Crédit Agricole CIB Research

China: a tale of two economies

CRÉDIT AGRICOLE
CORPORATE & INVESTMENT BANK

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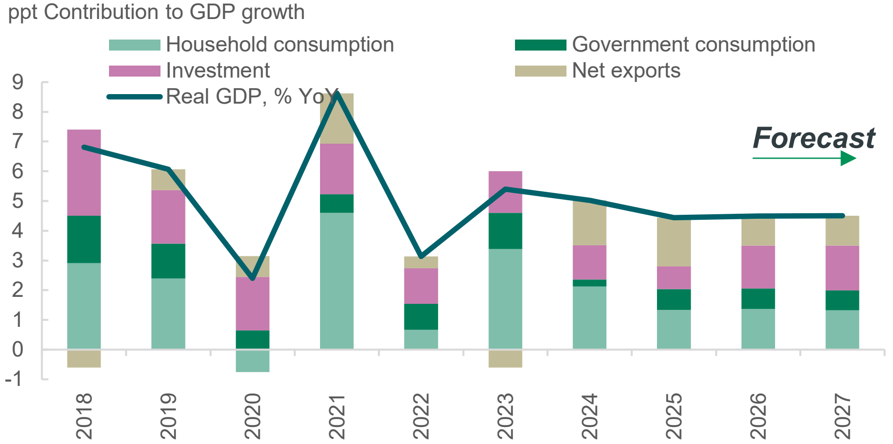
China: the growth imbalance

Tech resilience and demand fragility

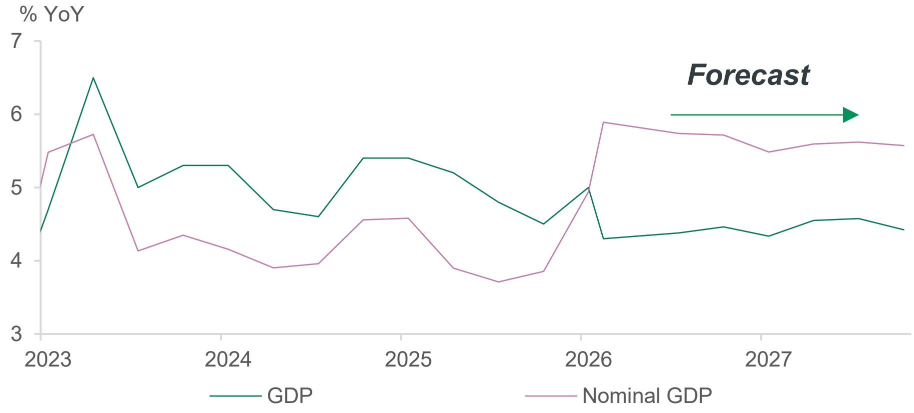
- China is playing a leading role in global AI development and has benefited from the global AI super cycle
- Rapid growth is concentrated in AI related supply chain. General weakness in domestic demand remains, with property sector as the primary drag. Elevated energy and raw material prices put higher cost pressures on mid-to-downstream sectors
- Growth could stabilise, driven by a turnaround in infrastructure investment while tailwinds from the AI boom continue. Property drag becomes smaller over time
- We expect 2026 and 2027 GDP growth to ease to 4.5% from 5.0% in 2025

Incremental policy easing to boost domestic demand



Tech related sectors outperformed

Only a modest growth rebound expected in H226



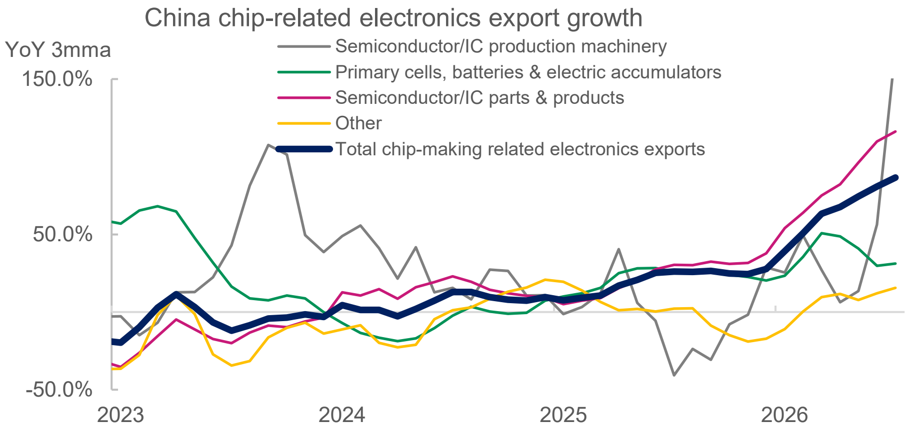
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: expanding role in the global AI supply chain

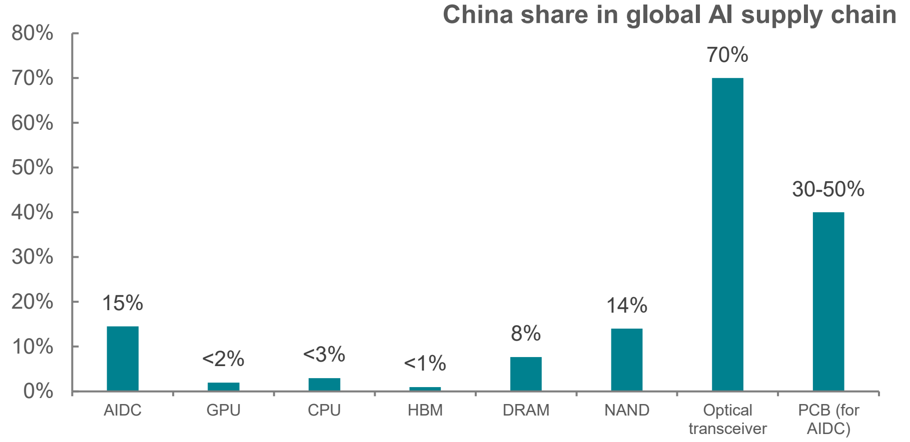
Global AI boom and China's expanding role in AI supply chain

- China has increasingly become a leading player in global AI development, as it plays a rapid catch up with the US
- China leads in AI patents and is rich in research, talent and data. Its AI models are rapidly grabbing global shares with its open source and cost efficiency. Empowered by a strong manufacturing base and vast market application, acceleration of AI adoption will drive China's capex and fosters productivity gains in the medium term
- The global AI boom has been benefiting China's related exports, in upstream raw materials and mid-stream components and machinery & equipment

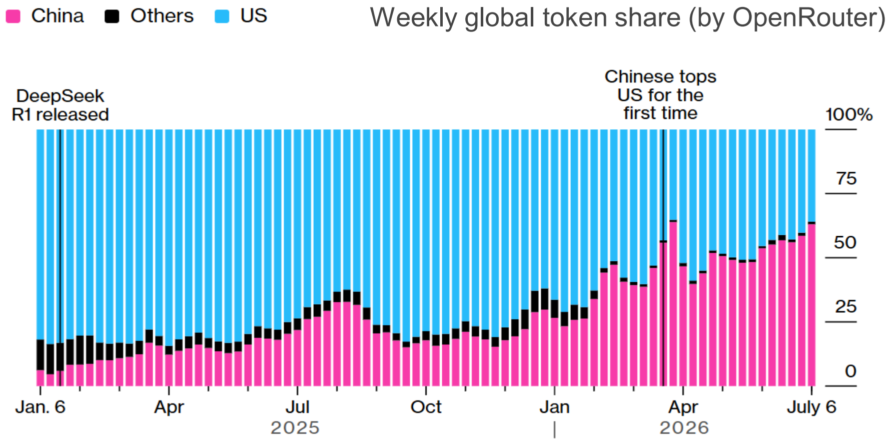
Rapid expansion of chip-making related exports



China's share in global advanced chips still small but with potential



China is leading in the open-source AI race



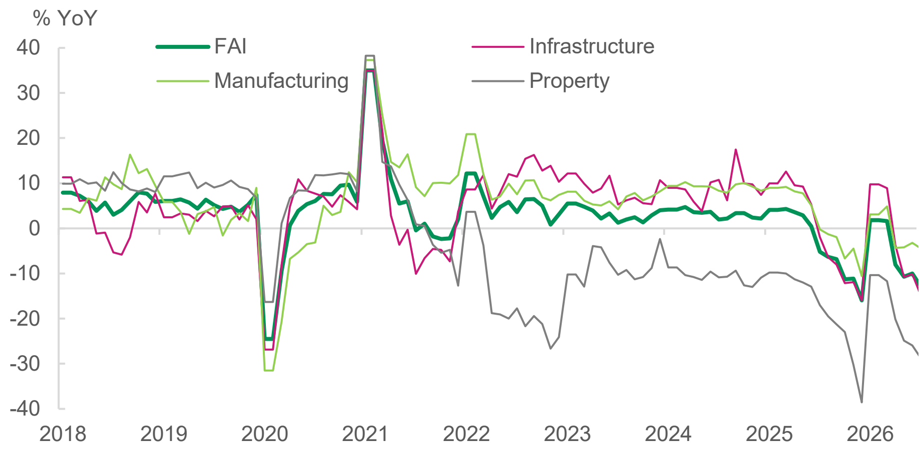
Source all charts: CEIC, China Customs, OpenRouter, Crédit Agricole CIB

China: broad domestic demand weakness despite selected bright spots

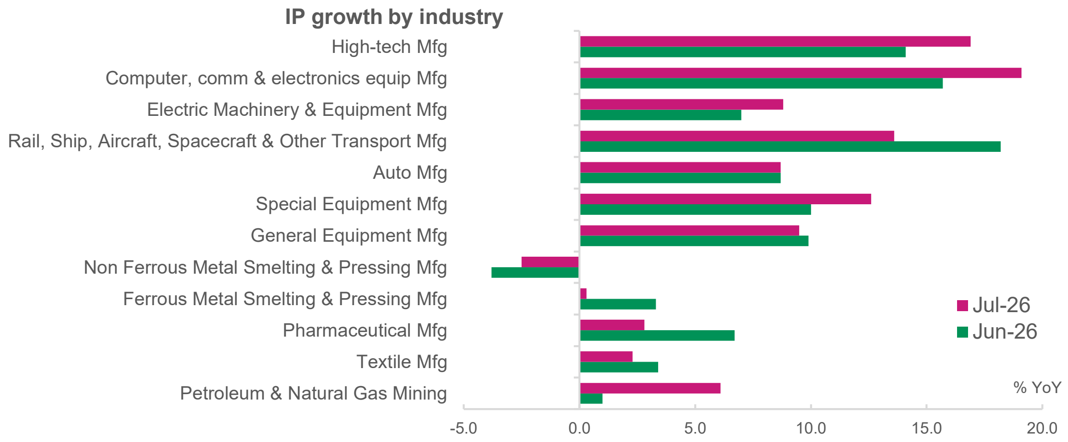
Export-driven production stayed solid amid weak domestic demand

- Growth divergence has remained apparent, with the global AI capex demand strength supporting trade and related manufacturing activities, with limited spillover to the non-tech sectors and household sector
- Growth could modestly improve in H2, as policy easing picks up, weather disruptions fade and favourable YoY base effects kick in, but a strong growth rebound is unlikely without major demand stimulus

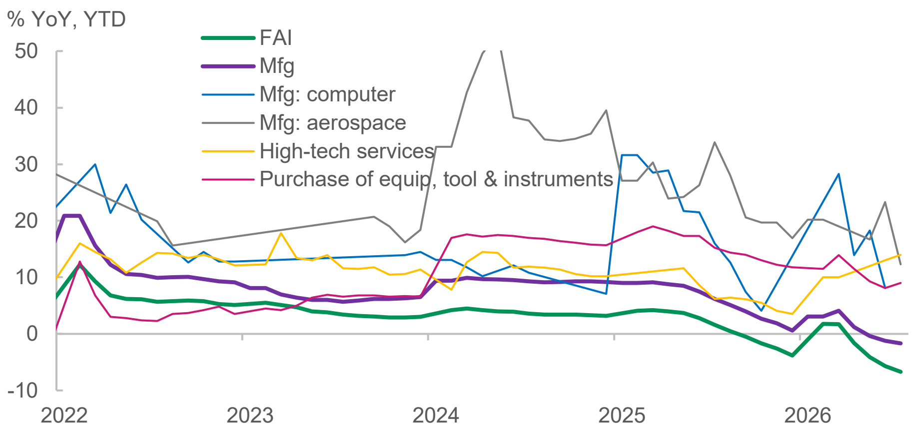
FAI further declined across the board…



IP growth underpinned by tech related strength



…despite selected strength in high-tech FAI



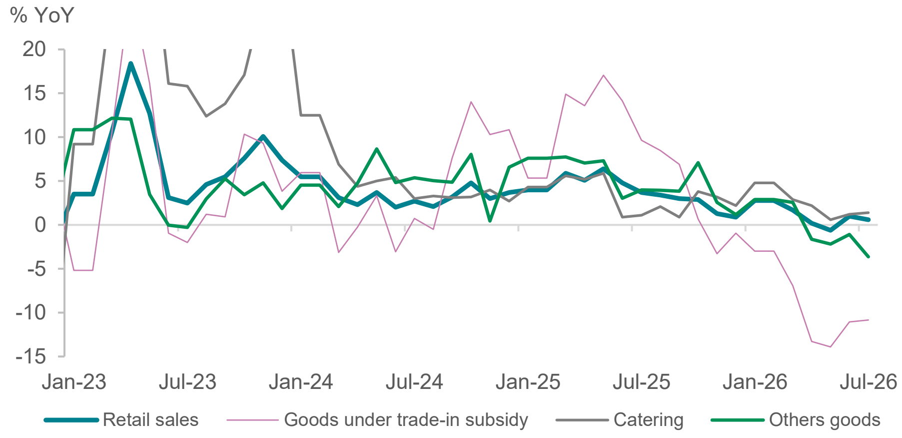
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: subdued retail sales growth

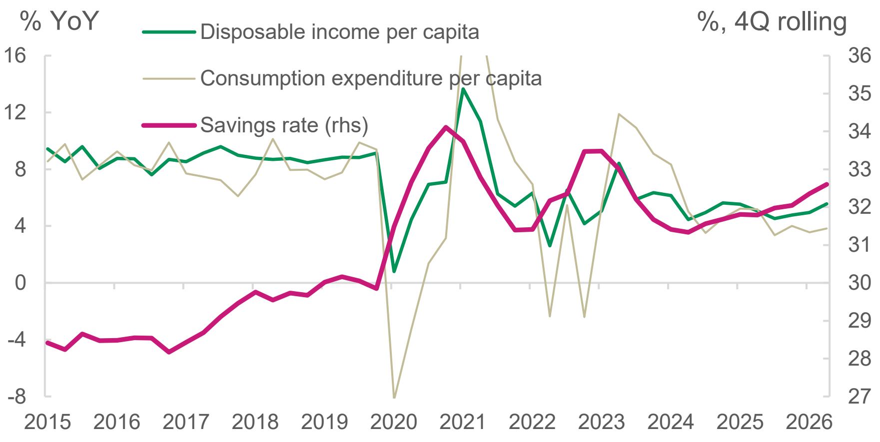
Bumpy road for domestic consumption with uneven growth recovery

- Retail sales growth has significantly slowed alongside subdued domestic demand, while government trade-in subsidies have been scaled back
- The Ministry of Commerce has targeted retail sales of consumer goods to reach RMB60trn by 2030 (CAGR of 3.7% in 2026-30), which is a challenging target without material demand-side stimulus measures
- China has ramped up support for services consumption so as to stabilise the labour market, while the still-insufficient social safety net would remain a drag

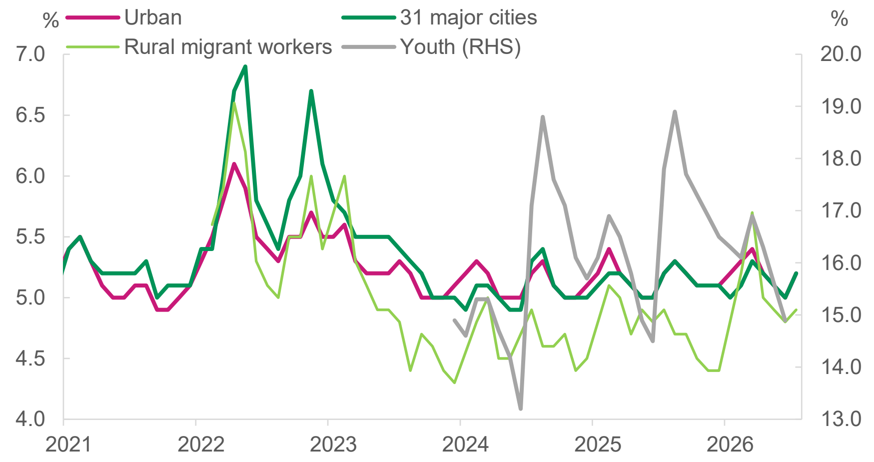
Retail sales growth reflected subdued domestic demand



Household savings rate has been grinding higher since 2024



Largely stable unemployment rate, but higher among youths



Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

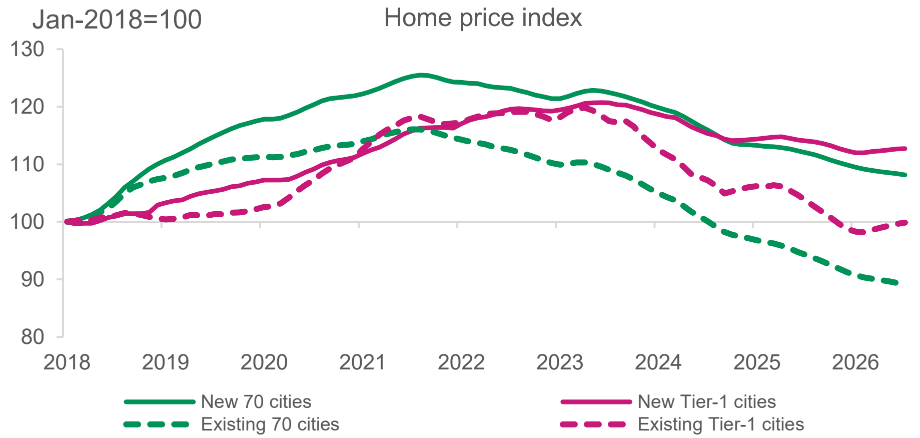
China: property market remained a drag, but not a risk

De-risking and de-stocking are prioritised over reviving

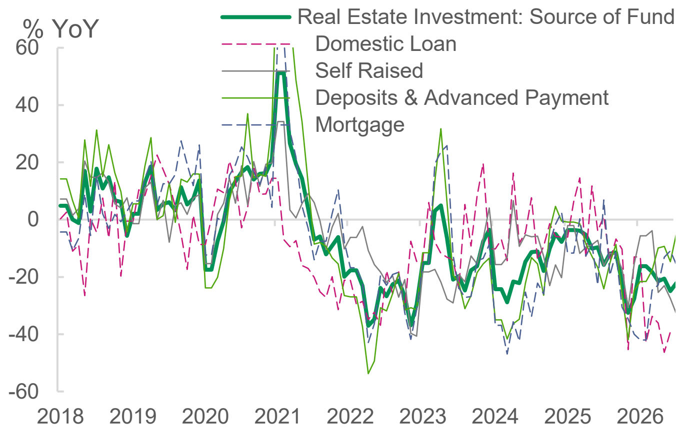
- China's property market remains in a deep, multi-year downturn
- China's government recently rolled out a slew of policy measures to stabilise the property market, but without direct demand stimulus. These include an extension of mortgage duration, support of developers' funding, as well as guiding home sales of completed units from pre-sales model
- China has largely controlled the systemic risks to the banking system stemming from the ongoing property downturn, while household consumption and local government fiscal resources remain constrained

Major property indicators remained in contraction

Home prices continued declining nationwide despite a rebound in tier-one cities



Widening contraction of property source of funding



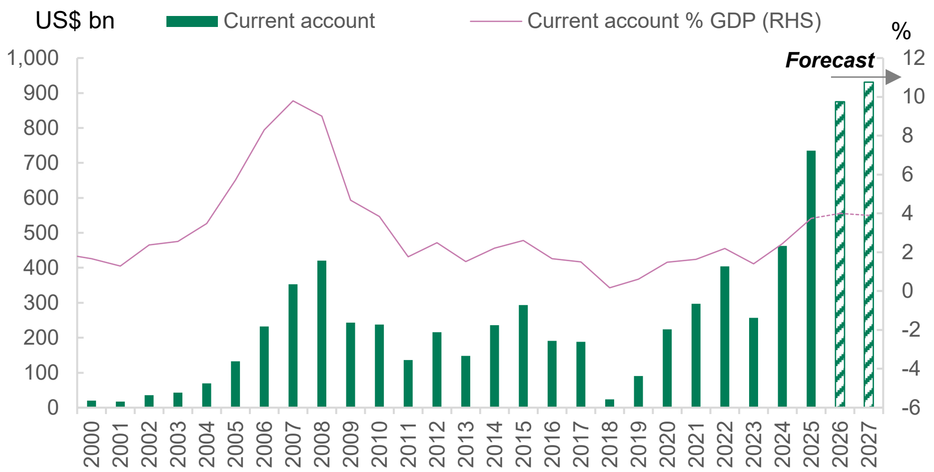
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: likely wider current account surplus in 2026-27

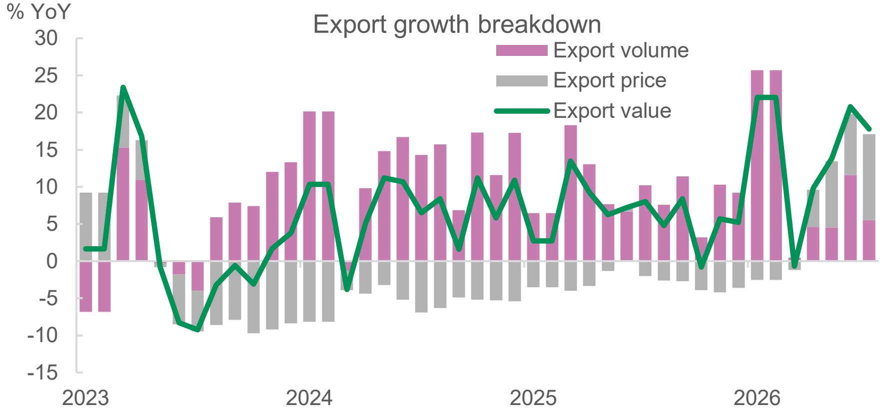
Current account surplus to remain sizable on growth imbalance

- We expect China's current account surplus to increase to 4.0% GDP in 2026 and 3.9% GDP in 2027 from 3.7% in 2025
- It reflects China's continued growth imbalance: external demand for Chinese manufactured goods remains resilient, while domestic demand has stayed weak amid the prolonged property-market correction and limited demand-side stimulus
- We forecast China's export and import growth will accelerate to 18.0% and 25.0% respectively in 2026 before some moderation in 2027. However, net exports are expected to contribute only 1.0ppt to real GDP growth, down from 1.6ppt in 2025, with import volumes rebounding more notably from the very weak level in 2025

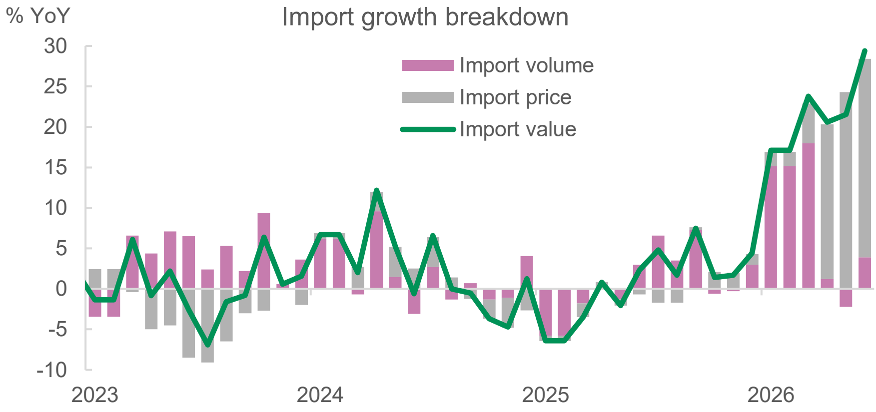
Wider current account surplus expected in 2026-27



Both volume and inflation contributed to export growth



Import prices have risen faster than export prices



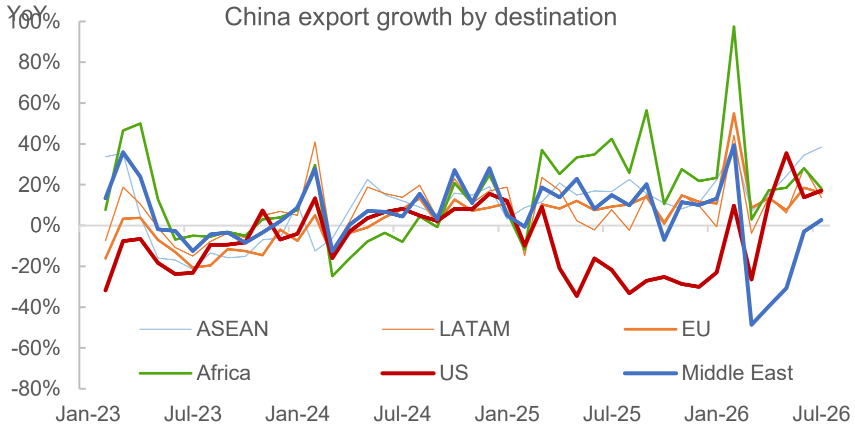
Source all charts: CEIC, China Customs, Crédit Agricole CIB

China: still solid exports so far on tech and green products

Exports surged on global AI demand, K-shaped export performance

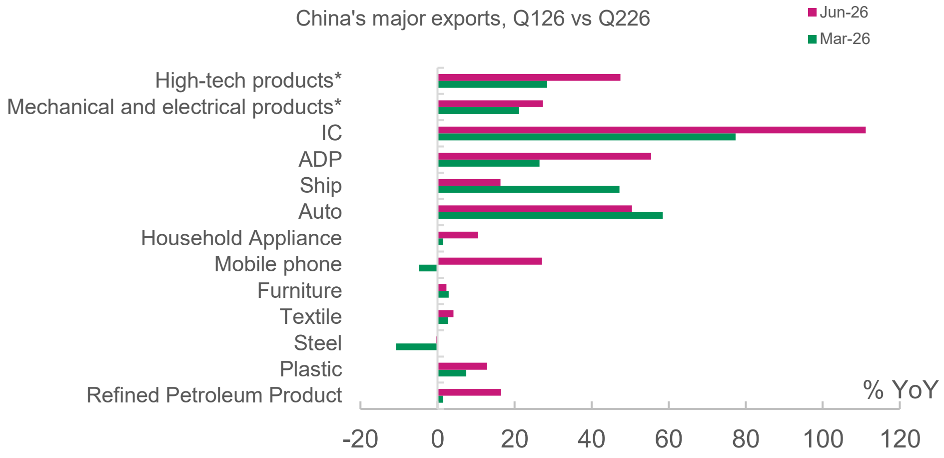
- China's exports showed solid growth led by AI-related products in 2026 so far. The K-shaped export performance between tech and non-tech sectors was similar to Korea and Taiwan – strong headlines support earnings and trade balances but may not translate into broader growth or employment
- Asian manufacturing supply chains, continue benefiting from the global AI boom and hyperscaler capex, though risks remain from potential Middle East escalation affecting semiconductor supply chains and energy prices

China's exports to the GCC improved from the weakest period

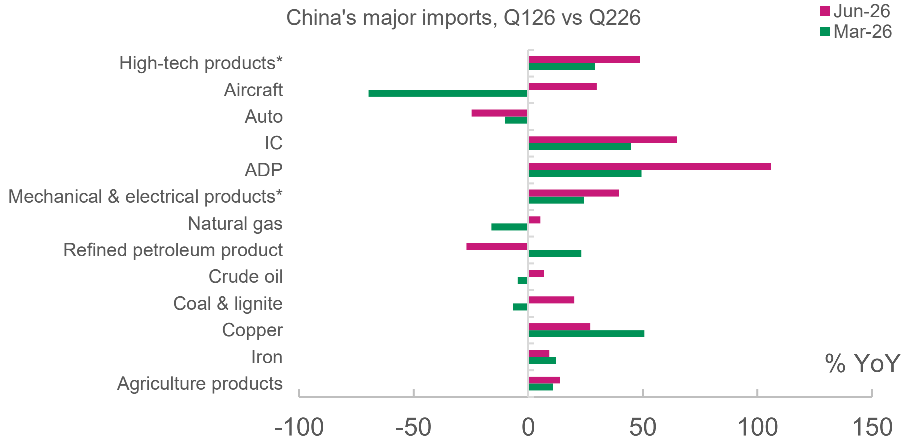


Source all charts: CEIC, China Customs, IMF, Crédit Agricole CIB

Tech and green products supported export growth



Tech import growth offset energy import decline



**High-tech products accounted for 25% of China exports, and mechanical and electrical products accounted for 61% of China exports in 2025*

China: second Trump-Xi summit seeks stability amid flare of tensions

24 September meeting a chance to build on positive May summit

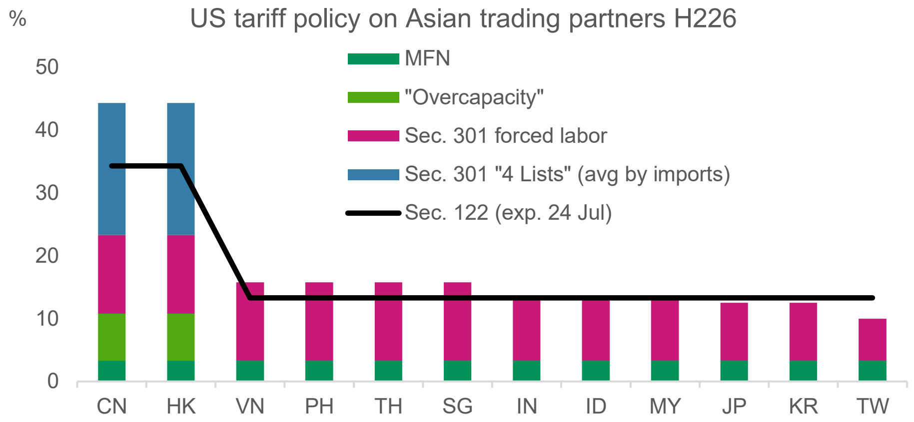
- A Chinese business delegation may join President Xi Jinping, opening opportunity for the leaders to discuss the Board of Trade's mutual tariff cuts (USD60bn total, c.10% of bilateral trade) or the Board of Investment
- Preparatory discussions hint at mutual desire to extend Busan truce (expires 10 November). The agreement limited reciprocal tariff actions and suspended China's harsh 0.1% affiliate rule for critical mineral export controls

Trump administration rebuilds tariff wall, expands tech restrictions

- On 24 July, the US imposed 12.5% tariffs on China under Section 301 "forced labor". There are also reports that the US is set to impose another 7.5% "overcapacity " tariff on Chinese goods ahead of the Trump-Xi summit, which would restore total second-term duties to around 20%
- US announced several key technology restrictions on China over the summer including: an Executive Order banning foreign electronic equipment for US bulk-power systems, several Federal Communication Commission's (FCC) "Covered List" import bans (drones, some humanoid robots, power inverters and potentially data centre components), and new Section 232 tariffs/import price floors on polysilicon

Source all charts: US Trade Representative, CEIC, Crédit Agricole CIB

US tariffs on China notably lowered but threats remain



Key Topics	Expectations
Expected focus	Opportunity for both leaders to address tech-related grievances, extend the Busan trade truce and build on Board of Trade progress
Board of Trade	Mutual USD30bn tariff reductions (USD60bn total, 10% bilateral trade). US to focus on non-critical sectors the US is trying to reshore. Beijing is expected to concentrate on agriculture to accommodate its agriculture purchase commitment (USD17bn)
Board of Investment	Little progress on this Board given expanding US investment restrictions on China and general hawkishness over sensitive sectors. A Chinese business delegation may prompt further discussion
Technology, Chips, AI	Tech remained sidelined during May summit, but recent tech-related bans on Chinese products will shift tech to the forefront of the summit.
Iran and sanctions	The US has threatened sanctions on global financial institutions which facilitate Iran's economy, but the OFAC has refrained from targeting significant Chinese entities

China: US-China trade shows partial recovery in Q2

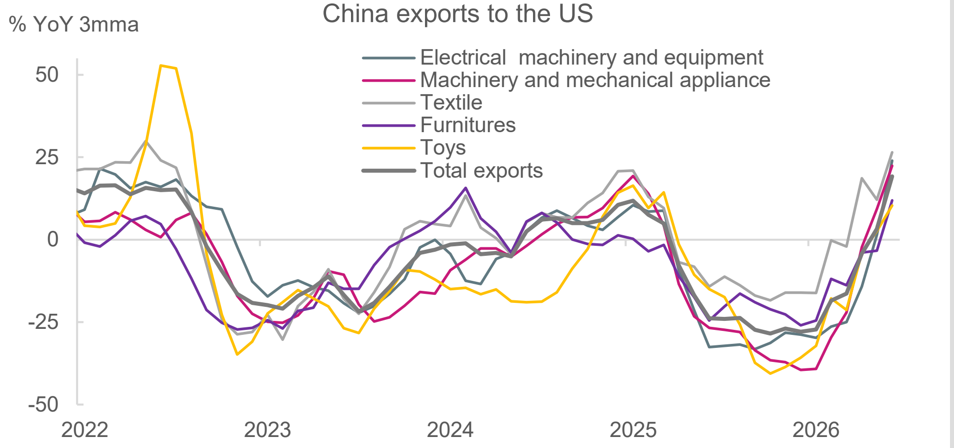
Lower tariffs and AI-related demand boost Q226 exports

- 2025 tariff war substantially reduced the size of bilateral trade (USD450bn), with exports declining 19.8% in 2025 and 16.4% YoY in Q126. The US accounted for 11.1% China's exports (vs a peak of 19.8% in 2018), while China accounted for 5.4% of US exports in 2025 (vs a peak of 8.9% in 2015)

- The Trump-Xi trade truce contributed to a rebound of Chinese exports to the US in Q226 by 19.2%, while rising AI-related demand frontloading imports ahead of anticipated new tariffs likely also acted as support. Electrical equipment remains the most important sector, with telephone equipment (USD1.9bn) and computers & laptops (USD0.9bn) leading in June

- US aircraft-related exports to China surged in June (USD1.7bn) after Washington relaxed export controls against China's COMAC following Beijing's reported commitment to purchase 200 Boeing commercial jets in May. Exports of integrated circuits followed on AI-related drivers (USD1.2bn)

China exports to the US rose in double digits in June 2026



US exports to China dropped 26% under Trump 2.0 tariff policy

Source all charts: Wind, Bloomberg, CEIC, Crédit Agricole CIB

China: EU-China moving closer to trade conflict

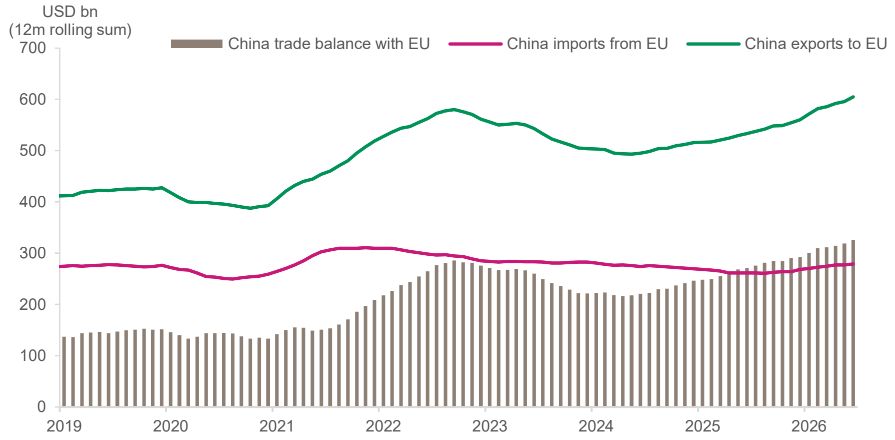
EU signals trade defence measures in response to high trade deficit

- EU shift to view China as a strategic challenge with unsustainable trade balance (China surplus USD273bn in 2025). Leaders have proposed trade measures such as stricter "Made in EU" sourcing obligations, diversification requirements for critical supply chains and a new "overcapacity" instrument
- In June, EU-China set an October deadline for a Trade and Investment Consultation (TIC) mechanism to address Europe's concerns, with a second round to take place in Beijing this autumn (TBC)

Import dependency and competition bring hardship to EU industry

- European advanced manufacturing industries have grown heavily reliant on Chinese imports, particularly in sectors at the heart of the EU's industrial base: green energy, advanced technology, aerospace and medicine. Of particular concern is critical minerals, batteries, permanent magnets and solar panels
- China's rise in advanced manufacturing and global export surge from domestic overcapacity has created negative spillovers for the EU's industrial competitiveness. The similarity in China vs EU export baskets reached 49.5% in 2025, up 6.1% from 2019

China exports to EU grew while imports stagnated



EU import dependencies on China across sensitive strategic sectors

Item	Industries	EU import reliance on China 2025	EU import reliance on China 2019	EU imports from China (2025, USDm)
Scandium & yttrium	Electronics, defense systems, medicine	78%	65%	10
Cobalt oxides	Lithium-ion batteries, superalloys (defense)	71%	95%	21
Magnesium & manganese	Aerospace alloys, automotive, electronics	88%	89%	559
Permanent magnets	Electronics, green energy, medicine, defense	88%	84%	1,058
Lithium-ion batteries	Energy storage, consumer electronics, defense	90%	47%	29,036
Solar cells and modules	Green energy transition	99%	57%	8,883

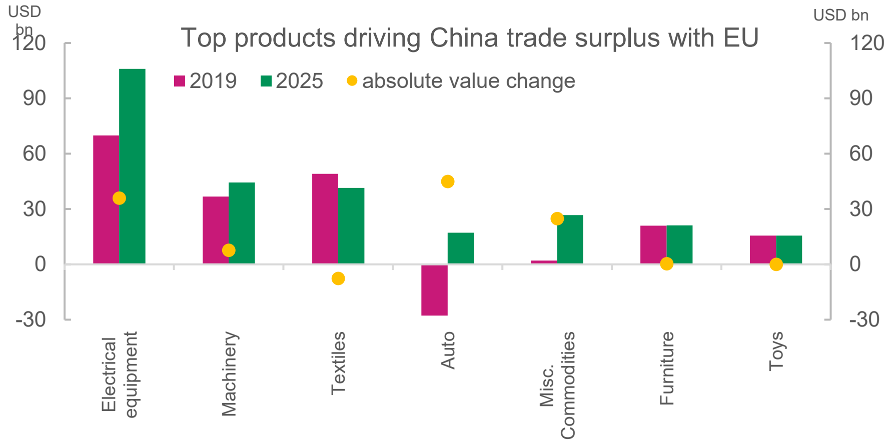
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: trade surplus with EU grows on electrical & manufactured goods

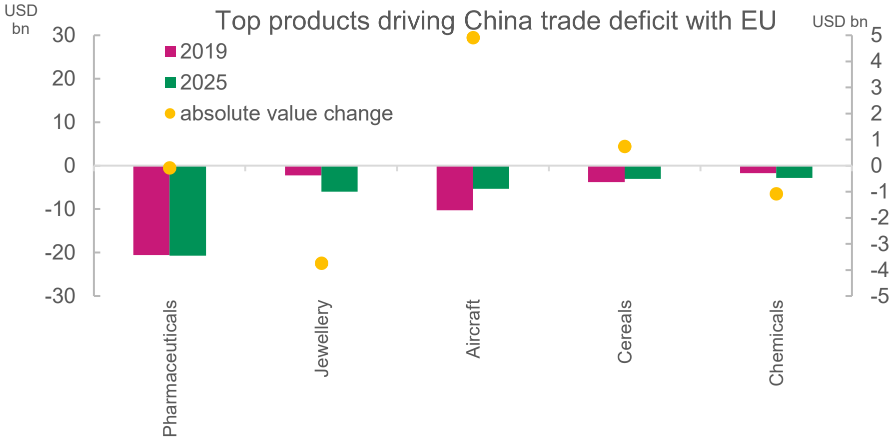
Lower tariffs and AI-related demand boost Q226 exports

- The largest source of China's goods trade surplus with the EU is electrical and machinery related products with a cumulative surplus of USD150bn in 2025 (51.5% of China's total trade surplus with the EU)
- China's auto trade with the EU shifted to a surplus of USD17.1bn in 2025 from a deficit of USD27.9bn in 2019, driven by China's onshore subsidy on domestic renewable energy vehicles and offshore demand for China-made autos due to its cost advantage. Chinese EVs remain, on average, 21% cheaper, while Chinese OEMs' share of vehicles shipped from China to Europe increased from 35% to 54%, while China imported less from European manufacturers and Tesla
- China's largest trade deficits are concentrated in pharmaceuticals, though modest growth of imports in this sector may reflect China's efforts to localise production despite the EU retaining a competitive advantage in high-value, patented medicines

Auto trade balance turned to surplus from deficit



Pharmaceuticals driving major trade deficit with EU



Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: China stands firm against US, EU “de-risking” trend

Beijing counters western “long-arm jurisdiction” mechanisms

- China seeks to neutralise foreign “long-arm jurisdiction” imposed by various US and EU trade restrictions and sanctions. Beijing has indicated willingness to use new regulations (countering US sanctions on refineries, warning EU against new trade measures)
- In 2025-26, the State Council has ramped up the legal authority to respond, with major regulatory updates to trade, national security and regulatory frameworks
- Trump administration still finalising new tariff regime to replace IEEPA, Section 122. The EU looks to expand trade defence mechanisms, including tariffs, localisation requirements and mechanisms to counter overcapacity

China’s expanded regulatory toolkit to counter US, EU “de-risking”

Regulatory Shifts	Date	Key Changes
Major amendments to Cybersecurity Law	October 2025	Expands legal reach to sanction overseas actors threatening Chinese data networks, implements new compliance framework for AI infrastructure
Revisions to Foreign Trade Law	March 2026	Implements authorisation for retaliatory trade bans against foreign entities that practice economic containment
Regulations on Countering Improper Extraterritorial Jurisdiction	March 2026	Provides legal framework to identify “unlawful” extraterritorial jurisdiction measures, allows China to prohibit such measures Creates a “Malicious Entity List” which could lead to various restrictions on business in China
Regulations on the Security of Industrial and Supply Chains	March 2026	Provides legal framework to identify a “violation of normal market transaction principles,” can prohibit entities from transacting with Chinese businesses
Regulations on Outbound Investment	June 2026	Broadens state oversight for the overseas transfer of goods, technologies, services and related data subject to export controls Authorises countermeasures against foreign entities deemed harmful to its national interests

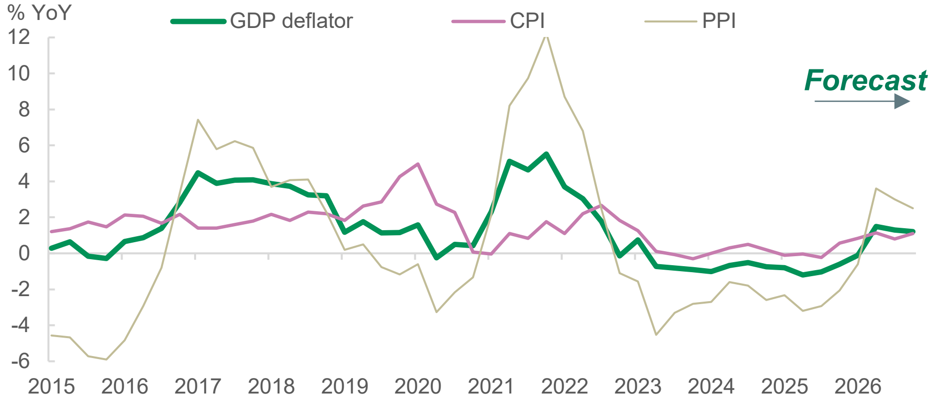
Source: US Department of Agriculture, US Trade Representative, CEIC, Crédit Agricole CIB

China: mild CPI recovery

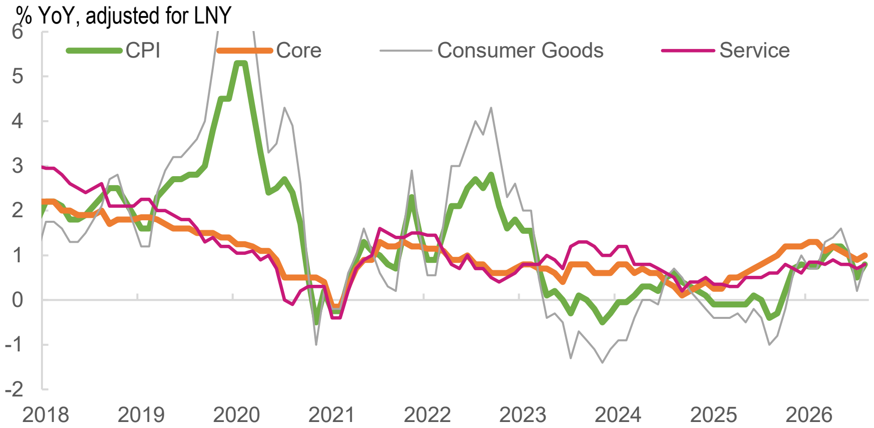
Higher energy and gold prices helped lift headline CPI

- We expect CPI inflation to increase to 1.0% in 2026 and 1.2% in 2027 from Authorizes 0% in 2025
- Higher fuel and gold price inflation have been major drivers for the higher CPI inflation so far in 2026. Services inflation also climbed
- We expect mild CPI inflation, as the positive impact from quicker fiscal spending gradually kicks in while inflation of those consumer electronics could remain supported by upstream price hikes of tech-related inputs

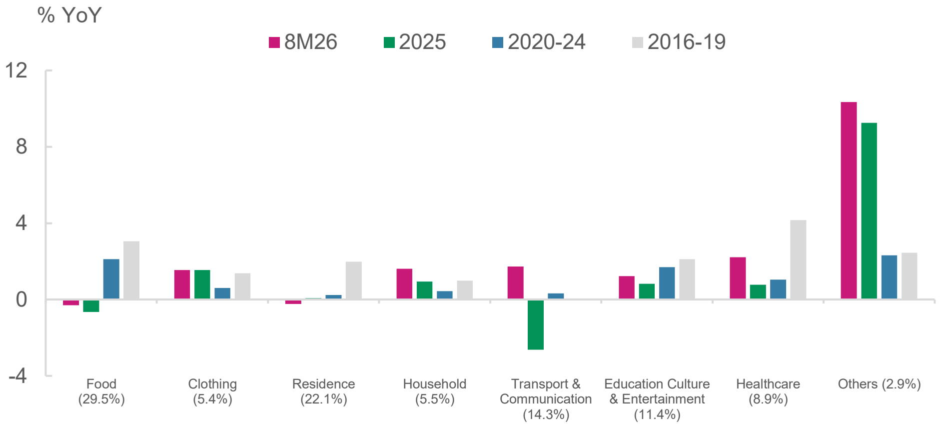
GDP deflator turned positive in Q226



CPI reflation has been mild and slow



CPI inflation rebound mainly led by fuel and gold



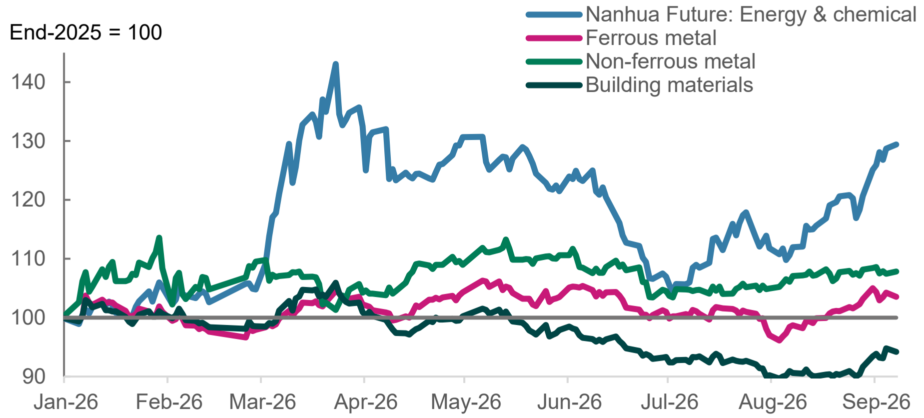
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: supply-led PPI reflation

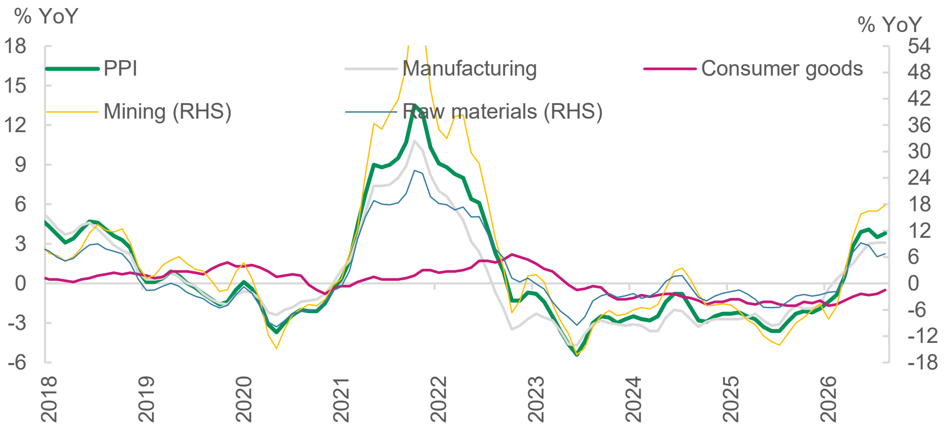
Upstream inflation, downstream deflation lingers

- We expect PPI inflation at 2.1% in 2026 and 1.1% in 2027, reversing the deflation seen in 2023-25
- The higher PPI inflation has been largely concentrated in AI-related inputs and capital goods, alongside higher energy prices, while prices in downstream sectors and consumer goods have remained in deflation
- We expect PPI inflation to ease gradually, though faster fiscal spending on strategic infrastructure could provide some support. A sustained return in PPI inflation would require a more durable recovery in domestic demand

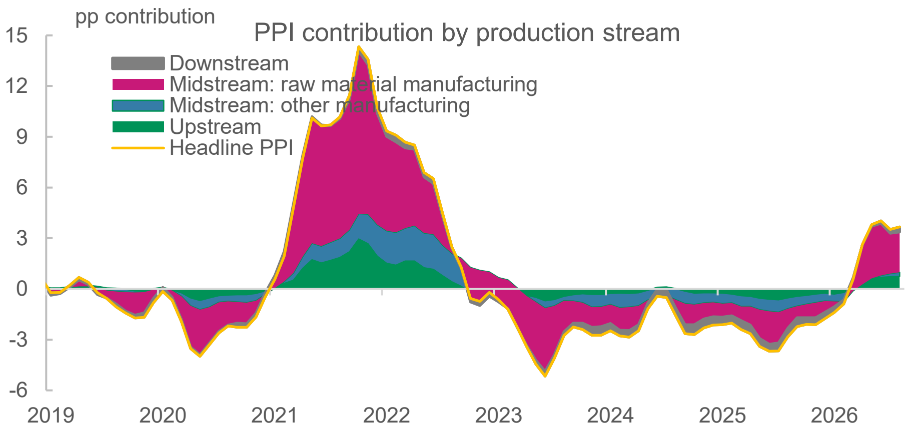
Energy and raw material prices rose materially this year



PPI inflation has been led by upstream price gains



Downstream inflation remained absent



Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: July Politburo meeting signalled incremental easing

July Politburo remained heavily focused on high-quality growth

- The July Politburo pledged to implement existing policies effectively, while preparing additional practical and targeted measures to be rolled out in a timely manner
- Various government bodies and financial regulators announced follow-up measures, signalling policy intention to stabilise near-term growth
- However, those measures remain measured and incremental and are more focused on supply-side upgrades. Any large-scale demand-side stimulus remains unlikely
- There is still room for further policy easing if growth appears likely to fall materially below 4.5%

Modest policy support after July Politburo

Category	Policy
Consumption	**Aug:** guidelines to **promote goods consumption** (target RMB60trn by 2030) **Aug:** unlock **county-level consumption** potential **Jun-July:** boosting "**AI plus consumption**"
Investment	**Aug:** State Council's commitment to construction of "**six networks**" and next-generation **communication networks** **Sep:** start to deploy RMB800bn of **policy financial tools**
Industry	**Aug:** State administration vow continue "anti-involution" campaign **Aug:** high profile World Robot Conference to promote robotics industry
Property	**Sept:** shift from pre-sale to priorities sale of completed homes **Sept:** extending the maximum mortgage terms to 40 years from 30 years **Aug:** revision of **housing provident fund rules** (expanding fund coverage to the entire housing lifecycle and broadening withdrawal scenarios)
Fiscal and monetary	**Sept:** RMB360bn of **capital injection** into state-owned insurers and banks **Aug:** new **fiscal-financial support measure** in H2 **Aug:** expand **interest subsidies** for small business and consumers

Key events to watch in 2026

Time	Events
12-13 September	**BRICS summit** in India
24 September	Potential **Trump-Xi meeting** in the US
20-21 October	**APEC Finance Ministers' meeting** in Hong Kong
26-29 October	5th Plenum of the 20th CPC Central Committee
10 November	Expiry of **US-China trade truce** arrangement
18-19 November	**APEC Economic Leader's** meeting in Shenzhen
14-15 December	**G20 leaders summit** in Miami
December	Politburo and **Central Economic Work Conference** to update policies

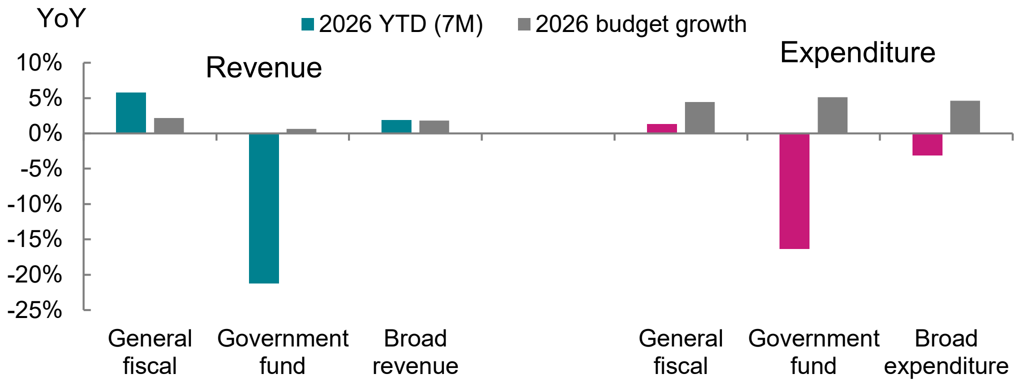
Source all charts: Government websites, Bloomberg, CEIC, Crédit Agricole CIB

China: modest fiscal expansion after de facto tightening in H1

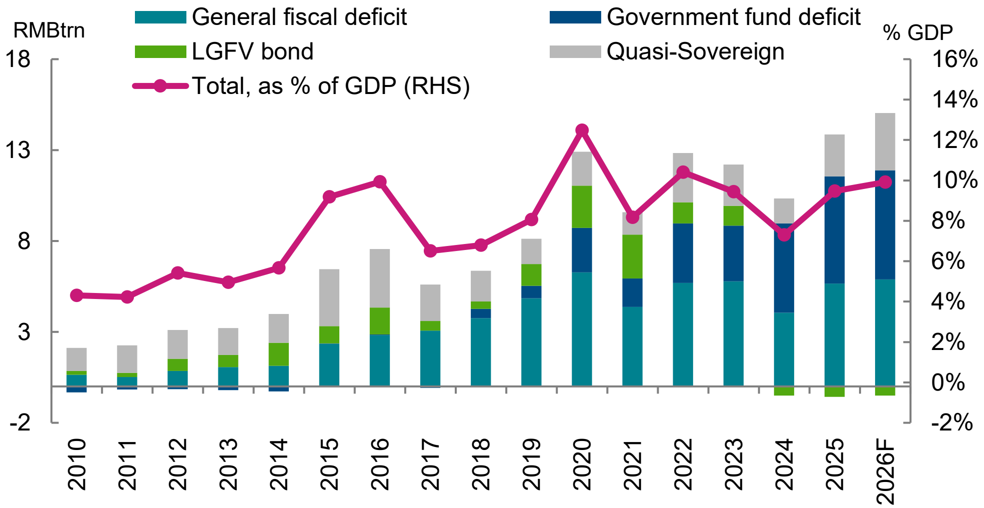
Policy pledges to quicken fiscal spending with room to expand

- China maintains a similar size of fiscal package in the 2026 budget vs 2025, with a slightly smaller on-budget fiscal deficit ratio but larger spending via its quasi-fiscal measures
- However, the pace of government bond issuance has been slow, while broad fiscal expenditure contracted and is far behind budget planning
- We expect China could boost its fiscal spending by 0.3-0.5% GDP later this year in case of major growth shocks

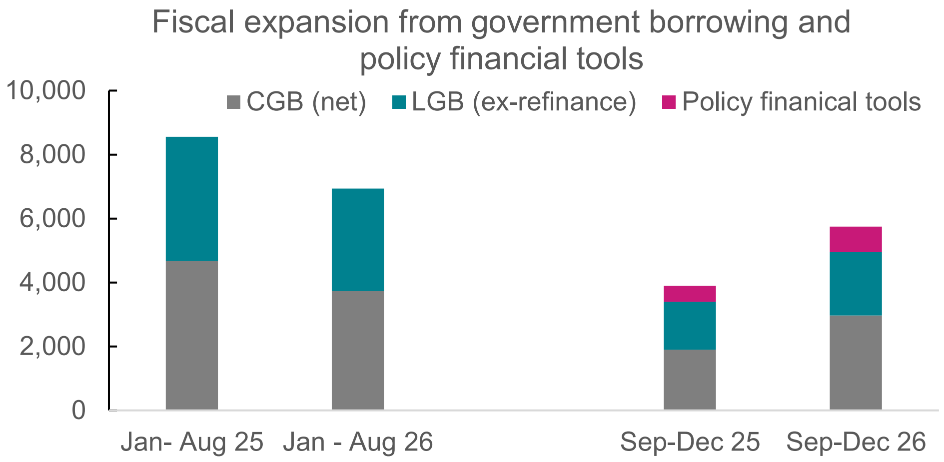
Fiscal tightening YTD rather than expansion



Augmented fiscal deficit ratio could pick up slightly



There is ample room for fiscal expansion in the rest of 2026



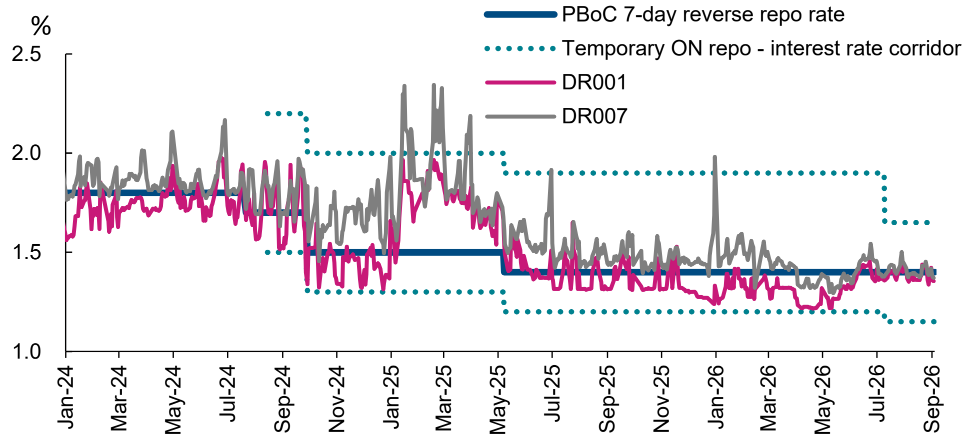
Source all charts: Government websites, Bloomberg, CEIC, Crédit Agricole CIB

China: the PBoC to focus on targeted easing for now

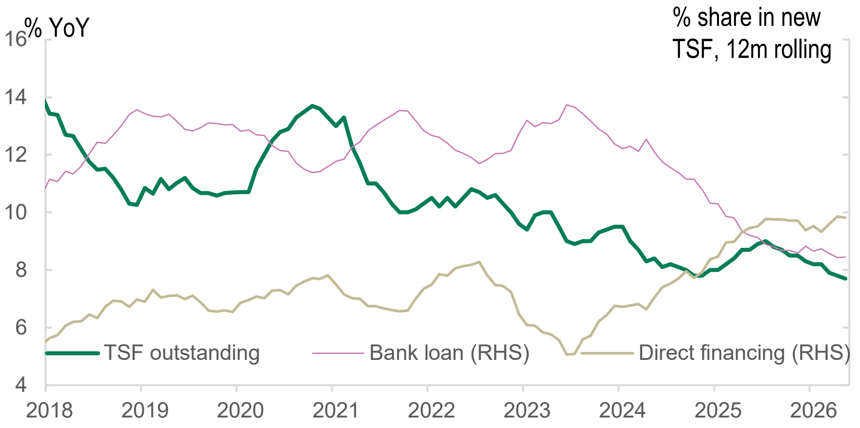
PBoC easing bias intact, but no imminent rate cuts

- The PBoC will likely maintain its overall easing stance, despite providing little hint of any broad easing. We expect no policy rate or RRR cuts in 2026
- The PBoC has pledged to keep interbank liquidity ample, support targeted credit growth and coordinate well with fiscal policy. We expect a greater emphasis on financial market stability (ie, bond, equity and FX)
- The PBoC continues its efforts to upgrade its monetary policy framework, towards more price-based (with more frequent ON reverse repo operations) to better anchor short-term market rates (ie, DR001)

The PBoC moves towards a more price-based monetary policy framework



Direct financing becomes increasingly important



Structural credit supports to targeted sectors

	Relending rate (1Y)	**Relending quota (RMB)**
2026	-25bp (to 1.25%) January	**+400bn:** technological innovation, industrial upgrades **+500bn:** agriculture, small business
2025	-25bp (to 1.50%) May	**+300bn:** agriculture, small business **+300bn:** technological innovation, industrial upgrades **+500bn new:** service consumption, elderly care
2024	-25bp (to 1.75%) January	**+100bn:** agriculture, small business **+300bn new:** affordable housing **+500bn new:** technological innovation, industrial upgrades **+800bn new:** stock buybacks and shareholding increases

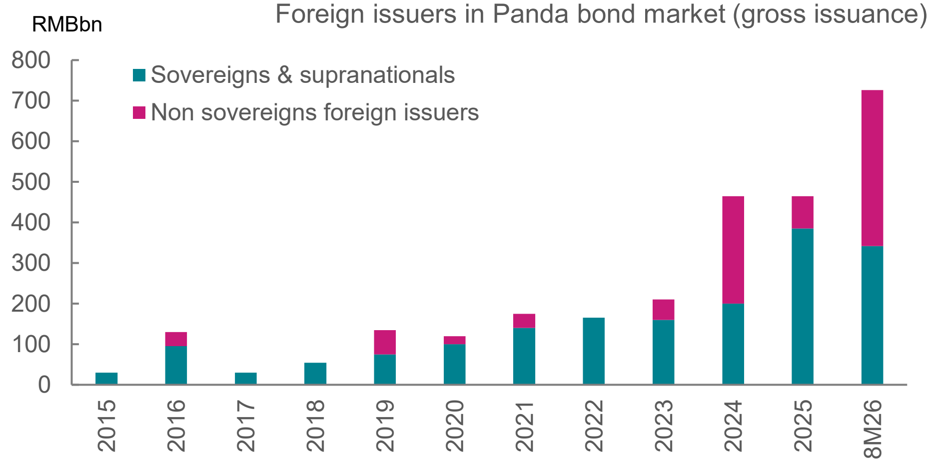
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: gaining momentum for RMB as funding currency

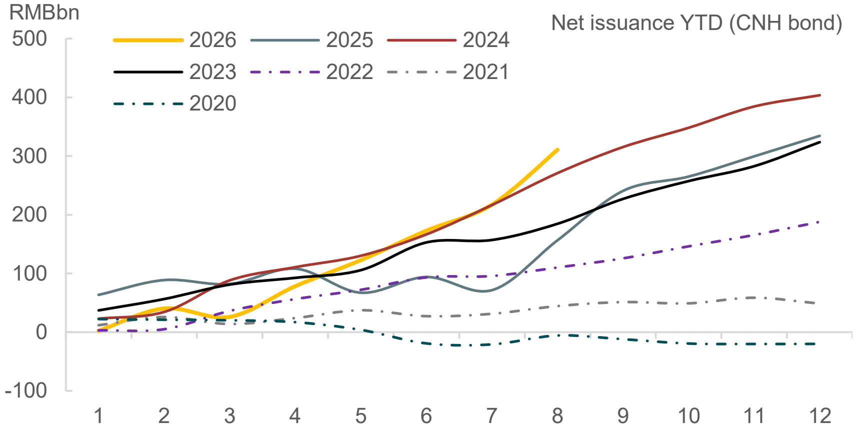
Macro tailwinds for expansion in Panda and Dimsum bond markets

- China's CNY and CNH bond markets have emerged as sources of stability and relatively cheap funding for global borrowers, amid the rapid correction in G3 bond markets
- Panda bond issuance from foreign financial institutions is rising, driven by low yields and tight credit spreads in the CNY onshore bond market
- Rising new sovereign issuers from BRICS, Gulf and Belt & Road economies are entering the market, on the back of broadening international use of the RMB

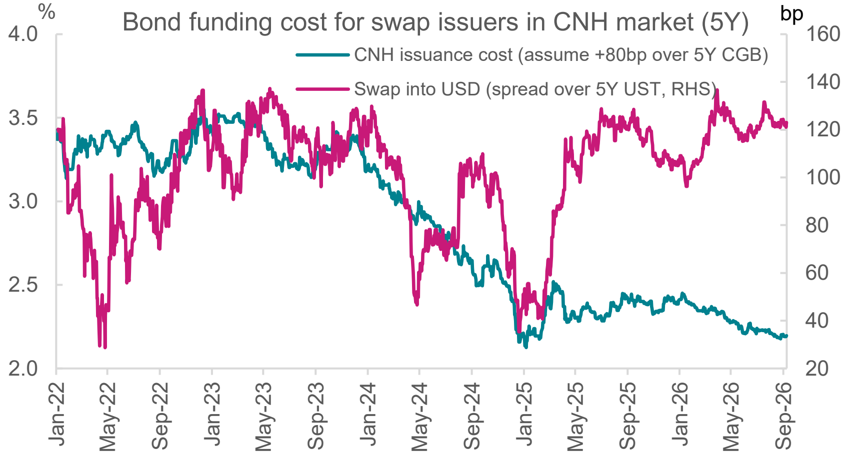
Strong momentum in Panda bond issuance in 2026YTD



CNH funding activities in Dimsum bond market remained active



Borrowing cost saving via CNH bond issuance



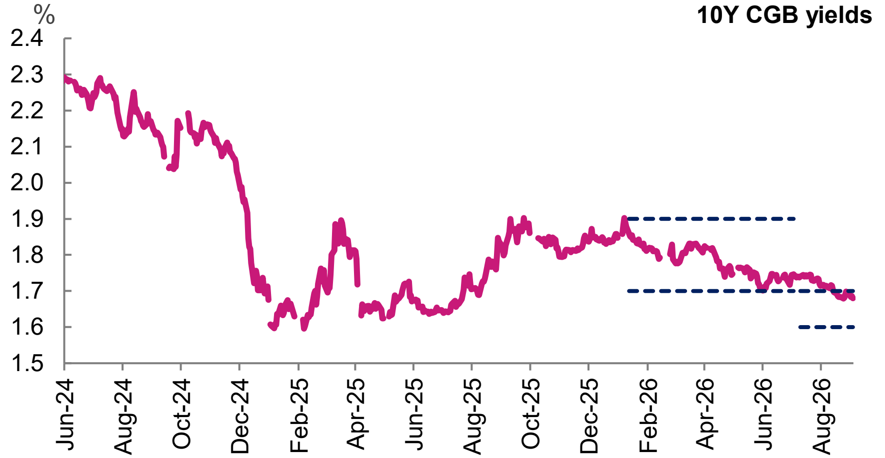
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: curve to stay flat with decent duration demands

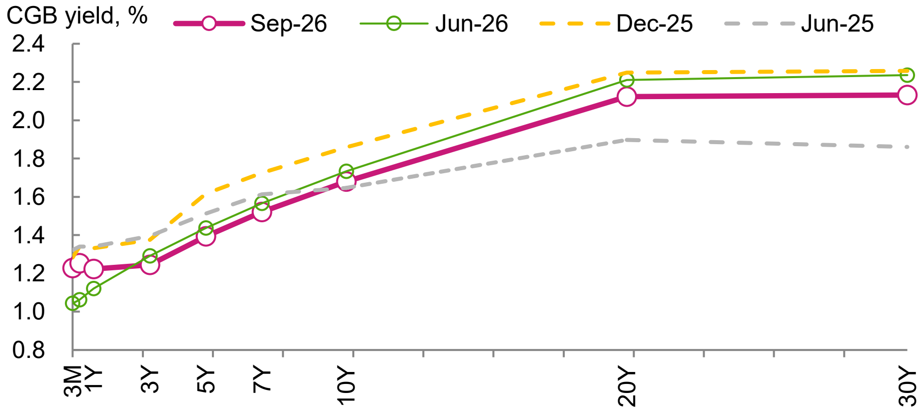
Favourable supply-demand, mild reflation and contained volatility

- We expect 10Y CGB yields to move in range of 1.60-1.70% in H226, down from 1.70-1.90% in H126, given limited incremental fiscal stimulus in response to softer growth while imported inflation pressure eased
- The CGB curve would likely to stay flat in the absence of a sizable fiscal package. The expected still-solid dip-buying demand from domestic buyers would cap the upside in CGBs yields
- The 30Y-10Y CGB yield spread is likely to trade at around 40bp towards end-2026 from current 45bp

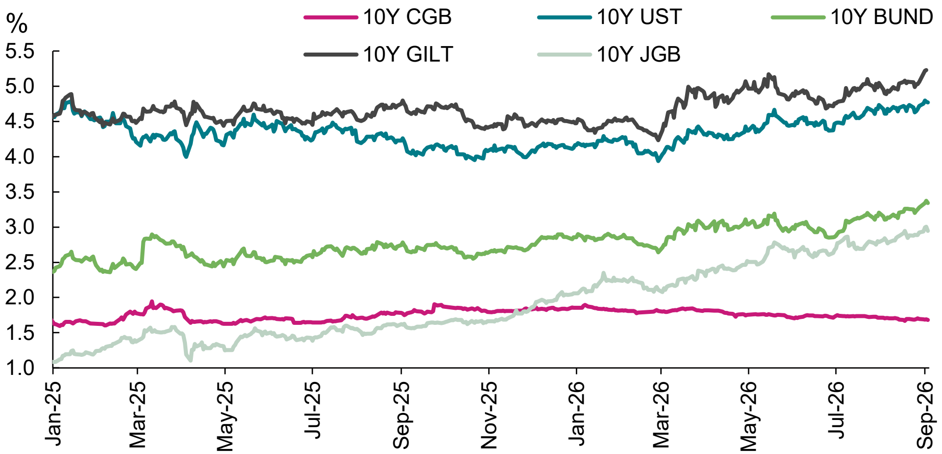
10Y CGB yield move into new range of 1.60-1.70% in H226



Contained volatility in the CGB yield curve



China rates are absent from global duration sell-off



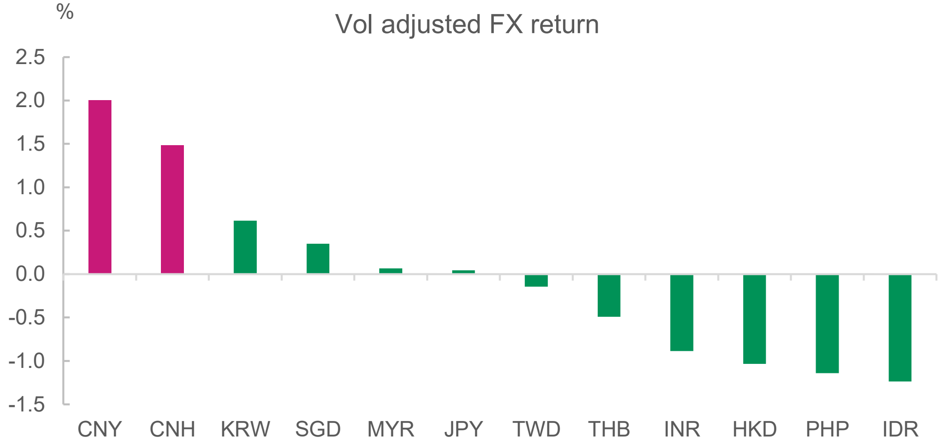
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: CNY a 2026 outperformer

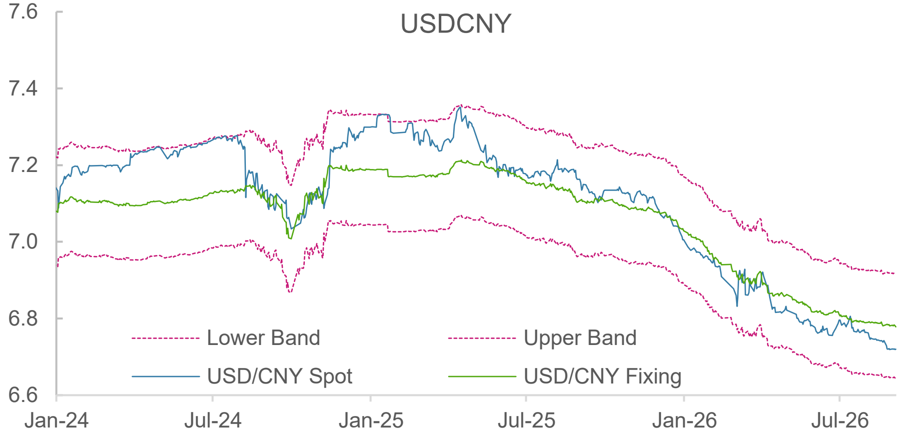
Lower USD/CNY in 2026, with gradual appreciation thereafter

- The CNY has gained more than 6% against the USD over the past 12 months with close to 4% of the appreciation in 2026
- CNY's outperformance reflects three main factors: resilient external balance, sustained FX settlement and supportive but managed policy stance
- We expect a gradual downward trajectory to 6.62 at end-2026 and 6.50 at end-2027

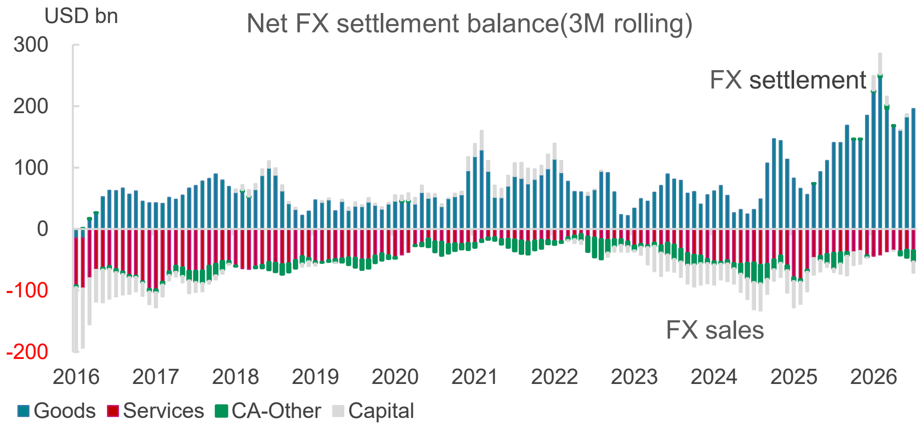
CNY has outperformed in 2026



USD/CNY spot trading below the fixing for much of 2026



Onshore FX settlement driven by the goods trade



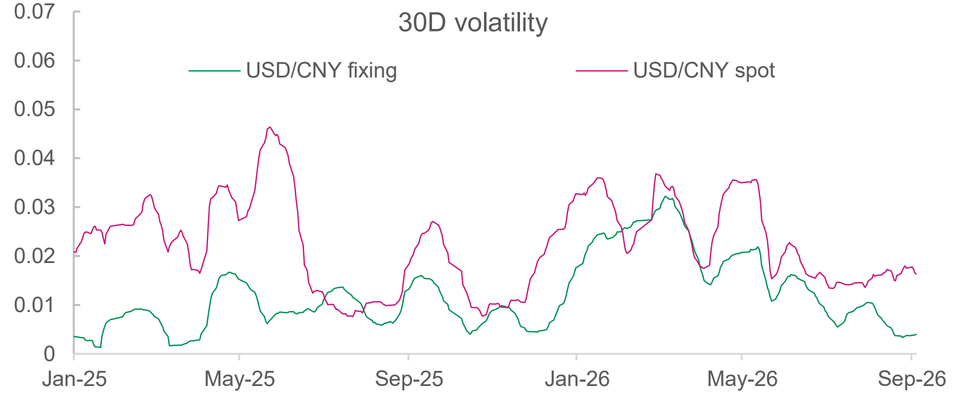
Source all charts: Bloomberg, CEIC, Crédit Agricole CIB

China: the CNY valuation debate

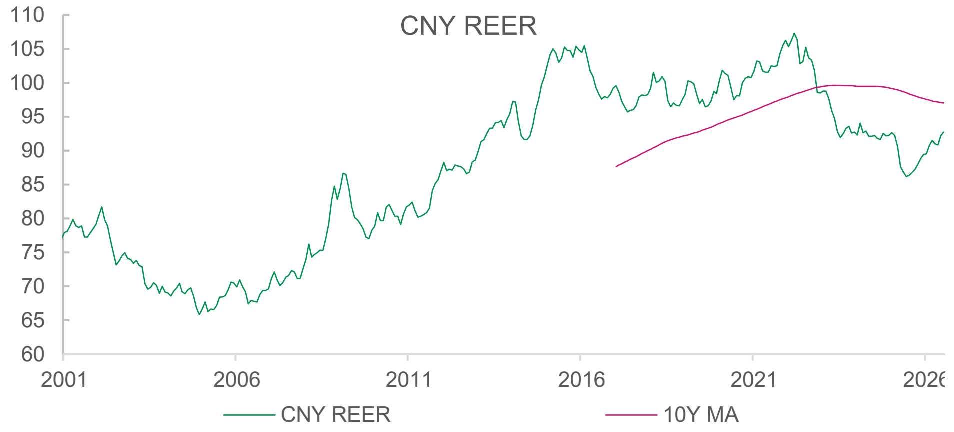
Valuation debate reinforces a case for gradual CNY gain

- Since mid-2025, the CNY REER has rebounded after falling to its lowest level since 2011, suggesting that the PBoC has become more willing to tolerate gradual CNY appreciation
- China's still-negative yield differential against the US continues to weigh on capital flows, while weak domestic demand and lingering deflationary pressure remain genuine headwinds
- The magnitude and speed of CNY appreciation is unlikely to be aggressive, given the needs to maintain stable financial conditions and accommodate domestic recovery and reflation process

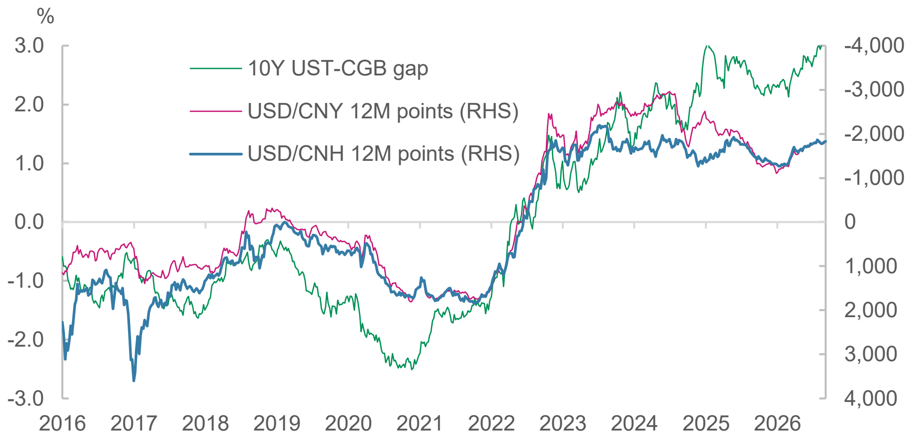
USD/CNY fixing volatility at 1Y lows



Climb in CNY REER points to narrowing undervaluation



USD/CNY diverging from US-CH rate gap



Source all charts: Bloomberg, CEIC, Council on Foreign Relations, Crédit Agricole CIB

China: summary of key macro forecasts

		2023	2024	2025	2026F	2027F
Real GDP	% YoY	5.4	5.0	5.0	4.5	4.5
Consumption	% YoY	8.5	4.2	4.6	3.7	3.6
Household consumption	% YoY	9.0	5.4	3.3	3.5	3.6
Investment	% YoY	3.4	2.9	2.0	3.8	4.0
Net exports	PPT contribution	-0.6	1.5	1.6	1.0	1.0
IP	% YoY	4.6	5.8	5.9	5.0	4.6
Retail sales	% YoY	7.2	3.5	3.7	1.5	3.2
FAI	% YoY	3.0	3.2	-3.8	-4.0	2.0
Exports, goods	% YoY	-4.7	5.8	5.4	18.0	8.0
Imports, goods	% YoY	-5.5	1.0	0.3	25.0	9.0
Current Account	% GDP	1.4	2.4	3.7	4.0	3.9
CPI inflation	% YoY, avg	0.2	0.2	0.0	1.0	1.2
PPI inflation	% YoY, avg	-3.0	-2.2	-2.6	2.1	1.1
Policy rate (7d reverse repo)	%, end period	1.80	1.50	1.40	1.40	1.30
Bank lending rate (1Y LPR)	%, end period	3.45	3.10	3.00	3.00	2.90
2Y CGB	%, end period	2.21	1.14	1.36	1.20	1.25
10Y CGB	%, end period	2.56	1.68	1.85	1.70	1.80
USD/CNY	end period	7.10	7.30	6.99	6.62	6.50

Source all charts: Government websites, Bloomberg, CEIC, Crédit Agricole CIB

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