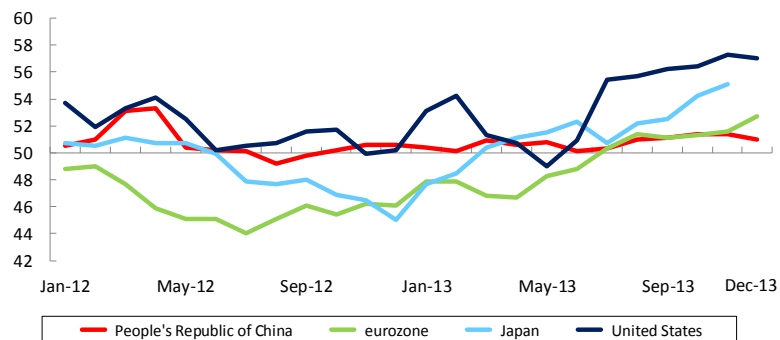


SPECIAL FEATURE: Early weakness in 2014?

Activity indicators in Asia are signaling some weakness ahead. Continued moderation in the PRC economy, and slowdown in economies that are open, globally connected, and beset by domestic challenges, may indicate some early weakness this year. The PRC's manufacturing purchasing managers' index (PMI) continues to lag behind the recovery of PMIs in the G3. GDP growth in the highly-open NIE (e.g. Hong Kong, China; Singapore; and Taipei, China) and in the ASEAN (e.g. Indonesia, the Philippines, and Thailand) has also diminished. This trend emanates from unwinding fiscal and monetary stimulus, evident from a decline of credit growth over the last 3 months. More so, another congressional debt ceiling battle could disrupt the US' solid momentum going into 2014, while Japan also faces a strong headwind from the implementation of the April tax hike.

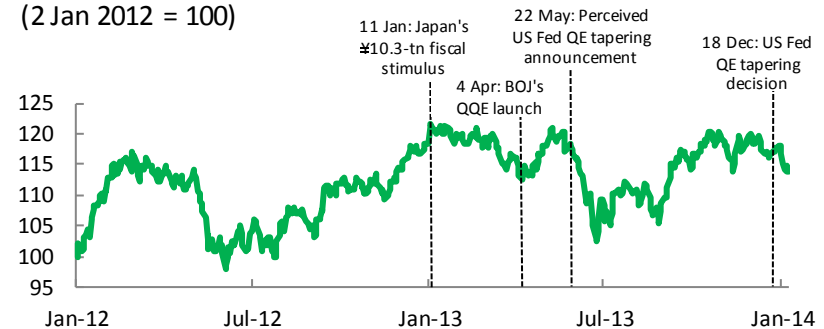
The region's financial markets were also dragged down by the combined weight of adverse domestic conditions and US Fed's QE tapering. For example, the MSCI index fell 5% over the last 3 months as investors readjusted portfolios back to advanced economies. Currencies in the region have depreciated more strongly as US economic conditions improved and capital inflows to emerging markets also weakened. More so, weaker current account data added to the pressure. Favorable data releases could lift the market in the short term—although in the medium to long term, inflation and interest rate adjustments in the US and other advanced economies will determine the outcome. If they start to rise due to strong recovery in developed economies, then portfolio inflows to the region may slow or even reverse, with currencies depreciating further. Meanwhile, inflation is rising in some Asian economies. Weaker currencies partly contribute to this, but rising housing costs in Singapore; energy price adjustments in Indonesia, Malaysia and Pakistan; rising food prices in India; and Japan's QE have added domestic pressures as well.

**Manufacturing Purchasing Managers' Index¹—
People's Republic of China and G3**



¹A manufacturing purchasing managers' index reading above 50 points indicates an expansion in the manufacturing sector while below 50 points indicates a contraction.
Source: Institute for Management Supply (US), national source (PRC), and Markit Economics (eurozone and Japan).

**Equity Index—Emerging Asia
(2 Jan 2012 = 100)**



BOJ = Bank of Japan, QQE = quantitative and qualitative easing, US Fed = US Federal Reserve.
Note: Based on Morgan Stanley Capital International (MSCI) Emerging Market Index. Daily up to 9 January 2014.
Source: ADB calculations using data from Datastream.