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APAC Market Outlook 2025

Global Influences,
Regional Opportunities



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PIMCO's Asia investment team analyse how domestic policies and external influences are shaping growth trajectories and investment opportunities across the APAC region.

In a world characterised by shifting economic conditions and rising uncertainty, the Asia Pacific region faces both challenges and opportunities. Building on the insights from our latest *Cyclical Outlook*, "*Uncertainty Is Certain*", we examine the specific implications for China, Australia, and Japan, as well as potential knock-on effects for the rest of the region and globally.

CHINA: POTENTIAL ECONOMIC STRATEGIES AND SPILLOVERS

China's economic landscape remains fraught with challenges, as growth and inflation risks continue to trend downward. The combination of constrained fiscal and credit support, high real interest rates, a significant overhang of housing inventory and excess manufacturing capacity underscores the precariousness of the current outlook.

While China has improved its manufacturing capabilities, particularly in semiconductors and other technologies, these advancements are being overshadowed by escalating trade tensions and a long-term decline in both population and productivity growth.

China's economic outlook is crucial for both regional and global markets. In our base case scenario, we project that China's real GDP growth will range from 4% to 4.5% in 2025, down from 5.0% in 2024. We expect this growth will be supported by a fiscal stimulus of 1% to 1.5% of GDP. In addition, we anticipate gradual policy easing, with the People's Bank of China (PBOC) likely to cut the 1.5% reverse repo rate (RRP) by approximately 50 basis points (bps) in 2025.

Despite the government's efforts to maintain a 5% growth target for 2024, China's growth model is increasingly strained. The prolonged downturn in the property sector, coupled with sluggish household spending, raises concerns about the sustainability of growth driven primarily by manufacturing and infrastructure investment.

To assess the potential impact on regional and global markets, along with our base case, we analysed three alternative fiscal scenarios: no direct stimulus, extra stimulus, and a scenario in which China doubles down on manufacturing.

Possible fiscal scenarios for China in 2025 – PIMCO's analysis

Scenario	Global growth	Commodity prices	Global inflation	Offshore yuan (CNH)
1. No direct fiscal stimulus (China GDP growth of around 3.0%)	↓	↓	↓	↓
2. Extra fiscal stimulus (China GDP growth of around 5.0% Direct fiscal stimulus of 2.0%–2.5% of GDP)	↑	↑	↑	↑
3. China doubles down on manufacturing (China GDP growth of around 3.5%–4.5% Stimulus to incentivise key sectors)	↓	→	↓	↓
Base case: China's real GDP growth projected at around 4%–4.5% in 2025 , down from 5.0% in 2024, supported by a fiscal stimulus of around 1%–1.5% of GDP . Gradual policy easing is anticipated, with the PBOC RRP rate expected to be cut by 50 bps in 2025.				

Source: PIMCO. As of 22 January 2025. **For illustrative purposes only.**

In the unlikely scenario of no direct stimulus, we expect a material decline in China's GDP growth to around 3%. This would significantly affect countries with strong trade ties to China, such as Korea, Malaysia, Thailand, and Australia, and place negative pressure on commodity prices, such as oil and metals. In contrast, economies less dependent on commodity exports, such as India, or those that are geographically distant, such as the U.S., would likely experience minimal effects.

Extra fiscal stimulus – the second scenario – would alter this landscape. Targeted transfers to low-income households would likely yield the highest economic multipliers by enhancing consumption, while broad-based transfers would have a more diluted impact.

The nature of the stimulus – whether focused on consumption or investment – also affects China's import dynamics, with investment-focused stimulus showing a clearer link to stronger imports. Countries closer to China, such as Taiwan and Vietnam, are more reliant on Chinese investment, while agricultural exporters like Brazil and New Zealand benefit from Chinese consumption. However, China's import growth has lagged export growth, signalling increased self-sufficiency. This trend may weaken the historical correlation between imports and exports as China continues to enhance its domestic production.

In the third scenario, if China doubles down on manufacturing through sector-specific stimulus, global competition may intensify, leading to greater losses (and therefore higher subsidies) for less competitive Chinese firms. Countries competing with China for the same markets will likely face greater challenges.

The path that China will take remains uncertain, but there is no doubt that its economic policies will continue to have a profound impact on global market conditions. For now, we are taking a cautious approach towards Chinese credit and the Chinese Yuan, while maintaining a neutral stance on China local duration, due to the recent substantive downshift in the yield curve.

AUSTRALIA: A GRADUAL RECOVERY AHEAD

Australia's economic outlook reflects a recovery in private demand following the challenges posed by high interest rates and significant tax burdens. In 2025, GDP growth is expected to show a modest improvement as real incomes rise and interest rates begin to decline from restrictive levels. This trajectory follows 2024's growth of approximately 1%, which was primarily driven by public demand, while household consumption and business investment remained flat.

Employment growth, which was robust in the second half of 2024 and largely dominated by the public sector, is anticipated to moderate in 2025, likely leading to an increase in the unemployment rate to the mid-4% range.

On the inflation front, we expect year-on-year core figures to return to the Reserve Bank of Australia's (RBA) target band of 2%–3% by the middle of 2025. With the near-term outlook for both the labour market and inflation consistent with the RBA's objectives, we anticipate that the central bank will begin lowering interest rates back towards neutral in the first half of 2025, with a reduction in the cash rate of 100 bps over the 2025 calendar year.

With the easing cycle set to commence, Australia's relatively lower fiscal deficits compared with other developed markets (resulting in lower relative bond supply), and ongoing constraints on consumption due to high household debt levels and tax burdens, we view Australian duration as attractive relative to many other developed market alternatives.

Within the Australian fixed income sector, several high-quality segments of the bond market present attractive opportunities in 2025, with some areas yielding over 5% while maintaining AAA or AA credit ratings. We believe this offers investors the chance to secure income without significant credit or liquidity risk.

The state government bond market in Australia offers appealing real income and diversification, with 10-year bond spreads ranging from 70 bps to 90 bps over Commonwealth government bonds, providing resilience in various economic scenarios.

The AAA-rated securitisation market, particularly residential mortgage-backed securities, is becoming increasingly attractive, with spreads exceeding the cash rate by 90 bps to 120 bps. Additionally, select 7-year to 10-year investment-grade corporate bonds in the infrastructure and regulated utilities sectors yield between 5.25% and 6.0%, benefiting from strong macroeconomic trends.¹

¹ All data in this paragraph as of 23 January 2025.

JAPAN: BALANCING GROWTH AND INFLATION

Japan's economic outlook is showing signs of improvement. The Bank of Japan (BOJ) hiked the official policy rate to 0.50% at its January Monetary Policy Meeting and we expect the rate to rise to 0.75% by year-end. This expectation for further policy rate adjustment reflects a more stable global macro backdrop, with reduced concerns about a U.S. economic slowdown relative to 3Q 2024, along with continued firmness in domestic wages.

The BOJ has reaffirmed its commitment to policy normalisation, indicating that it will adjust interest rates based on economic activity and the outlook for inflation and wages. Domestic macroeconomic data aligns with the BOJ's forecasts, with firm wage growth anticipated for 2025. We expect around 1% GDP growth for 2025, rebounding from around 0% growth in 2024. We anticipate inflation will hover around the BOJ's 2% target, primarily due to expected real wage increases, which should expand personal consumption and drive wage-related inflation, offsetting the effects of rising (albeit moderating) costs of goods and services.

In terms of investment strategy, we are neutral on Japan duration overall with market pricing for the BOJ looking fair for the rest of 2025, while we view relative value opportunities as more attractive. On the Japanese yield curve, we are relatively cautious on the 5- to 10-year part of the Japanese government bond (JGB) yield curve, since valuations do not adequately reflect the risk of further rate hikes beyond 2025 and the BOJ is expected to gradually reduce its purchases of these bonds. In contrast, long-term JGBs, particularly those in the 20- to 40-year range, are becoming more appealing as they have recently become cheaper relative to historical levels and are reasonably priced compared to other global alternatives.

CONCLUSION: ASIA PACIFIC CONTINUES TO OFFER OPPORTUNITIES, BUT CAREFUL PORTFOLIO POSITIONING IS REQUIRED

In summary, the outlook for the Asia Pacific region in 2025 presents a complex landscape of challenges and opportunities. We do not expect China to emerge from its challenging growth phase this year, which will continue to impact regional dynamics and economies. In Japan, active management will be critical given the market's increasing sensitivity to global interest rates and the anticipated BOJ policy decisions, which will influence bond yields and the shape of the yield curve. Meanwhile, Australia is set to join the rest of the developed world in normalising its monetary policy.

Amidst this regional and global uncertainty, we continue to see opportunities in Asia Pacific fixed income markets for active investors who can take advantage of structural inefficiencies in markets and short-term volatility. However, as countries respond to both domestic pressures and external influences, investors should prioritise caution and flexibility in their portfolio positioning.

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