

May 26, 2026 08:38 PM GMT

Asia Economics | Asia Pacific

The Viewpoint: Marketing Feedback – Addressing Questions From Investors

We address key questions we have received from investors regarding Asia's macro outlook. The questions were mainly tied to the breadth and longevity of this cycle and what level of oil prices will break this cycle. We also highlight areas where we agree and disagree.

Key questions from investors:

- 1) Asia – How broad-based is this industrial super-cycle?
- 2) Aren't Asia's exports just about AI capex?
- 3) Which economies have seen the benefit of this turnaround in non-tech exports?
- 4) So far, the recovery has been K-shaped – is that a threat to the sustainability of this cycle?
- 5) How long can this cycle last? How does it compare with the previous cycles?
- 6) Will a re-escalation of geopolitical tensions in the Middle East break this cycle?
- 7) Which central banks could face the predicament of managing FX with rate hikes in response to higher oil prices?
- 8) China – What is the progress on exiting deflation to entering normalized inflation?
- 9) India – Why is the rupee so weak?
- 10) Japan – Is BOJ behind the curve?

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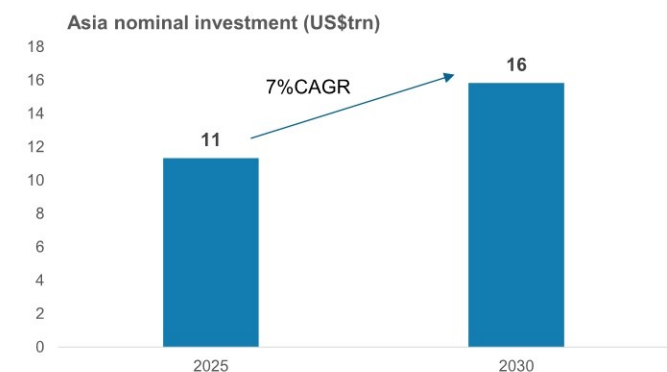
1) Asia – How broad-based is this industrial super-cycle?

Investors perceive this to be just an AI / tech driven cycle: Investors are constructive on Asia, but that is mainly driven by a bullish view on the tech cycle and Asia's role in the global AI / tech supply chain.

Our view – this is broader than a tech cycle: Asia is entering what we think will be its strongest industrial cycle since the mid-2000s, underpinned by a sustained, multi-year rise in capex. The drivers are no longer confined to semiconductors. AI and AI-related infrastructure are important, but energy and energy-transition spending and defense outlays are also key pillars to what will sustain capex spending and the industrial super-cycle. What's more, these will then create second-order demand for other products and create positive spillovers through the supply chain and lead to a broader industrial capex cycle too. At the same time, economies are working to invest to secure their supply chains, which also creates a structural need for rising capex.

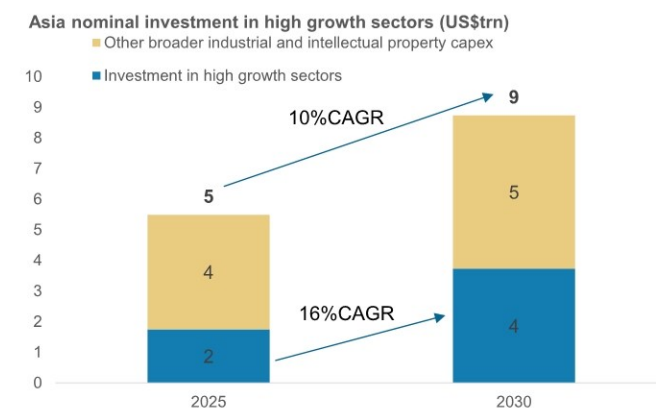
Asia's capex to grow at 3x the pace of 2023-25: We project Asia's capex to rise from US \$11trn currently to US\$16trn by 2030, implying a 7% CAGR, around three times the pace of 2023-25. Total spending in these four high-growth sectors is expected to grow at a 10% CAGR, reaching US\$9trn by 2030.

Exhibit 1: Asia's gross fixed investment to rise to US\$16trn by 2030



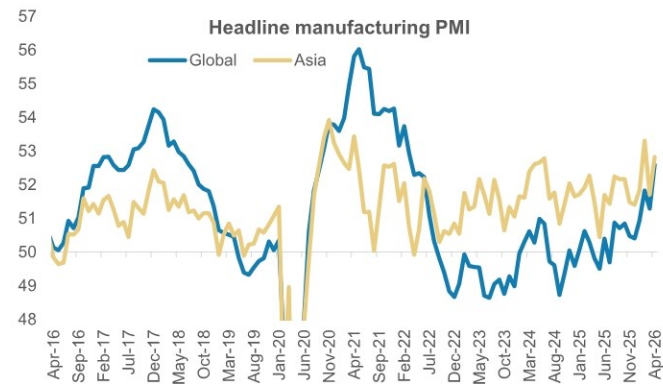
Source: CEIC, Haver, IEA, Lowy Institute, Morgan Stanley Research estimates; Note: *We exclude China's real estate capex given the structural decline in property demand.

Exhibit 2: The rise in capex is to be driven by new structural demand drivers – AI and AI infrastructure spending, energy and energy transition, and defense spending



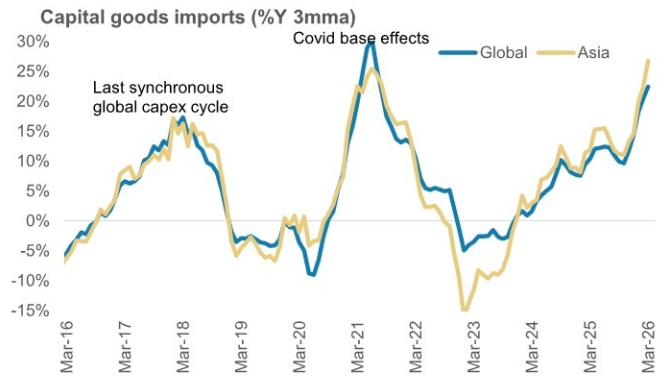
Source: CEIC, Haver, IEA, Lowy Institute, Morgan Stanley Research estimates; Note: *We exclude China's real estate capex given the structural decline in property demand.

Exhibit 3: The breadth is already visible in the data – PMIs have picked up in broad-based manner



Source: Haver, Morgan Stanley Research

Exhibit 4: Capital goods imports growth – the key equipment capex proxy – is accelerating to beyond 2017-18 highs (excluding the pickup in 2021-22 driven by Covid base effects)



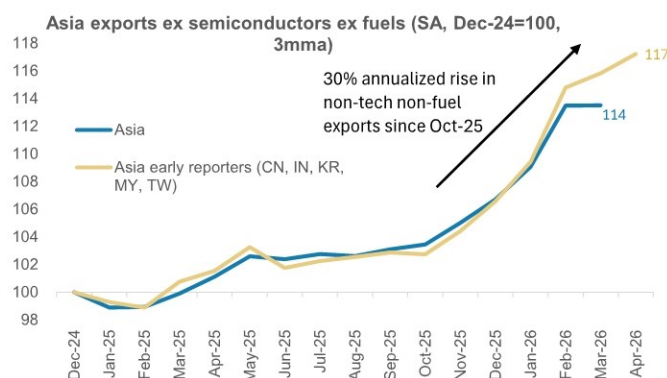
Source: Haver, CEIC, Morgan Stanley Research

2) Aren't Asia's exports just about AI capex?

A 30% annualized jump in Asia's non-tech exports: It was the case that Asia's exports were mainly tech driven for the first nine months for 2025, but from October 2025 to March 2026 the region's non-tech exports have risen at an annualized 25% in US dollar terms. This strength has extended into April. For the select early reporting Asian economies – China, India, Korea, Malaysia and Taiwan (which account for about 66% of Asia's exports) – non-tech exports have risen at an annualized 30% between Oct-25 and Apr-26.

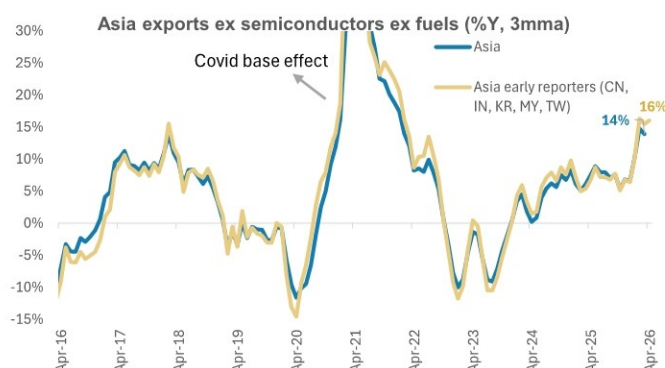
Broad-based rise across product segments: Within non-tech exports, the clearest pickup has been in capital goods and intermediate goods, while consumer goods have also joined in the recovery since Oct-25. Key non-tech exports include ships, networking and telecom equipment, industrial machinery (generators, pumps, and lifting systems), power and electronics components (transformers, motors, capacitors) and construction machinery.

Exhibit 5: A sharp rise in Asia's non-tech exports since October 2025



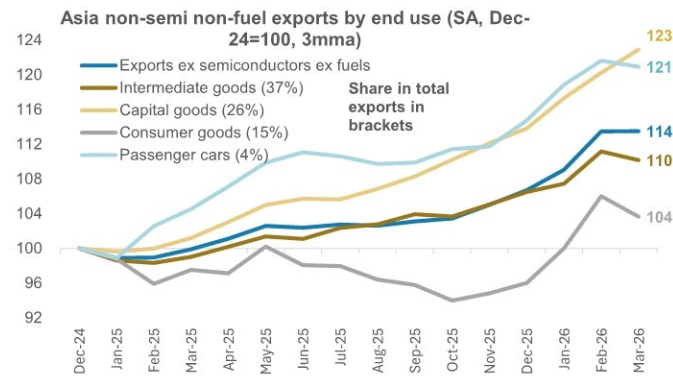
Source: CEIC, Haver, Morgan Stanley Research; Note: Asia includes China, India, Indonesia, Korea, Malaysia, Thailand, Taiwan, Australia, and Japan. Non-tech non-fuel exports have risen at an annualized run rate of 25% (and 30% for the early reporters – China, India, Korea, Malaysia and Taiwan – which account for 66% of Asia's exports) since October 2025 when the US signed trade deals with most Asia economies.

Exhibit 6: Non-tech exports for early reporters in Asia grew at 16%Y in April



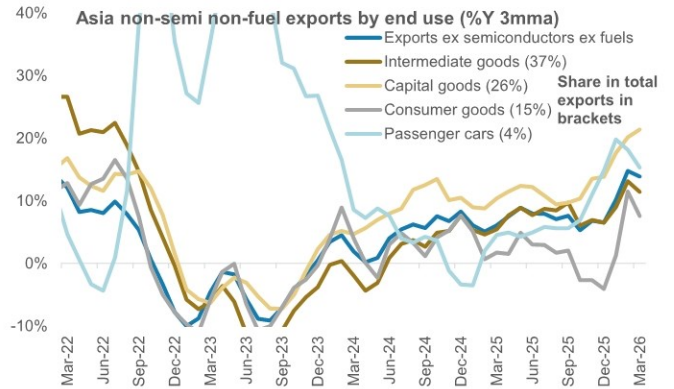
Source: CEIC, Haver, Morgan Stanley Research; Note: Asia includes China, India, Indonesia, Korea, Malaysia, Thailand, Taiwan, Australia, and Japan. Non-tech non-fuel exports have risen at an annualized run rate of 25% (and 30% for the early reporters – China, India, Korea, Malaysia and Taiwan – which account for 66% of Asia's exports) since October 2025 when the US signed trade deals with most Asia economies.

Exhibit 7: The non-semis export recovery has been broad-based across end-use product segments



Source: Haver, Morgan Stanley Research; Note: Capital goods are durable assets used by firms to produce other goods and services, such as computers, machinery and equipment, and transport equipment used in production. Intermediate goods are goods that are processed further or incorporated into final products. Intermediate goods include raw materials (e.g. crude oil, iron ore), processed materials (e.g. steel, chemicals), components and parts (e.g. electronic components, auto parts). We excluded semiconductors and fuels from intermediate goods.

Exhibit 8: Capital goods and intermediate goods drove the first leg of the recovery, while consumer goods exports have also joined in the recovery



Source: Haver, Morgan Stanley Research; Note: Capital goods are durable assets used by firms to produce other goods and services, such as computers, machinery and equipment, and transport equipment used in production. Intermediate goods are goods that are processed further or incorporated into final products. Intermediate goods include raw materials (e.g. crude oil, iron ore), processed materials (e.g. steel, chemicals), components and parts (e.g. electronic components, auto parts). We excluded semiconductors and fuels from intermediate goods.

3) Which economies have seen the benefit of this turnaround in non-tech exports?

Most economies have benefitted from this upswing in non-tech exports: Looking at the indexed trend in non-tech non-fuel exports across the region, most economies have been on this generally rising trend which then accelerated post Oct-25 as we highlighted earlier. For India, non-tech exports had improved between Oct-25 and Jan-26 but have slipped more recently. We attribute this to the onset of geopolitical tensions, as India is one of the more exposed economies which export to the Middle East.

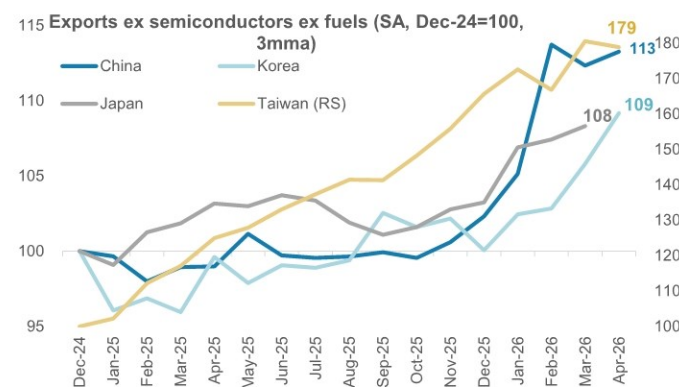
Who will be the key beneficiaries of the industrial and capex super-cycle? While this will be an upswing that will lift all economies in Asia, given the region's inherent strong capabilities in manufacturing, there will still be some economies which will benefit more.

We highlight **Taiwan, Korea, China, and Japan**: They are more exposed to the high growth sectors of AI, energy and defense, and these economies will benefit from a pickup in domestic capex and export opportunities.

India will also benefit – from the pickup in the industrial cycle, alongside a pickup in domestic capex via the boost to domestic demand from easy fiscal and monetary policy. From a market perspective, this also lines up, given that the industrial sector accounts for a larger weight in the respective markets' MSCI indices.

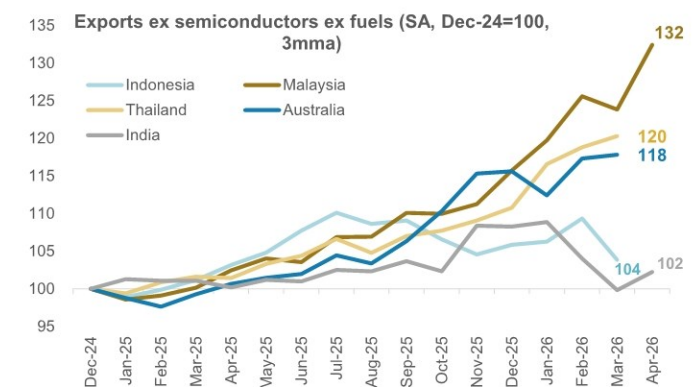
Australia and Indonesia will benefit as commodity exporters: The CRB raw materials index has been moving higher to reach a four-year high, reflecting this industrial recovery.

Exhibit 9: Non-tech exports strength...



Source: CEIC, Morgan Stanley Research

Exhibit 10: ...has been relatively broad-based across economies



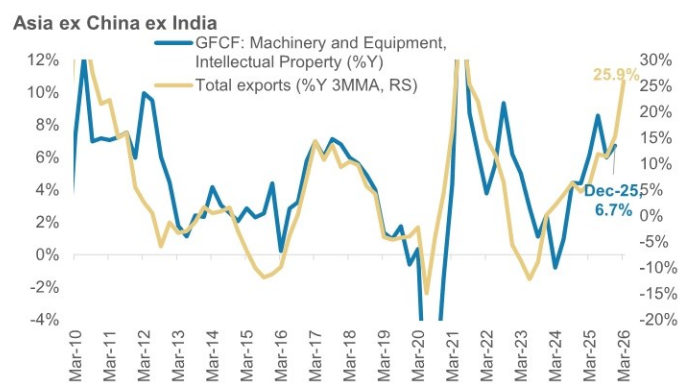
Source: CEIC, Morgan Stanley Research

4) So far, the recovery has been K-shaped – is that a threat to the sustainability of this cycle?

Investors are concerned over a K-shaped recovery: Some investors have expressed the view that the narrow base of the exports recovery is also leading to a K-shaped recovery, especially when you consider the differing trajectories of growth in exports vs consumption. The concern has been that tech exports are capital-intensive and therefore generate limited spillovers to employment, wages and consumption.

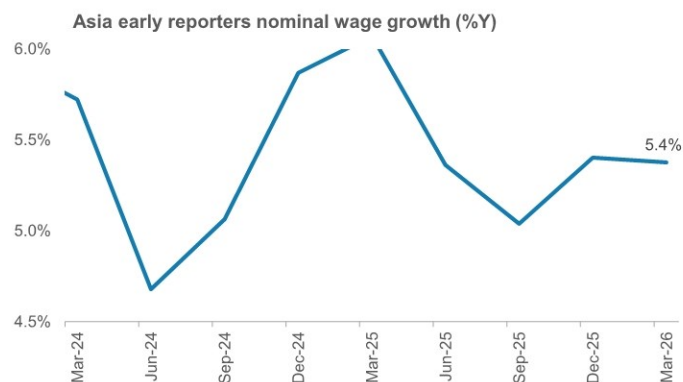
But we are already seeing signs of positive spillovers into capex, labour market and consumption: That was indeed the issue through much of 2025 – exports were strong predominantly due to tech, but labor market conditions were subdued, keeping consumption relatively weak. But the key change since 4Q25 is that non-tech exports have joined the recovery. Because non-tech exports account for about 75% of the region's export basket, this improvement is already starting to show up in improvements in wage growth. Retail sales – the key high-frequency indicator for consumption – have been steadily rising in YoY growth terms since Sep-25. Looking ahead, we expect the strength in both tech and non-tech exports to be sustained, which will create positive spillovers to capex and then help broaden the cycle from exports to domestic demand.

Exhibit 11: Exports are creating positive spillover to capex



Source: Haver, CEIC, Morgan Stanley Research

Exhibit 12: The spillover to the labour market will help broaden the cycle to domestic demand



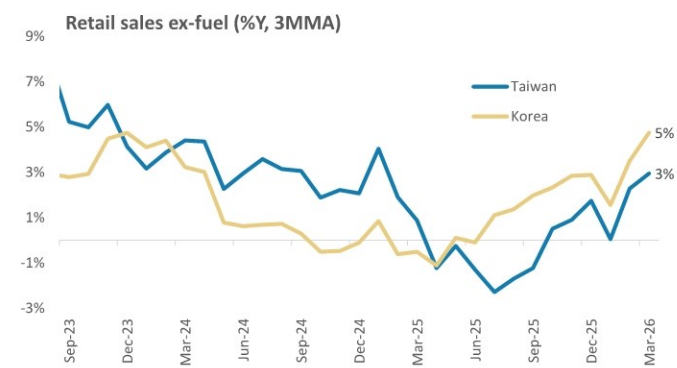
Source: Haver, CEIC, Capitaline, Morgan Stanley Research

Exhibit 13: Retail sales had been picking up in Asia ex China ex India



Source: Haver, CEIC, Morgan Stanley Research

Exhibit 14: Excluding fuel, we see signs of consumption recovery in Korea and Taiwan



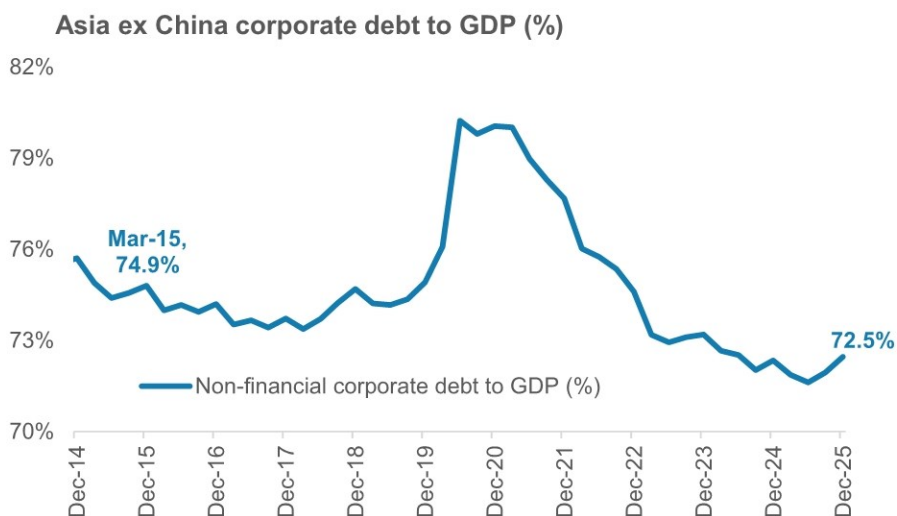
Source: Haver, CEIC, Morgan Stanley Research

5) How long can this cycle last? How does it compare with the previous cycles?

Structural factors are driving this cycle: In assessing the longevity of this cycle, we highlight that this cycle is underpinned by structural factors as we highlighted above and that itself will lend a longer lifespan to the expansion cycle than if it were just driven by cyclical factors.

Duration of expansion will hinge on the health of balance sheets: Moreover, because this will be a capex-driven cycle, we are also looking at the state of corporate balance sheets to help us assess the runway of growth. Asia ex China's corporate debt-to-GDP ratio is now even lower than it was a decade ago. The healthy private corporate sector balance sheets suggest that there is meaningful room available to fund and sustain the private capex cycle. More importantly, it also implies a buffer to mitigate the downside and potential non-linear risks that could result in swings in corporate confidence than prior cycles.

Exhibit 15: Asia's corporate debt-to-GDP ratio is at a decade low



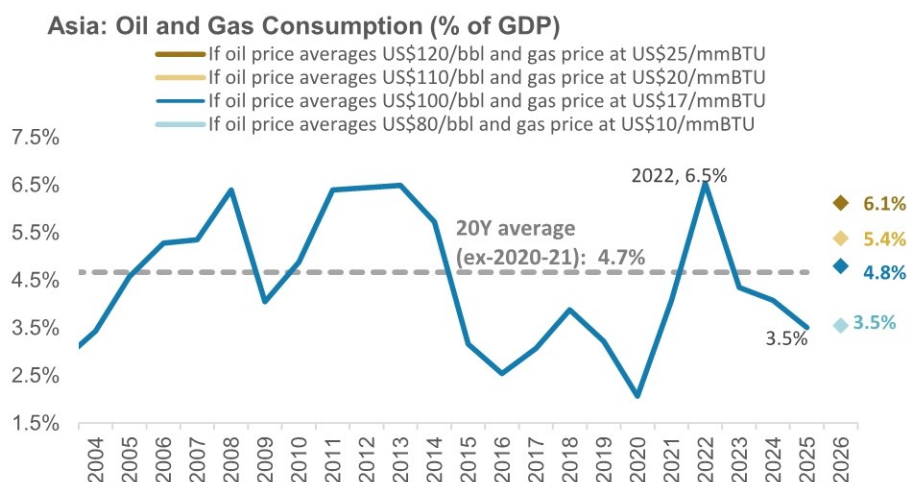
Source: Haver, CEIC, Morgan Stanley Research

6) Will a re-escalation of geopolitical tensions in the Middle East break this cycle?

In our view, the breaking point will be if oil prices are sustained above US\$120/bbl:

The key variables are the level and duration of oil prices, and whether there would be supply disruptions (e.g., LNG constraints, knock-on effects into key industrial inputs). The way we have been looking at this issue is to look at the level of oil burden – which is the oil and gas consumption over nominal GDP – to assess the trend relative to history. By this metric, if oil prices sustain over US\$120, we would expect to see more meaningful damage to the cycle even if it does not break the cycle. In a more severe escalation, with oil above US\$150/bbl, the global outlook becomes recessionary, with demand destruction and supply-chain disruption.

Exhibit 16: If oil and gas prices rise to US\$120/bbl and US\$25/mmBTU, respectively, Asia's oil and gas burden would rise significantly above historical average



Source: Haver, IEA, Morgan Stanley Research forecasts; Note: JKM used for Asia gas prices. IEA forecasts for oil and gas consumption are used for 2026.

7) Which central banks could face the predicament of managing FX with rate hikes in response to higher oil prices?

Who is more exposed? The central banks most exposed are those facing a combination of energy-import dependence, currency sensitivity, a higher starting point of inflation, as well as the rising inflationary pressure imparted by higher energy prices and their second-round effects. In our view, the central banks which are more exposed are the Philippines, Indonesia, India, Korea, and Japan. For EM Asia central banks like BSP, BI and RBI, external balances and FX dynamics are more sensitive to a supply-driven oil shock. As oil prices rise, they tend to create challenges for macro stability in the form of wider current account deficits, which tend to feed into current depreciation pressures and consequently higher inflation. BSP and BI have already hiked interest rates by 50bps each and we expect more rate hikes in the coming months.

For **India**, because this is a supply driven oil price shock, we believe that the RBI will make use of its flexible inflation-targeting framework and will likely be more tolerant of headline inflation rising to the 6% upper threshold of the target range. This is why we expect RBI to remain on hold in 2026.

While RBI won't be pre-emptive, they will still be focused on the second-round effects on core inflation and will react to that. According to our estimates, in 2027, as core CPI ex-gold and silver rises more durably above the 4% target range midpoint, we expect RBI to hike by 25bps each in 2Q27 and 3Q27.

For **Korea**, we expect the BoK to react to the demand-pull pressures to build sufficiently before taking action. As we expect these pressures to be more salient by 3Q26, and we forecast the first hike for Oct-26.

For **Japan**, we had, before the onset of geopolitical tensions, built in a rate hike by the BoJ at the June meeting and we retain that view. But looking further out, our forecasts for the rate path are more gradual than what the market is pricing in as we expect the next hike in Apr-27.

8) China – What is the progress on exiting deflation to entering normalized inflation?

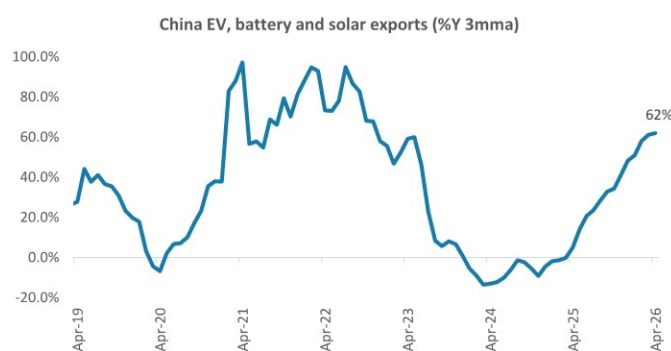
Investors are asking if China is making progress towards normalized inflation:

Investors have asked if the continued strength in China's exports, recent PPI reflation, and better secondary market property transaction data in select tier-1 cities are signs of a sustainable exit from deflation.

Our view – China is moving from deflation to low-flation: We see progress being made as there is a transition from deflation towards low-flation. While headline rates of PPI inflation are improving, this is still mainly driven by a rise in commodity prices. With the strength in exports, we will see an underlying improvement in capacity utilization that will help to lift nominal GDP and wage growth and by extension support consumption. However, for a more sustainable transition towards more normalized levels of inflation, we believe that policy measures will still be needed to support consumption.

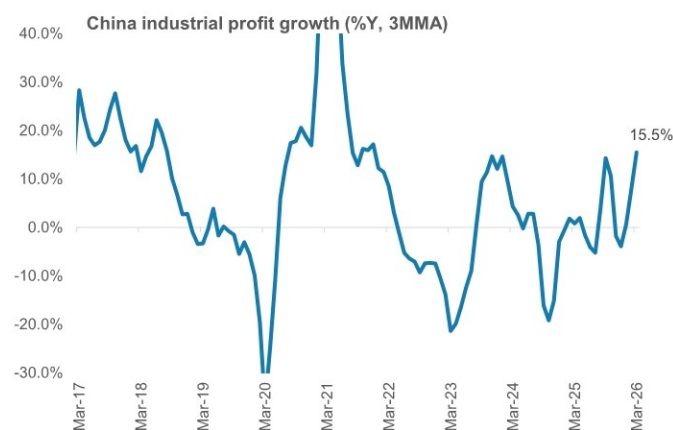
China's strength in exports will help: We see China as one of the key beneficiaries of the upswing in the industrial and capex cycle given it is positively levered to a pickup in both export opportunities and domestic capex in the high-growth sectors of energy and energy transition, defense, and AI and AI infrastructure. On a 3M trailing basis, China's exports in the key products of solar products, EVs and lithium batteries have increased 62%Y in April, vs. 48%Y in Dec-25. March industrial profit growth also picked up to 16%Y, partly reflecting higher upstream sector profit margins but also stabilization in non-commodity sector margins as well.

Exhibit 17: China's exports in the key products of solar products, EVs and lithium batteries have increased 62%Y in April on a 3M trailing basis



Source: Haver, CEIC, Morgan Stanley Research

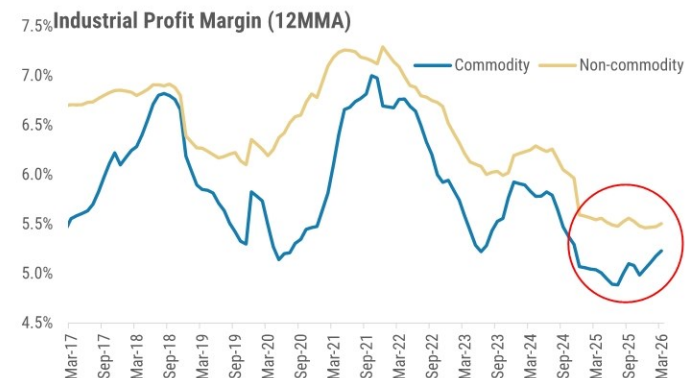
Exhibit 18: March industrial profit growth picked up to 16%Y...



Source: Haver, CEIC, Morgan Stanley Research



Exhibit 19: ...reflecting higher upstream sector profit margins but also stabilization in non-commodity sector margins as well



More data needed to verify the property sector rebound: One of the key variables in the broader domestic demand recovery remains the stabilization in the property sector. On this, our China property analyst Stephen Cheung *believes* that the recent rebound in secondary property market sales suggests the worst has passed in select high-tier cities and sales in cities with recent easing measures may stay robust in 2Q. However, he also highlights the narrow nature of the rebound (in particular around older, smaller lump-sum properties in higher demand districts), and growth in other cities has already shown signs of rapid deceleration in the past few weeks. As such, he is awaiting further signals before turning more constructive on the sustainability of the recovery. In particular, more housing stimulus and further mortgage rate cuts are needed for a more constructive outlook given still-soft labor market conditions, fragile home-buyer sentiment and still-falling rental rates.

Exhibit 20: Slower pace of fiscal easing likely led to weaker near-term data

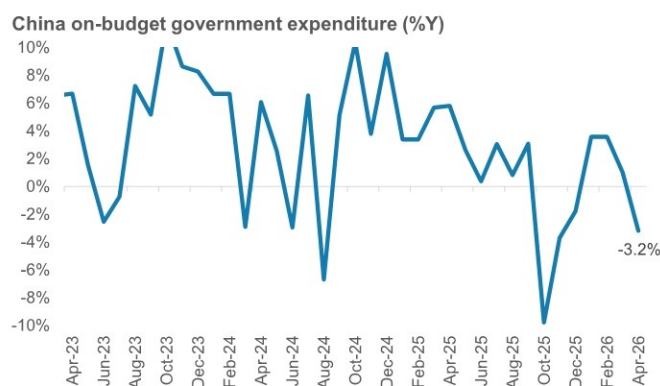
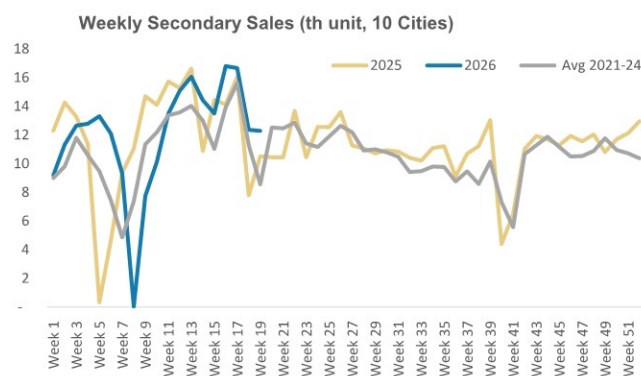


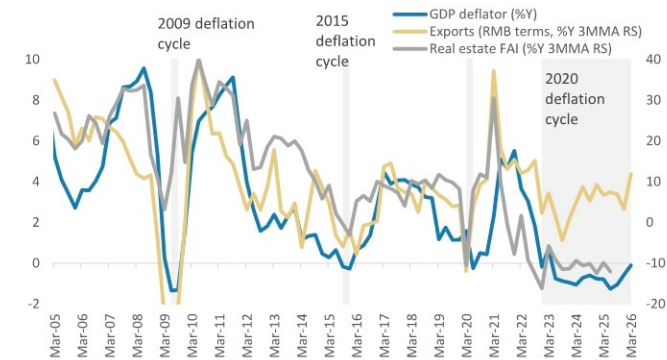
Exhibit 21: More data needed to verify the property sector rebound



Watching for signs of broader reflation beyond cost-push factors: Our China economics team now sees the GDP deflator sustaining its positive growth trend and averaging 0.5%Y in 2026, with CPI averaging 0.8%Y and PPI at 1.5%Y. For China, considering the starting point of excess capacity and disinflationary pressures, we think that the strength in exports will first show up in improving capacity utilization, which will then reduce deflationary pressures and improve nominal GDP growth. As that unfolds, corporate

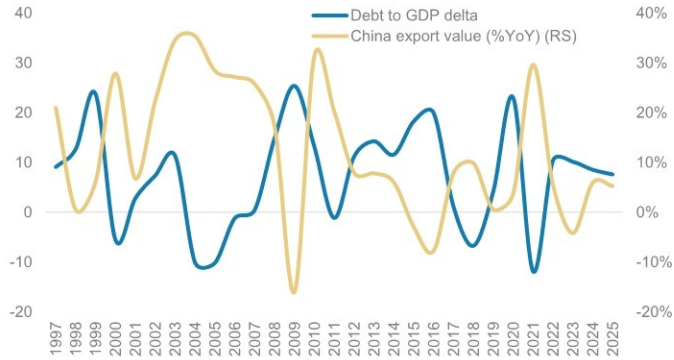
revenue growth picks up, followed by wage growth. Meanwhile, job creation should improve with a lag, as companies will first utilize the slack in their capacity before looking to start hiring.

Exhibit 22: In past cycles, exports and reflation went hand in hand



Source: CEIC, Haver, Wind, Morgan Stanley Research

Exhibit 23: Stronger external demand environment enabled policymakers to pull back on policy easing and deleveraging



Source: CEIC, Haver, Wind, Morgan Stanley Research

9) India – Why is the rupee so weak?

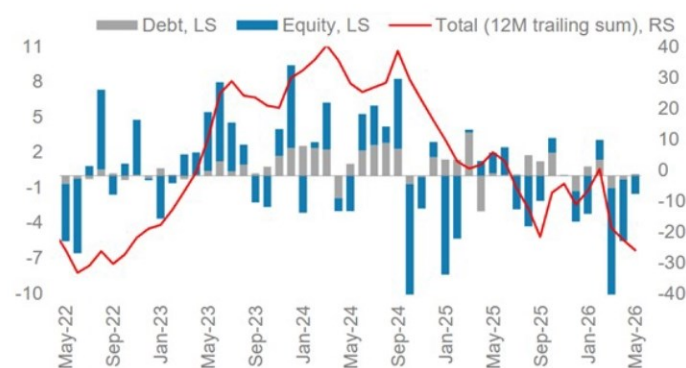
Rupee has been one of the weakest Asian currencies: Year-to-date, the INR has depreciated by 5.8% vs. the US dollar, and is one of the weakest Asian currencies. In our view, the key reason for this is weaker balance of payments dynamics. Net capital inflows have been affected by the relative underperformance of earnings growth while there are concerns about the current account deficit widening as a result of the energy shock.

India's relative growth story has become less attractive: Prior to the energy shock, corporate India had seen decelerating earnings growth in earlier quarters. While the earnings growth was showing signs of improvement, the year-to-date strength in other regional markets more levered to the AI thematic, including Korea and Taiwan, has led to a reduced attractiveness of the growth differentials. 1Q earnings growth in India was at 11%Y, but Korea, Taiwan and US earnings growth rates were much higher at 245%, 48% and 27%Y respectively.

India is also one of the more exposed economies to the energy shock: Within the region, India's relatively wider oil and gas trade deficit at the starting point has posed headwinds. Pre-energy shock, India's oil and gas trade deficit was 3.6% of GDP, and accounted for US\$127bn of the US\$334bn overall trade deficit on a 12-month trailing basis. Our India economics team expects the current account deficit to widen to 1.8% of GDP in F27 from a deficit of 1% in F26.

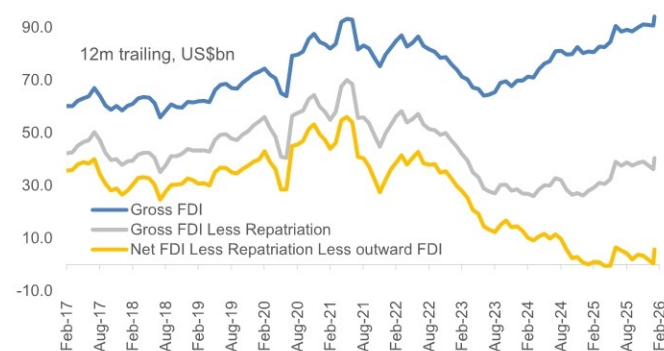
Both these concerns were reflected in weaker BoP dynamics: From an FII flows perspective, investor confidence was just beginning to show signs of recovery at the start of the year as the US-India trade deal provided relief from tariffs. Flows briefly turned positive in February before the energy shock hit and outflows resumed. While there have been fairly persistent FII outflows, the domestic bid for equities has been strong. Relatedly, there has also been less favorable net FDI inflows, weighed down by continued outward FDI flows and repatriations amid PE/VC exits against a backdrop of a strong deal pipeline. These factors have combined to take the INR on a REER basis 3.7 standard deviations below the trailing 10-year mean.

Exhibit 24: FII has recorded outflows in the past three months



Source: RBI, CEIC, Bloomberg, Morgan Stanley Research

Exhibit 25: Net FDI has been depressed amid outward FDI and repatriations



Source: RBI, CEIC, Bloomberg, Morgan Stanley Research

Investors are asking what can be done to augment capital flows: In our base case, we

expect oil prices to come down and that will help alleviate some of the concerns over the current account deficit. However, the capital outflow situation was an issue before the oil shock and will likely remain so, prompting investors to ask what policy measures can be taken up to augment capital flows.

We'd highlight four possible policy measures:

First, the use of the NRI deposit scheme. This tool had been successfully utilized during the taper tantrum episode. However, considering that the spread between US and India rates are narrower this time around, this scheme may not be as attractive enough to fully augment the needed capital flows.

Second, asking corporates to raise external commercial borrowings while providing the corporate with the FX hedge.

Third, reduce or remove the withholding tax that investors have to pay on their debt investments.

Fourth, reduce the capital gains tax for foreign investors.

10) Japan – Is BOJ behind the curve?

Both we and consensus expect a rate hike in June: Our Chief Japan Economist Takeshi Yamaguchi continues to expect BOJ to hike at the upcoming June meeting. He notes that the three dissents from board members for a rate hike at the April meeting, alongside a significant upward revision to inflation forecasts in the April outlook report and the emphasis on upside inflation risks in the Governor's press conference all suggest BOJ is inclined towards a June rate hike (see [April MPM Review: A June Rate Hike Hinges on Middle East Developments](#), Apr 28, 2026).

But the path beyond June is the subject of debate: Post-June, Yamaguchi-san forecasts one further rate hike in April 2027, bringing the policy rate to 1.25%. In contrast, markets have currently priced in over a 90% probability of another rate hike by end-2026 – and expects BOJ to deliver two more hikes in 2027, lifting the policy rate to 1.75% by end-2027.

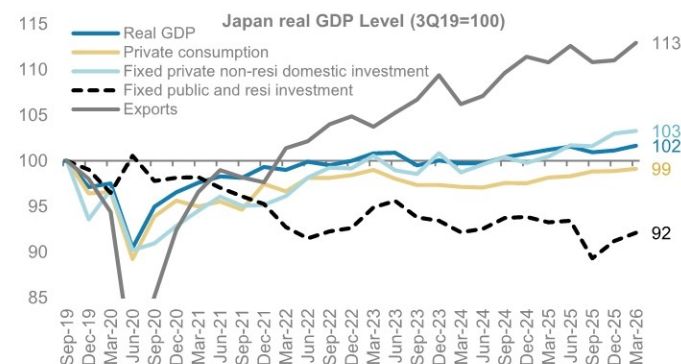
Reasons why we expect less hikes than the market:

First, the strength of domestic demand. Overall GDP is just 101% of pre-covid levels and crucially real private consumption remains below its pre-covid level. Our Japan economics team [expects](#) sequential growth to soften to -0.7%Q SAAR in 2Q26 (vs. 2.1% in 1Q), before recovering to 1.2% in 1Q27, which suggest that there will be limited demand-pull pressures on inflation.

Second, while nominal wage growth has improved, real wage growth has been subdued. Moreover, the momentum in this year's Spring wage negotiations bears watching. In past years, the aggregate base pay increase tends to decline with each response tabulation round, as more lower-wage-hike unions report. However, this year's pace of deceleration has been sharper than in past years, with the base pay increase declining from 3.85% in the first tally to 3.53% in the fourth tally (see [Japan Economics: Mar Monthly Labour Survey: Solid Wage Growth Intact; Sentiment Deterioration Warrants Caution](#), May 8, 2026).

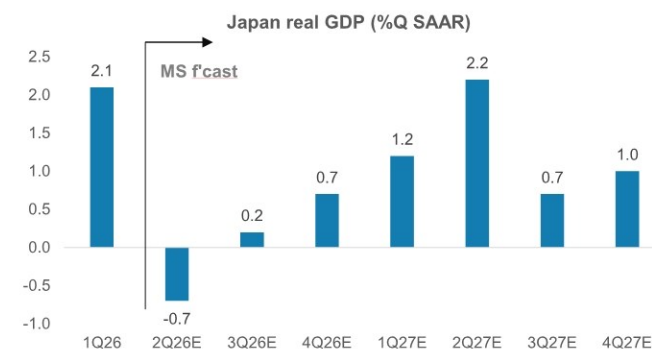
Third, uncertainties related to the energy shock. Our Japan economics team sees some near-term growth headwinds from higher energy prices, with weaker terms of trade and supply tightness in areas such as construction and naphtha-related products.

Exhibit 26: Private consumption remains below pre-covid level



Source: Haver, Morgan Stanley Research

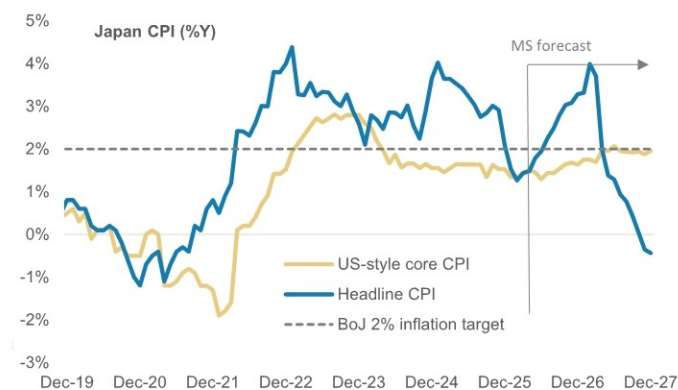
Exhibit 27: Our Japan Economics team expects Japan's sequential growth to gradually recover



Source: Haver, Morgan Stanley Research forecasts

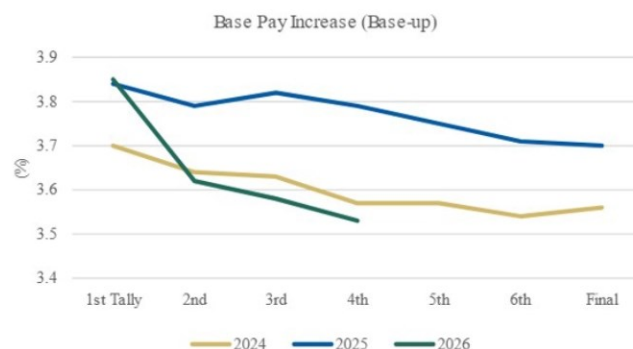
Indeed, underlying inflation has not shown significant upward momentum. April CPI – after adjusting for special factors – is still relatively benign at 1.7%Y. More importantly, April services inflation – the usual month of the year when many Japanese firms adjust their service prices – remains subdued. Overall, we see the rise in US-style core CPI as more gradual, only reaching 2% by Apr-27. While we do expect the transmission from higher wages to prices to take hold, given the current backdrop, we think that the BOJ will take a more cautious approach in assessing these dynamics but looking to raise rates further.

Exhibit 28: Inflation trajectory not yet factoring incoming government subsidies, we see a more gradual rise in underlying inflation



Source: Haver, Morgan Stanley Research forecasts

Exhibit 29: 2026 Spring wage negotiations: This year's base pay increase has decelerated at a faster pace than in past years through tabulation rounds



Source: Rengo, Morgan Stanley Research

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