China Economic Quarterly Q3 2026

In Brief

How China's Economy Performed in H1 2026

- China's economy grew 4.7% in the first half, within the government's target. Momentum eased from Q1 to Q2, and growth was uneven across the economy.

- Exports and technology manufacturing led the way. Factories making AI hardware, semiconductors and other high-tech goods saw strong growth and rising profits, helped by global demand for AI infrastructure and clean-energy products such as EVs.

- The weaker areas were closer to home: consumers spent cautiously, with retail sales up just 1.3%, while private investment and property remained soft.

- Inflation remained low, but the trend is turning. Core consumer prices have gradually firmed since 2024, and producer prices turned positive in March, partly due to higher global energy prices.

- Borrowing costs are low, but borrowing hasn't picked up much — a sign that willingness to spend and invest matters more than further rate cuts.

- **What this means:** opportunities remain strongest in sectors tied to technology and global trade, while those linked to property, big-ticket consumer goods and traditional construction are likely to stay under pressure.

What to Expect in the Second Half of 2026

- Government spending is expected to take on a bigger role in supporting growth. The central bank, meanwhile, is expected to keep policy supportive without moving to steeper rate cuts.

- Exports should remain a bright spot, particularly in AI-related and clean-energy products, though trade tensions with the US and EU are the key wildcard to watch.

- Consumer support is likely to stay targeted rather than broad-based. The bigger shift is structural: reforms aimed at raising consumption's share of the economy over time, with more spending on services such as healthcare, tourism and education.

- Infrastructure spending should provide some support, but fixed-asset investment is likely to stay weak overall. A fuller recovery will hinge on the property market stabilising and a genuine improvement in private-sector sentiment — both of which will take time.

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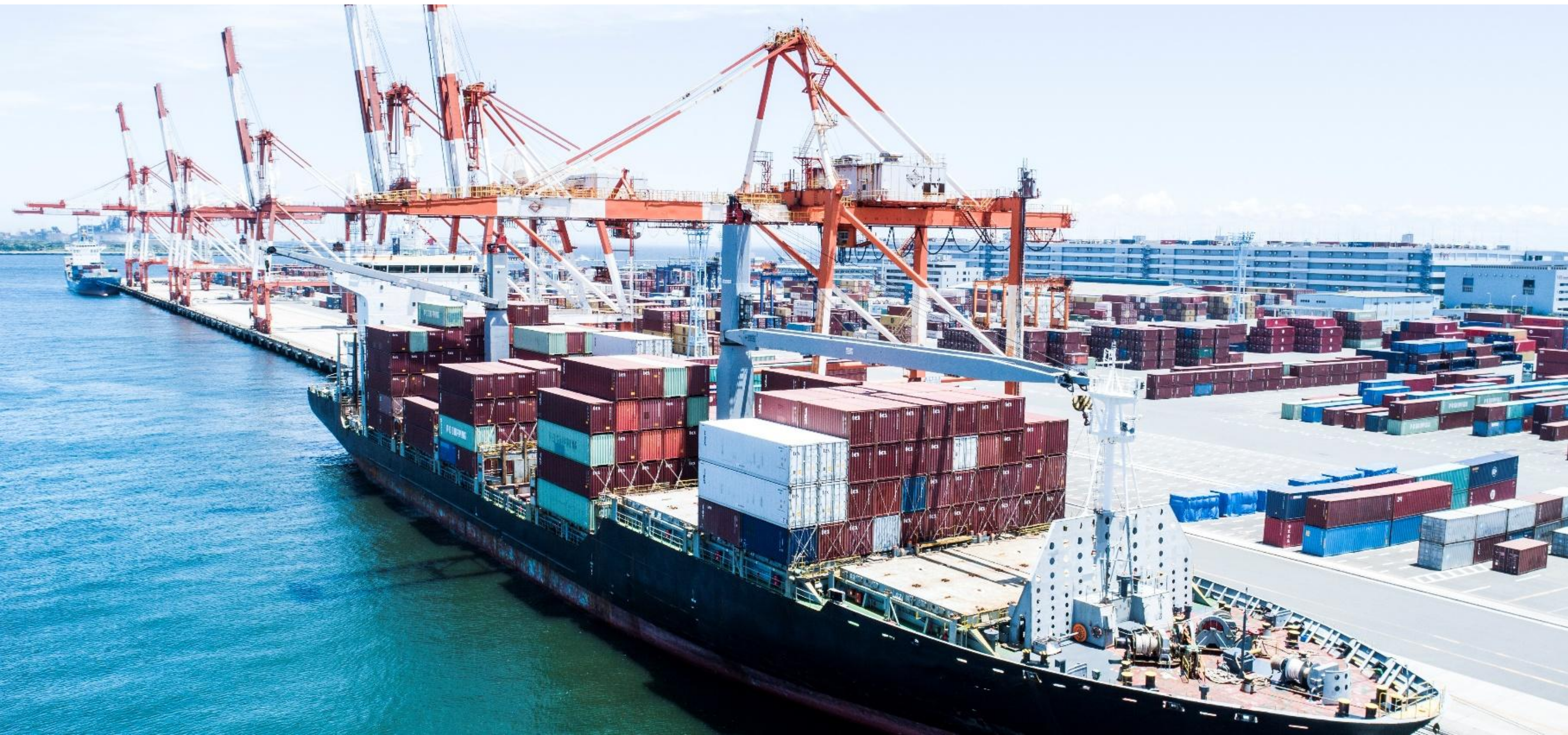
Key Takeaways from the First-Half Data

China's first-half data suggest that growth held up well against a more volatile external backdrop. GDP rose 4.7% year-on-year, within the official target range, although momentum softened as growth slowed from 5.0% in Q1 to 4.3% in Q2. More importantly, the growth mix stayed uneven: manufacturing was relatively solid and exports continued to provide an important source of support, while construction and property continued to lag, along with goods consumption and private investment. The first-half picture therefore showed growth concentrated in a few sectors, rather than a broad-based expansion.

One of the clearest themes in the first-half data was the divergence between external and domestic demand. Exports performed strongly, buoyed by sectors linked to the global AI investment cycle and the broader energy transition. Industrial output and profits also benefited, particularly in high-tech manufacturing and selected upstream industries. Domestic demand, by contrast, was softer: consumption improved only gradually, with performance mixed across categories, while fixed-asset investment weakened further and private investment was increasingly held back by cautious sentiment.

A second key theme was the ongoing shift in China's growth mix. Services accounted for a larger share of activity, while manufacturing continued to outperform construction, extending the move away from property-led expansion. Investment and credit data suggest, however, that this shift is far from complete: capital continues to flow into high-tech manufacturing, modern services and other policy-supported sectors, but private investment more broadly has yet to pick up.



The inflation data point to a gradual return to normal, rather than a strong rebound in prices. Consumer inflation stayed subdued, but core prices continued to edge up from their 2024 lows, while producer prices turned positive from March. This points to some easing of earlier deflationary pressure, helped by firmer energy and commodity prices as well as improving pricing conditions in selected sectors. At the same time, inflation is low enough to preserve room for further policy support if needed. Credit data convey a similar message: borrowing costs were low, but credit demand was still uneven, suggesting that lower borrowing costs alone are unlikely to generate a much stronger pickup in domestic demand.

For businesses, the first-half data underscore the need to look beyond headline growth and focus on where momentum is actually concentrated. The economy is still expanding at a meaningful pace, but opportunities are increasingly concentrated in areas linked to advanced manufacturing, digitalisation, services and export competitiveness. By contrast, sectors more directly exposed to property, traditional construction activity, and big-ticket items like autos and appliances are likely to stay under pressure. For the second half, the key question is whether policy support can broaden growth beyond the sectors currently leading it.

02

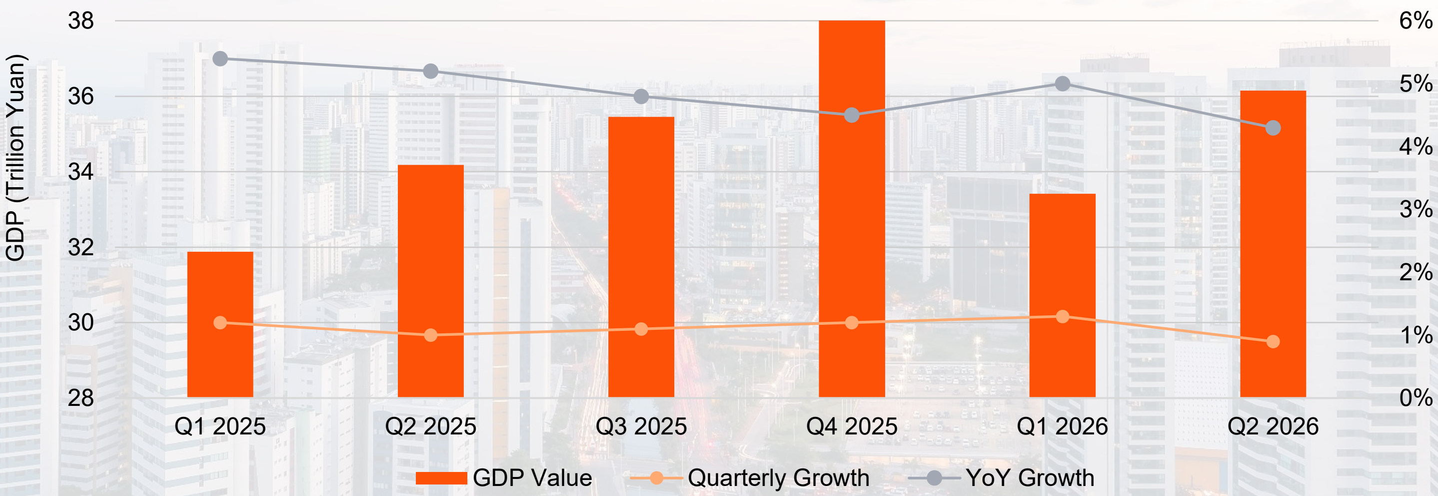
China’s Economic Momentum: A Snapshot

GDP

China's GDP rose 4.7% year-on-year in real terms in the first half, reaching RMB 69.57 trillion. Growth slowed from 5.0% in Q1 to 4.3% in Q2, yet still held within the official target range. Despite heightened geopolitical tensions and energy price volatility, the direct impact on overall growth has, so far, been limited.

Services increasingly drove growth, while ongoing weakness in construction continued to weigh on industrial activity. The tertiary sector expanded 5.2% in H1, accounting for 63.2% of GDP growth in Q1 and rising to 69.4% in Q2. Within services, information transmission, software and IT services rose 10.7%, while leasing and business services grew 11.9%. Financial services (6.7%) and accommodation and catering (5.0%) also posted steady gains. Manufacturing remained a bright spot within the secondary sector, with value added up 5.5%, helping to lift overall secondary-sector growth to 3.9%. Construction told a different story, contracting 4.0% amid persistent property-related weakness and softer investment momentum.

Quarterly GDP Values and Quarterly and Annual GDP Growth Rate



Source: Unless otherwise stated, economic data are from the National Bureau of Statistics of China, the People's Bank of China, and Wind.

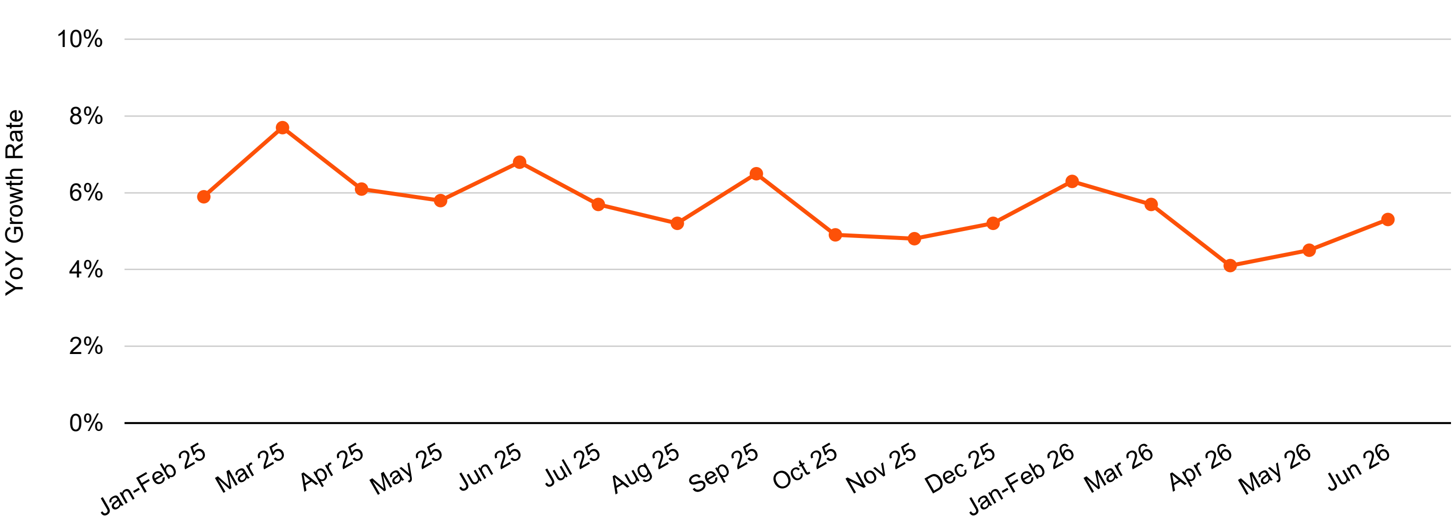
Industrial Output

Industrial output was solid in the first half, rising 5.4% year-on-year, with manufacturing slightly ahead at 5.6%. Despite uneven domestic demand, industrial activity was supported by strong exports and continued momentum in advanced manufacturing.

The sectoral breakdown points to further industrial upgrading. Equipment manufacturing expanded 9.3%, while high-tech manufacturing climbed 13.3%, both outpacing overall industrial growth. Demand linked to AI applications drove rapid output gains in products such as integrated circuits (+23.1%), optical fibre (+19.2%) and electronic components (+13.0%). Robotics-related industries also performed well, with output of related components surging 57.3%, alongside gains in industrial robots (+28.0%) and service robots (+11.9%).

Profitability improved markedly in the first half. Industrial profits rose 18.7% year-on-year, up from 15.5% in Q1. Profit growth was especially strong in computers, communications and other electronic equipment (+96.9%), driven by the global technology cycle. Upstream sectors also benefited from firmer global pricing for energy and industrial materials: profits in raw materials manufacturing climbed 71.7%, including chemical raw materials and products (+67.8%), coal mining and washing (+41.1%), and oil and gas extraction (+16.6%). In non-ferrous metals, profits nearly doubled, up 99.4%, helped by stronger demand for copper- and aluminium-related products.

Industrial Output

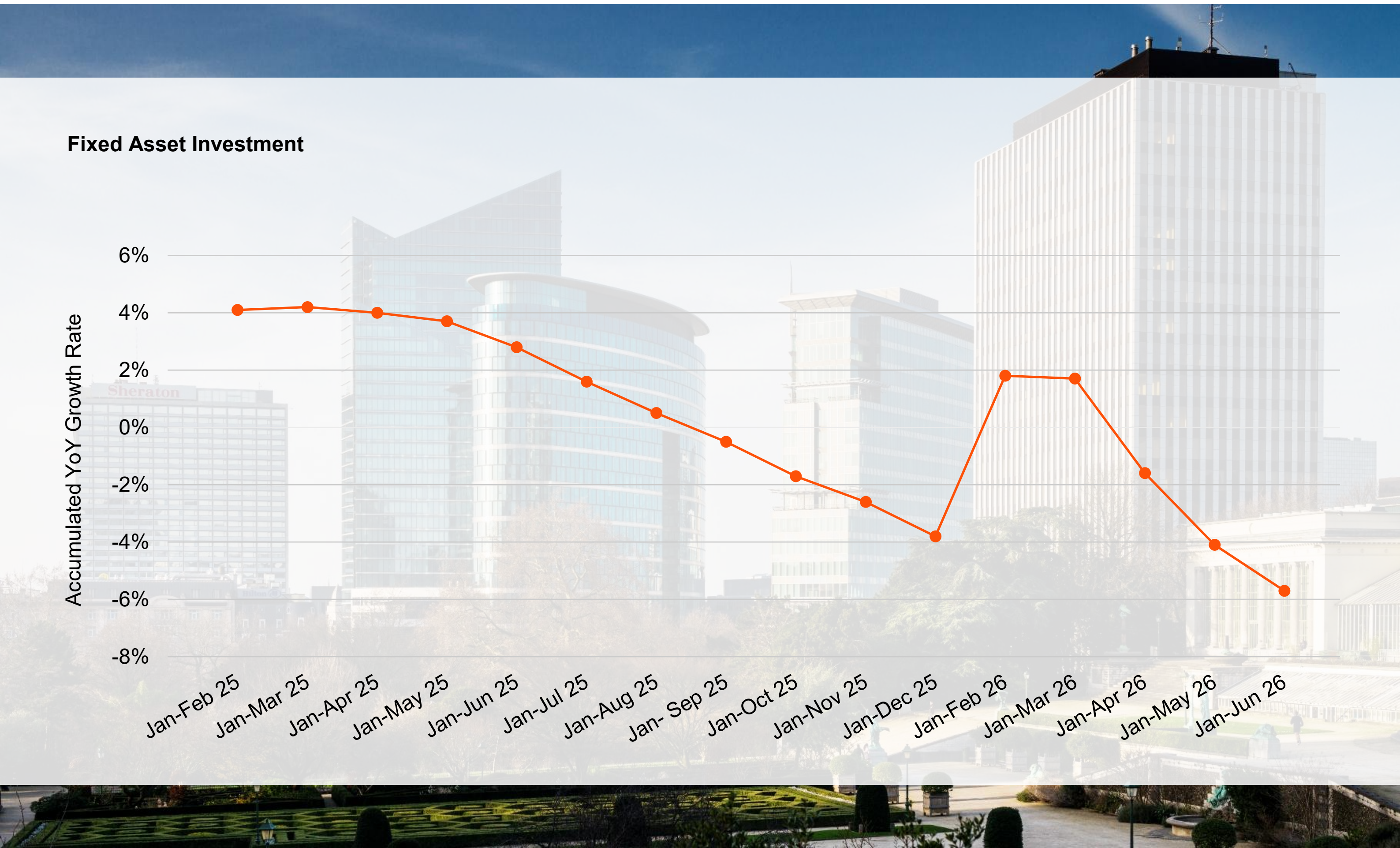


Fixed Asset Investment

Fixed-asset investment stayed soft in the first half, falling 5.7% year-on-year in January–June, compared with growth of 1.7% in January–March. Even excluding real estate development, the decline was 2.7%, indicating that the slowdown extended well beyond the property sector. Across major categories, infrastructure fell 2.4%, manufacturing slipped 1.2%, and real estate development dropped 18.0%.

Private investment was especially weak, falling 8.5% overall, or 4.9% excluding real estate. This likely reflects a mix of weaker demand, continued caution about debt levels, and an uncertain external environment. In practice, many firms appear to be focusing on efficiency and selective growth rather than broad-based capital spending.

Against that backdrop, a narrower set of sectors continued to defy the broader slowdown. High-tech industry investment rose 4.6%, including gains in high-tech manufacturing (+3.2%) and high-tech services (+7.5%). Spending was strongest in railway, shipbuilding, aerospace and other transport equipment manufacturing (+24.7%), as well as computer, communications and other electronic equipment manufacturing (+6.5%). Despite the broader softness in investment, capital remained concentrated in strategic and technology-related sectors.



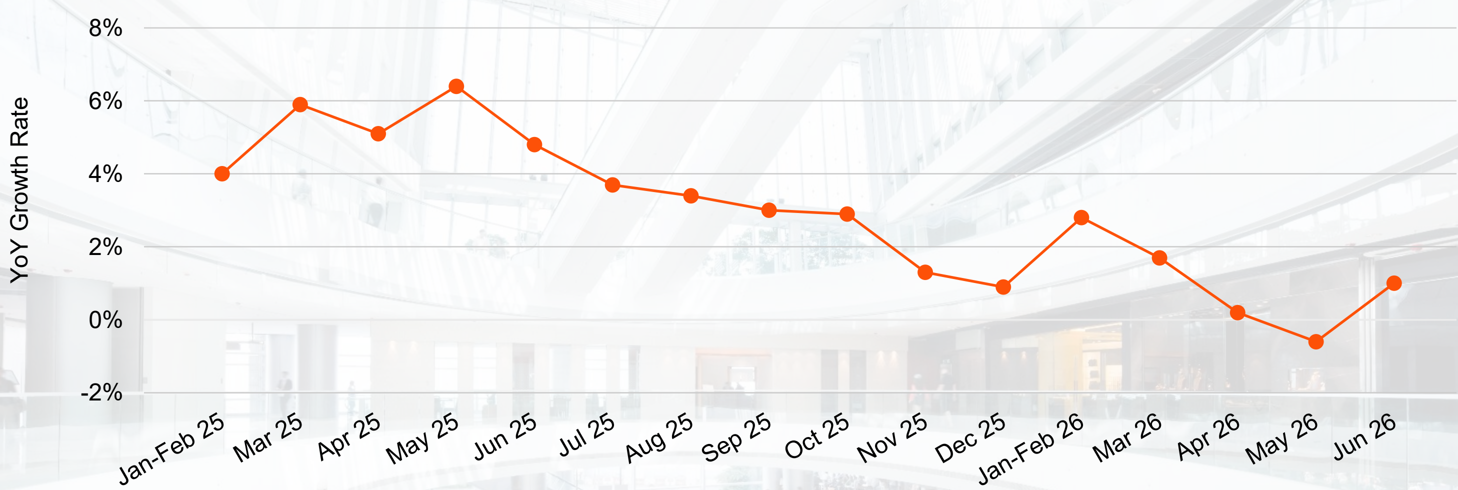
Consumption

Consumption stayed subdued in the first half, with household spending still cautious overall. After retail sales rose 2.4% year-on-year in Q1, growth slowed to 1.3% for the first half as a whole. In June, retail sales increased 1.0%, recovering from a 0.6% decline in May. While this points to some near-term stabilisation, it does not yet signal a broad-based pickup in household demand.

The main drag came from autos and property-related goods. Domestic auto sales fell 12.6% year-on-year through June, weighing on headline retail growth. Excluding autos, retail sales climbed 2.8%, suggesting somewhat firmer underlying demand. Sales of household appliances (-7.4%), furniture (-3.7%) and building and decoration materials (-8.8%) also declined, reflecting both continued weakness in the property market and a pullback after earlier rounds of trade-in incentives pulled demand forward.

Spending in other categories held up better. Sales of telecommunications equipment jumped 14.4%, tobacco and liquor gained 13.2%, clothing, shoes, hats and textiles rose 6.7%, cosmetics grew 6.3%, beverages advanced 6.0%, and cultural and office supplies rose 5.8%. Services spending continued to outperform goods, expanding 5.4% year-on-year in the first half. On a per capita basis, spending on transport and communications rose 4.7%, while education, culture and entertainment increased 4.9%. The overall pattern was one of divergence, with services and selected discretionary categories holding up better than big-ticket items.

Retail Sales of Consumer Goods



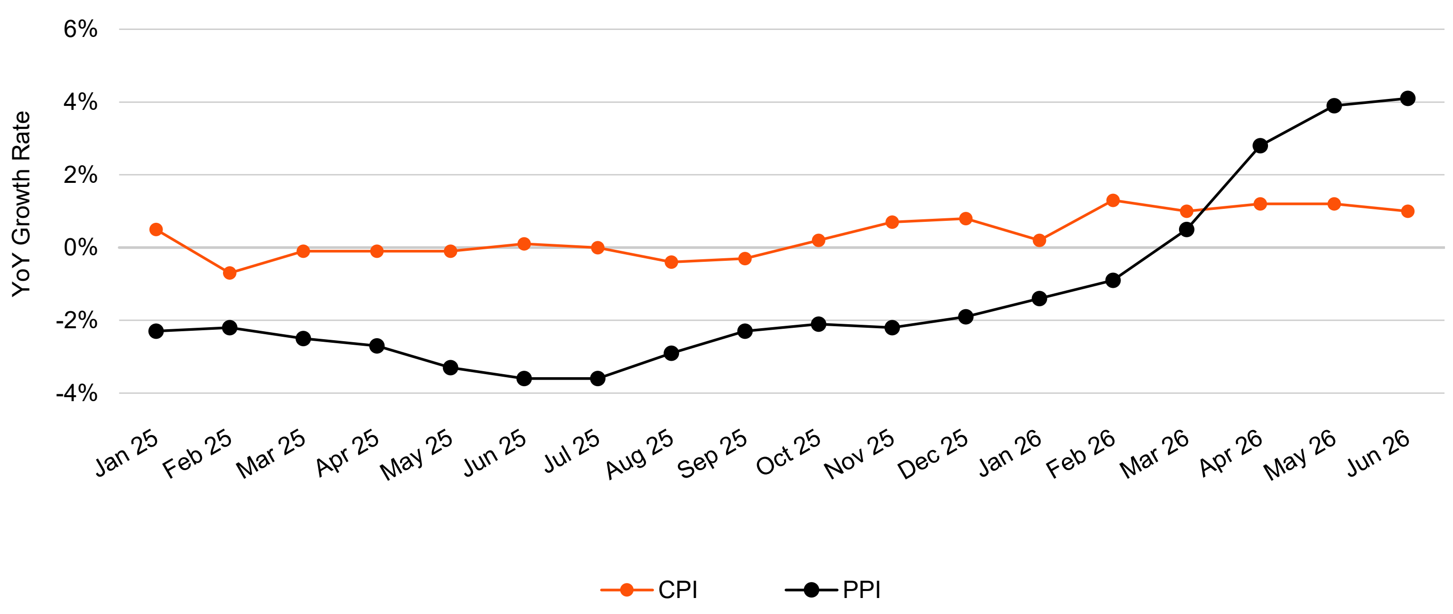
Consumer Price Index (CPI) and Producer Price Index (PPI)

Consumer price inflation stayed muted in the first half, with CPI rising 1.0% year-on-year, picking up from 0.9% in Q1 to 1.1% in Q2. Core CPI, which excludes volatile food and energy prices, rose 1.2% over the same period. Underlying core inflation has been gradually rising since its 2024 lows, and that trend continued through the first half.

Energy and select technology goods helped push up headline CPI. Domestic energy prices, which fell 2.5% year-on-year in Q1, climbed 3.0% in the first half overall, as higher global commodity prices fed through to local prices. AI-related product upgrades also lifted pricing in consumer electronics, with mobile phone prices up 4.0% and wearable smart device prices gaining 2.7%. Service prices rose 0.8% in the first half, unchanged from Q1. Within services, the recovery in travel demand pushed airfares up 7.2% and travel agency charges up 3.5%, while medical service prices advanced 3.1%.

Producer prices turned positive in March, rising 1.5% in the first half as prices moved from a 0.6% decline in Q1 to a 3.6% increase in Q2. The improvement was driven by higher prices in oil-related industries and better pricing conditions in selected sectors. Momentum slowed toward the end of the quarter, however: PPI fell month-on-month in June after eight straight monthly increases, mainly due to lower international crude prices.

Consumer Price Index and Producer Price Index



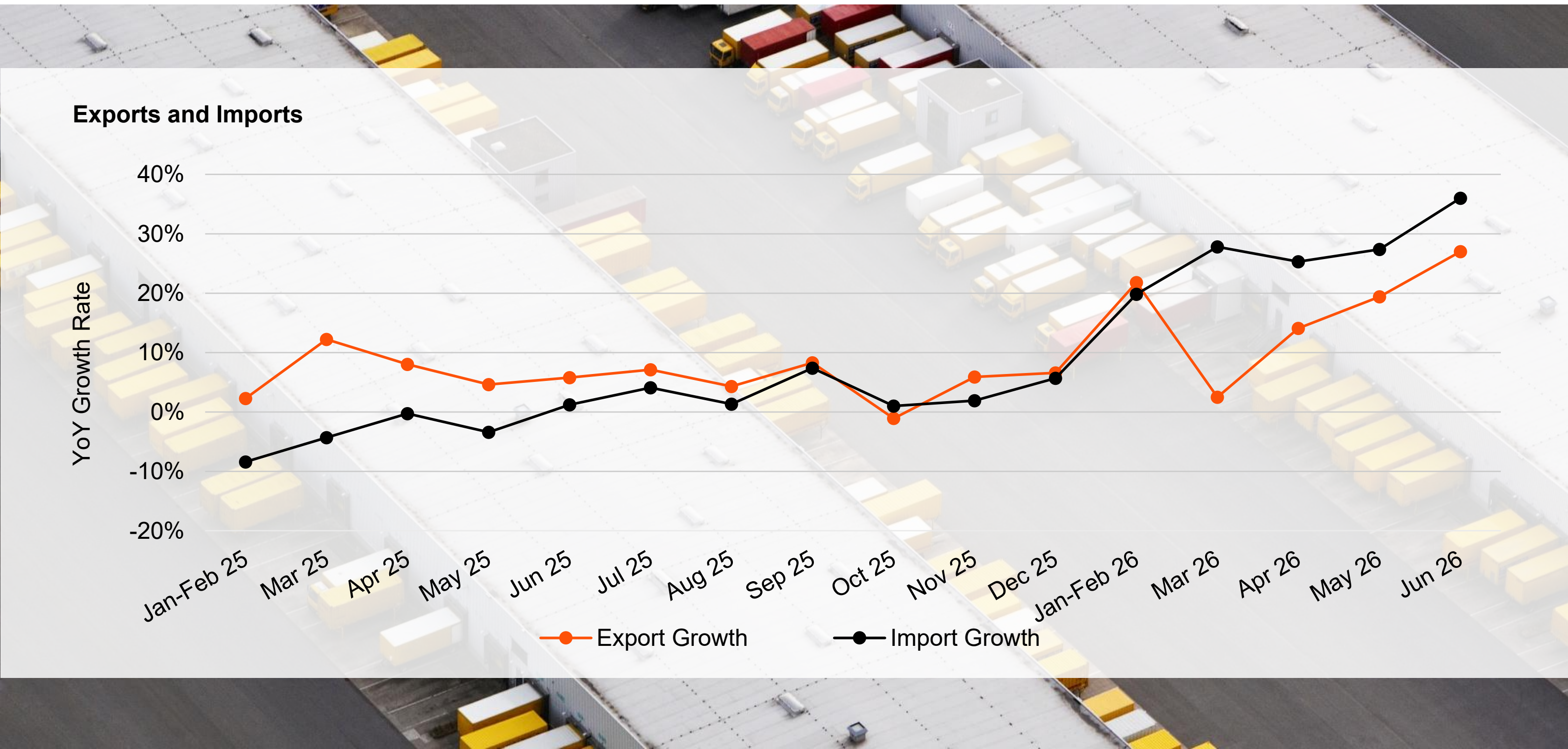
Trade

Trade was an important source of support in the first half, with exports rising 17.6% year-on-year in US dollar terms. Momentum accelerated in June, when exports and imports reached their highest levels since October 2021. Export growth climbed to 27.0% year-on-year in June, up from 19.4% in May.

Export gains stayed concentrated in sectors benefiting from the global AI investment cycle and the broader energy transition. High-tech exports increased 38.5% in the first half. Semiconductor exports surged 96.1%, although the increase was driven more by prices than volumes, with shipment volumes up by only around 7%. Exports of automatic data processing machines and parts climbed 41.3%. Auto exports also rose sharply, up 72% year-on-year, driven by continued overseas demand for Chinese vehicles, particularly EVs.

Exports to major markets held up well. Shipments to the European Union rose 16.8%, while exports to ASEAN grew 22.9% in the first half. Exports to the United States improved after a weak start: following a 16.3% contraction in Q1, growth turned positive in April (+14.1%), May (+35.4%) and June (+13.8%), bringing first-half growth to 0.2%.

Imports grew even faster, rising 26.6% in the first half and 36.0% in June, up from 27.4% in May. The increase was concentrated in high-tech categories, including automatic data processing machines and parts (+78.9%) and electronic integrated circuits (+55.8%). Crude oil import volumes, by contrast, fell 11.4%, possibly reflecting some drawdown of existing stockpiles amid higher energy prices. Faster import growth narrowed China's trade surplus by 1.3% year-on-year in US dollar terms over the first half.



Foreign direct Investment (FDI)

Inbound foreign direct investment showed early signs of stabilisation in the first half, although overall inflows stayed below year-earlier levels. Actual use of FDI fell 5.0% year-on-year in January–June, but the pace of decline narrowed by 10.2 percentage points compared with the same period last year. The number of newly established foreign-invested enterprises rose 5.3% over the same period, suggesting that foreign companies kept entering the market even as investment decisions became more selective in scale and sector. Monthly data were more encouraging: FDI increased 5.9% year-on-year in May and 15.1% in June.

FDI continued to shift toward technology-focused sectors. FDI in high-tech industries jumped 33.2% in the first half, lifting their share of total inflows to a record 42.4%. Within high-tech manufacturing, investment in electronic and communications equipment manufacturing climbed 52%. Modern services accounted for 57% of total inflows, with technology transfer and commercialisation services up 57.1% and R&D and design services surging 82%.

Purchasing Managers Index (PMI)

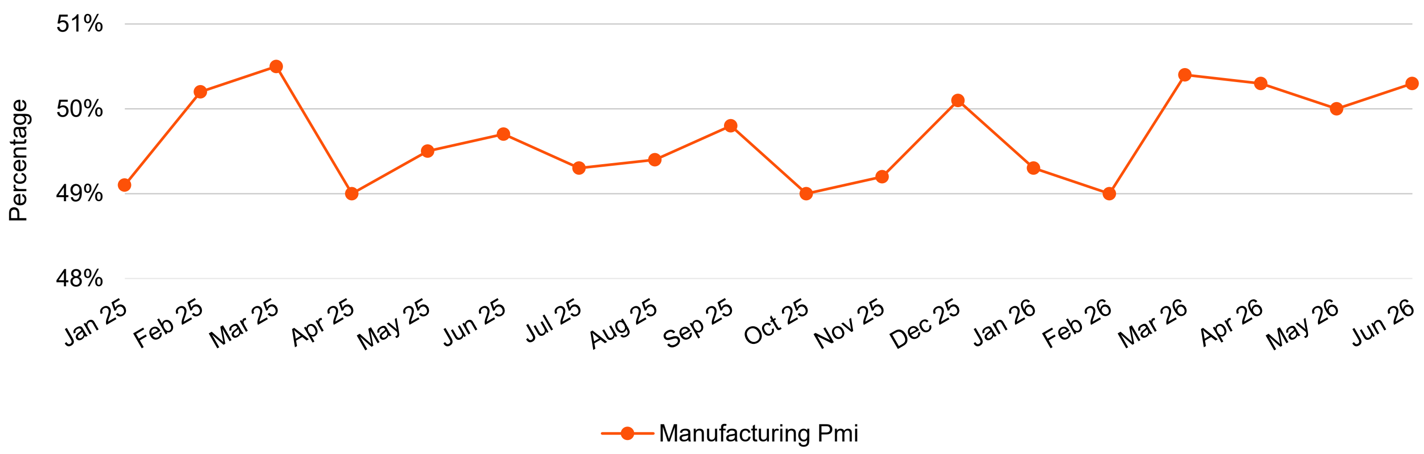
Business surveys pointed to a modest improvement in activity through the first half. The manufacturing PMI moved back above the 50-point mark (which signals expansion) at the end of the first quarter — after spending much of the period since last April below it — and stayed in expansion through June. This suggests manufacturing conditions improved overall, though momentum was uneven beneath the surface.

In June, the index was lifted mainly by stronger production and new orders. New export orders also returned to expansion in Q2, after staying below the 50-point mark since May 2024. By contrast, the employment index and raw materials inventory index stayed below 50, pointing to continued caution in hiring and inventory rebuilding.

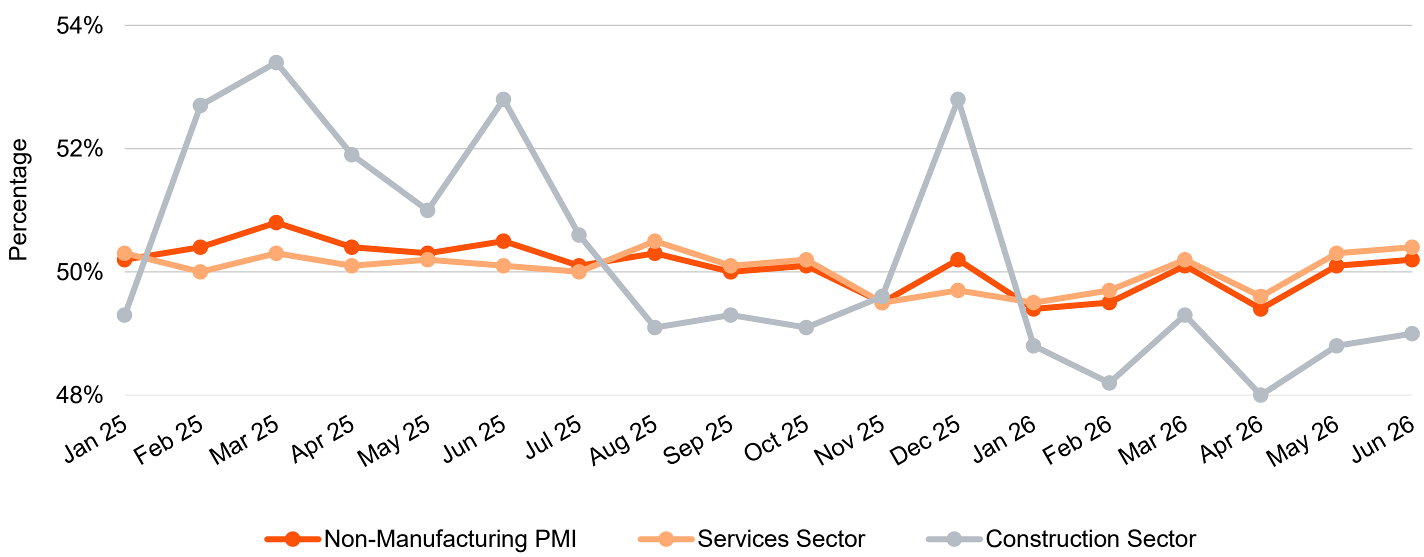
Performance also varied across manufacturing sub-sectors. High-tech equipment manufacturing outperformed the broader factory sector, with its PMI rising to 53.5 in June, while consumer goods manufacturing was more subdued at 50.2.

Non-manufacturing activity was comparatively stable. The non-manufacturing PMI edged up to 50.2 in June from 50.1 in May. Within this, the construction business activity index stayed below the 50-point expansion mark, at 49.0.

Manufacturing PMI



Non-Manufacturing PMI



Total Social Financing and new bank loans

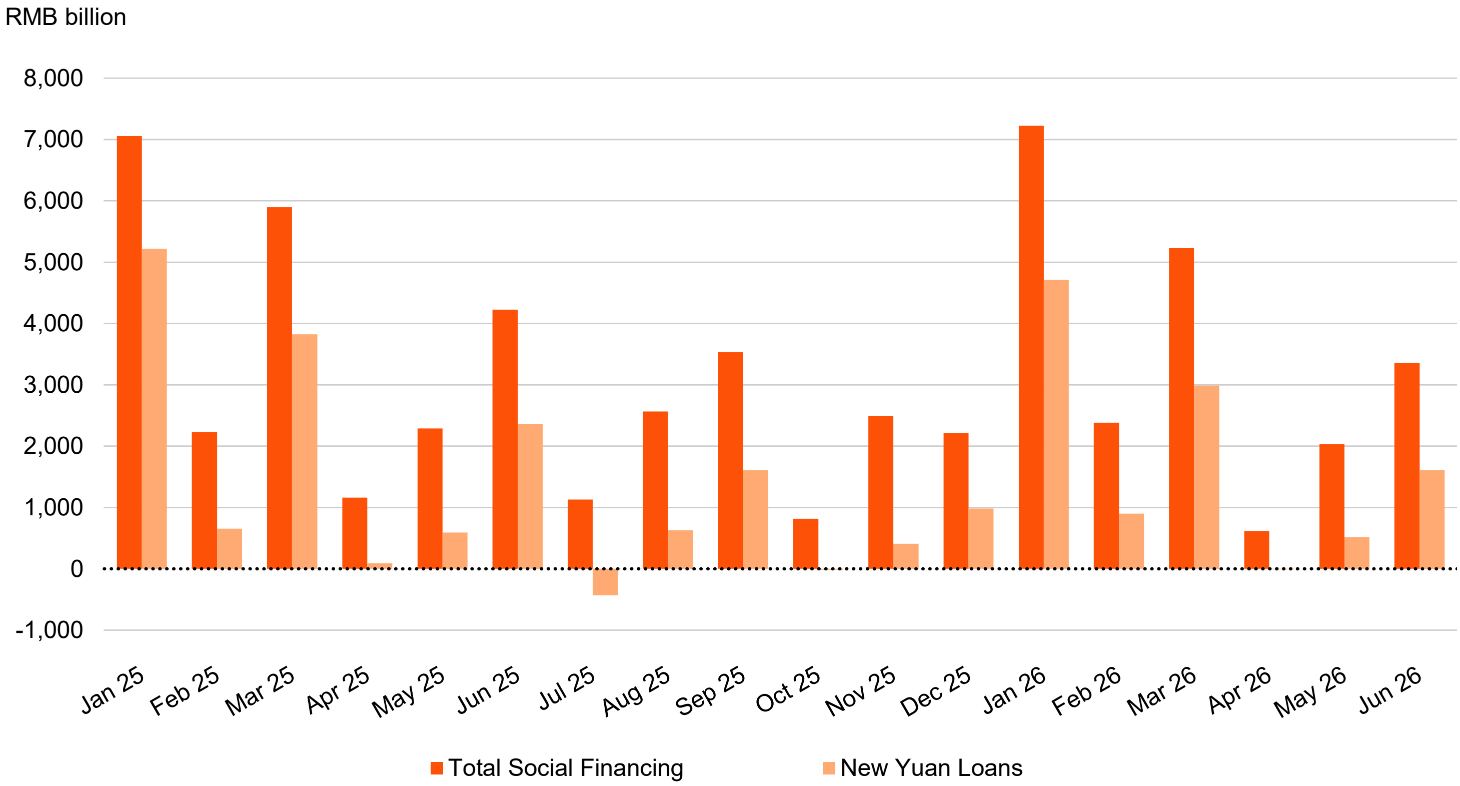
Bank credit was subdued in the first half. New RMB loans totalled RMB 10.72 trillion, down from RMB 12.92 trillion in the same period of 2025. Demand for traditional bank lending continued to be weighed down by the property downturn, weak household demand for loans, and cautious corporate investment plans.

Monthly data show a pick-up in June, though this should be read against the soft first-half trend rather than as a standalone signal. New RMB loans rose to RMB 1.61 trillion, up from RMB 520 billion in May. Household lending, including mortgages, rose by RMB 264.6 billion after a decline of RMB 141.2 billion in May, while new corporate loans climbed to RMB 1.5 trillion from RMB 640 billion. Whether this marks the start of a more durable recovery in credit demand, or just a temporary rebound, should become clearer over the coming months. Borrowing costs stayed low throughout the first half: the average interest rate on new corporate loans fell by around 20 basis points year-on-year to approximately 3.0%, while new mortgage rates held near 3.1%.

Broader financing activity was somewhat stronger than bank lending alone would suggest, though it points to the same underlying picture. New total social financing amounted to RMB 22.83 trillion in the first half, RMB 4.74 trillion more than a year earlier. Non-bank financing also climbed to RMB 3.36 trillion in June from RMB 2.03 trillion in May.

Taken together, borrowing remains cheap, but lower interest rates are not translating into much stronger demand for credit. A lasting pickup in lending will likely depend on stronger demand for investment and consumption, rather than on the cost of credit alone.

Credit Growth



Source: People’s Bank of China, PwC Analysis

The Second Half: Economic Trajectory and Policy Direction

Policy outlook: fiscal policy takes the lead

The slowdown in Q2 points to a greater need for policy support in the second half. Fiscal policy is likely to play the leading role, while monetary policy is expected to stay supportive. Although first-half growth remained within the official target range, domestic demand has not yet strengthened enough to sustain momentum on its own.

Recent policy signals point in this direction. The latest Politburo meeting reiterated the need to support growth, although it did not announce a major new stimulus package. The focus in the second half is therefore likely to shift to execution — deploying funds that have already been approved, particularly through local governments. New special-purpose local-government bond issuance reached 47% of the annual quota in the first half, before picking up to 66.5% by the end of August — suggesting the Q3 acceleration is already under way. That still leaves roughly a third of the quota available, giving policymakers considerable fiscal room to step up support in the months ahead. This should boost infrastructure spending, helping to stabilise broader fixed-asset investment even without a large new stimulus package.

Monetary policy is likely to remain accommodative, though the backdrop has become more nuanced. Domestic inflation remains subdued enough to leave room for a supportive stance: some of the improvement in producer prices during the first half reflected firmer global energy prices, a tailwind that could fade if external tensions ease, while consumer price inflation, despite some pickup, remains low overall. At the same time, global tightening is pulling in the opposite direction. With the Fed and ECB leaning towards tighter policy and yield gaps with China widening, the PBoC may take a more measured approach to any further easing.

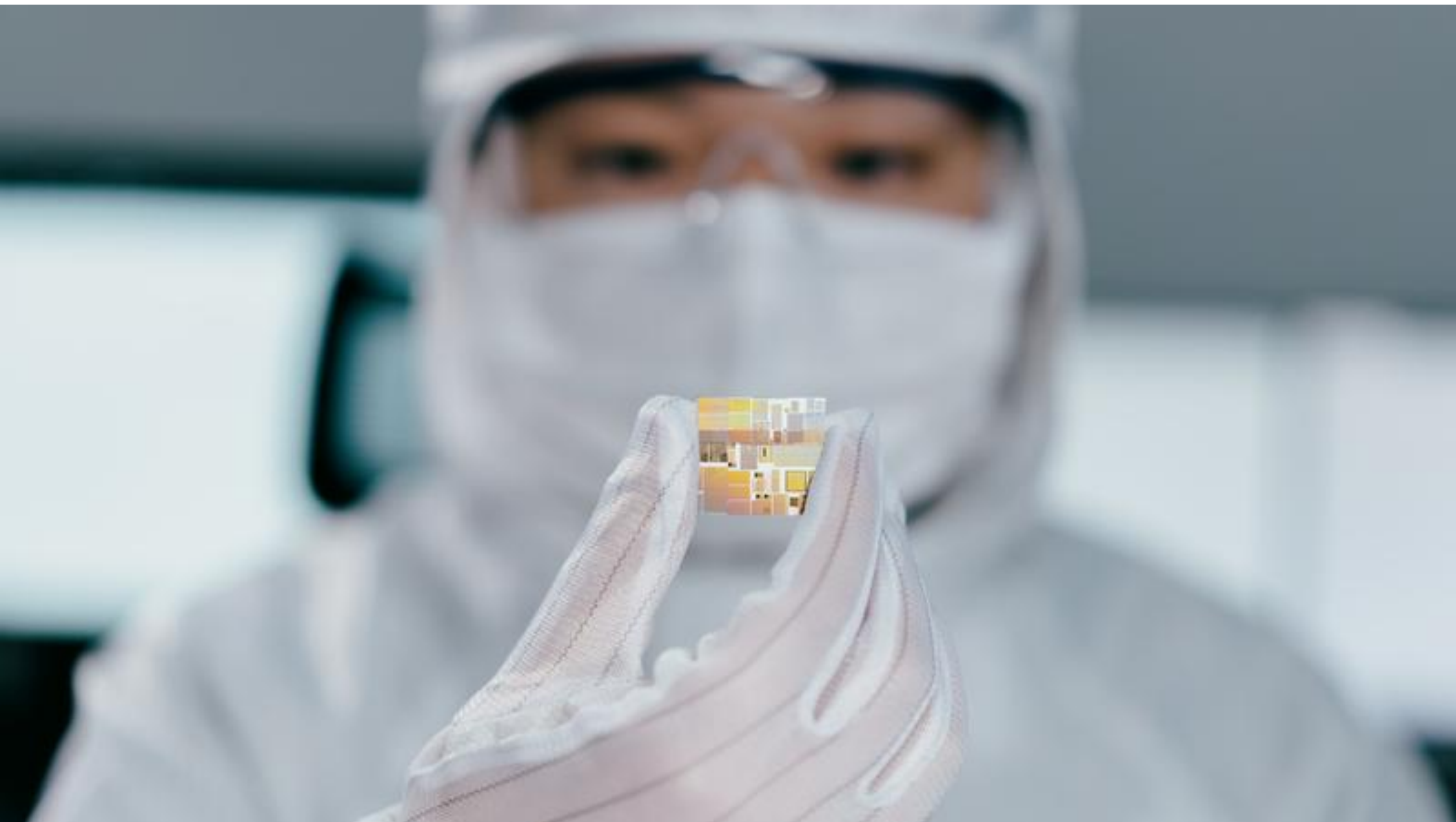
The bigger constraint now is demand for credit, not its cost. Borrowing is already cheap, but demand for loans and private investment remains uneven. The emphasis in the second half will likely be on combining near-term fiscal support with longer-term measures that strengthen consumption and investment.

Export Outlook: Global Demand Stays Strong, but Trade Tensions Are the Wildcard

Exports should remain a key pillar of growth in the second half, particularly for technology-related manufacturing. China continues to benefit from two major sources of external demand: the global boom in AI investment and the broader shift toward clean energy, both of which should help offset weaker momentum elsewhere in the domestic economy.

The AI investment boom is likely to be the more significant of the two. Trade in computing-related hardware, including electronic components and computer parts used in data centres and other computing infrastructure, rose 56.6% year-on-year in the first half and contributed 6.9 percentage points to export growth. As global investment in data centres, semiconductors and computing capacity continues, China's electronics and advanced manufacturing exports should stay well supported. The shift to clean energy, meanwhile, is expected to keep supporting demand for EVs and related equipment.

Trade tensions with the United States and the European Union remain the clearest risk to this outlook, particularly in sectors where trade policy and geopolitical competition increasingly overlap. The medium-term picture remains positive, but growth is likely to vary across products and markets.

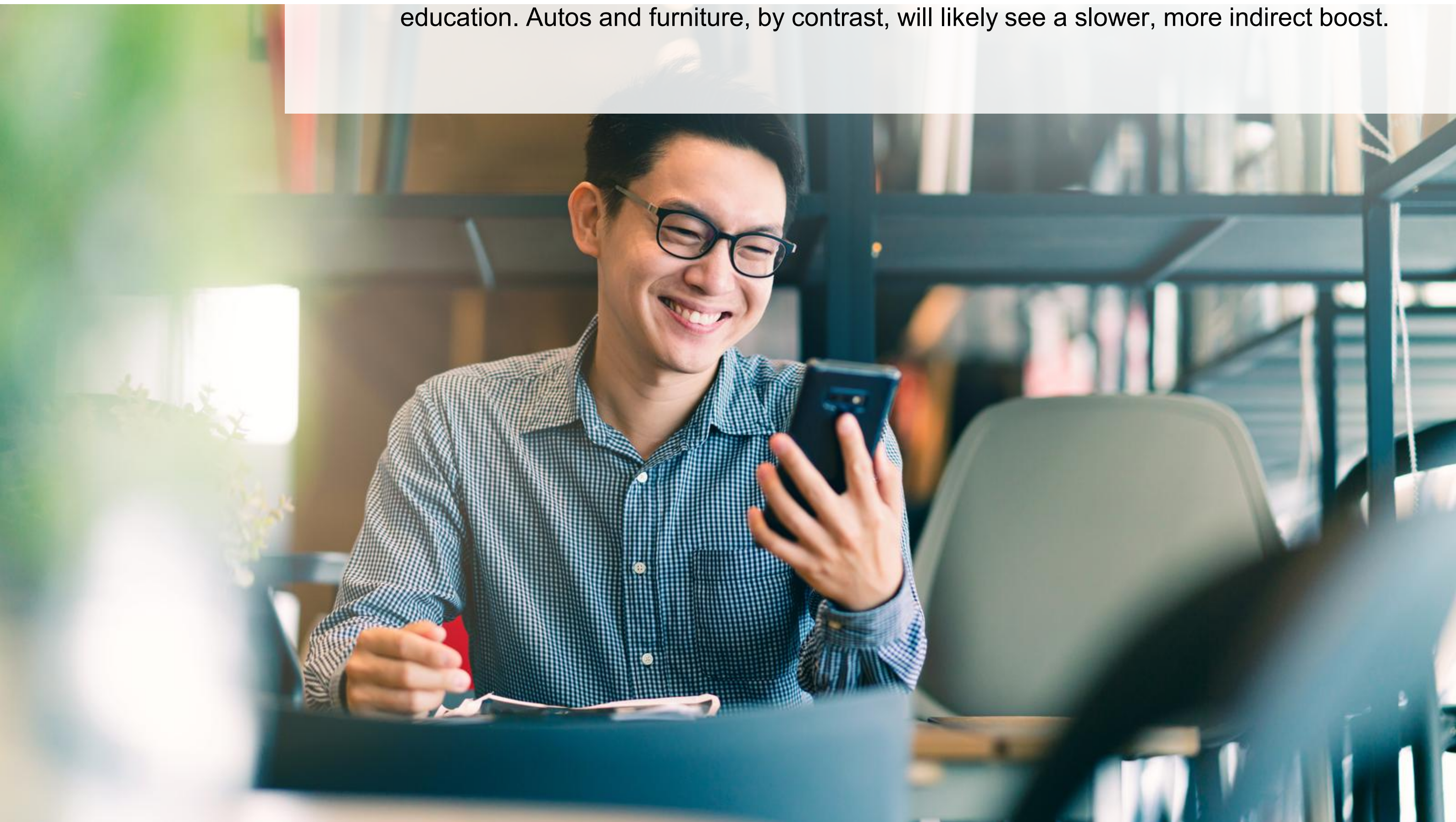


Consumption outlook: near-term support, longer-term rebalancing

Consumption's softness reflects a mix of temporary factors and longer-term structural change. Earlier rounds of trade-in incentives pulled purchases forward, and the payback from that has weighed on recent readings. Growth should stay soft in the near term before picking up gradually as replacement demand rebuilds.

Policymakers are likely to add further support, though targeted and incremental rather than broad-based. Should export growth slow later in the year, household spending will need to carry more of the growth burden. Expect another round of trade-in incentives, potentially covering a wider range of products than earlier rounds, which focused mainly on big-ticket household items. Recent measures targeting smaller cities and county-level markets point in the same direction. The priority will likely be preventing further weakness rather than forcing a quick rebound.

The more important shift is structural: raising consumption's share of GDP on a lasting basis through what policymakers call "investing in people" — meaning higher household income and more social spending on healthcare and elderly care, so households feel secure enough to save less and spend more. This underpins the 15th Five-Year Plan's consumption agenda, which now carries a concrete target: the State Council's first standalone five-year consumption plan (2026–30) targets RMB 60 trillion in retail sales by 2030, implying annual growth of roughly 3.7%. Services are a particular focus within this agenda, both as a core part of "investing in people" and as a reflection of the broader shift in household spending toward culture, tourism, and education. Autos and furniture, by contrast, will likely see a slower, more indirect boost.



Fixed-asset investment outlook: likely to improve, but still shaped by structural adjustment

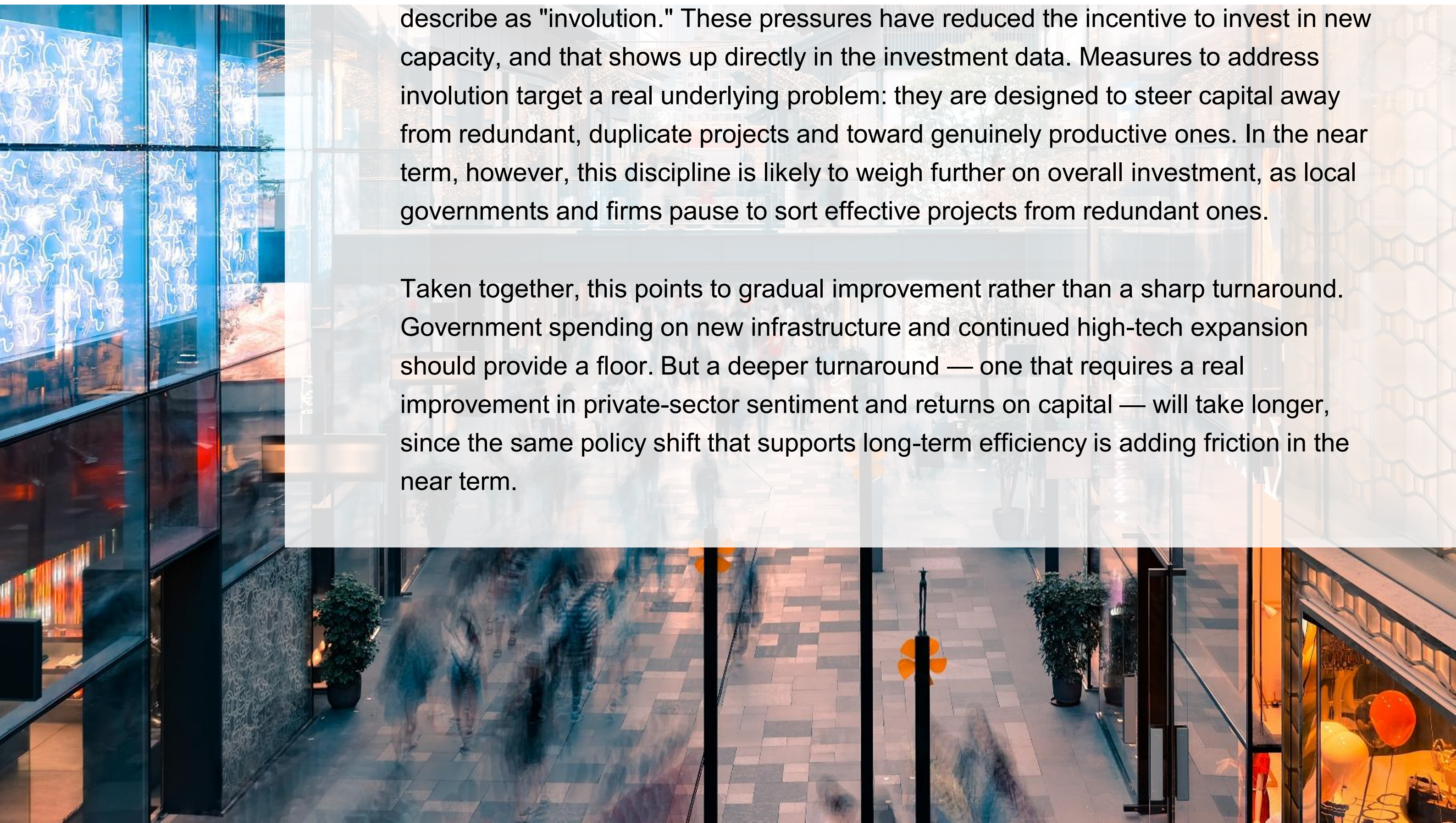
Fixed-asset investment is likely to stay soft heading into the second half, even if government spending helps steady the picture. This is not simply a temporary dip: investment first turned negative in mid-2025 and stayed in decline for the rest of that year — a pattern not seen in decades — and the underlying causes behind that shift remain largely in place. Weak credit data tell a similar story: this looks less like a lack of available financing and more like a lack of demand, with investors simply not seeking capital at the pace they once did.

Some of this reflects a deliberate shift in priorities rather than a broader loss of momentum. The property downturn remains the single largest drag on headline investment, but the capital once tied up in real estate is gradually being redirected toward more productive, policy-backed sectors.

The more telling signal is that the weakness has spread well beyond property. Manufacturing investment has started to decline too, and private investment continues to fall further behind government-led spending — even as high-tech manufacturing defies the trend and keeps expanding. That divide points to a two-speed investment economy: capital is flowing confidently into strategic, government-favoured sectors, while broader private-sector demand stays on the sidelines.

Profit margins in several industries have been squeezed for years by low factory usage and aggressive price wars — a pattern of intense, cut-throat competition policymakers describe as "involution." These pressures have reduced the incentive to invest in new capacity, and that shows up directly in the investment data. Measures to address involution target a real underlying problem: they are designed to steer capital away from redundant, duplicate projects and toward genuinely productive ones. In the near term, however, this discipline is likely to weigh further on overall investment, as local governments and firms pause to sort effective projects from redundant ones.

Taken together, this points to gradual improvement rather than a sharp turnaround. Government spending on new infrastructure and continued high-tech expansion should provide a floor. But a deeper turnaround — one that requires a real improvement in private-sector sentiment and returns on capital — will take longer, since the same policy shift that supports long-term efficiency is adding friction in the near term.



Author

Jackie Yan
PwC China Economist
+852 2289 5460
jackie.z.yan@hk.pwc.com

www.pwchk.com