

Asia 2026: The Divergence Trade

A Macro Outlook Across Eight Economies — Growth, Policy, and the Bets We'd Make

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Abstract

Asia enters 2026 as the fastest-growing major region globally, projected to contribute roughly 60% of world GDP growth. But the aggregate masks extreme divergence. India grows at 6.5% while South Korea struggles at 1.8%. Japan embarks on its first sustained monetary tightening cycle in decades while China's PBoC eases into a deflationary void. Singapore delivered a stunning 5.0% growth in 2025 and has upgraded its 2026 forecast to 2.0–4.0%. Thailand's growth stalls below 2.5%. This paper maps the divergence across eight Asian economies, identifies the macro forces driving each trajectory, and presents Darmine Capital's views on where the opportunities and risks concentrate. This is not a consensus forecast. It is an opinionated assessment of where we think the smart money should be paying attention.

1. The Regional Picture

The IMF projects Asia-Pacific GDP growth at roughly 4.4% in 2026, down modestly from 2025 but still comfortably above the global average. The World Bank estimates East Asia and Pacific growth at around 4.5% excluding China, with China itself projected at 4.2–4.5% depending on the source. The WTO projects global merchandise trade volume growth of just 0.5% in 2026, down sharply from above 2% in 2024–2025 — a headwind for the region’s export-oriented economies.

Economy	2024	2025E	2026F	Key Driver
China	5.0%	5.0%	4.4–4.5%	Exports fading
Japan	0.1%	1.1%	0.6–1.0%	Wage cycle
India	7.0%	6.5%	6.5%	Dom. demand
Singapore	5.3%	5.0%	2.0–4.0%	AI/semicon
Indonesia	5.0%	5.0%	5.0%	FDI + dom.
Vietnam	7.1%	6.5%	6.0–6.5%	FDI/manuf.
S. Korea	2.0%	1.1%	1.8%	Cons. recovery
Thailand	2.7%	2.7%	1.8–2.5%	Tourism/fiscal

Note: Singapore’s 2025 actual came in at 5.0%, revised up from the 4.8% advance estimate, with Q4 2025 GDP surging 6.9% year-on-year driven by AI-related electronics demand and a large pharmaceutical order. MTI upgraded the 2026 forecast range to 2.0–4.0% from the earlier 1.0–3.0%. Singapore’s 2024 growth was also revised up to 5.3%.

The divergence is not merely in growth rates. It extends to inflation dynamics (Japan tightening while China eases), currency trajectories (yen weakness versus SGD appreciation), industrial composition (AI beneficiaries versus commodity dependents), and demographic profiles (India’s dividend versus China’s burden). Managing a pan-Asian portfolio requires understanding these divergences and positioning for them deliberately rather than taking blunt regional exposure.

2. Japan: The Normalization Experiment

Japan is conducting the most consequential monetary policy experiment in Asia. After decades of ZIRP and QE, the Bank of Japan is gradually hiking rates, with expectations of reaching 0.75–1.0% by mid-2026. The 10-year JGB yield has jumped above 2.3% for the first time since 1998. The Shunto wage negotiations are expected to deliver ~5.5% gains for the second consecutive year, creating a genuine wage-price cycle that Japan has not seen in a generation.

Prime Minister Sanae Takaichi's administration has announced expansionary fiscal measures: abolishing the provisional gasoline tax, raising defense spending, and investing in AI and advanced technologies. The 2026 budget is a record high. This combination of fiscal expansion and monetary tightening is steepening the yield curve and creating a fundamentally different environment for Japanese financial assets.

Our view: Japan's normalization is real but fragile. The BOJ will hike cautiously — we expect the next move around mid-2026 — because inflation is forecast to dip below 2% target on an annualized basis, averaging 1.6% in FY2026. The risk is that yen weakness persists despite rate hikes, reflecting fiscal concerns rather than carry-trade dynamics. Japanese banks and insurers are the clearest beneficiaries through improved net interest margins. The TOPIX target of 3,350–3,400 by year-end feels about right.

3. India: The High-Conviction Structural Story

India remains the fastest-growing major economy in the world at a projected 6.5% for 2026. S&P; upgraded India's sovereign credit rating to BBB from BBB- in 2025. Domestic demand, not exports, drives the growth engine, which provides natural insulation from trade war dynamics. The government's fiscal consolidation and monetary easing cycle create a constructive policy mix.

India's equity market underperformed in 2025 — one of the worst in the region — primarily because both fiscal and monetary policy were tight and Liberation Day tariffs singled India out at a 36% effective rate, among the highest applied to any major economy. This repricing created what we view as a more attractive entry point. The recently concluded India-EU trade deal provides additional structural support.

Our view: India is the highest-conviction long-term structural story in Asia. The combination of demographic dividend, infrastructure investment cycle, digital transformation, and growing domestic capital markets creates compounding opportunities that are genuinely rare in emerging markets. We would overweight financials and domestic demand sectors.

4. South Korea: The Recovery Play

South Korea was the major underperformer in 2025, with GDP growth falling to just 1.1% amid prolonged political uncertainty and trade policy headwinds. The consensus expects a recovery to 1.8% in 2026, driven by domestic consumption revival and the ongoing semiconductor export cycle. But the recovery thesis depends on political stability returning after the constitutional crisis and on the global AI capex cycle sustaining demand for Korean memory chips and display technology.

Our view: Korea is a high-beta cyclical play on the AI semiconductor cycle and political normalization. If both resolve favorably, the market offers significant upside from depressed levels. If either disappoints, the downside is equally sharp. We view Korea as a tactical opportunity, not a structural allocation.

5. The ASEAN Five: Diverging Trajectories

5.1 Singapore

Singapore's economy delivered 5.0% growth in 2025, with Q4 surging 6.9% year-on-year — the strongest quarterly print in years. Manufacturing expanded 18.8% in Q4, led by AI-related electronics. For 2025 as a whole, manufacturing grew 8.7%. MTI has upgraded the 2026 forecast to 2.0–4.0%, citing stronger global momentum and sustained AI-driven demand for semiconductor chips.

MAS maintained its S\$NEER appreciation path in January 2026, with core inflation expected to normalize at 1.0–2.0%. The construction pipeline — Changi Terminal 5, Tuas Port, the North-South Corridor — provides domestic cushion. Enterprise Singapore upgraded its non-oil domestic exports growth forecast to 2.0–4.0% for 2026.

Our view: Singapore is the highest-quality defensive exposure in ASEAN. The key risk is AI capex cycle peaking. Modern services (finance, professional services, infocomm) provide more stable growth than manufacturing.

5.2 Indonesia

Growth projected at 5.0%, steady and resource-backed. The nickel downstream strategy and EV battery investments provide structural support. The domestic market of 270 million consumers is an underappreciated asset. FDI inflows remain strong. Indonesia is a medium-term accumulation story, not a trading opportunity.

5.3 Vietnam

Growth projected at 6.0–6.5%, driven by continued manufacturing FDI and electronics export momentum. The transshipment enforcement risk is the primary concern. The EU free-trade agreement provides market diversification. Attractively positioned but requiring active monitoring of US trade enforcement developments.

5.4 Thailand

Growth at just 1.8–2.5%, the regional laggard. The automotive transition, political uncertainty ahead of the March 2026 election, elevated household debt, and weak tourism recovery from China create a challenging cocktail. We are underweight Thailand.

5.5 Philippines

Growth projected at 5.6%, among the fastest in ASEAN, driven by remittance inflows and domestic consumption. Infrastructure spending under the “Build Better More” program provides fiscal multiplier. An interesting consumption-driven story with limited correlation to the AI/semiconductor theme.

6. Cross-Cutting Themes

6.1 The AI Capex Question

The sustainability of AI-related capital expenditure is the single most consequential variable for Asian markets in 2026. Singapore, Taiwan, South Korea, and Malaysia are directly exposed through semiconductor and electronics supply chains. J.P. Morgan estimates roughly 30% of total AI capex flows to Taiwan and South Korea, driving earnings growth of 12–13% for Asia ex-Japan. Singapore's Q4 2025 manufacturing surge of 18.8% demonstrates the magnitude of this tailwind.

Our view: We expect AI capex to sustain through 2026 but at a decelerating growth rate. The base effects that powered 2025 outperformance will not repeat. We would reduce exposure to pure-play AI hardware and rotate toward domestic demand and services beneficiaries.

6.2 Central Bank Divergence

Asia's central banks are moving in starkly different directions. The BOJ is tightening. The PBoC is easing (described as “moderately loose”). The Fed is expected to cut. MAS is maintaining gradual S\$NEER appreciation. This divergence creates significant FX volatility and carry-trade opportunities but complicates portfolio construction.

6.3 Trade Regime Uncertainty

The US-China trade truce holds at a 47.5% effective tariff rate. India faces a 36% effective rate. Vietnam is under scrutiny. The US tariff rate on Chinese goods means direct export profitability is near-zero, forcing the geographic diversification that produced the \$1.2 trillion surplus. For any Asian economy with significant export exposure, the tariff regime is a first-order risk.

6.4 Demographics as Destiny

India's median age is 28; China's is 39. South Korea's birth rate has collapsed to the lowest in the world. India, Indonesia, Philippines, and Vietnam are on the right side of the demographic divide. China, Japan, Korea, and Thailand are on the wrong side. For multi-year investors, demographic profiles remain the single best predictor of sustained consumption growth, fiscal capacity, and real estate demand.

7. Portfolio Positioning Summary

Overweight: India (structural domestic demand), Singapore (quality defense + wealth management + upgraded 2026 outlook), Indonesia (resource-backed steady growth). These are the economies where domestic drivers provide downside protection against trade volatility.

Market weight: Japan (selective financials exposure), Vietnam (attractive but monitor transshipment risk), Malaysia (semiconductor packaging beneficiary with China oversupply risk).

Underweight: China domestic demand (deflation trap persists), Thailand (structural transition + political uncertainty), South Korea (high beta, requires conviction on AI + political normalization).

Key catalyst to reassess: Chinese demand-side fiscal pivot at scale (upgrade China, upgrade commodities). AI capex deceleration (downgrade Singapore/Korea/Taiwan hardware). US tariff escalation on ASEAN (downgrade Vietnam, reassess Indonesia).

8. Conclusion

Asia 2026 is a divergence story, not a convergence story. The aggregate growth numbers mask dramatically different trajectories driven by domestic policy choices, industrial composition, demographic profiles, and geopolitical positioning. The smart money is not making a “long Asia” bet. It is identifying which Asian economies are structurally positioned for the specific challenges of 2026.

At Darminé Capital, our highest-conviction views are structural long India, quality-defensive Singapore (reinforced by the upgraded 2026 growth outlook), and cautious on Chinese domestic demand. We view the ASEAN reconfiguration as a decade-long theme. And we believe the tariff regime is underpriced as a source of tail risk across the region.

The final observation is epistemological. Asia macro research in 2026 requires humility about prediction and conviction about framework. No one predicted Singapore would grow 5.0% in 2025 when 2.5% was the consensus. No one predicted South Korea would collapse to 1.1%. The specific numbers will surprise. What matters is having the right analytical scaffolding to interpret surprises productively. That is what this paper attempts to provide.

Sources and Further Reading

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