Executive Summary

The outlook for Asia and the Pacific is being shaped by three major factors: the energy shock arising from the conflict in the Middle East, the AI-driven technology boom, and continued trade reconfiguration. The region overall has shown resilience so far. However, the effects are uneven across the region, and even within economies, where tech-related sectors are benefiting more than other parts of the economy. Furthermore, buffers are not unlimited and, going forward, the resilience is likely to be tested.

- Large economies have mitigated disruptions from the oil shocks through inventory drawdowns, diversifying energy sources, and substituting toward alternative energy inputs, supplemented by other policy support. By contrast, many low-income, agricultural, and Pacific island economies have been harder hit, by higher fuel, transport, electricity, and fertilizer costs, despite policy support, intensifying cost-of-living pressures and straining public finances.

- The AI-driven technology boom has provided an important offset for economies in East and Southeast Asia, although the evolution of AI investment and its long-term economic effects are uncertain. Strong global demand for semiconductors, AI infrastructure, and related technology products has boosted exports and investment, particularly in economies integrated into technology supply chains.

- Robust intra-Asian trade, supported by expanding trade agreements, and growing services exports have also reinforced the region's resilience, despite elevated tariffs and export restrictions.

As a result, aggregate regional growth in the first half of 2026 has outperformed earlier projections, but has been uneven across economies. Regional growth is expected to moderate from 5 percent in 2025 to 4.8 percent in 2026, up from 4.4 percent in our April forecasts. Growth projections have been revised up sizably for those benefitting from the ongoing technology boom—notably Korea and several ASEAN economies—and also for China, India, and Japan. Downward revisions have been seen in countries facing higher inflationary pressures without gains from the technology boom, particularly low-income and Pacific Island economies.

Risks remain tilted to the downside. A prolonged conflict in the Middle East could sustain high energy prices. A correction in AI-related investment or asset valuations could weigh disproportionately on Asia given its central role in global technology supply chains. Higher global sovereign yields could spill over to regional bond markets and worsen fiscal vulnerabilities. In addition, a severe El Niño episode could disrupt agriculture, fisheries, and hydropower generation, adding to food and energy inflation. Conversely, stronger productivity gains from AI and deeper trade integration could provide upside potential.

Policies should balance near-term stabilization with rebuilding buffers. Monetary policy should remain focused on price stability and respond promptly where inflationary pressures become more persistent. Fiscal policy should prioritize preserving sustainability while protecting vulnerable households . Targeted and time-bound fiscal measures are preferable to broad-based fuel subsidies or price controls, which can be more costly and weaken price signals and incentives to reduce demand. Supervisors should remain vigilant to market and technology-related risks. Over the medium term, labor market reforms, stronger social safety nets, deeper services trade integration, investment in digital infrastructure and skills, and enhanced energy security will be critical to sustaining growth and promoting a more resilient and inclusive growth model.