grew 3.7 percent in 2013, an improvement over 0.9 percent growth in 2012, due to stronger tourism. As the global economy recovers, growth is forecast to increase, but remain under 5 percent, through 2019. Bhutan’s growth slowed to 5.0 percent in 2013 because of government policies that discouraged consumption in order to relieve pressure on its exchange rate and reserves balance. Growth should pick up as planned hydropower projects come on line later in the decade.

Business Environment and Competitiveness: Challenges Hinder Growth

One reason for slow economic growth in South Asia is the challenging business environment in many of the region’s countries. The recent election in India brought the issue to the forefront, as Modi’s successful campaign focused heavily on improving the Indian economy and making it more business-friendly. Currently, India ranks 134th out of 189 countries in the World Bank’s overall *Ease of Doing Business 2014* ranking. This is worse than Bangladesh (130th), Nepal (105th), and Sri Lanka (85th). Although it performs in the top quarter of countries for the Getting Credit and Protecting Investors subrankings, India performs in the worst quarter on four subrankings: Paying Taxes, Starting a Business, Dealing with Construction Permits, and Enforcing Contracts. Corruption, red tape, and a slow court system make investment difficult in India.



Despite its poor showing on the *Ease of Doing Business*, India performed better on a different measure, the World Economic Forum's *Global Competitiveness Index (GCI)*. The GCI is composed of twelve pillars, which are organized into three sub-indices. India performed better than the average for USAID-assisted countries on all except one pillar, Macroeconomic Environment. The *Global Competitiveness Report* indicates that India, the 60th most competitive country in the world, has been on a downward trend in the GCI rankings since 2009. Basic drivers of economic competitiveness, especially insufficient infrastructure, hinder India in the rankings. India also struggles with bribery and corruption, and low productivity due to poor health and education systems.

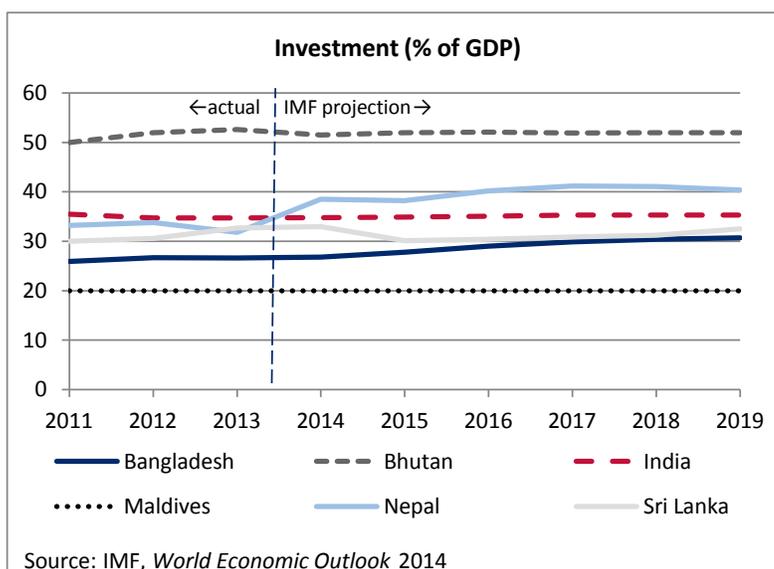
Bangladesh and Nepal perform below average on the GCI and its sub-indices, with Nepal performing especially poorly in the infrastructure pillar. Bangladesh and Nepal respectively rank 110th and 117th on the index, far below India. In the *Doing Business* index, Bangladesh improved two spots in the ranking in 2013, surpassing India to move from 132nd to 130th. It made it easier to start a business by automating registration and reducing time required for registration procedures. Nepal dropped slightly in the *Doing Business* ranking, falling from 103rd to 105th. Nepal made it easier to start a business by reducing time at the company registrar and creating a data link between agencies involved in the registration process, moving up 6 places in the subranking.

Sri Lanka made several reforms listed in the *Doing Business Report*, including making it easier to get construction permits and electricity, to file taxes, and to trade. Despite these positive changes, Sri Lanka slipped from 83rd to 85th in the overall ranking, falling in the subrankings for Ease of Registering Property, Resolving Insolvency, and Starting a Business. As other countries make reforms, countries can lose ground in comparison.

Like India, Sri Lanka performs better than average for USAID-assisted countries on the GCI and its three sub-indices, ranking 65th in the world. The only GCI pillars in which Sri Lanka performed below average for USAID-assisted countries are Labor Market Efficiency and Macroeconomic Environment.

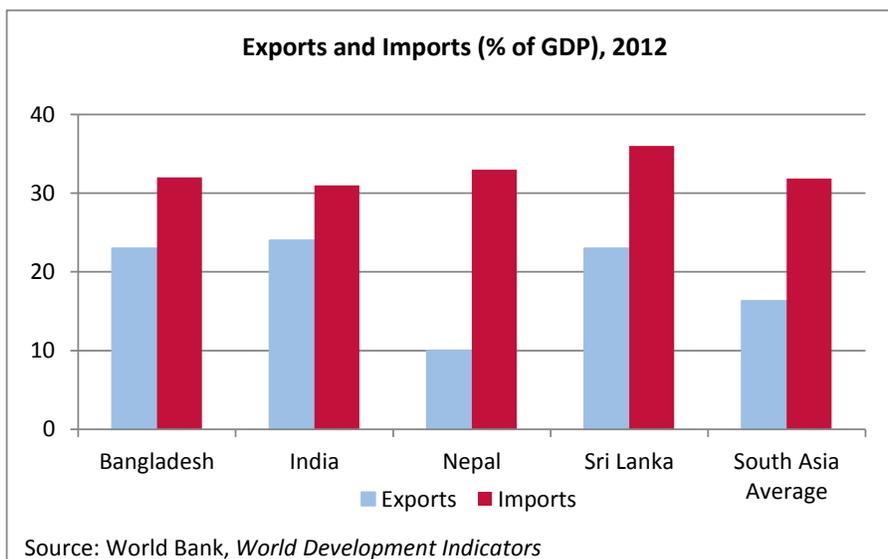
Investment and Trade: Growth in some economies, no change in others

Although investment is forecast to grow for some South Asian countries, the IMF expects investment levels in many of the region's economies to remain flat. Bhutan has the highest investment in the region as a share of GDP, at over 50 percent, due to continuing investments in hydropower projects. The high investment rates are forecast to continue, and the projects should create strong economic growth, especially later in the decade. Bangladesh invested 26.6 percent of GDP in 2013. According to the ADB, Bangladesh needs approximately 32–33 percent of GDP as investment as a percent of GDP to grow at a rate of 7–8 percent. The IMF projects that Bangladesh's investment should reach 31 percent of GDP in 2019. There is some question whether foreign investment will slow as countries will be cautious investing in the garment industry until safety and fire standards are improved, following a deadly fire in at a garment factory in 2013. Both Afghanistan and Pakistan register less than 20 per-



cent of GDP as investment.

Business Monitor International (BMI) expects India to have low investment and revised down its growth projections. However, it predicted a possible increase in capital spending because BJP won the elections. India's investment was second-highest in the region in 2013, at 35 percent; the IMF expects it to remain around that level through 2019. Sri Lanka is expected to have high infrastructure investment from the government, and investment is expected to remain largely steady as a percent of GDP.



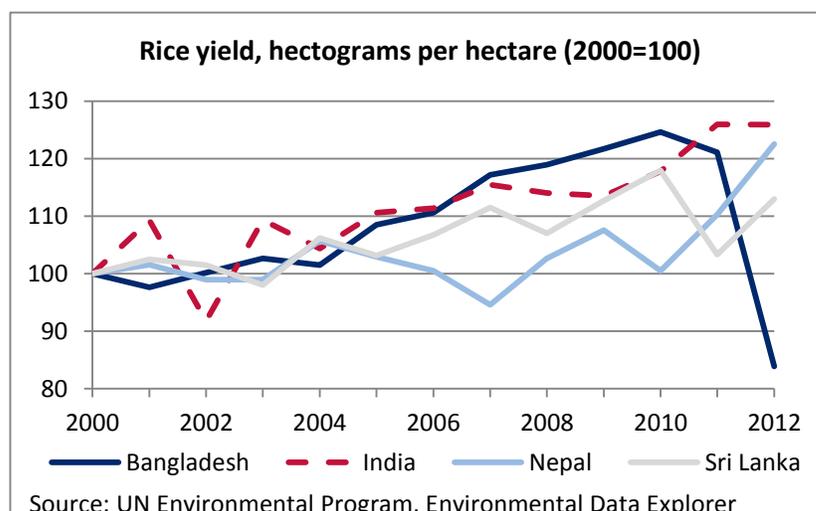
In the Maldives, both exports and imports (including services, which account for most exports) were over 100 percent of GDP in 2012. In Nepal, by contrast, trade was only 43 percent of GDP and exports only 10 percent. Bangladesh and India both had nearly a quarter of their GDP as exports in 2012, and in Bangladesh, trade volume is forecast to grow at high rates between now and 2019, with double-digit growth in exports. The ADB

states that Bangladesh is the least expensive garment producer in the region when comparing wages and labor productivity. A minimum wage increase and new safety standards may raise the average cost, but it will still be competitive with East Asian producers. Bhutan's exports are forecast to spike in 2018, registering over 25 percent growth, due to new hydropower plants. The IMF forecasts Sri Lanka's export growth to decline, dropping by nearly half from 8.9 percent in 2014 to 4.6 percent in 2019. After strong export growth in 2010 and 2011, India's export growth dropped from 8.9 percent in 2011 to 1.5 percent in 2012. Although it is recovering and is expected to increase as the economies of India's trading partners improve, it is not forecast to match the high growth in Bangladesh, instead staying at 8.1 percent from 2015 to 2019. India has chronic trade deficits, at 7 percent of GDP in 2012, and they may increase in the coming years, especially considering that India eased restrictions on gold imports in May 2014.

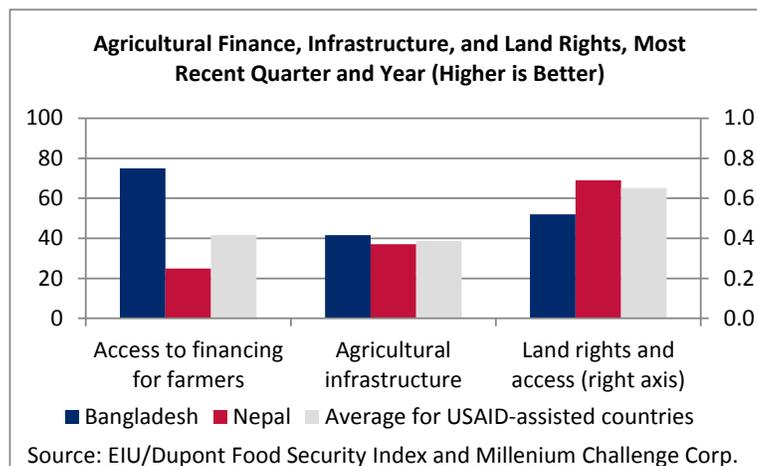
Agriculture: Favorable Weather, Tough Business Environment

South Asia is home to two Feed the Future countries, Bangladesh and Nepal, and its countries have large populations employed in the agricultural sector. Two-thirds of the population of India depends on farming for their livelihoods. Agriculture across the region is often inefficient and dependent on weather, particularly the annual monsoon. The region is also vulnerable to climate change, with low-lying areas, extensive coastlines, and vulnerability to floods. The sources used for predictions in this report (the IMF, ADB, and BMI) expected the 2014 monsoon to be favorable, but as the monsoon season is underway, the levels of rainfall have been erratic and lower than average in much of the region. As of the writing of this report, the monsoon was later than usual, and India was expected to receive only 87 percent of the rainfall of a normal year.

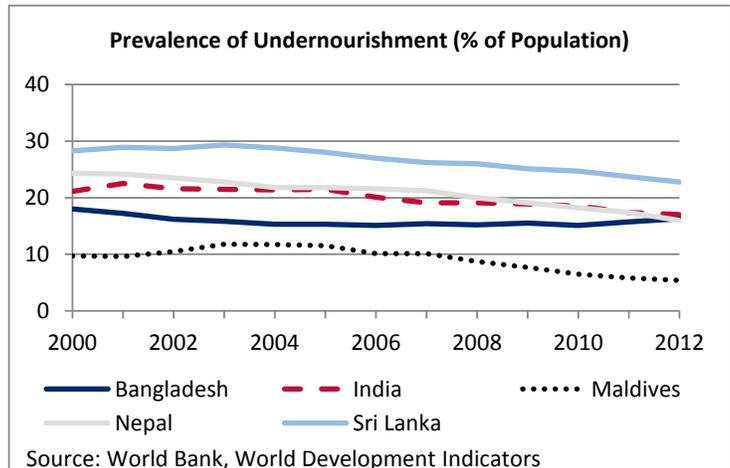
Yields of rice, the staple crop of much of the region, have generally been rising since 2000, though the increase has been smaller in South Asia than in all USAID-assisted countries. Bangladesh saw a steep decline in yields in 2012, following a slight decline in 2011; previously, it outperformed its neighbors in actual yields (please note that yields in the graph have been indexed so that yields in 2000 have a value of 100). Favorable weather could cause Bangladesh's agricultural growth to rebound to 3.0 percent in 2014 and 3.5 percent in 2015, according to the ADB. Agricultural growth is forecast at 3.5 percent in 2015. In India, the ADB expected a strong monsoon in 2014 to lead to agricultural growth of 3.0 percent, following a good season in 2013 with 4.6 percent growth. In Nepal, agricultural growth was down in 2013, but could pick up if there is a good monsoon season in 2014. Historically, Nepal had fairly low rice yields for the region, lagging behind Bangladesh (until Bangladesh's steep drop in 2012), India, and Sri Lanka in actual yields. Nepal and Bangladesh have consistently imported more food than they exported, in contrast with India and Sri Lanka. Favorable weather in 2013 contributed to agricultural growth of 4.7 percent in Sri Lanka.



Challenges with the overall business environment discussed previously also affect farmers and the agricultural sector. Agricultural infrastructure is poor in many USAID-assisted economies, rated an average of 39, far below a possible 100, on the EIU and Dupont's Global Food Security Index (GFSI). The measure includes the existence of adequate crop storage facilities; the extent and quality of road infrastructure; and the quality of port infrastructure. Nepal, however, performs even more poorly than the USAID-assisted average on the agricultural infrastructure rating, and Bangladesh fares only slightly better, reflecting their poor scores on the Global Competitiveness Index's infrastructure pillar. The GFSI also includes a score assessing access to finance for farmers. Bangladesh performs very well (75 out of 100) on this measure and Nepal performs poorly (25 out of 100). However, Nepal outperforms Bangladesh on the Access to Credit subscore on the *Doing Business Index* (where both countries perform above the global median) and the Financial Market Development pillar of the GCI (where Nepal performs above average for USAID-assisted countries, and Bangladesh below), indicating that Nepal struggles to extend credit to farmers, as opposed to other sectors. On a land rights score reported by the Millennium Challenge Corporation, Nepal performs slightly better than average and Bangladesh slightly worse. A similar indicator from the *Doing Business Index* is the Registering Property subranking, on which Bangladesh performs very poorly, at 177 out of 189, and Nepal performs very well, at 24 out of 189, a ranking that does not seem to be entirely reflected in their score for land rights.



South Asia has seen a decrease in malnourishment. Since 2000, malnourishment has decreased in all countries in the region for which data are available. However, Bangladesh’s previous downward trend has been reversed since 2011, when crop yields began to decline and malnourishment began to increase. Despite the slight increase, Bangladesh still has lower rates of undernourishment than India or Sri Lanka, where more than one in five residents are undernourished, despite both countries being net food exporters.



Additional Information

For questions or more information, please contact the author, Katherine Shanahan, at kshanahan@usaid.gov.

For country-specific data and additional information about the countries covered in this report, please visit the ESDB Country Portal at <https://eads.usaid.gov/esdb/data/country/index.cfm>.