

PIMCO

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APAC Market Outlook 2026

Diverging Policies,
Enduring Opportunities

A company of **Allianz** 



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Moderating growth and increasingly divergent policy responses define Asia Pacific in 2026, underscoring the need for disciplined, relative value investing across markets.

Asia Pacific enters 2026 facing diverging policy paths, shifting global trade patterns, and the after-effects of recent U.S. policy changes. As outlined in our latest [*Cyclical Outlook: Compounding Opportunity*](#), fiscal easing in China, Japan, and the U.S. is helping to stabilise regional growth, while inflation remains largely contained.

China aims to maintain growth in the 4%–5% range, a target that calls for continued policy support amid persistent downward price pressures and weak domestic demand, even as exports remain resilient. Japan is set for modest expansion, supported by fiscal stimulus and gradual policy normalisation. Australia is on track for steady, close to trend growth, supported by improved private demand but still-restrictive policy stance, with inflation having recently risen back above target.

Smaller open economies, such as Korea, Taiwan, and Singapore, continue to benefit from the AI-driven investment cycle and resilient electronics exports. They remain comparatively insulated from tariffs, though outcomes across countries are becoming increasingly uneven.

By contrast, more domestically-focused markets, including Indonesia, India, and the Philippines are already experiencing slower credit growth, signalling a need for stronger public investment and deeper structural reforms.

Against this backdrop, investors will need to be selective – focusing on relative value opportunities as policy paths diverge and remaining alert to shifts in interest rates, currencies, and credit conditions.

KEY MARKET SNAPSHOT

Country	Opportunities	Areas of caution
China	Duration overweight; policy support; export resilience	Deflationary pressures; property sector weakness; limited spillovers to the region
Japan	Long-end JGBs	Fiscal uncertainty
Australia	Modest duration overweight; improved private demand; high-quality credit spreads	Inflation risks; household budget pressures

Source: PIMCO as of 23 January 2026

CHINA: POLICY SUPPORT, PERSISTENT DEFLATION

After a solid 2025, China's growth is set to slow toward the low-4% range as the boost from export diversification and AI-driven industrial upgrades begins to fade.

China's manufacturing scale and cost advantages remain considerable, and the 15th Five-Year Plan (2026–2030) places greater emphasis on productivity, technology development, and strategic infrastructure. These priorities should help China continue expanding its global export share and climb further up the value chain.

Domestic demand, however, shows little sign of recovery. Retail sales are losing momentum as the effect of last year's goods trade-in programme weakens, while investment is held back by slower infrastructure activity and ongoing restructuring in the real estate sector, which remains a major drag on confidence and a driver of high precautionary savings.

Inflation is expected to remain subdued, with the government's "anti-involution" policy to curb excessive price competition and overcapacity helping to offset some of the demand-supply imbalances.

Fiscal deficits are likely to widen as authorities expand support for consumption, social welfare, strategic infrastructure, and real estate stabilisation. The People's Bank of China (PBOC) is likely to extend monetary easing through lower rates, ample liquidity and other special tools.

Despite ongoing U.S.-China trade frictions, China's export capacity and cost advantages should underpin its global market share, although positive spillovers to the region will be more limited than in previous cycles.

Export momentum in the rest of Asia will likely soften from last year's high base as lingering tariff effects and intensifying competition from China weigh on trade. Economies less connected to the semiconductor cycle may face more current account pressure, even as more open economies continue to benefit from firmer demand for tech-related goods.

Softer Chinese export prices will help contain inflation across Asia but may also weigh on trade balances and corporate earnings in several markets. China's slow progress on consumption rebalancing and its focus on domestic technology development will continue to shape regional dynamics.

Investment opportunities:

The near-term outlook for Chinese bonds remains favourable, particularly for longer-dated government securities, amid subdued inflation and continued monetary easing.

A strong current account and return of capital flows should support a gradual rise in the renminbi (RMB) against the U.S. dollar and other key trading partners, with the PBOC likely to manage the pace to maintain broader stability. While a stronger RMB may increase consumers' purchasing power, it is unlikely to drive a meaningful rise in consumption, and its side effects could squeeze corporate margins and exacerbate employment challenges.

If efforts to stimulate domestic demand gain traction, conditions for a rally in credit and equities can be sustained. Conversely, a renewed property downturn and tariff pressures would weigh on risk assets.

JAPAN: IMPROVED VALUATIONS AMID GRADUAL MONETARY POLICY NORMALISATION

The yield on 10-year Japanese Government Bonds (JGBs) has recently risen to above 2% – a level not seen in three decades – bringing valuations more closely in line with Japan's evolving macroeconomic fundamentals. Underlying inflation appears to be stabilising in the 1.5%–2% range, in line with our medium-term outlook.

Looking ahead to 2026, we expect 10-year JGB yields to trade broadly around current levels in our baseline scenario of modestly above-trend economic growth and an annual average core inflation rate slightly below 2%. Under this backdrop, the BOJ is likely to continue policy normalisation at a gradual pace, potentially raising the policy rate by 25 to 50 basis points toward 1%–1.25% over the next 12 months.

Several risks could push yields outside this expected range. A weaker yen or an unexpected acceleration of inflation could prompt faster or larger policy rate hikes. At the same time, the Takaichi administration's more expansionary fiscal stance introduces additional uncertainty, though we expect financial market pressures to ultimately limit the scope for policy excesses. Conversely, global growth shocks or corrections in AI-related equities could push JGB yields lower.

Investment opportunities:

Current yield levels in Japan are starting to present attractive investment opportunities, after a prolonged period of low yields. We can construct portfolios which now provide the potential for total income return of above 3% in yen terms by selecting maturities, sectors, and securities, while maintaining duration risk and credit quality comparable to broad Japanese bond benchmarks. Such portfolios should become increasingly appealing to local investors, even with inflation near 2%.

Higher yields also offer potential for capital gains if interest rates fall and can serve as a hedge against economic shocks, stock market volatility, or a sharp yen appreciation.

For global investors, currency-hedging costs currently work in their favour, enhancing the relative appeal of Japanese bonds and offering additional yield compared with global peers.

We maintain a preference for the long end of the curve, such as 30-year JGBs. While concerns about fiscal risks persist, the steepness of the yield curve and incentives for the Ministry of Finance to limit long-end issuance support this positioning. By contrast, intermediate maturities appear more vulnerable, particularly in scenarios of yen weakness or accelerating inflation.

AUSTRALIA: RESTRICTIVE POLICY AMID RESILIENT GROWTH

Australia's economy continues its transition from public-led to private-led growth. Inflation has recently risen back above the Reserve Bank of Australia's (RBA) 2%–3% target band, raising an important question: can current policy settings support a sustained consumer-led recovery that delivers above-trend growth? We believe this is unlikely.

Interest and tax payments as a share of household income remain near historic highs, indicating that conditions at the household level are still restrictive (see Figure 1). While a modest tightening of monetary policy cannot be ruled out, we view a cash rate of 3.6% as already restrictive, which should enable inflation to return to target over 2026.

With policy restrictive, we expect the unemployment rate to drift higher as private-sector activity struggles to fully offset reduced government spending. We estimate the longer run

neutral cash rate near 3%, which is where policy is likely to settle once inflation stabilises and growth returns to trend.

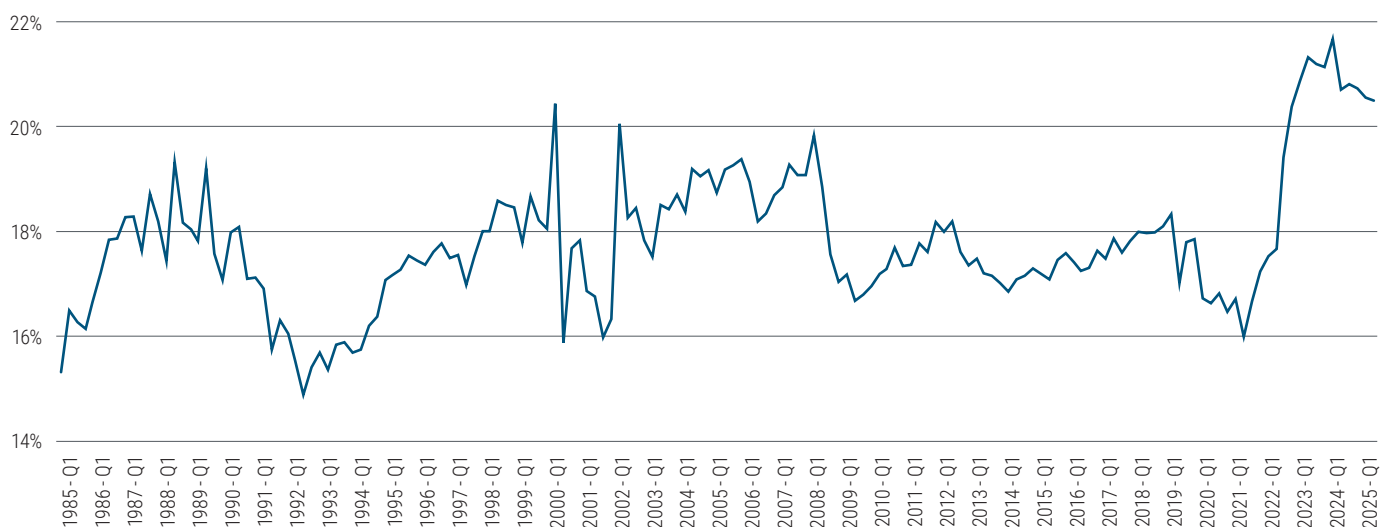
Investment opportunities

The outlook for Australian fixed income remains compelling over the coming year. With the market now pricing in rate hikes for 2026 and 10-year Australian Commonwealth Government bond yields around 50 basis points higher than 10-year U.S. Treasuries, these bonds offer attractive income, diversification, and the potential for capital appreciation.

Corporate spreads remain tight, but AA rated Australian state government bonds and AAA rated residential mortgage-backed securities (RMBS)/ asset-backed securities (ABS) are trading at the wider end of historical ranges, offering scalable, high-quality spread alternatives.

Figure 1: Household interest and tax payments remain near historic highs

Australia Household Interest & Taxes as % of Gross Income



Source: Haver Analytics. As of 23 January 2026.

CONCLUSION: NAVIGATING DIVERGENCE WITH SELECTIVITY

As Asia moves into 2026, growth is moderating, inflation remains contained, and policy paths are diverging. This environment calls for a highly selective approach across countries and asset classes.

- **Rates:** Most smaller open economies are nearing the end of their easing cycles. Japan is likely to continue its gradual normalisation while China maintains an accommodative stance. Rich valuations in some markets heighten the risk of corrections, reinforcing the importance of relative value positioning across curves and countries to capture differences in fiscal policy and supply-demand dynamics.

- **Currencies:** A gradual appreciation of the RMB should support currencies in open economies, while domestically-focused markets may face pressure from weaker growth and trade flows. Volatility in some currencies highlights the need for active management.
- **Credit:** Technical conditions remain supportive. Banks are well-capitalised and technology sectors continue to benefit from structural investment. High quality spread alternatives in Australia and new issuance in Japan offer attractive yield opportunities, although price discipline remains essential.

Investors who lean into regional differences, prioritising high quality carry and relative value, will be best placed to capture opportunities in a fragmented landscape.

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