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Upside inflation risks in Asia outweigh downside growth risks

Growth in Asia has proven relatively resilient, but inflation risks are building as elevated energy prices and food supply risks persist. With upside inflation pressures dominating, regional monetary policy is likely to shift further towards tightening

Myeong-dong, Seoul, South Korea. Resilient growth has led us to upgrade our 2026 GDP forecast for Korea

Better-than-expected growth despite energy headwinds

Growth across developed Asia continued to outperform in the first quarter and is expected to remain resilient in the second quarter, driven by factors extending beyond the technology export cycle. This resilience was helped by releasing strategic oil reserves to ease supply shortages, alongside government subsidies that took some pressure off households and businesses facing higher inflation. These factors have helped sustain activity despite elevated energy and geopolitical risks. Against this backdrop, we have upgraded our 2026 GDP growth forecasts for Taiwan and Korea.

At the same time, economies with high dependence on energy imports – most notably India and Singapore – are faring better than expected. In India's case, diversification of crude purchases and increased reliance on multiple supply sources have reduced vulnerability to energy supply shortages. Gas and fertiliser supplies have been secured, limiting spillovers into food inflation and agricultural output. Singapore has similarly benefited from stable energy access and effective policy management, supporting growth outcomes despite elevated import prices.

Inflation spillovers are starting to show up more clearly

The Philippines stands out as a notable outlier, having experienced a significant slowdown in GDP growth. This divergence highlights differences in domestic demand conditions and policy buffers across the region. The Philippines also experienced a sharp rise in CPI inflation, reaching a three-year high of 7.2%. While the increase in transport inflation was largely anticipated amid higher oil prices, the magnitude of the upside surprise was driven by a pronounced acceleration in food inflation. This was compounded by second-round effects stemming from the continued pass-through of elevated global oil prices into electricity, gas, and restaurant prices.

Looking ahead, inflation pressures are likely to pick up. Even if oil supply disruptions ease significantly by June as per our base case, global oil prices are expected to stay high into the third quarter, leaving countries with thinner fiscal buffers. At the same time, rising El Niño risks could keep upward pressure on food prices for longer.

Economies, such as India, which have thus far kept retail gasoline prices unchanged, limiting the impact of oil price hikes, are also likely to see headline inflation edge above the central bank's target by year-end as fuel subsidies ease, particularly if food price pressures also materialise. In Korea, we expect inflation to rise further despite government measures, reaching around 3% as early as June, while steady wage gains are strengthening the case for a Bank of Japan rate hike in June.

Higher rates for most of Asia

Even as GDP growth across developed Asia slows in the second half of the year from a strong first half, upside risks to inflation are likely to dominate. The upward inflation trajectory across most Asian economies – as elevated energy prices persist for longer due to the war – should outweigh the growth drag over at least the next two quarters.

Accordingly, in addition to the rate hikes for Korea and Japan already incorporated into our profile, we are now adding hikes for the Philippines (75bp), Indonesia (25bp), and Taiwan, and pushing out our rate cut in China to the final few months of the year.

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