

## **“Asia: Sailing in Turbulent Times”**

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**Asian economies face choppy waters, including headwinds from an uncertain global environment.** The global recovery has been weaker than expected, on top of which world trade has been sluggish and financial conditions have been volatile. The rise of China as an economic superpower has also created challenges, as China’s necessary rebalancing from manufacturing towards services and from investment to a consumption-driven economy—critical for both China’s and global growth over the medium term—remains challenging. At the same time, Asia remains the major engine of the global economy, providing nearly two-thirds of global growth. The region also enjoys policy buffers such as current account surpluses and high reserve levels, and is likely to benefit from further economic integration and regional and multilateral trade agreements such as the Trans-Pacific Partnership.

**Asia’s growth is slowing slightly, in line with the rest of the global economy.** According to the latest IMF Asia-Pacific *Regional Economic Outlook* ([www.imf.org/delhi](http://www.imf.org/delhi)), real GDP growth for the region is forecast at 5.3 percent in both 2016 and 2017, slightly lower than in 2015. While external demand for Asian output is relatively weak, domestic demand—particularly consumption—is expected to remain resilient across most of the region. The relative strength of domestic demand is due to generally low unemployment, falling

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commodity prices (which are a boon to oil and commodity importers), economic stimulus in some countries, and ongoing secular trends, including steadily rising disposable income.

**The moderation in Asia's growth nevertheless masks important differences within the region.** *India* is expected to remain the fastest-growing large economy in the world, with GDP expanding by 7.5 percent in 2016-17, underpinned by private consumption which has benefited from lower energy prices and higher real incomes. Positive policy actions, improved confidence, and reduced external vulnerabilities, have solidified the Indian recovery, while inflation has declined sharply. In *China*, GDP growth is expected to moderate to 6.5 percent this year and 6.2 percent in 2017, reflecting ongoing rebalancing and other structural reforms. In *Japan*, GDP growth is projected to remain at 0.5 percent in 2016, slowing to -0.1 percent in 2017 as the widely anticipated consumption tax rate hike kicks in (though this forecast does not incorporate likely offsetting measures to support activity). *Indonesia*, which is exposed to commodities, is expected to benefit from a large infrastructure push.

**Despite a robust outlook, downside risks continue to dominate the economic landscape.** Global growth could slow by more than expected or financial conditions could tighten suddenly. As many economies in the region have seen debt levels rise rapidly over the last decade, a combination of slower growth and higher borrowing costs could tip some corporates and households over the edge and further constrain growth. In India, elevated corporate vulnerabilities and weakened bank balance sheets, especially in public sector banks, pose headwinds for economic growth.

**In addition, regional growth is increasingly dependent on China.** While rebalancing in China is needed to ensure durable and resilient growth over the longer term, the short-term transition is likely to be bumpy and the impact on countries and markets will vary. Countries exporting goods that support Chinese investment and construction (producers of metals, for example) would be adversely affected, while exporters of consumer goods to China (or countries that are destinations for rapidly-growing Chinese tourism) could benefit. In addition, China's move to higher value-added production will provide opportunities for lower-income Asian countries, particularly in labor-intensive sectors such as apparel, footwear, furniture, and plastic toys. Given limited trade linkages, the slower growth in China should have only modest adverse spillovers to India. However, continued anemic growth of India's other trading partners could weaken the sustainability of India's recovery, and intensified global financial market volatility may also be disruptive.

**A wide range of policies can be used to harness the region's potential.** Policymakers should deploy macroeconomic policies to boost demand if needed and fiscal space permits. Structural reforms will be key to bolstering potential growth and strengthening the region's resilience to global shocks. Policy reforms should also tackle long-standing challenges, such as rising inequality, to make growth more inclusive. These reforms should aim to promote equality of opportunities by broadening access to education and health, and promoting financial and gender inclusion. In addition, addressing long-standing supply bottlenecks, particularly in the mining and power sectors, labor and product market reforms, agricultural

sector reforms, and improving the business climate are all needed to improve medium-term growth prospects and boost employment in India.