



CHAPTER 1

A PRECARIOUS PATH: Building Resilience amid Uncertainty

Chapter 1. A Precarious Path: Building Resilience amid Uncertainty

Growth prospects are dimming across South Asia. Tariffs, policy uncertainty, and financial market volatility have increased substantially. After an unexpectedly weak outturn of 6.0 percent in 2024, growth in South Asia is expected to soften further to 5.8 percent in 2025—0.4 percentage point below October forecasts—before ticking up to 6.1 percent in 2026. The region’s economies face heightened downside risks, including from a highly uncertain global landscape. After a decade of shocks, South Asian economies have limited capacity to cushion new ones. In particular, South Asia’s high debt remains a source of vulnerability to rising borrowing costs or declining funding inflows from private or official sources. The more challenging global environment, combined with domestic fragilities, could be navigated more easily if the region tackled areas of particularly large inefficiency or vulnerability. Domestic revenue mobilization could lessen South Asia’s vulnerability to fiscal and external pressures. The region’s unproductive agriculture sectors could benefit from more efficient pricing of inputs, as well as broader access to modern technologies and practices.

Introduction

Global growth is showing signs of widespread weakness in 2025. Tariffs, policy uncertainty, and financial market strains have increased substantially, and are weighing on activity (figure 1.1).

In South Asia too, growth prospects are dimming. Growth outcomes for 2024 have disappointed and forecasts for 2025 have been downgraded for most countries in the region. Fiscal consolidation is expected to continue, especially in countries implementing programs supported by the International Monetary Fund (IMF). South Asia’s growth was unexpectedly weak at 6.0 percent in 2024, and is expected to weaken further to 5.8 percent in 2025—0.4 percentage point below October forecasts—before ticking up to 6.1 percent in 2026.

After several years of synchronous decline, inflation dynamics have started to diverge across countries. Inflation rebounded in many countries in late 2024 and early 2025, and surveys point to increasing concerns about further acceleration. In South Asia, inflation differences across countries have widened, with Sri Lanka tipping into deflation and Bangladesh struggling with persistently above-target inflation.

Global financial markets are increasingly affected by heightened policy uncertainty. Rising tariffs, shifting government priorities, and conflicting signals about the state of the economy have led to significant volatility in exchange rates, stock market valuations, and bond yields. A severe global downturn has become a possibility.

Financial market movements in South Asia have been more muted than elsewhere, in part because of more limited direct exposures to the global economy and central bank interventions. Nonetheless, South Asian economies face heightened downside risks and, after a decade of shocks, their ability to cushion new shocks is limited. Large government debt stocks and below-average international reserves depress the credit ratings of South Asian countries and render their economies vulnerable to financial stress. Half the countries in the region are undertaking reforms with IMF support. Failure to implement these reforms as planned could delay IMF financing, reignite capital outflows, and add to fiscal pressures. The region would also suffer slower growth if its exporters faced higher tariffs abroad—although in the short term the slowdown would be less than in regions that are more open to foreign trade.

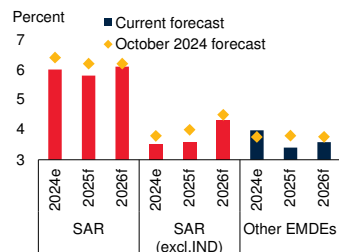
The more challenging global environment, against the backdrop of domestic fragilities, could be navigated more easily if the region tackled some of the areas of particularly large inefficiency or vulnerability. Low revenues are at the root of South Asian countries’ fiscal fragilities; they could be increased by streamlining tax systems, better

Note: This chapter was prepared by Patrick Kirby.

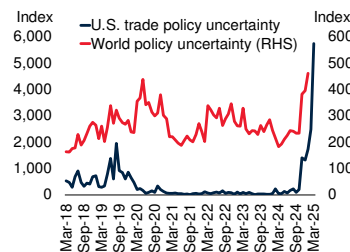
FIGURE 1.1 Overview

After a disappointing 2024, growth in South Asia is expected to weaken further in 2025 and tick up only slightly in 2026. The outlook is subject to downside risks, including from a potential global recession. The synchronous decline in global inflation has ended. Higher borrowing costs would add to fiscal pressures, especially in South Asia where credit ratings are lower than in other EMDEs. Revenue mobilization will be critical to restore and preserve fiscal sustainability. A more dynamic non-agriculture sector could help raise labor productivity in agriculture, which is currently low by international standards.

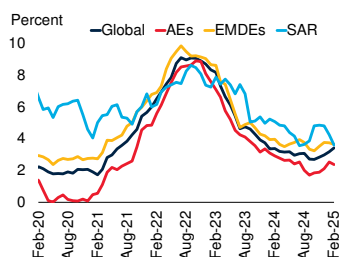
A. Output growth



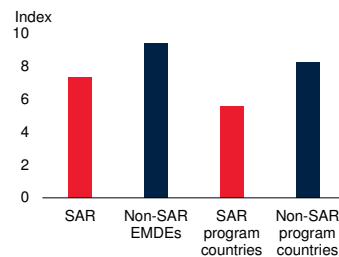
B. Policy uncertainty



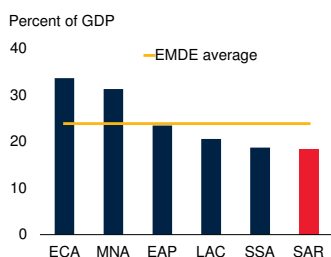
C. Headline CPI inflation



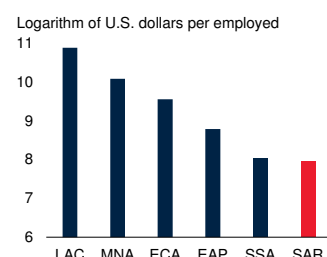
D. EMDE credit ratings



E. General government revenues, 2019–23



F. Agricultural value added per worker, 2020s average



Sources: Baker, Bloom, and Davis (2016); Eurostat; Fitch Ratings; FRED (database); Haver Analytics; Moody's Ratings; S&P Global; UNU-WIDER; World Bank Macro Poverty Outlook; World Bank Fiscal Survey (database); World Bank.

Note: AEs = advanced economies; EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging markets and developing economies; IND = India; LAC = Latin America and the Caribbean; MNA = Middle East and North Africa; SAR = South Asia; SSA = Sub-Saharan Africa.

A. Real GDP-weighted (at 2010–19 average prices and market exchange rates) average real GDP growth rates for 8 South Asian economies and 139 other EMDEs. October 2024 forecasts exclude Afghanistan.

B. Last observation is March 2025 for U.S. trade policy uncertainty, and January 2025 for world policy uncertainty.

C. Median year-on-year inflation for each aggregate. Last observation is April 15, 2025.

D. Credit ratings from S&P, Moody's, and Fitch were mapped to a unified 1–22 scale (1 = lowest, 22 = highest), and a simple average was computed for each country. The sample includes South Asian countries (Bangladesh, India, Maldives, Pakistan, Sri Lanka), South Asian program countries (Bangladesh, Pakistan, Sri Lanka), 96 non-SAR EMDEs, and 40 non-SAR program countries. Last observation is April 15, 2025.

E. Total revenue excludes grants. EMDE average is nominal GDP-weighted average of 140 EMDEs. Regions are nominal GDP-weighted average of country group.

F. Annual averages from 2020 to latest available data. Sample includes 14 economies in EAP, 22 in ECA, 24 in LAC, 17 in MNA, 7 in SAR, and 38 in SSA. Bars show logarithm of real GDP-weighted ratio of real GDP in agriculture (at 2010–19 average prices and market exchange rates) relative to number of people employed in agriculture.

enforcing collection, and facilitating compliance. South Asia's agriculture sector, which accounts for 16 percent of GDP but employs 42 percent of the workforce, suffers from particularly low labor productivity. A more efficient agriculture sector, combined with a more buoyant non-agriculture sector, could help shift workers, private finance, and government resources into more productive and climate-resilient activities.

Global developments and outlook

The U.S. administration announced new tariffs of 145 percent on imports from China, and 10 percent on most imports from the rest of the world (figure 1.2). Effective U.S. tariffs have increased to a level not seen in a century, and further tariff increases are a possibility. Some trading partners have responded with tariffs of their own on U.S. exports. In particular, China has raised tariffs on imports from the United States to 125 percent.

Policy uncertainty has soared to unprecedented levels. The global economy grew steadily at 2.7 percent in 2023 and 2024, but consensus forecasts point to a sharp deceleration in global growth in 2025. Many major economies had already been expected to slow at the beginning of this year, but the degree of anticipated deceleration has increased significantly in recent weeks, according to most forecasters. Business and consumer confidence have fallen (figure 1.3).

Global financial markets have been roiled by volatility. Stock market indexes have fallen sharply around the world, and measures of volatility have spiked, particularly in the United States. Many categories of borrowing cost have increased, with a notable uptick in yields on U.S. treasuries. Risk spreads on high yield debt, including both below investment-grade corporates and sovereigns, were generally narrow at the beginning of the year, but have expanded significantly in recent weeks. A growing share of debt has become distressed, and a growing share of borrowers have been locked out of markets by prohibitive lending rates.

The U.S. dollar and many EMDE currencies have depreciated, while other advanced-economy currencies have generally appreciated. This is

consistent with continued weakness in inflows of portfolio and foreign direct investment into EMDEs (figure 1.4).

Prior to the introduction of new tariffs in April, global inflation had leveled off, and national inflation was at or below target in about 60 percent of inflation-targeting economies (figure 1.5). Newly introduced tariffs will increase the price of many imported goods, however, and add to concerns about inflation that are increasingly apparent in surveys and financial market data. Inflation concerns are rising despite a sharp decline in oil prices; the Brent price stood at about US\$75/bbl at the beginning of the year, but has fallen more recently.

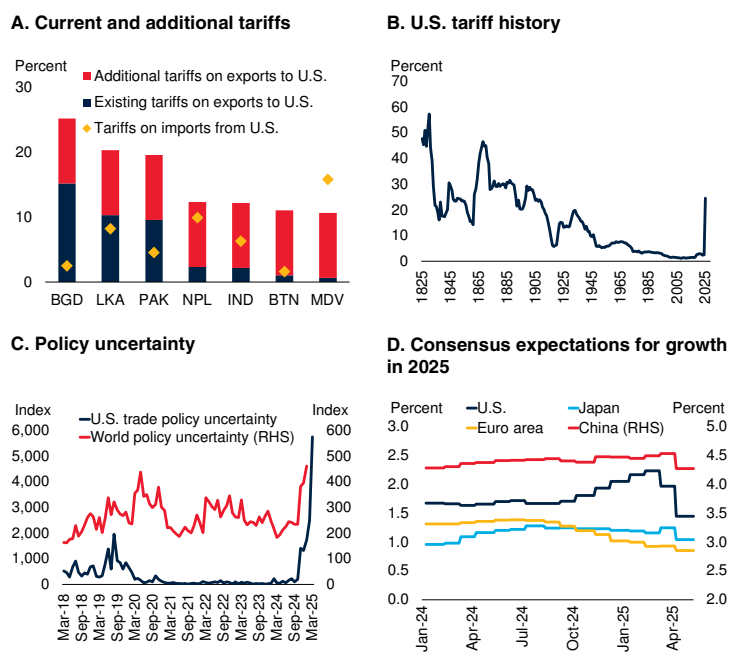
Central banks had already slowed their pace of monetary policy easing, and now face an increasingly challenging environment of rising prices and slowing growth. In the United States, the Federal Reserve cut its policy rate by a full percentage point between September and December 2024, but it has since kept it unchanged. The pace of future cuts is expected to be gradual, with policy rates staying well above their pre-pandemic levels. In the euro area, similarly, the pace of policy cuts by the European Central Bank is expected to slow sharply.

In the *United States*, activity at the beginning of the year appeared robust, but more recent indicators point to a sharp slowdown in economic activity as a result of tariffs, policy uncertainty, and the depletion of consumer savings. Some forecasters anticipate the economy will experience a recession (defined as two consecutive quarters of negative growth) in 2025. Consumer price inflation stood at 2.4 percent in March, slightly above the Federal Reserve's 2 percent target, prior to the introduction of new tariffs in April.

Growth in the *euro area* has been anemic, and consensus forecasts are for growth of around 1 percent in 2025 and 2026. Consumption and exports grew by about 1 percent in 2024, while investment contracted sharply. Consumer confidence has remained weak, despite growth in real incomes since the October edition of this report. In the area's largest economy, Germany, the manufacturing sector has contracted steadily since mid-2023 in the face of weak domestic

FIGURE 1.2 Global economic activity

Tariffs have been increased sharply. Policy uncertainty has increased to historic highs. Forecasts for growth in several major economies in 2025 have been downgraded.



Sources: Baker, Bloom, and Davis (2016); Budget Lab at Yale; CEIC; Consensus Economics; Haver Analytics; U.S. Bureau of Economic Analysis; WTO Tariff Analysis Facility; World Bank.
Note: BGD = Bangladesh; BTN = Bhutan; IND = India; LKA = Sri Lanka; NPL = Nepal; MDV = Maldives; PAK = Pakistan; RHS = right scale.
A. "Existing tariffs" and "Tariffs on imports from U.S." refer to effectively applied tariffs in 2023. "Additional tariffs" are the 10 percent tariffs imposed in April.
B. 2025 value is average effective tariff rate on April 15, 2025, estimated by the Budget Lab at Yale.
C. Last observation is March 2025 for U.S. trade policy uncertainty, and January 2025 for world policy uncertainty.
D. Figure shows the evolution of GDP growth forecasts for 2025 from Consensus Economics. The April value for China is the moving average of latest changed forecasts. Last observation is on April 15, 2025.

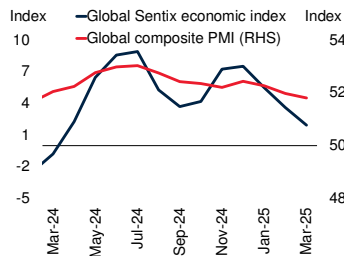
demand, increased competition from EMDE exporters, and high energy prices.

In *China*, domestic demand has been dampened by persistent weakness in the property sector. Mortgage lending has remained stagnant, and property prices had been declining for several years before a recent rebound. Consumer price inflation has remained well below the official target of 3 percent a year. The government's announcement of a stimulus package in September was followed by signs of recovery. Prior to the recent increase in tariffs, exports had been growing rapidly, largely offsetting weakness in domestic demand, so that output growth reached 5 percent in 2024, only slightly less than the 5.2 percent increase in 2023. For 2025–26, growth is expected to slow further as global trade tensions add to the continuing weakness in domestic demand.

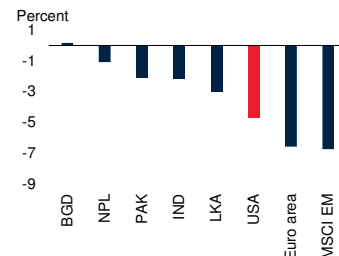
FIGURE 1.3 Global financial conditions

Falling global confidence has coincided with falling stock market valuations in many countries, elevated volatility, and significant moves in exchange rates.

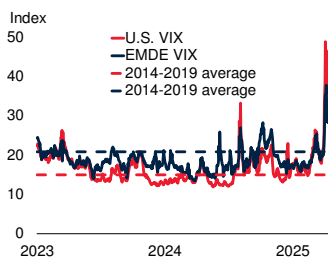
A. Global composite PMI



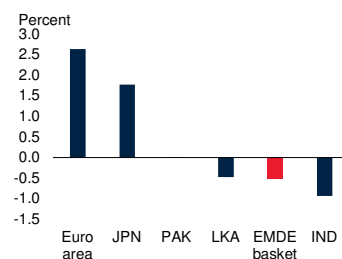
B. Change in stock market valuations since early April



C. Financial market volatility



D. Change in currency valuations relative to U.S. dollar since early April



Sources: CEIC; Haver Analytics; Morgan Stanley; Trading Economics; World Bank.

Note: AEs = advanced economies; BGD = Bangladesh; ECB = European Central Bank; EMDEs = emerging market and developing economies; EUR = Euro; EMDEs = emerging market and developing economies; IND = India; JPY = Japanese Yen; LKA = Sri Lanka; MSCI EM = Morgan Stanley Capital International Emerging Markets Index; NPL = Nepal; PAK = Pakistan; PMI = purchasing managers' index; VIX = Chicago Board Options Exchange volatility index.

A. Sentix economic index and global composite PMI series show 3-month moving averages; for PMI, readings above (below) 50 indicate expansion (contraction). Last observation is April 15, 2025.

B. Figure shows the changes of stock market price indexes since April 2, 2025. Latest data for Bangladesh and Nepal is April 10, 2025, for India and Sri Lanka is April 11, 2025 and all others are April 14, 2025. "USA" is the S&P 500 (1941-43=10), "Euro area" is the S&P Euro (Dec-31-97=1000), "PAK" is the KSE 100 (Nov-91=1000), "BGD" is the DSEX (Jan-17-08=2951.91), "IND" is the NSE Nifty (Nov-3-95=1000), "NPL" is the NEPSE (Feb-12-94=100), and "LKA" is the ASPI (Jan-1-85=100). The last observation is April 15, 2025.

C. The VIX captures 30-day volatility of the S&P500. The EMDE VIX is 30-day volatility of returns on the MSCI EEM index. Last data point is from April 14, 2025.

D. Figure shows the change in value of currencies relative to the U.S. dollar since April 3, 2025. The last observation is from April 11, 2025 for all currencies.

Growth in other emerging market and developing economies (EMDEs) has generally been healthy. Solid consumption and investment activity have been supported by continued monetary easing, growing real incomes, and strong industrial activity. High-frequency indicators, however, point to a deceleration in early 2025, especially in services activity.

Developments in South Asia

Financial conditions have tightened in South Asia, as in other parts of the world. Stock market booms in *Sri Lanka* and *India* ended and equity valuations in the rest of the region remained largely flat. As in other EMDEs, net foreign direct investment and portfolio inflows into South Asia have weakened since mid-2024. Inflows of remittances, however, have remained robust.

Overall, the South Asian economy grew by 6.0 percent in 2024, 0.4 percentage points below the rate projected in the October edition of this report. Growth outcomes fell short of forecasts in most countries, particularly in Bangladesh as a result of anti-government protests and the abrupt change in government in August (figure 1.6).

South Asia remained the fastest-growing EMDE region, but the gap with other EMDEs has narrowed as the region's growth has decelerated. The region's relative strength reflected above-average policy support in 2024, as macroeconomic stabilization allowed monetary policy easing (in Pakistan) and fiscal deficits widened in most countries. In most of South Asia, as in the median EMDE outside the region, fiscal deficits and monetary policy rates were well above pre-pandemic (2010–19) averages.

The synchronous rise and fall of global inflation during the pandemic and the post-pandemic recovery has given way to widely divergent price dynamics, including in South Asia. Sri Lanka has tipped into deflation while in Bangladesh inflation is persistently above target. The divergence of inflation across the region has been accentuated by idiosyncratic movements in food inflation, with food prices falling in Afghanistan, Pakistan and Sri Lanka, and rising elsewhere.

Meanwhile, after several years of balance-of-payments pressures, current account deficits across the region (except in Maldives) have narrowed or stabilized, reflecting robust remittance inflows, slowing import growth, and a long-awaited rebound in tourism. These developments, combined with limited exposure to the U.S. economy and, in some cases, exchange rate management, have resulted in smaller movements of most South Asian currencies against the U.S. dollar than those of other EMDEs.

Country developments

After two years of sharp contraction, *Afghanistan's* economy grew by 2.3 percent in FY23/24 and an estimated 2.5 percent in FY24/25. Growth was driven by agriculture, mining, construction and commerce. Modest gains in private consumption and real estate investment contributed to growth; however, rising imports widened the trade deficit, increasing external vulnerabilities. The recovery in activity has been accompanied by the first signs of positive inflation after two years of falling prices.

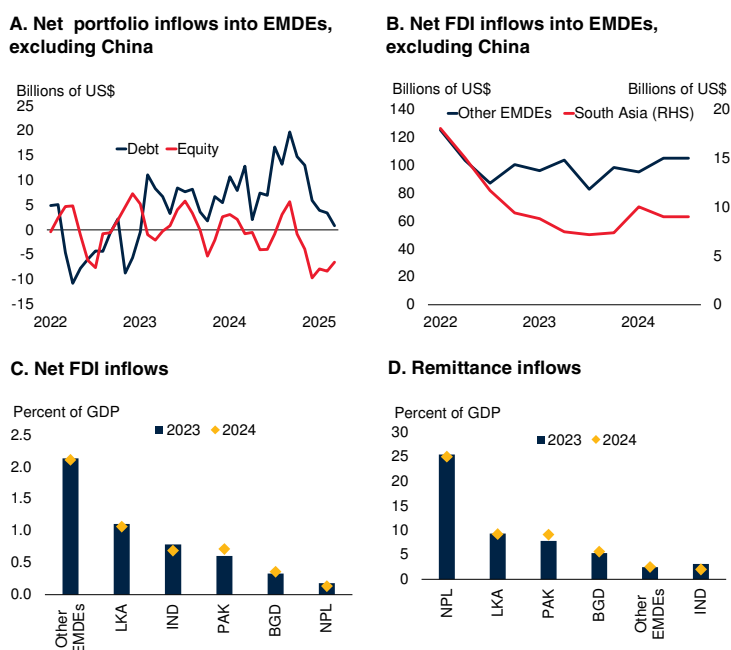
In *Bangladesh*, real GDP growth moderated to 4.2 percent in FY23/24 from 5.8 percent in FY22/23, primarily driven by a sharp decline in exports. Supply chain disruptions, combined with currency depreciation and rising domestic energy prices, added to inflation pressures in 2024. Consumer price inflation peaked at 11.7 percent in July and remained elevated at 9.3 percent in February 2025. The current account balance has improved as a result of rising exports and strong remittance inflows, which have increasingly been channeled through the formal financial system as the curb market premium has narrowed.

As a result of persistent inflationary pressures, Bangladesh's central bank has continued tightening monetary policy when other countries have been lowering policy rates. Since the tightening phase began in May 2022, the policy rate has been increased by 5.25 percentage points to 10 percent. Monetary policy transmission, however, is impaired by financial system weaknesses. Non-performing loans, which are concentrated in state-owned banks, have risen significantly in recent years, reaching 17 percent of all loans in September. The government is providing occasional liquidity support to some crisis-hit banks. Meanwhile, the transition from a managed to a fully flexible exchange rate has been delayed.

In *Bhutan*, the economy grew by 4.9 percent in FY23/24, about the same as in FY22/23. Services sector growth was broad-based, with strong rebounds in finance and tourism—supported by the reopening of borders following the COVID-19 pandemic. But agriculture yields grew modestly and hydropower exports declined because of growing domestic electricity consumption by energy-intensive cryptocurrency mining operations. Robust

FIGURE 1.4 Capital flows

The slowdown in capital flows to EMDEs, including to South Asia, since mid-2024 has continued.



Sources: Haver Analytics; IIF Portfolio Flow Tracker; IMF Balance of Payments and International Investment Position Statistics; World Bank.

Note: BGD = Bangladesh; BTN = Bhutan; EMDEs = emerging market and developing economies; FDI = foreign direct investment; IND = India; LKA = Sri Lanka; NPL = Nepal; MDV = Maldives; PAK = Pakistan.

A. Three-month rolling average of net inflows of debt and equity into up to 23 EMDEs. Data available for 3 South Asian countries (India, Pakistan, Sri Lanka). Last available data is for March 2025.

B. "Other EMDEs" includes 78 economies and excludes China. Last available data is for 2024Q3.

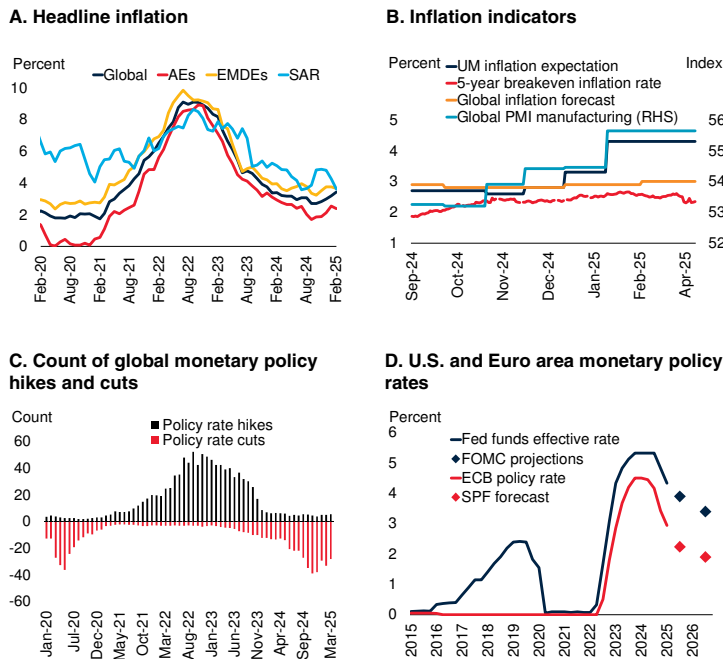
C-D. "Other EMDEs" includes 103 economies in 2023 and 72 economies in 2024. 2024 data are estimated based on available quarterly data for FDI, remittances, and GDP.

growth momentum continued in the early part of FY24/25, boosted by the removal of policy measures that had previously been implemented to support the balance of payments (such as a moratorium on the import of vehicles and a ban on construction loans). Inflation fell from 5.0 percent in early 2024 to 3.1 percent in January 2025, in part due to slowing non-food inflation. The current account deficit has remained elevated, at an estimated 17.6 percent of GDP in FY24/25. Nevertheless, robust growth in remittances increased gross international reserves to the equivalent of just under 5 months of imports in June 2024.

In *India*, growth slowed from 9.2 percent in FY23/24 to an estimated 6.5 percent in FY24/25—the slowest pace in four years, although broadly in line with the economy's long-term average. The economy was unexpectedly weak

FIGURE 1.5 Inflation and monetary policy

The synchronous decline in inflation around the world has ended, and inflation expectations in some countries have increased. Central banks are generally still easing policy, but many have paused or slowed their rate cuts.



Sources: Board of Governors of the Federal Reserve System; CEIC; Consensus Forecast; ECB Survey of Monetary Analysts (SMA); Haver Analytics; World Bank.

Note: AEs = advanced economies; BGD = Bangladesh; BTN = Bhutan; ECB = European Central Bank; EMDEs = emerging market and developing economies; IND = India; LKA = Sri Lanka; FOMC = Federal Open Market Committee; NPL = Nepal; MDV = Maldives; PAK = Pakistan; PMI = purchasing manager's index; SAR = South Asia.

A. Median year-on-year inflation for each aggregate. Last observation is April 15, 2025.

B. The chart shows three indicators of inflation expectations. These are the University of Michigan's inflation expectation ("UM inflation expectation"), which is the median expected price change over the next 12 months based on consumer surveys; the Federal Reserve Bank of St. Louis's breakeven inflation rate, which is a measure of expected inflation derived from 5-year Treasury constant maturity securities and 5-year Treasury inflation-indexed constant maturity securities; and the evolution of global Consensus Forecast consumer prices for 2025. We also show the global manufacturing new input prices Purchasing Managers' Index which is a survey-based economic indicator of the manufacturing sector. Values above 50 mean improving economic conditions.

C. 3-month average count of monetary hikes (above X axis) and cuts (below X axis) for global 107 economies, the last available data is from March 2025.

D. "SPF" is the ECB's Survey of Professional Forecasters. Last data points for ECB and Fed policy rates are from the first quarter of 2025. FOMC projections are those of the March 2025 meeting.

around the middle of 2024 but regained its footing by the end of the year. Manufacturing growth was sluggish and public investment growth fell short of budget projections. Consumption growth accelerated thanks to robust employment growth and increasing real wages, particularly in rural areas. Declining food price inflation helped lower headline inflation to 3.6 percent in February 2025, close to the middle of the Reserve Bank of India's 2–6 percent target range and substantially below the recent peak of 6.2 percent in October 2024. The current account deficit has narrowed to about 1 percent of GDP. Moderating inflation and limited external financing needs allowed the

Reserve Bank to support domestic demand by cutting its policy rate by 25 basis points in February—its first policy cut in almost five years. The Indian rupee's value in terms of the U.S. dollar held steady between mid-2022 and end-2024, partly supported by foreign exchange market intervention by the central bank. It has fallen by about 2 percent so far this year, more than the average depreciation of the currencies of EMDEs with flexible exchange rates.

India's equity markets have grown rapidly in recent years, in terms of both listings and valuations, and have attracted significant, although volatile, net inflows. In 2024, India led the world in the number of initial public offerings (IPOs) and was second only to the United States in the value of new listings. Equity derivatives markets have grown particularly quickly, prompting interventions from regulators concerned about investor protection. Since peaking late last year, however, stock market valuations have undergone a correction. For now, this has not had broader ripple effects, but the decline in equity prices could dampen private consumption or investment over the medium term.

In *Maldives*, tourist arrivals remained strong throughout 2024, and annual GDP growth increased to an estimated 5.5 percent. However, despite strong tourism revenues, the estimated current account deficit remained elevated at about 20 percent of GDP in 2024, and the economy has been subjected to severe financial pressures.

Rising external debt service obligations have led to a sharp decline in official reserves to critically low levels. Last October, a US\$400 million currency swap agreement with the Reserve Bank of India lifted gross official reserves to US\$614.6 million, equivalent to only 1.4 months of imports. Usable reserves (total reserves net of predetermined short-term drains such as debt payments) are even lower, at a precarious level. The fiscal deficit is forecast to increase further to 13 percent of GDP in 2024. Spending on subsidies remained high, which has thus far helped keep inflation low, at 1.4 percent in 2024. Several ratings agencies downgraded Maldives' sovereign credit rating in 2024, citing rising liquidity concerns. Although some pandemic measures, such as monetization of the government deficit, have been phased out, the

exposure of the domestic financial sector to sovereign and state-owned enterprise debt continued to increase in 2024: more than one-third of bank assets are sovereign or state-owned enterprise debt.

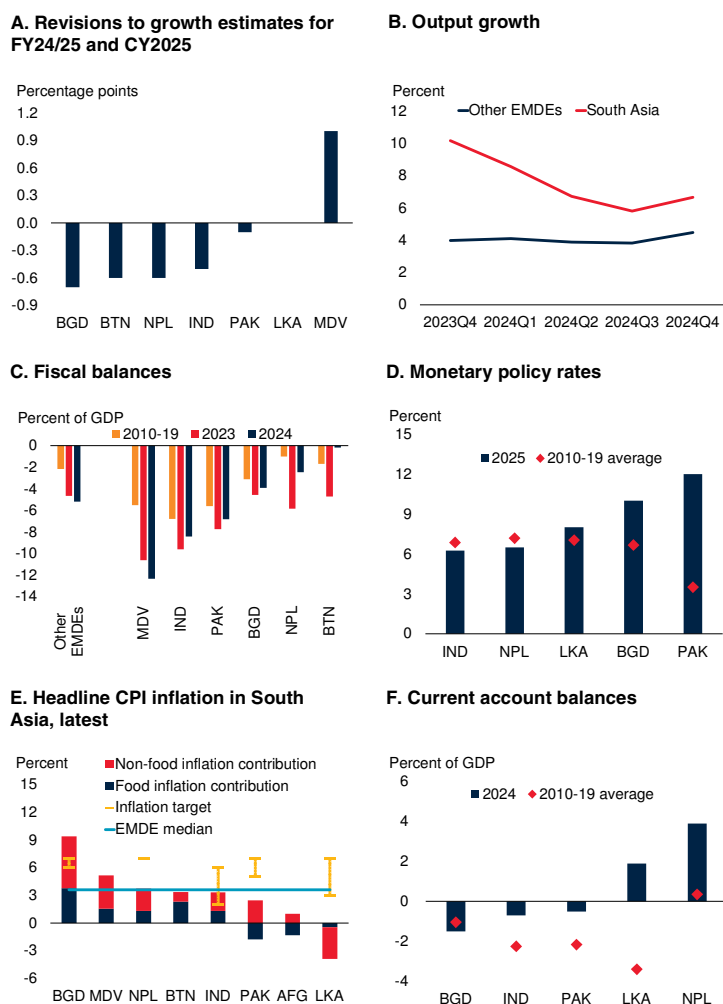
In *Nepal*, GDP growth accelerated to 3.9 percent in FY23/24 from 2.0 percent in FY22/23. The strengthening of growth was driven mainly by increased hydroelectric capacity and the effect of a favorable monsoon on paddy production. This was partially offset by weakening activity in construction and financial services. A sharp decline in non-food and services inflation helped lower headline inflation to about 5 percent in the second half of 2024.

Meanwhile, robust remittance inflows led to a sharp turnaround in the current account balance, from a deficit of 12.5 percent of GDP in FY22/23 to a surplus of 3.9 percent of GDP in FY23/24—the first surplus in eight years. This helped increase official foreign reserves to the equivalent of more than 14 months of imports. The country's IMF program is on track to be completed in 2025.

In *Pakistan*, GDP grew by 2.5 percent in FY23/24, after a small contraction in FY22/23. Robust remittance inflows supported private consumption, but private investment growth continued to be weak, dampened by double-digit real interest rates and political uncertainty. On favorable weather conditions, agricultural growth reached a 19-year high while industrial activity contracted and services growth remained muted. Weak growth has carried over to first half of FY24/25. Output increased by an average of 1.5 percent y-o-y in the first half of FY24/25, slower than the 2.1 percent expansion in the first half of the previous year. After last year's surge, agriculture posted muted growth in the first half of FY24/25 amid drought-like conditions and pest infestations. Industrial output contracted, driven by high input costs, increased taxes, and lower government development spending, and services growth was dampened by spillovers from weak agricultural and industrial activity. The government achieved a primary surplus in the first half of FY24/25, with fiscal consolidation efforts supported by an IMF program. The current account was in surplus at the end of 2024, helped by higher remittances, stemming from reduced

FIGURE 1.6 Regional economic activity

Growth in most South Asian countries has been weaker than expected. The region is still growing more rapidly than other EMDEs, but the gap has narrowed. Fiscal and current account balances improved across the region but fiscal deficits remain well above pre-pandemic averages. In most South Asian countries, inflation has fallen below the upper bounds of target ranges. Monetary policy rates have fallen from post-pandemic highs but in several countries remain well above pre-pandemic averages.



Sources: CEIC; Haver Analytics; IMF *Fiscal Monitor*; World Bank *Macro Poverty Outlook*; World Bank. Note: AFG = Afghanistan; BGD = Bangladesh; BTN = Bhutan; EMDEs = emerging market and developing economies; IND = India; LKA = Sri Lanka; MDV = Maldives; NPL = Nepal; PAK = Pakistan. A. Revisions relative to forecasts from October 2024 South Asia Development Update. Maldives and Sri Lanka use calendar year.

B. Year-on-year growth. "South Asia" consists of countries with available quarterly data: Bangladesh, India, and Sri Lanka. "Other EMDEs" include 61 economies. Real GDP-weighted averages (at 2010–19 average market exchange rates).

C. 2024 data are estimates from Macro Poverty Outlook. "Other EMDEs" include 132 economies. Real GDP-weighted averages (at 2010–19 average market exchange rates). Among South Asian countries, the data for Maldives is for the calendar year, while other countries show the fiscal year.

D. The data point for 2025 refers to the monetary policy rate for each country as of April 15, 2025.

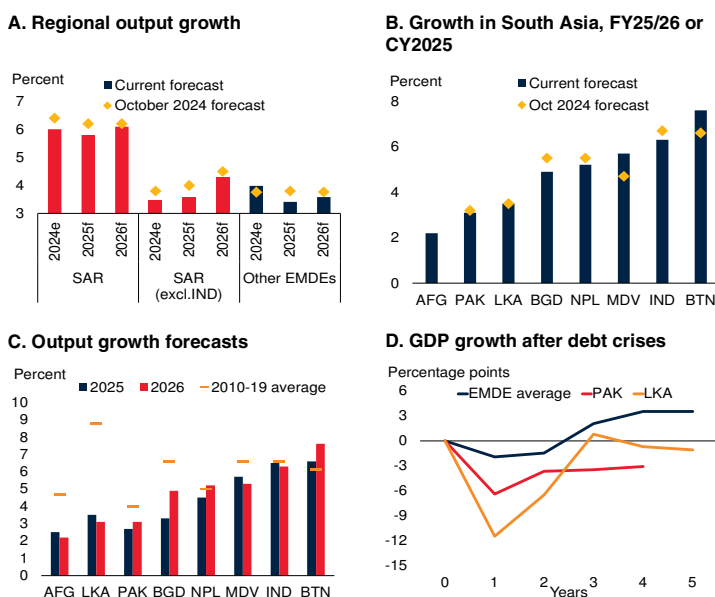
E. Data for Afghanistan, Sri Lanka, Bhutan and Maldives correspond to February 2025; all other countries correspond to March 2025. The EMDE median (February 2025, year-on-year) covers 92 economies. The last observation is April 15, 2025.

F. Figure shows the 24/25 fiscal year for all countries except Sri Lanka, which uses calendar years.

political uncertainty and exchange rate stability, that more than offset the wider trade and primary income deficits.

FIGURE 1.7 Economic activity in South Asian countries

In the majority of South Asian countries, growth prospects have dimmed as policy support is withdrawn and sentiment weakens.



Sources: Haver Analytics; World Bank Macro Poverty Outlook.

Note: AFG = Afghanistan; BGD = Bangladesh; BTN = Bhutan; EMDEs = emerging market and developing economies; IND = India; LKA = Sri Lanka; MDV = Maldives; NPL = Nepal; PAK = Pakistan; SAR = South Asia.

A. Real GDP-weighted average real GDP growth rates for 8 South Asian economies and 139 other EMDEs. October 2024 forecasts exclude Afghanistan.

C. For countries that use fiscal rather than calendar years, "2025" and "2026" represent FY24/25 and FY25/26, respectively.

D. Percentage points represent the difference in GDP growth compared with the initial year.

The agreement reached in September 2024 on an IMF-supported policy program helped stabilize the exchange rate and reduce the risk of debt default, as reflected in ratings upgrades from several credit rating agencies and a narrowing of borrowing spreads. With depreciation pressures on the currency subsiding, a robust agricultural harvest, and administrative prices stabilizing, inflation declined steadily to 0.7 percent in March 2025 from its peak of nearly 40 percent in mid-2023. This allowed the central bank to lower its policy rate by 10 percentage points since June 2024 to 12 percent in January.

Sri Lanka has restored macroeconomic stability following the severe economic crisis of 2022–23, but the recovery remains tenuous. Output grew by 5.0 percent in 2024, driven by a rebound in the industrial sector and strong performance in tourism. Current account and fiscal balances improved during the year, aided by the suspension of external debt servicing, strong tourism activity, and robust remittance inflows. As the economy stabilized, usable official reserves increased to the

equivalent of 3.4 months of imports by the end of October 2024, compared with 1–2 weeks in the depths of the crisis in late 2022. Deflation set in from September 2024; prices declined 4.2 percent year-on-year in February 2025 due to reductions in administered prices and a gradual appreciation of the currency. The central bank cut its policy rate again in November 2024 but has held it steady at 8 percent since then.

Progress in restructuring external debt has followed the domestic debt restructuring that was completed in 2023. Formal agreements were signed in 2024 with the Export-Import Bank of China, the China Development Bank, and other official creditors. An ad hoc group of bondholders (representing about 50 percent of outstanding bonds) also agreed in September 2024 to restructure holdings of the country's international sovereign bonds. By the end of 2024, about 98 percent of the country's international sovereign bonds had been restructured. Bilateral debt negotiations have concluded, with only the finalization of formal agreements still pending.

Outlook for South Asia

After growing at a weaker-than-anticipated pace of 6.0 percent in 2024, growth in the region is forecast to slow to 5.8 percent in 2025 (figure 1.7). The deceleration in 2025, and the 0.4 percentage point downgrade relative to the October forecast, in part reflects prospects of weakening global trade, rising global inflation, and tightening global financial conditions.

The region is more insulated from global trade shocks than most other EMDEs, as nearly all the region's economies are among the quarter of EMDEs least open to global trade and investment and have some of the highest tariff and non-tariff barriers to trade. With energy imports averaging about 4 percent of GDP, South Asia is also benefiting from weakening oil prices. Nonetheless, trade barriers and policy uncertainty are expected to weigh on both exports and investment across the region.

After several years of large swings in growth caused by the pandemic and the post-pandemic recovery, three countries in the region—Bhutan, India, and Nepal—are now growing at rates broadly consistent with their 2010–19 averages. The other

TABLE 1.1 Growth in South Asia

Country fiscal year		Real GDP growth at constant market prices (Percent)				Revision to forecast from October 2024 (Percentage points)		
		2023	2024(e)	2025(f)	2026(f)	2024(e)	2025(f)	2026(f)
Calendar year basis								
South Asia region		7.4	6.0	5.8	6.1	-0.4	-0.4	-0.1
South Asia region excluding India		2.8	3.5	3.6	4.3	-0.3	-0.4	-0.2
Maldives		4.7	5.5	5.7	5.3	0.8	1.0	0.7
Sri Lanka		-2.3	5.0	3.5	3.1	0.6	0.0	0.0
Fiscal year basis		22/23	23/24(e)	24/25(f)	25/26(f)	23/24(e)	24/25(f)	25/26(f)
Afghanistan	mid-March to mid-March	-6.2	2.3	2.5	2.2	N/A	N/A	N/A
Bangladesh	July to June	5.8	4.2	3.3	4.9	-1.0	-0.7	-0.6
Bhutan	July to June	5.0	4.9	6.6	7.6	-0.4	-0.6	1.0
India	April to March	7.6	9.2	6.5	6.3	+1.0	-0.5	-0.4
Nepal	mid-July to mid-July	2.0	3.9	4.5	5.2	0.0	-0.6	-0.3
Pakistan	July to June	-0.2	2.5	2.7	3.1	0.0	-0.1	-0.1

Sources: Macro Poverty Outlook (World Bank); World Bank staff calculations.

Note: (e) = estimate; (f) = forecast. GDP measured in average 2010–19 prices and market exchange rates. Pakistan is reported at factor cost. To estimate forecasts for regional aggregates in the calendar year, fiscal year forecasts for Bangladesh, Bhutan, Nepal and Pakistan are converted by averaging two consecutive fiscal years, and fiscal year forecast for Afghanistan are converted by taking 25 percent and 75 percent of two consecutive fiscal years, as quarterly GDP forecasts are unavailable.

five countries—Afghanistan, Bangladesh, Maldives, Pakistan, and Sri Lanka—are recovering from, or in the midst of, economic stress or political uncertainty. Macroeconomic stability has taken hold in Pakistan and Sri Lanka, but both countries are returning to their average growth rate before their debt crises more slowly than other EMDEs affected by debt crises.

Inflation is expected to remain stable and near official targets in most South Asian countries, assuming continued stability in commodity prices and exchange rates. Risks to the inflation projections include a resumption of currency depreciations and failures to maintain exchange rate pegs.

Fiscal balances remain in deficit across the region, particularly in Maldives and Pakistan. These deficits are expected to narrow over the projection period, although at differing paces. Current account deficits have narrowed in most countries, and have almost disappeared in some cases. They are expected to remain close to historical averages in the forecast period. Inflation is expected to moderate in countries where it is currently unusually high (Bangladesh) or low (Sri Lanka) as the impact of temporary factors such as tax rate changes or currency depreciations fades.

Outlook for South Asian countries

For *Afghanistan*, economic projections have been prepared for the first time since official data publication was halted in 2021. Agriculture will remain the key growth driver, outpacing other sectors. The economy grew by an estimated 2.5 percent in 2024/25 and is forecast to remain weak in 2025/26 due to aid disruptions, growing 2.2 percent. With annual population growth of about 2.4 percent, this implies stagnant per capita incomes. Official development assistance has been declining in recent years but remains substantial and further reductions would weigh on growth.

In *Bangladesh*, growth is expected to slow from 4.2 percent in FY2023/24 to 3.3 percent in FY2024/25 before rebounding to 4.9 percent in FY2025/26. The projections have been downgraded since October for both years. This primarily reflects the disruptions arising from last summer's social unrest and political tensions. It also reflects the trade disruptions, the persistence of inflation, worsening bank health, governance challenges, and general uncertainty about the country's political future, all of which will contribute to an expected decline in investment.

Real GDP is expected to gradually rise in the medium term, however, driven by critical reforms.

In *Bhutan*, growth is forecast to accelerate to 6.6 percent in FY24/25 and 7.6 percent in FY25/26. The forecast upgrade in the latter year is largely due to stronger construction activity related to a large hydropower project for which planning was recently finalized. This is partially offset by weak growth in the agriculture sector as the transition to export-oriented agribusiness proceeds more slowly than expected. The government deficit is expanding because of higher capital expenditures, weaker-than-expected revenue collection as a result of goods and services tax reform, and increasing interest payments on commercial loans.

In *India*, growth in FY24/25 disappointed because of slower growth in private investment and public capital expenditures that did not meet government targets. In its budget for FY24/25, the government announced fiscal consolidation but also tax cuts to support private consumption and regulatory streamlining to spur private investment. GDP growth is expected to slow from 6.5 percent in FY24/25 to 6.3 percent as in FY25/26. The benefits to private investment from monetary easing and regulatory streamlining are expected to be offset by global economic weakness and policy uncertainty. Private consumption is expected to benefit from tax cuts, and the improving implementation of public investment plans should boost government investment, but export demand will be constrained by shifts in trade policy and slowing global growth.

In *Maldives*, tourism accounts for about 70 percent of the economy, directly and indirectly, and strong growth of tourist arrivals is expected to continue. The completion of a new airport terminal in the second half of the year is contributing to growth accelerating to an expected 5.7 percent in 2025. Activity is forecast to moderate to 5.3 percent in 2026. The country's challenges in meeting its external debt obligations continue to pose a significant downside risk to projected growth.

In *Nepal*, the economy is expected to grow 4.5 percent in FY24/25 and 5.2 percent in FY25/26—for both years, less than expected in the October edition of this report. The downgrade is due to

persistent weakness in the financial system. Private sector credit has been contracting as a share of GDP, and many financial sector cooperatives have suffered losses or gone bankrupt because of nonperforming loans, particularly to the real estate sector. Nepal has also been relisted by the Financial Action Task Force, for the second time, on the grey list of countries that require greater financial monitoring due to not fully implementing money laundering and terrorist financing reforms.

In *Pakistan*, the economy continues to recover from a combination of natural disasters, external pressures, and inflation. Inflation has slowed more quickly than expected, providing room for further monetary easing. Incoming data on economic activity have been weaker than expected, but strong imports of capital goods and high consumer confidence suggest accelerating private sector growth. Banking sector lending to the private sector has picked up substantially as government borrowing needs have declined. Economic growth is projected to continue gradually gathering strength, rising to 2.7 percent in FY24/25 and 3.1 percent in FY25/26.

In *Sri Lanka*, the modest growth forecast reflects the scarring effects of the crisis, structural impediments to growth, and global economic uncertainty. Progress with debt restructuring has contributed to a normalization of financial markets and will allow a resumption of large infrastructure projects funded by bilateral lenders. Overperformance of revenues relative to targets after a large increase in the value-added tax in 2024 has improved fiscal balances, but this is being somewhat offset by significant increases in government salaries.

Risks and vulnerabilities

The uncertain global environment presents heightened downside risk to South Asia's growth prospects. Rising tariffs, policy uncertainty, and financial turmoil could result in a severe global downturn. South Asia may be more insulated from global shocks than other EMDE regions because of its limited trade integration with the rest of the world, but domestic vulnerabilities could amplify any direct impacts. High government debt and

debt service burdens, limited international reserves in some countries, and reliance on official development assistance in others make several countries in the region vulnerable to shifts in international financial market sentiment. Financial pressures could also arise from policy surprises abroad as well as slippages in the implementation of key domestic reforms, which could erode confidence and threaten macroeconomic stability.

Severe global downturn

The two countries facing the highest new tariff barriers are the United States and China. These are the world's two largest economies, accounting for more than 40 percent of global GDP and 20 percent of global trade.

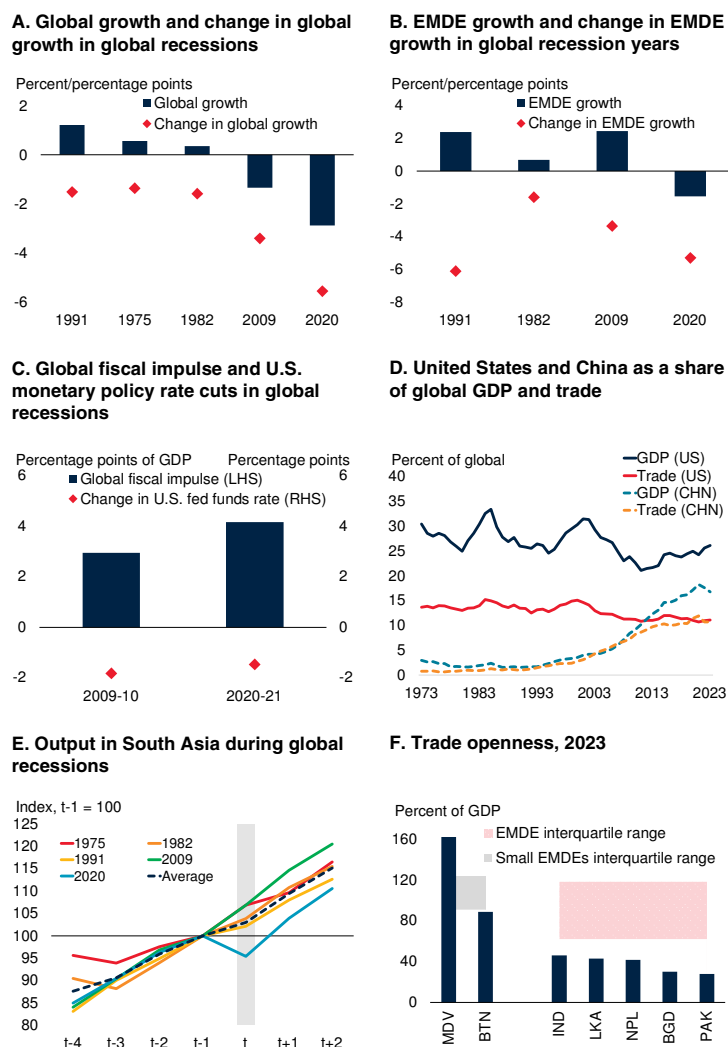
Any slowdown affecting these countries would have substantial spillovers to the rest of the world. In 2023, the United States was the most important export destination for about one-fifth of countries and China was the most important destination for almost another fifth. U.S. financial markets can also transmit domestic shocks abroad through their impact on portfolio and credit flows. China is deeply embedded in global value chains, particularly with other countries in the East Asia and Pacific region. The country is also a major importer of commodities, such that a slowdown in activity can weigh on demand and prices for metals and energy.

Market participants believe the probability of the United States falling into recession has increased substantially. All five global recessions over the past 50 years have coincided with recessions in the United States. Only twice in this time has the United States fallen into recession without the global economy doing the same but, even in those years, the global economy tipped into severe downturns.

Consensus forecasts point to a moderate global growth slowdown, but not a severe one, let alone a global recession. But an intensification in global financial strains, a broadening of tariff increases, and persistent and rising policy uncertainty could eventually combine to tip the global economy into a severe slowdown or even recession (figure 1.8).

FIGURE 1.8 Severe global downturn

Tariff increases, policy uncertainty, and financial market volatility in an environment of elevated debt could result in a severe global downturn. There have been five global recessions and three severe global downturns in the past 50 years. Monetary and fiscal policy have supported activity during past global recessions, but the inflationary effect of tariffs and sizable fiscal deficits may now limit this response. Weakening activity in the United States and China would have widespread spillovers, given the size of these economies. South Asia has slowed during some global recessions and emerged largely unscathed from others. The region's lack of openness limits its exposure to global shocks, but also limits opportunities to benefit from productivity-enhancing foreign technology and practices.



Sources: IMF World Economic Outlook (database); Kose, Sugawara, and Terrones (2020); World Development Indicators (database); World Bank.

Note: BGD = Bangladesh; BTN = Bhutan; CHN = China; EMDEs = emerging market and developing economies; IND = India; LKA = Sri Lanka; MEX = Mexico; MDV = Maldives; NPL = Nepal; PAK = Pakistan; US = United States.

A, B. Real GDP-weighted averages (at 2010-19 average market exchange rates and prices). Data for EMDE growth not available for 1975.

C. Nominal U.S. dollar GDP-weighted averages for fiscal impulse; fiscal impulse defined as the decline in the structural fiscal balance for 84 and 85 countries between 2008-10 and 2019-21. Change in U.S. federal funds rate over two year period from June 2008 and from December 2019.

E. The chart shows an index equal to 100 in global recession years (shaded in gray). Average refers to the average of the last five global recessions.

F. Trade is defined as the sum of goods and services exports and imports. For Maldives, 2022 data are shown. "Other EMDEs" includes 72 economies, and "Small EMDEs" includes 13 economies.

The world economy has fallen into recession—defined as a contraction in per capita GDP—five times over the past 50 years: 1975, 1982, 1991, 2009, and 2020. These episodes were characterized by highly synchronized downturns in global trade, industrial production, and capital flows, alongside financial crises (Kose and Ohnsorge 2019). In global recession years, global growth slowed sharply by more than 2 percentage points, on average, and EMDE growth slowed even more, with the most severe recessions being the two most recent ones in 2009 and 2020. Global inflation and oil prices typically fell. In the three global downturns over the past five decades (1998, 2001, and 2012), global growth slowed by 1.4 percentage point, on average.

Policy makers responded to previous downturns and recessions with significant monetary and fiscal stimulus. Governments around the world supported economic activity with fiscal stimulus: in the last two global recessions of 2009 and 2020, global fiscal stimulus averaged 3.5 percent of GDP over a two-year period. Central banks, too, provided monetary stimulus. For example, the U.S. Federal Reserve cut policy rates by more than 1 percentage point in the last two global recessions and maintained low rates for the subsequent two years or longer.

Currently, however, the scope for significant fiscal and monetary policy support is limited in many countries. Monetary policy may be constrained by the inflationary impact of tariffs, and by the fact that inflation concerns were rising in many economies even prior to the latest tariffs. Fiscal policy provided considerable support during the pandemic and many countries still have fiscal deficits that are considerably wider than their pre-pandemic level. Further increases may be difficult to finance, particular given rising borrowing costs.

Growth in South Asia slowed considerably during past global recessions, although the region only fell into outright contraction in 2020. Nearly all the region's economies are among the quarter of EMDEs least open to global trade and investment, and have some of the highest tariff and non-tariff barriers to trade. The closed nature of the region's economies limits its exposure to adverse global spillovers, such as those stemming from increasing tariffs or slowing growth in major economies, but these would still be considerable. Being less open also limits opportunities to benefit from trade or investment diversion (World Bank 2024b).

The damage from tariff increases also has long-term impacts. If trade tensions lead to the fragmentation of global trade into separate blocks, it would weaken an important engine of growth and technology transfer for many EMDEs. In a scenario in which global trade fragments into two blocks centered on the United States and China, the losses from trade inefficiencies and capital accumulation have been estimated to be as large as 7 percent of global GDP (IMF 2023b). Whether South Asia would suffer below-average or above-average losses in such a scenario would depend on the degree to which the region can benefit from the rerouting of trade between the world's two largest economies.

Policy uncertainty and financial stress

Some indicators point to improved macroeconomic resilience since the October 2024 edition of the *South Asia Development Update*. For most countries in the region, current account deficits have largely been closed, currencies that had been under pressure have stabilized, foreign exchange reserves have been bolstered, and borrowing spreads have narrowed (figure 1.9).

But these improvements are built on fragile foundations. Many countries in South Asia have only recently exited crises and needed external support to do so. The region is still the most heavily indebted among EMDEs, with particularly high levels of public debt. Even after the recent improvements, foreign exchange reserves remain limited in many cases. Current financial market stability and anticipated improvements in fiscal balances are predicated upon ambitious reform programs that may prove difficult to implement fully, especially if they trigger social unrest.

Policy uncertainty in major economies could generate financial market gyrations and discourage economic activity. In times of uncertainty, firms may postpone investments and be more cautious in hiring (Bloom et al. 2014; Schaal 2017). Households may postpone purchases of durable goods and increase their savings. Commercial banks may increase lending rates to compensate for the risk of increased defaults (Segal, Shaliastovich, and Yaron 2015).

Both global financial shocks and global uncertainty shocks can have strong and persistent contractionary

effects on output in individual countries (Cesa-Bianchi, Pesaran, and Rebucci 2020). In the past, a 1-standard-deviation increase in global economic policy uncertainty is estimated to have lowered global output by more than 1 percent over two to three years (Ahir, Bloom, and Furceri 2022).

South Asia has limited exposure to global *trade* shocks. But the region's high debt stocks, low foreign exchange reserves, and reliance on official development assistance make it vulnerable to *financial* shocks.

An abrupt flight of capital from riskier to safer assets could have significant consequences for most countries in South Asia. Such events could be triggered by a global increase in risk aversion, policy uncertainty, or shifting trade policy. Capital flight could also result from domestic developments, such as an unexpected increase in inflation or a failure to satisfy the conditions for IMF support of a policy program.

Governments in *India, Maldives, Pakistan, and Sri Lanka* are already liable for above-average net interest payments relative to GDP, and will seek to finance fiscal deficits of between 7 and 17 percent of GDP in 2025. In some countries, growing debt service pressures could generate cycles of rising risk premia and debt distress.

Some countries in the region could experience financial pressures from policy changes in major donor countries that result in a slowdown or sudden stop in official financing. Several advanced economies have recently announced budget reductions for development assistance.

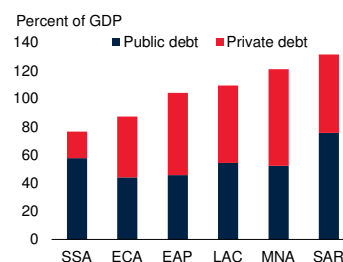
Several countries in South Asia are highly dependent on official development assistance (figure 1.10). This is especially true for Afghanistan, which had development assistance inflows equivalent to more than one-quarter of its economy in 2022, though donors have scaled down their engagement more recently. Five of the region's eight countries—Afghanistan, Bangladesh, Bhutan, Maldives, and Nepal—have aid inflows equivalent to at least 1 percent of GDP. For all South Asian countries except India, Maldives, and Sri Lanka, aid inflows are substantially larger than inflows from foreign direct investment.

Currency instability has been associated with an increased probability of balance-of-payments crises

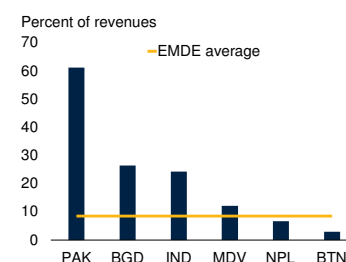
FIGURE 1.9 Policy uncertainty and financial stress

South Asian countries are more indebted than those in any other EMDE region, on average, and need to finance sizable fiscal deficits in 2025. They also have limited foreign exchange reserves and above-median shares of foreign currency-denominated government debt. These features make the region particularly vulnerable to financial stress.

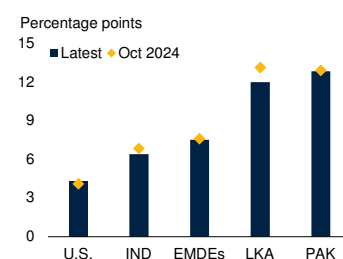
A. Public and private debt, latest



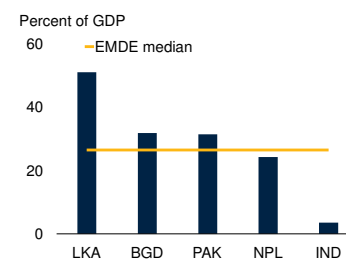
B. Government net interest payments, 2023



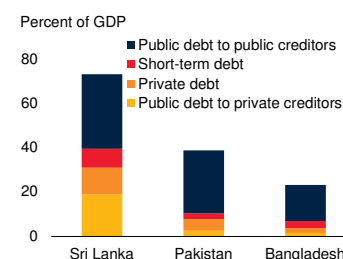
C. Sovereign borrowing costs



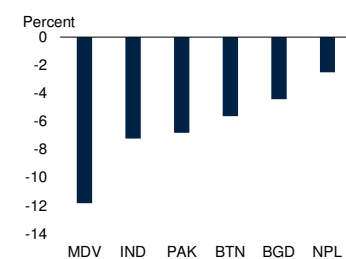
D. Foreign currency-denominated government debt, 2023



E. External debt, 2023



F. Fiscal balance, 2025



Sources: CEIC; IMF Global Debt Database; IMF Staff Country Reports 2024; IMF World Economic Outlook (database); Kose et al. (2022); Macro Poverty Outlook; Trading Economics; World Bank Macro Poverty Outlook; World Bank Debt Statistics; World Bank.

Note: BGD = Bangladesh; BTN = Bhutan; EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging market and developing economies; IND = India; LAC = Latin America and the Caribbean; LKA = Sri Lanka; MDV = Maldives; MNA = Middle East and North Africa; NPL = Nepal; PAK = Pakistan; SAR = South Asia; SSA = Sub-Saharan Africa.

A. Public debt refers to the total liabilities of the central government, while private debt includes loans and securities. Both reflect the median country level for each region in 2022, with Sri Lanka data from 2019 and Bhutan data from 2021 in the South Asia region.

B. Bars show government interest spending, derived from the difference between the overall and the primary balance. Orange line shows the GDP-weighted EMDE average. Data for Maldives is calendar year, while the rest is fiscal year.

C. Figure shows the 10-year government bond yield. "EMDEs" refers to the median for 17 EMDEs. Last observation is April 16, 2025.

D. For India, proxied by nonresident-held debt. EMDEs include 39 economies.

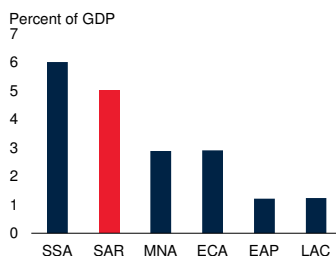
E. Public debt to public creditors includes long-term public debt to bilateral and multilateral creditors as well as IMF and SDR allocations. Public debt to private creditors is long-term. Private debt is long-term private external debt to any creditor. Short-term debt cannot be decomposed.

F. Data not published for Sri Lanka. 2025 refers to calendar year for Maldives, fiscal year 2024/25 for Pakistan, Bhutan, Bangladesh and Nepal, and fiscal year 2025/26 for India.

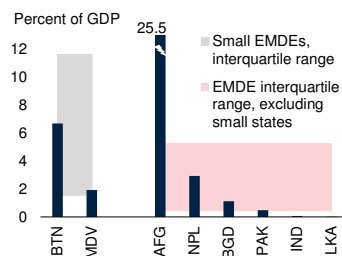
FIGURE 1.10 Official development assistance

Many countries in South Asia are dependent on inflows of official development assistance. These inflows are often larger than inflows of foreign direct investment.

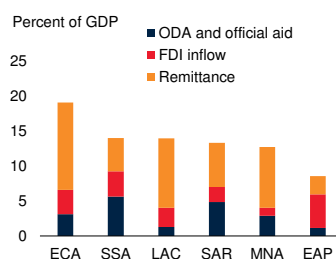
A. Net official development assistance by region, 2022



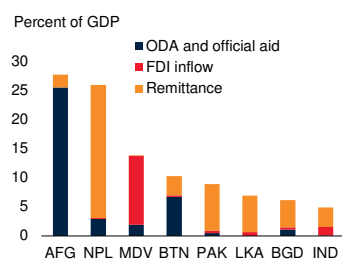
B. Net official development assistance by country, 2022



C. Composition of foreign exchange inflows, 2022, by region



D. Composition of foreign exchange inflows, 2022, by country



Sources: World Development Indicators (database); World Bank.

Note: AFG = Afghanistan; BGD = Bangladesh; BTN = Bhutan; EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging market and developing economies; FDI = foreign direct investment; IND = India; LAC = Latin America and the Caribbean; LKA = Sri Lanka; MDV = Maldives; MNA = Middle East and North Africa; NPL = Nepal; ODA = official development assistance; PAK = Pakistan; SSA = Sub-Saharan Africa; SAR = South Asia.

A. Regional aggregates use simple average and exclude small states. SAR includes Afghanistan, Bangladesh, India, Nepal, Pakistan, and Sri Lanka. Sample includes 17 countries in LAC, 11 in EAP, 10 in MNA, 39 in SSA, and 17 in ECA.

B. “Small EMDEs” includes 23 economies, and “EMDEs excluding small states” includes 100 economies. ODA flows to Afghanistan have declined substantially since 2022 according to estimates based on engagement with donors and UN agencies.

C. Sample includes 16 economies in ECA, 35 in SSA, 16 in LAC, 8 in SAR, 10 in MNA and 10 in EAP. Regional aggregates use simple average. Economies with missing values for any type of foreign exchange flow in 2022 are excluded. South Asia aggregation uses Sri Lanka’s data for 2021 to avoid the temporary disruption in inflows caused by the country’s debt default in 2022, and has no data for Afghanistan’s FDI in 2022.

in EMDEs (IMF 2023a). Currency depreciations could result from slowing inflows of capital, and would push up inflation and increase servicing costs on debt denominated in foreign currencies. In countries with pegged exchange rates, a depletion of foreign exchange reserves could culminate in an abrupt devaluation, which could have particularly severe consequences for those that have borrowed in foreign currencies on the assumption that the exchange rate would remain stable. Interest rate hikes by EMDE central banks to contain currency and capital outflows would tighten domestic borrowing conditions and slow the growth of credit and domestic demand. Higher borrowing costs could prolong a decade of private investment weakness in South Asia (World Bank 2024a).

Reform slippage

Many countries in South Asia have recently struggled with some combination of weak growth, high inflation, sizable current account deficits, fiscal pressures, and financial sector weakness. In 2024, these pressures caused three countries in the region to experience debt distress. To reduce their vulnerabilities and build resilience, governments have embarked on reform programs, often supported by the IMF. Half of the countries in the region are in IMF programs—*Bangladesh*, *Nepal*, *Pakistan*, and *Sri Lanka*—which is a higher proportion of the total in South Asia than any other EMDE region except Sub-Saharan Africa (figure 1.11).

These programs come with reform commitments and conditions designed to restore or preserve macroeconomic stabilization—in particular by undertaking fiscal consolidation and increasing foreign exchange reserves—while also enhancing social protections. Foreign exchange buffers have increased in some program countries since last year, even though they remain low. All four South Asian countries with IMF programs have narrowed or closed their current account deficits, and are also expected to show greater improvements in their fiscal positions than non-program countries.

The specifics of each program differ by country. In *Pakistan*, the government has committed to raising tax revenues by the equivalent of 4–5 percentage points of GDP, reforming the energy sector, and allowing the exchange rate to be flexible. *Bangladesh* entered a program to strengthen the financial sector and modernize its macroeconomic framework. *Sri Lanka*’s program aimed to restore debt sustainability, growth, and financial sector stability. *Nepal*’s program is an older vintage, as it was introduced to address the effects of the pandemic and is on track to conclude in 2025.

In the medium term, estimates of the effect of IMF programs on growth vary widely. In principle, bolstering macroeconomic stability should support output growth, but this may be partly offset by the negative effect on growth from the austerity measures required in the IMF program. A plurality of studies find positive effects from IMF programs, but a substantial minority find no effect or even

negative effects (Balima and Sokolova 2021; Bird and Rowlands 2017; Dreher 2006; ECB 2019).

In the short term, however, IMF programs help protect South Asian countries from financial turmoil. South Asian countries—particularly those in IMF programs—tend to have lower credit ratings than other EMDEs. Furthermore, their credit-rating assessments more often explicitly reference the IMF program.

Historically, countries in South Asia have met program conditions about as often as other EMDEs. Inability to implement program-critical reforms can delay or interrupt the flow of IMF support. This could reignite exchange rate depreciations and capital outflows, which would raise borrowing costs and add to fiscal pressures.

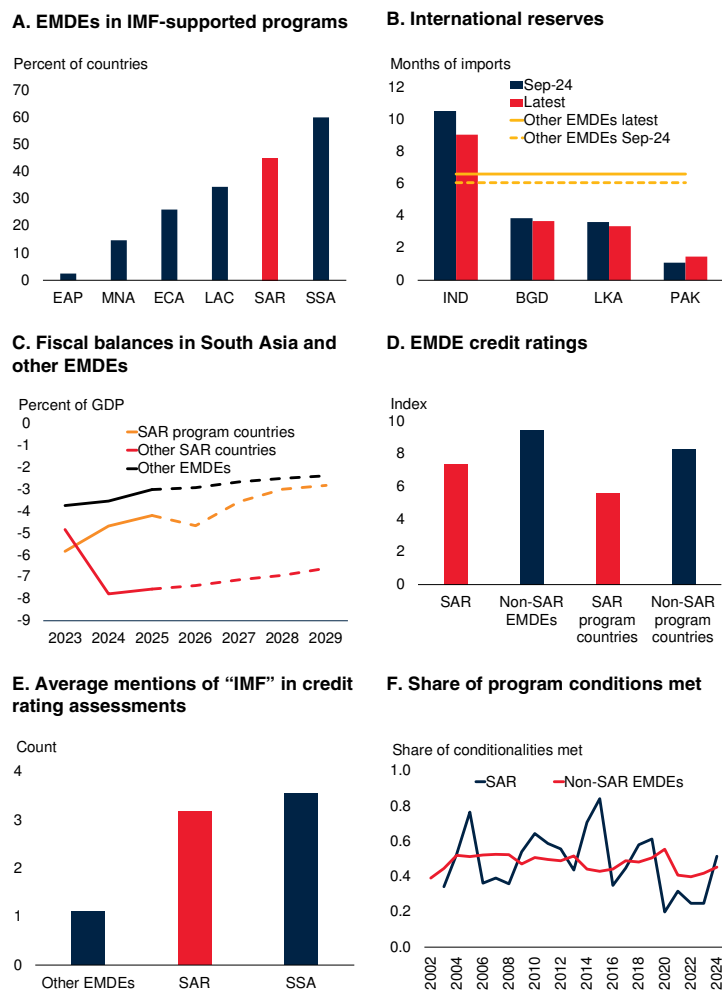
Implementing structural reforms is not only about avoiding a financial crisis, however. In the longer term, the successful implementation of planned reforms can help countries unlock stronger structural growth alongside macroeconomic stability.

Policy challenges

South Asian governments could seize the opportunity provided by the current upheaval in global trade to make their economies more attractive for trading partners interested in diverse and stable supply chains. This would require a readiness to sharply lower tariff and non-tariff trade barriers to trade as part of ongoing or new bilateral or regional trade negotiations. Given how closed South Asian economies currently are, and given the region's demographic potential and growing domestic markets, opening up could generate substantial productivity and employment benefits over the medium-term. In the short term, however, it could temporarily weigh on employment and output growth if South Asian product, labor, and capital markets are too rigid to allow for a quick expansion of more profitable activities and reduction in less profitable ones. The disruption could be particularly large in agriculture (Gulati et al. 2025). The sector is sheltered by average tariffs of 24 percent in 2022 (compared with a global average of 15 percent) and it employs 42 percent of South Asia's workforce.

FIGURE 1.11 Reform slippage

Half of the countries in South Asia are implementing IMF-supported policy programs. These have helped to contain currency pressures, stabilize or improve fiscal balances, and reduce inflation. Countries remain vulnerable to slippages in their policy programs—not only because slippages tend to weaken economic performance, but also because credit ratings often depend on IMF support. South Asian countries have in the past met program conditions about as often as other EMDEs.



Sources: Bloomberg; Oxford Economics; World Development Indicators (database); WTO Tariff Sources: Fitch Ratings; Haver Analytics; IMF Monitoring of Fund Arrangements (MONA) database; IMF Fiscal Monitor; Moody's; S&P Global; World Bank.

Note: BGD = Bangladesh; EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging market and developing economies; IND = India; LAC = Latin America and the Caribbean; LKA = Sri Lanka; MNA = Middle East and North Africa; PAK = Pakistan; SSA = Sub-Saharan Africa; SAR = South Asia.

A. Figure shows the average share of countries in IMF programs between 2020 and 2024, by region. B. "Other EMDEs" includes 37 countries. Latest data are from January 2025. Comparison data is from September 2024.

C. South Asian program countries are Bangladesh, Nepal, Pakistan, and Sri Lanka. Other EMDEs include 74 economies. Data from October 2024 IMF Fiscal Monitor.

D. Credit ratings from S&P, Moody's, and Fitch were mapped to a unified 1–22 scale (1 = lowest, 22 = highest), and a simple average was computed for each country. The sample includes South Asian countries (Bangladesh, India, Maldives, Pakistan, Sri Lanka), South Asian program countries (Bangladesh, Pakistan, Sri Lanka), 96 non-SAR EMDEs, and 40 non-SAR program countries. Last observation is April 15, 2025.

E. Counted mentions of "IMF" in the credit assessment reports for EMDE countries and regional aggregates use simple averages; South Asian countries include Bangladesh, India, Maldives, Nepal, Pakistan and Sri Lanka; Sub-Saharan Africa region includes 28 economies, and "other EMDEs" includes 64 countries. Last observation is April 10, 2025.

F. The unit of observation in the MONA dataset is the Arrangement/loan-conditionality-review round. Each arrangement/loan has several conditionalities. A conditionality is counted as a reform in all years where it is met. Figure shows the share of conditionalities met in each review round. The share ranges from 0 to 1.

BOX 1.1 Branching Out: The Economic Potential of South Asians Abroad^a

Dimming growth prospects across South Asia amplify the challenge of creating jobs. Many in South Asia's rapidly growing workforce are likely to continue to seek opportunities abroad. Migrants from South Asian countries—mainly to countries outside the region—account for about 3 percent of South Asia's working-age population. About one-half of them work in Gulf Cooperation Council countries, are typically low-skilled, and on short-term contracts. Another one-quarter work in advanced economies and tend to be highly skilled and longer-term migrants. While the challenges of emigration have been well documented, South Asian countries' large diasporas also bring economic benefits to the home countries, both while workers are abroad and after they return home—through remittances, improved skills, investments, and trade ties.

Introduction

Among emerging market and developing economy (EMDE) regions, South Asia is the second-largest source of international migrants after Europe and Central Asia. In 2020, the number of international migrants from South Asian countries to other countries, mainly outside but also within the region, was equivalent to 3 percent of South Asia's working-age population. For example, the number of Nepalis living abroad was equivalent to 14 percent of Nepal's working-age population, and the corresponding proportion for Afghanistan was 27 percent. The remittances sent by migrants are a critical source of income for households and a source of foreign exchange inflows for financial systems (World Bank 2024b). During 2020–23, remittance inflows from international migrants averaged 4 percent of GDP in South Asia and, in Nepal, 24 percent. The largest source of remittance inflows to the region was Gulf Cooperation Council (GCC) countries (Ratha, Plaza, and Kim 2022).

Globally, almost half of all migrants return home (World Bank 2023a). Both returnees and those who remain abroad can benefit their home economies, in different ways. This box reviews evidence and the literature to answer the following questions:

- What are the characteristics of South Asia's migrant population abroad?
- How can South Asia's governments better leverage the economic potential of their large diasporas?

This box reports the following findings.

First, the GCC countries host one-half of South Asian migrants, while advanced economies host about one-

quarter. On average, South Asian migrants in advanced economies are better educated than both the average South Asian and the average migrant from South Asian countries to other EMDEs. More than half of South Asian migrants in advanced economies have received tertiary education, compared with less than one-third of all South Asians and one-fifth of South Asian countries' migrants in other EMDEs.

Second, international experience suggests that international migrants can benefit their origin economies both while they are abroad and after they return home. Returning migrants bring home enhanced human capital and savings, and diaspora networks foster knowledge spillovers, trade, and investment. Formal agreements—such as those arranged by the Philippines as an origin country, and by New Zealand and the Republic of Korea as host countries—can help improve predictability and working conditions.

Third, South Asian governments could better harness the potential of lower-skilled, temporary migrants abroad by ensuring better working conditions and formal training through bilateral agreements, facilitating remittance flows, and supporting entrepreneurship among returning migrants. To unlock greater benefits from highly skilled, long-term migrants, South Asian countries could leverage existing networks through policies that attract foreign direct investment (FDI) or joint ventures and remove obstacles to trade between host and home countries.

South Asia: Migration trends and patterns

Migration trends. About 40 million people born in South Asian countries lived abroad in 2020—equivalent to about 3 percent of the region's working-age population (McAuliffe and Oucho 2024). Migrant populations from Afghanistan, Bhutan, Nepal, and Sri Lanka were especially large relative to their populations,

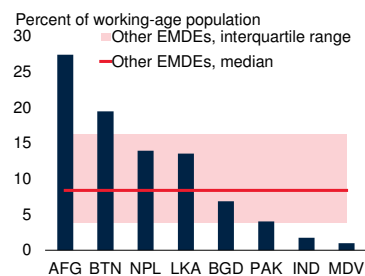
^a This box was prepared by Hagen Kruse and Zoe Xie.

BOX 1.1 Branching Out: The Economic Potential of South Asians Abroad (continued)

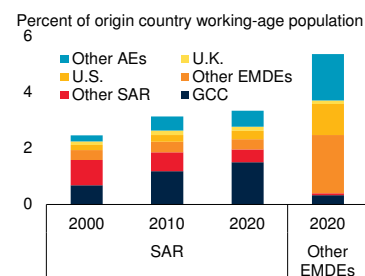
FIGURE B1.1 Migration trends and patterns

The number of international migrant workers was equivalent to about 3 percent of South Asia's working-age population in 2020. The most common destinations are countries in the Gulf Cooperation Council.

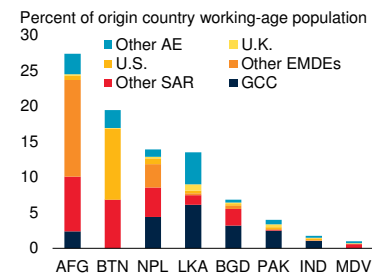
A. Migrant population overseas, by country of origin, latest



B. Host country of migrant population from South Asia versus other EMDEs, latest



C. Host country of migrant population from South Asia, by country of origin, latest



Sources: Global Bilateral Migration Matrix 2000–2020 (database); World Development Indicators (database); World Bank.

Note: AEs = advanced economies; AFG = Afghanistan; BGD = Bangladesh; BTN = Bhutan; EMDEs = emerging market and developing economies; GCC = Gulf Cooperation Council (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and United Arab Emirates); IND = India; LKA = Sri Lanka; MDV = Maldives; NPL = Nepal; PAK = Pakistan; SAR = South Asia. Migrant population from South Asia include South Asian migrants in other South Asian countries. EMDE and South Asia aggregates exclude small states (population below 1.5 million). Migrants are defined as people born in a country that is different from the country where they currently reside. Numbers for Afghanistan include family refugees, including children who have not yet reached working age. People who were born in India and are living in Pakistan, and vice versa, are excluded from the migrant population, due to historical reason.

A. Red horizontal line is the median of other EMDEs. Shaded region represents the inter-quartile range of other EMDEs. EMDEs exclude small states (population below 1.5 million). Latest data are for 2020.

C. Latest data are for 2020.

and much larger than the EMDE median (figure B1.1). In contrast, Maldives is a major migrant host country, with immigrants constituting one-third of the country's working-age population (Maldives Bureau of Statistics 2024). In Nepal and Sri Lanka, the pace of net emigration during 2010–20 was well above the EMDE median, amid job market weakness and, in 2020, the COVID-19 pandemic, which stranded many migrants abroad (World Bank 2022). Since 2020, emigration from Bhutan, Nepal, and Sri Lanka appears to have surged further due to continued weakness in labor markets (Alaref et al. forthcoming; World Bank 2024c, 2025). The number of South Asians living abroad grew by 13 percent between 2020 and mid-2024.

Migration destinations. The main destinations of South Asian migrants in 2020 were GCC countries—in particular, Qatar, Saudi Arabia, and the United Arab Emirates. After efforts in several GCC countries in the late 2000s to better protect immigrant workers, these countries' share as a destination for South Asian nationals living abroad increased from 28 percent in 2000 to 45 percent in 2020. At least one-third of the

migrant populations from Bangladesh, India, Nepal, Pakistan, and Sri Lanka lived in GCC countries, compared with less than 10 percent of migrants from other EMDEs. Meanwhile, the number of intra-regional migrants declined from 37 percent of South Asian countries' nationals living abroad in 2000 to 15 percent in 2020.^b This decline has been attributed to the lack of job opportunities in South Asia and the acceleration in demand for low-skilled labor in the GCC countries (Ahmed and Bossavie 2022; World Bank 2024a). South Asian migrants have been hosted by a number of advanced economies, and mainly Anglophone ones. In 2020, about 20 percent of Indian migrants were in either the United States or the United Kingdom, about 20 percent of Sri Lankan migrants were in either Australia, Canada, or the United Kingdom, and about 20 percent of Pakistani migrants were in either Canada, the United Kingdom, or the United States.

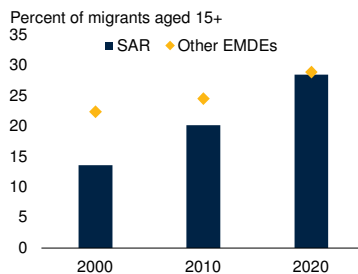
^b People who were born in India but are living in Pakistan, and vice versa, are excluded from the migrant population as these are legacies from the partition in 1947. The decline in intra-regional migration, therefore, is not related to the aging of those people.

BOX 1.1 Branching Out: The Economic Potential of South Asians Abroad (continued)

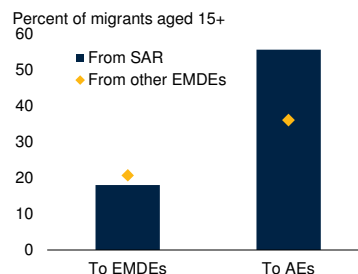
FIGURE B1.2 Migrant skills

South Asian migrants in advanced economies are better educated than both South Asians in EMDEs and non-South Asian migrants in advanced economies.

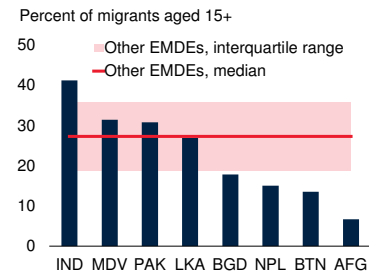
A. Migrants with tertiary education from South Asian countries, latest



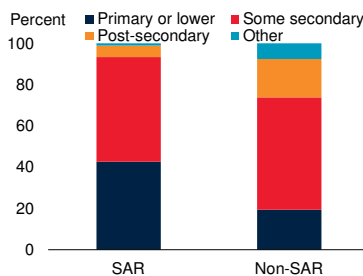
B. Migrants with tertiary education from South Asia versus other EMDEs, by host country type, latest



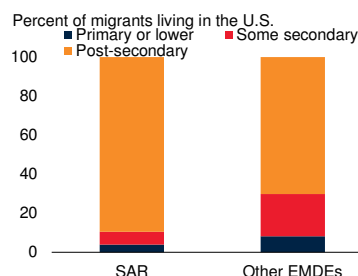
C. Migrants with tertiary education from South Asian countries, latest



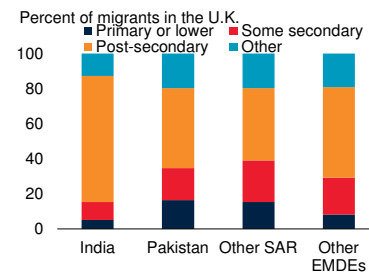
D. Education level of migrant workers in GCC by country of origin, 2014–15



E. Education level of migrants in the United States by country of origin, 2019



F. Education level of migrants in the U.K. by country of origin, 2023



Sources: American Community Survey 2009, 2019; Bossavie and Özden (2023); Global Bilateral Migration Matrix 2000–2020 (database); KNOMAD-ILO Migration Costs Surveys 2015 and 2016; U.K. Annual Population Survey 2019, 2023; U.S. Census 2000 5 percent sample data; World Development Indicators (database); World Bank.

Note: AEs = advanced economies; AFG = Afghanistan; BGD = Bangladesh; BTN = Bhutan; EMDEs = emerging market and developing economies; GCC = Gulf Cooperation Council (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and United Arab Emirates); IND = India; LKA = Sri Lanka; MDV = Maldives; NPL = Nepal; PAK = Pakistan; SAR = South Asia. Migrant population from South Asia include South Asian migrants in other South Asian countries. EMDE and South Asia aggregates exclude small states (population below 1.5 million). Migrants are defined as people born in a country that is different from the country where they currently reside. People who were born in India and are living in Pakistan, and vice versa, are excluded from the migrant population, due to historical reason.

A.B. Numbers showing migrants aged at least 15 years old with tertiary education as a percent of all migrants who are at least 15 years old, by origin and destination country group.

C. Numbers showing migrants aged at least 15 years old with tertiary education as a percent of all migrants who are at least 15 years old, by origin country group.

D. "Primary or lower" indicates no education, primary incomplete, and primary complete. "Some secondary" indicates secondary incomplete and secondary complete. "Post-secondary" indicates post-secondary technical, some tertiary, university and higher. "Other" indicates adult education and literacy programs.

E. Bars show the percentage of immigrants aged 18 and older living in the United States in 2000, 2010, or 2020, by the highest education attainment. "Primary or lower" indicates no education, pre-primary, and up to grade 6. "Some secondary" indicates grade 7 to 12 with or without a high school diploma or GED. "Post-secondary" indicates some college, associate's, bachelor's, master's, professional, and doctoral degrees.

F. "Other EMDEs" indicates immigrants with country of birth as European Union EU2 (Bulgaria and Romania), Middle East and Central Asia, North Africa, Southeast Asia, Sub-Saharan Africa, Central and South America, Other Europe (non-European Union), and Poland. China and Mongolia (part of East Asia), Hungary (part of EU8), and Mexico (part of North America) are not included in "Other EMDEs" because they are not separately identified in the data. Bars show the percentage of immigrants in the United Kingdom by highest qualification. "Primary or lower" indicates no qualification. "Some secondary" indicates GCSE grades A–C and GCE-A level or equivalent. "Post-secondary" indicates high education and degree or equivalent. "Other" indicates other qualifications.

Migrants' skills. South Asian migrants are less well-educated than those from other EMDEs, although the gap has been shrinking (figure B1.2). Across destinations, South Asian migrants in advanced economies are more educated than those from other EMDEs: more than half of the former have tertiary education, compared with 40 percent of the latter. For

example, in 2023, almost 60 percent of South Asian migrants—and 72 percent of migrants from India—in the United Kingdom had a post-secondary education, compared with about 50 percent of migrants from other EMDEs. In contrast, South Asian migrants living in other EMDEs are, on average, slightly less educated than migrants from other EMDEs. The latest available

BOX 1.1 Branching Out: The Economic Potential of South Asians Abroad (*continued*)

data for South Asian migrant workers in GCC countries, which are for 2014–15, show that they were overwhelmingly low-skilled—with 90 percent having, at most, a secondary education, compared with 70 percent for migrants in GCC countries from other EMDEs. Among South Asian countries, migrants from India have the highest share with tertiary education—40 percent, which is above the EMDE median. Migrants from Afghanistan, Bangladesh, Bhutan, and Nepal are the least educated, with shares of migrants having received tertiary education below those of migrants from three-quarters of other EMDEs.

Duration of migrants' stays. The duration of the stays of South Asian migrants in advanced economies has resembled that of migrants from other EMDEs. For example, among South Asian migrants living in the United Kingdom in 2023, the median length of stay had been 13 years, similar to that for migrants from other EMDEs (Office for National Statistics 2024). In contrast, low-skilled labor migration from South Asian countries, especially to the GCC countries, is usually temporary by design, with migrants returning home upon contract completion (World Bank 2022). The most recent multi-country survey of migrant workers, conducted in 2014–15, indicates that almost all of the migrant workers from South Asia in GCC countries were on short-term visas, compared with about one-quarter of migrants from other EMDEs (KNOMAD and ILO 2021). In 2019, one-quarter of Bangladeshi migrants had been abroad for less than two years, with a median stay of 4.7 years (Bossavie et al. 2025).

International experience with large diasporas

International migration can benefit origin economies both while workers are abroad and after they return home. Returning migrants bring home enhanced human capital and savings; diaspora networks foster knowledge spillovers, trade, and investment. Particularly given the differences in educational backgrounds and skills between South Asian migrants living in other EMDEs and those living in advanced economies, South Asian countries require different strategies to better leverage the economic potential of these two kinds of migrants (Bossavie and Özden 2023). This includes negotiating bilateral migration agreements to improve the working conditions for low-skilled workers abroad—for example, by establishing

legal frameworks for the protection of labor rights, formalizing training programs, and reducing visa fees (Ahmed and Bossavie 2022).

Returning low-skilled migrants. Temporary migrants, particularly low-skilled ones, tend to have a stronger motivation to accumulate savings and send home remittances than permanent migrants (World Bank 2023a). For instance, migrants from EMDEs who entered the Netherlands between 1999 and 2007 were more likely to return to their origin country after they had met a savings target; this tendency was particularly strong among low-skilled migrants (Bijwaard and Wahba 2014). Savings and remittances have also been the primary benefits of temporary migrants from South Asia to GCC countries. Among returning Bangladeshi and Pakistani workers, savings were later often used to finance entrepreneurial activities at home, which in turn increased family income (Bossavie et al. 2025; Bossavie and Wang 2022).

Returning highly skilled migrants. More than 20 percent of highly skilled workers born in low-income countries work abroad (World Bank 2019). This has been characterized as a “brain drain”—a term used to describe the negative effects of highly skilled emigration on production, research and development, the provision of public services, such as health or education, tax revenues, and political institutions in the origin countries (for example, Agrawal et al. 2011; Docquier and Rapoport 2012; Gibson and McKenzie 2011). But when migrants return home with improved skills, this brain drain can turn into a “brain gain” because of these workers’ transfer of knowledge from advanced economies (Harrington and Seabrooke 2020; Kerr et al. 2016). Highly skilled refugees from the former Yugoslavia, for instance, became “guest workers” in Germany in the 1990s, and upon their return home, productivity in the Yugoslav industries employing them increased as a result of the new practices and knowledge they brought, with a resulting boost to export performance (Bahar et al. 2024).

Incentivizing the return of highly skilled migrants. Given the longer average stays of highly skilled migrants abroad, several EMDEs have launched targeted government programs to incentivize their return. For example, the Chinese *Thousand Talent Program*, launched in 2008, has resulted in the return

BOX 1.1 Branching Out: The Economic Potential of South Asians Abroad (continued)

of more than 7,000 scientists previously working abroad, using tax exemptions, housing subsidies, and preferential access to start-up and research grants (Jia 2018). Besides incentivizing the return of highly skilled workers, the program's research-related financial benefits have also raised productivity more than among their overseas research peers (Shi, Liu, and Wang 2023).

Highly skilled diasporas: Knowledge and business spillovers. The permanent return of highly skilled migrants is not a necessary condition for positive spillovers to origin countries. The large group of Indian-born, U.S.-educated engineers working in Silicon Valley on the U.S. H1-B visa program, for instance, have in many cases maintained professional and business connections with their home country and contributed to the upgrading of its information technology industries (Docquier and Rapoport 2012; Saxenian 2023). Strong knowledge network effects between Indian and U.S. cities have also been associated with a higher likelihood of innovation in the origin city (Agrawal et al. 2011). Similarly, the recent migration of European innovators to the United States not only improved their own productivity, but also increased the innovation rate of their former colleagues in Europe by 16 percent (Prato 2025). And the prospects of working in the United States increased the incentive to invest in information technology-specific education in India and elsewhere (Khanna and Morales 2024).

Diasporas: Trade and FDI. Diaspora networks have been associated with deeper trade and investment ties. After the United States lifted its trade embargo on Viet Nam in 1994, trade with Viet Nam grew 5 to 14 percent more in those U.S. states with 10 percent larger populations of former Vietnamese refugees than in other states during the period 1995–2010 (Parsons and Vézina 2018). Similarly, immigrant populations are a strong predictor of U.S. regions' outward FDI flows to origin countries, with historically large effects for diasporas from the former Soviet Union and Viet Nam and highly skilled immigrant groups (Javorcik et al. 2011; Mayda et al. 2022). In the first two decades after China started reforms to open its economy in 1979, FDI inflows were dominated by Chinese diaspora from high-income neighboring economies (Chen, Xiong, and Zhang 2023).

Circular migration

A special case of temporary migration is circular migration, referring to repeated movements between a migrant's origin and host countries. This type of temporary migration is most common among low-skilled migrants from origin countries with relatively weak domestic labor markets and host countries that provide some degree of legal certainty for re-entry (Constant and Zimmermann 2011; Dustmann and Görlach 2016; World Bank 2025). Common examples of circular migrants include seasonal workers in agriculture and construction.

The role of formal agreements. In contrast to highly skilled migrants—who are often directly recruited by international companies under formal contracts with clearly specified working conditions—low-skilled migrants often face substantial risks of financial exploitation, poor working conditions, and high migration costs (Kerr et al. 2016; McAuliffe and Oucho 2024).^c For example, in 2015–16, Pakistani migrants on average paid US\$4,500—more than 10 months' worth of their monthly destination wage—to work temporarily in Saudi Arabia (Ahmed and Bossavie 2022). Bilateral migration agreements between countries provide a systematic and institutionalized approach to reduce the uncertainty of workers in low-skilled occupations abroad and improve their working conditions (Adhikari et al. 2024; World Bank 2025).

Formal agreements: Philippines. In 2022, the Philippines' government efforts to protect and negotiate the interests of Filipinos who temporarily work abroad culminated in the establishment of a Department of Migrant Workers. Negotiations included a temporary ban on migration of workers to Saudi Arabia until commitments to improve working conditions were made in 2022 (McAuliffe and Oucho 2024). Among other services, the Department of Migrant Workers provides migrants with a list of licensed international recruitment agencies. As a result, Filipino workers have come to be employed in more skill-intensive occupations in GCC countries and face

^c In "Global Skill Partnership" agreements, destination countries—often aging, advanced economies—even invest into the origin countries' education and training systems to mitigate brain drain concerns (Acosta et al. 2025).

BOX 1.1 Branching Out: The Economic Potential of South Asians Abroad (continued)

substantially lower migration costs than South Asian migrants (Bossavie and Wang 2022). Filipinos' average cost to start working in Saudi Arabia, for instance, was less than 10 percent of the cost for Pakistani migrants. The vast majority of this cost difference can be explained by lower visa fees negotiated for Filipino workers through formal migration agreements (Ahmed and Bossavie 2022).

Formal agreements: New Zealand. New Zealand's Recognized Seasonal Employer program, introduced in 2007, facilitates temporary, low-skilled migration from small neighboring island countries. This increased migrant households' long-run income, consumption, savings, and human capital investment upon their return home (Gibson and McKenzie 2014).

Formal agreements: Korea. The Republic of Korea's Employment Permit System for temporary, low-skilled immigrants was introduced in 2004. Since then, Korea has signed bilateral agreements with 16 EMDEs—including Bangladesh, Nepal, Pakistan, and Sri Lanka—and has hosted about 56,000 migrants annually in recent years, with about one-third being return

migrants. The program features mandatory training, a guaranteed minimum wage, health insurance, and a transparent legal framework for disputes between workers and employers (CGD 2025; Cho et al. 2018).

Policy priorities

International experience suggests that the policy approaches needed in origin countries to optimize their benefits from lower-skilled, temporary migrants—for example, to GCC countries—are different from those needed in the case of highly skilled, long-term migrants to advanced economies. For lower-skilled migration, government-negotiated bilateral agreements could be prioritized to improve working conditions, increase knowledge spillovers, and boost remittances, which in turn can support entrepreneurship in the home country. For more highly skilled and longer-term migration, which tends to create diaspora networks, greater benefits may be unlocked through incentives to return and by policies that remove obstacles to trade and investment between home and host countries, including the creation of platforms for cross-border collaboration and knowledge exchange.

The more challenging global environment could also more easily be navigated if the region prioritized reforms to tackle areas of particularly large inefficiency or vulnerability. *First*, low domestic revenue mobilization and fragile fiscal positions have been a source of macroeconomic instability in the past, and have absorbed financing that might have been more productively used for private investment. *Second*, the agriculture sector is unusually unproductive, and exceptionally vulnerable to climate damage. Policies to boost its productivity could unlock growth and structural transformation. *Third*, weaker growth prospects will amplify the long-standing challenge of creating jobs for South Asia's rapidly growing populations. Emigration pressures are therefore unlikely to ease but policies could aim to achieve greater benefits from South Asia's large diasporas (box 1.1).

Increasing revenues

Low revenues are the root of South Asia's fiscal problems that have repeatedly threatened

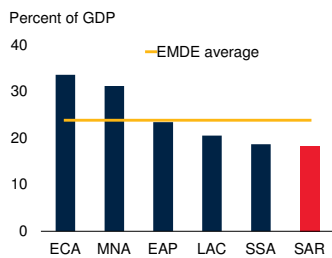
macroeconomic stability over the past decade. In 2023, government revenues in the region averaged 18 percent of GDP, well below the EMDE average of 24 percent of GDP, and well below the region's expenditures of 27 percent of GDP (figure 1.12). Other than Maldives all countries had government revenues that were 2 to 18 percentage points of GDP less than the average for EMDEs.

The effect of low revenues can be seen in the region's large public debt and debt service burdens. Government debt in 2023 averaged 77 percent of GDP in South Asia, compared with an EMDE average of 64 percent of GDP. South Asian governments spent an average of 26 percent of their revenues on interest payments—almost three times the EMDE average of 9 percent. These fiscal pressures are broad-based across South Asia: Nepal is the only South Asian country whose government debt-to-GDP ratio and share of revenues committed to interest payments are below the EMDE average.

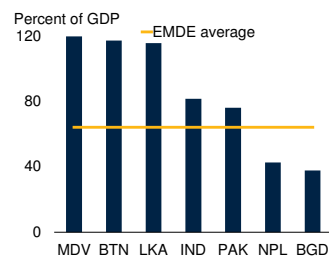
FIGURE 1.12 Government revenues

Low revenues lie at the root of South Asia’s high public debt levels and low spending on health and education. Despite high tax rates, shortfalls in revenues are particularly large in consumption taxation and can only partially be explained by the characteristics of South Asian economies, such as pervasive informality. Revenues could be bolstered in a variety of ways, including reforms that strengthen tax administration.

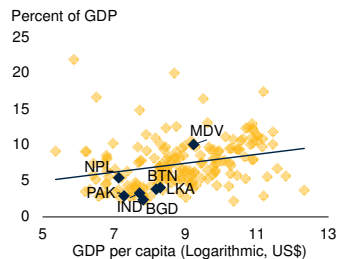
A. General government revenues, 2019–23



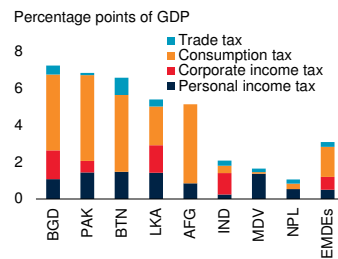
B. General government debt, end-2023



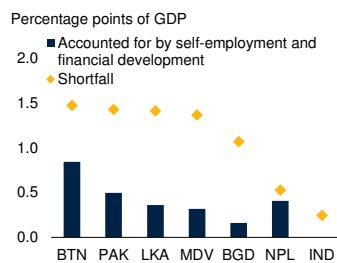
C. Health spending and per capita GDP, 2021



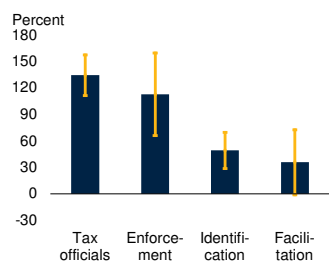
D. Total tax revenue shortfalls



E. Personal income tax revenue shortfall accounted for by country characteristics



F. Revenue increase from tax administrative interventions



Sources: Haver Analytics; IMF Financial Development Index (database); IMF Government Finance Statistics (database); International Labour Organization; Haver Analytics; UNU-WIDER; USAID Collecting Taxes Database; Vegh and Vuletin (2015); World Development Indicators (database); World Bank Fiscal Survey; World Integrated Trade Solution Database; World Bank.

Note: AFG = Afghanistan; BGD = Bangladesh; BTN = Bhutan; EAP = East Asia and Pacific; ECA = Europe and Central Asia; EMDEs = emerging market and developing economies; IND = India; LAC = Latin America and the Caribbean; LKA = Sri Lanka; MDV = Maldives; MNA = Middle East and North Africa; NPL=Nepal; PAK= Pakistan; SAR = South Asia; SSA = Sub-Saharan Africa.

A. Total revenue excludes grants. EMDE average is nominal GDP-weighted average of 140 EMDEs. Regions are nominal GDP-weighted average of country group.

B. “EMDE average” is nominal U.S. dollar GDP-weighted averages for 135 EMDEs. For Bhutan, around two-thirds of general government debt is in hydropower debt.

C. Latest available data are for 2021. Per capita income in nominal U.S. dollars. Straight line represents linear relationship between GDP per capita and health or education spending. Sample includes 146 EMDEs and 37 advanced economies.

D. Estimated shortfall for trade tax revenue does not include the shortfall accounting for para-tariffs. Estimated shortfall for corporate income tax revenue is available for four South Asian countries (Bangladesh, India, Pakistan, and Sri Lanka).

E. Personal income tax rate is the average of the highest and lowest tax rates. Potential tax base for personal income tax revenue is labor income (percent of GDP). Robustness check and estimation results can be found in chapter 2.

F. Blue bars indicate average revenue impact of 87 interventions in 17 countries, estimated in 26 studies. Yellow whiskers indicate 95 percent confidence intervals.

Low revenues make it difficult to deliver basic government services. All South Asian countries except Maldives spend less on healthcare than would be expected based on their per capita incomes. Three of the four South Asian countries with the highest interest burdens spend less than half as much as the average EMDE on education—and much less than would be expected based on their per capita incomes.

South Asian countries’ consumption tax rates, corporate tax rates, and tariff rates are in line with, and often above, EMDE averages. Given these tax rates and their potential tax bases, South Asian countries’ revenues from these taxes fall short of their potential by 1–7 percentage points of GDP (chapter 2). Shortfalls are particularly pronounced in consumption tax revenues, but are also sizable in personal income tax revenue and, in the larger economies, corporate income tax revenue.

No more than half of these shortfalls can be explained by the particular features of South Asia’s economies—such as widespread informality and large agriculture sectors. The sizable tax gap that remains illustrates the scope for improving tax revenues by streamlining tax policy, strengthening enforcement, and facilitating compliance.

An unusually large share of South Asian income earners is exempt from personal income taxation entirely. In all South Asian countries except Sri Lanka and Nepal, tax thresholds for personal income tax are above GDP per capita. These income tax thresholds are among the highest of all EMDEs. Exemptions from other types of taxes are also pervasive. In all South Asian countries, the paring back of tax exemptions is a priority. In fact, this is the most frequently mentioned policy recommendation in recent World Bank and IMF documents on improving tax systems in South Asia.

South Asian governments’ revenues could also be raised by tax policy measures to unify, simplify, and harmonize tax rates. Such streamlining could help both compliance and enforcement. Reduced exemptions and streamlined rates would also curtail tax evasion and opportunities for corruption in tax enforcement. Efforts to strengthen

enforcement, including through increased incentives for tax officials, have proven successful in raising revenues in countries in other regions.

Pollution pricing—through pollution taxation or pollution trading schemes that are increasingly used around the world—offers another means of raising South Asian governments' revenues. It would also help to address another of the region's critical challenges: severe air pollution, which is the worst among all EMDE regions.

Agricultural reform for climate adaptation

Agriculture is critical to South Asian economies. But it is also an area of particularly pronounced inefficiencies.

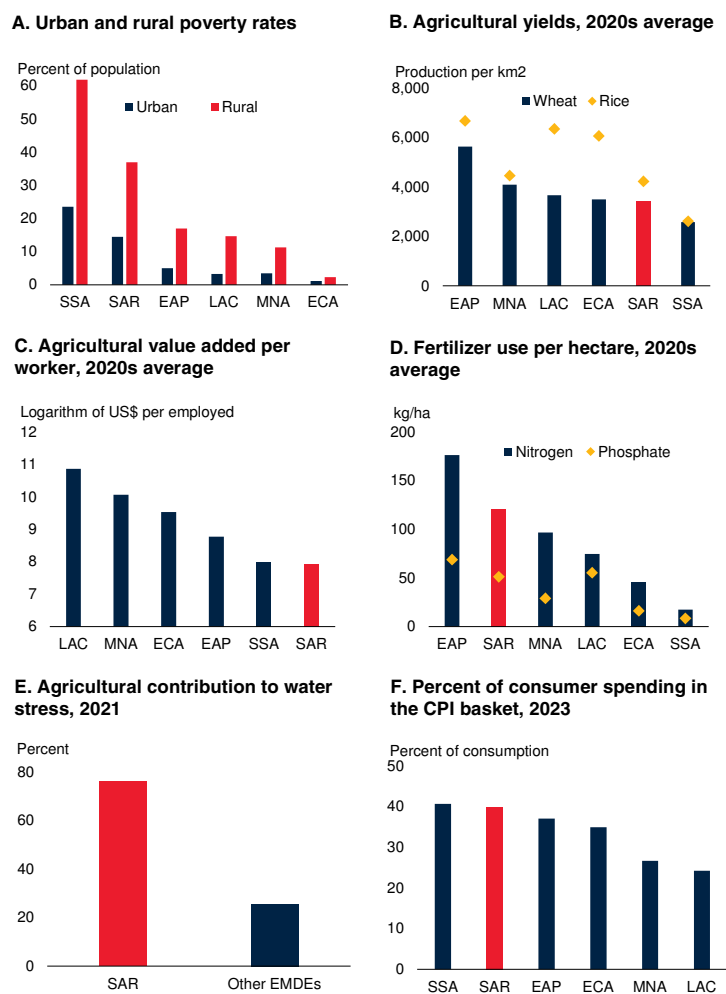
The sector generates 16 percent of the region's GDP and employs 42 percent of its workforce, including a disproportionate share of women. Agricultural workers are far more likely to be poor than workers outside agriculture (figure 1.13).

South Asia's agricultural land generates yields that are broadly in line with those in the Middle East and North Africa, and Latin America and the Caribbean, and are well above those in Sub-Saharan Africa. These yields, however, are achieved in a considerably more resource-intensive manner than in other EMDE regions. Many workers in the sector are under-employed and under-equipped with capital equipment, which has resulted in labor productivity in South Asian agriculture that is the lowest among EMDE regions—it was 7 percent lower than in Sub-Saharan Africa during the 2020s, for example. Inefficiencies extend to the use of fertilizers and water. South Asia's fertilizer use is the second highest among EMDE regions, much of it reportedly wasted (Damania et al. 2023). Agriculture accounts for three-quarters of water stress in South Asia, three times as much as in other EMDEs, in part because of leakage and evaporation in low-quality irrigation systems (FAO 2022).

The agriculture sector must also contend with rising global temperatures and extreme weather events. Rising global temperatures and extreme weather events have already reduced global total

FIGURE 1.13 Agriculture and climate adaptation

Poverty is concentrated in rural regions dependent on agriculture. Agricultural yields in South Asia are broadly in line with those in other EMDE regions. However, these yields are achieved less efficiently: labor productivity in agriculture is the lowest among EMDE regions, fertilizer use is the second highest, and agriculture contributes more than twice as much to water stress. More efficient resource allocation could raise productivity without jeopardizing food consumption.



Sources: Alkire, Kanagaratnam and Suppa (2024); Aquastat; FAOstat; Global Multidimensional Poverty Index (MPI) 2024, ILOStat; IMF Consumer Price Index database; OECD Agri-environmental indicators database; OECD Nutrient Balance, 2020; World Development Indicators (database); World Bank.

Note: EAP = East Asia and Pacific; EMDEs = emerging market and developing economies; ECA = Europe and Central Asia; LAC = Latin America and the Caribbean; MNA = Middle East and North Africa; SAR = South Asia; SSA = Sub-Saharan Africa; kg/ha = kilograms/hectare.

A. Reference year is different for each country and depends on data availability. Regional calculations use available data for the period 2014–2023. South Asia includes Afghanistan, Bangladesh, India, Nepal and Pakistan. Sample includes 36 economies in SSA, 9 in EAP, 13 in LAC, 8 in MNA, and 9 in ECA.

B. Annual averages from 2020 to latest available data. Real GDP-weighted averages (at 2010–19 average prices and market exchange rates) for 13 economies in EAP, 19 in ECA, 19 in LAC, 10 in MNA, 6 in SAR, and 30 in SSA.

C. Annual averages from 2020 to latest available data. Sample includes 14 economies in EAP, 22 in ECA, 24 in LAC, 17 in MNA, 7 in SAR, and 38 in SSA.

D. Data for 151 EMDEs. Annual average of available data since 2020.

E. GDP-weighted average (at 2010–19 average prices and market exchange rates) of agriculture's contribution to water stress. "Other EMDEs" include 128 economies. The most recent data available is for 2021.

F. Chart shows the weight of food and non-alcoholic beverages on the consumer price index basket, in an unweighted average across countries. South Asia includes Bangladesh, Bhutan, Nepal, Pakistan, and Sri Lanka. Includes 35 economies in SSA, 17 in ECA, 10 in EAP, 17 in LAC and 13 in MNA.

factor productivity in agriculture by an estimated 21 percent since 1961, and by as much as 40 percent in tropical areas (Ortiz-Bobea et al. 2021). South Asia is expected to warm more than other EMDE regions, and most crops are hurt by higher maximum temperatures (special focus). Such effects are already becoming apparent: India recently experienced its hottest February in 125 years, threatening many crops and draining reservoirs. In the medium term, rising global temperatures are also expected to increase the variability of precipitation, which will have particularly severe consequences for crops that depend on rainfall, which account for most agricultural production in the region.

An increase in labor productivity in agriculture could benefit not only household incomes but also climate resilience (World Bank 2024a). Higher labor productivity would help to lower the price of food, which makes up about 40 percent of consumption baskets in the region, more than in any other EMDE region. It would also help reduce stunting and undernourishment, which are prevalent in South Asia.

More productive farms would also help the accumulation of savings, which could spur the growth of manufacturing and services (World Bank 2024d). They could also free up labor for more productive jobs in the manufacturing and services sectors. Workers freed from agricultural work could also move to jobs abroad, which could boost the domestic economy through repatriated savings and trade and investment networks (box 1.1).

To become more productive, farmers in the region must overcome problems associated with small farm size, in terms of both land area and the number of employees (Lopez-Acevedo and Medvedev 2017). Although small farms are not necessarily less productive than larger ones, land fragmentation for non-economic reasons increases cultivation costs (Deininger et al. 2017). Small farm size tends to limit economies of scale, and often results in farmers having limited resources, and limited access to credit, insurance, and extension services that could boost productivity and market access. In many cases, their small size

prevents South Asian farms from utilizing the high-quality agricultural capital that accounts for a large part of higher agricultural labor productivity in other countries (Caunedo and Keller 2020).

Tenancy without legal protection is commonplace throughout the region, as are patchy land titles and records (World Bank 2024c). These undermine incentives to invest and limit farmers' access to credit. Many policy initiatives focus on formalizing and digitalizing land records to establish more secure property rights. In India, the SVAMITVA scheme was launched in 2020 to provide residents in rural villages with the equivalent of a title. The initiative has mapped millions of parcels and issued millions of titles. Punjab Province in Pakistan has made similar progress.

Even with clear titles, however, restrictions on land use and transfer can still hinder the functioning of the market for land and discourage investment. In *Bhutan*, there are restrictions on the conversion of some types of farmland to other uses. In *Nepal*, land rental markets are thin mainly because tenure laws impose a risk that rented land may be lost by the landowner if the renter stays long enough (World Bank 2017). In *Sri Lanka*, where about 80 percent of land is government-owned, land use is widely restricted to rice cultivation.

Policy makers can promote productivity growth in agriculture in a variety of ways. The redeployment of subsidies on fertilizers and water can encourage more efficient use of these inputs. For example, Pakistan provides a guaranteed price for sugarcane production, while subsidizing its consumption of water. Such subsidies that encourage the wasteful use of inputs could be replaced by direct, targeted transfers, with higher transfers for farmers that adopt sustainable land management practices (OECD 2019).

Better infrastructure has sizable positive spillovers for agricultural productivity (Burki, Shabbir, and Khan 2022). Irrigation investment programs can bring large returns, while also helping to preserve water and increase the resilience of farm yields in

the face of increasingly erratic rainfall and temperature (Morita 2021). Research into the development of more climate-resilient crops and practices can also often bring high returns, by some estimates averaging more than 40 percent of the investment (Furceri et al. 2021).

Governments can also remove impediments to the efficient operation of markets. Burdensome licensing and size restrictions, labor regulations and financial restrictions can limit growth of efficient firms. Trade policy barriers can prevent successful agribusinesses from competing in international markets. Digitizing and modernizing land records can help facilitate efficient land transfers, while also incentivizing investment by giving farmers more secure titles. Caps on foreign investment discourage

foreign direct investment, and the finance and technology that come with it. Supporting the functioning of markets through smart regulations can underpin the productive re-allocation of the resources used in the agriculture sector.

Farmers can achieve many efficiency improvements without government involvement through farmer producer organizations. Such cooperative associations can unlock economies of scale in obtaining access to markets and credit for individual members and for common investments in logistics and infrastructure, such as connectivity and cold storage. The knowledge and resources shared in these networks can also facilitate diversification into the production of higher-value exportable commodities.

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