China’s mid-year economic review: forging ahead amid volatility and divergence

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China’s H1 growth holds steady as new engines emerge

- Gross domestic product (GDP) posts five-year high incremental growth amid a pronounced K-shaped economic pattern: China’s GDP totaled RMB69.57 trillion in the first half of the year (H1), rising 4.7% year-on-year (YoY)[1] and recording its biggest incremental increase over the past five years for the same period. Real GDP growth moderated to 4.3% in the second quarter (Q2), while improved price indicators pushed nominal GDP growth to 5.9%.[2] The GDP deflator turned positive for the first time in 12 quarters, reflecting a pattern of weaker real output amid rising prices. A K-shaped landscape was evident across the economy – emerging growth drivers including high-end manufacturing, the digital economy and modern services contributed over 40% of total GDP growth.

- Consumption divergence accelerates with new drivers gaining momentum: China’s total retail sales of consumer goods hit RMB24.87 trillion in H1, up 1.3% YoY.[3] While households turned more conservative on big-ticket spending, demand for services, premium upgraded goods and new consumption continued to expand. Markets showed clear divergence across distribution channels and geographic tiers, with online retail sales outpacing offline brick-and-mortar consumption. Rural consumption growth maintained its outperformance over urban consumption, with lower-tier markets emerging as a key driver of new consumption growth, underpinning domestic demand expansion and urban-rural integrated development.

- Fixed-asset investment (FAI) records deepening declines amid periodic headwinds: FAI fell 5.7% YoY in H1[4], with downward momentum accelerating markedly in Q2. Most traditional infrastructure projects saw delayed progress due to slower issuance of local special bonds, however, FAI in new infrastructure such as computing power and next-generation communication networks defied the broader downturn. Looking ahead to the second half of the year (H2), FAI in high-end manufacturing and infrastructure is set for a steady recovery, with the implementation of major infrastructure and manufacturing projects and the gradual deployment of RMB800 billion new policy financial instruments. The construction of the “six networks” will serve as a critical lever to mobilize private capital.

- Foreign trade remains resilient amid a narrowing surplus: China’s total goods trade reached RMB25.47 trillion in H1, rising 16.9% YoY[5] with a moderate narrowing in the accumulated trade surplus. Robust artificial intelligence (AI) industry expansion and global low-carbon transition served as core growth drivers for outbound shipments, while imports of tech-related goods also picked up momentum. Exports from the private segment kept rising, with new materials, electronic information products and high-end equipment increasing by 44.5%, 43.1% and 29.8%[6], respectively. Looking ahead to H2, export growth will be increasingly underpinned by structural advantages, though price volatility will remain a persistent downside risk to trade volumes.

1. National Bureau of Statistics (NBS), https://www.stats.gov.cn/sj/zxfb/202607/t20260716_1964142.html
2. The State Council of the People’s Republic of China (PRC), https://www.gov.cn/lianbo/202607/content_7075685.htm
3. NBS, https://www.stats.gov.cn/sj/zxfb/202607/t20260715_1964127.html
4. NBS, https://www.stats.gov.cn/sj/zxfb/202607/t20260715_1964124.html
5. General Administration of Customs (GAC), http://www.customs.gov.cn/customs/2026-07/14/article_2026071409284053539.html
6. The State Council of the PRC, https://www.gov.cn/lianbo/fabu/202607/content_7075392.htm

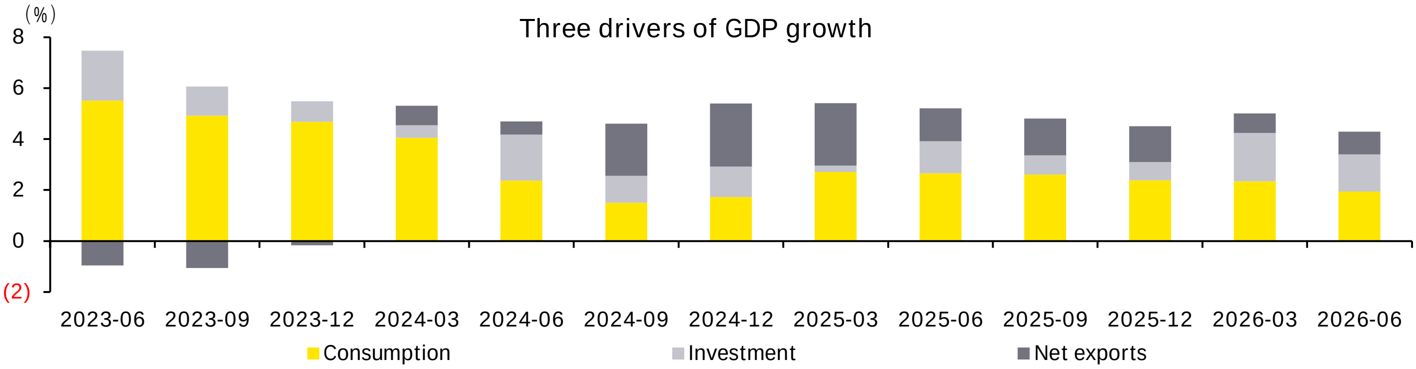
Strengthening counter-cyclical adjustment in H2 to stabilize growth and advance industrial transformation

- Accelerating fiscal spending and doubling down on hard tech: Against sustained K-shaped economic divergence, the July Politburo meeting set the core policy tone of "fully leveraging the existing policies and rolling out incremental measures in a timely manner" and reiterated the need to strengthen counter-cyclical adjustment. On the fiscal side, authorities will speed up the issuance and deployment of proceeds from local special bonds and ultra-long-term special treasury bonds, and more capital expenditures are poised to shift toward hard tech such as AI and advanced manufacturing. From a monetary perspective, the central bank will maintain a moderately accommodative stance while enhancing policy adjustments and a targeted approach. Reserve requirement ratio cuts and interest rate reductions will be implemented on a discretionary basis.
- Services and innovative consumption usher in a new era of high-quality development: Services consumption is expected to sustain robust growth in H2, with structural divergence further intensifying across sub-sectors. The recently unveiled 17 new measures for AI-enabled consumption drive coordinated advancement across five key dimensions: supply, demand, infrastructure, business models and regulatory governance. These efforts empower the intelligent transformation of consumer service sectors, smart elderly care and large language models in education, accelerating product iteration and the large-scale commercialization of high-value scenarios. Smart home devices, lightweight wearables and service robots are expected to see explosive growth.
- Policy tailwinds fuel scaled AI commercialization: Since the start of the year, integration between domestic AI agents and the real economy has deepened substantially. The industry is rapidly shifting its focus from foundational computing infrastructure construction toward high-value, large-scale commercial rollout. The 2026 Digital-Physical Synergy Initiative addresses core bottlenecks in industrial transformation, covering 20 pillar industries including steel, automotive manufacturing, aerospace, advanced equipment manufacturing and new materials. The initiative aims to build a mature industrial AI application ecosystem by year-end and to form a virtuous closed loop of "data collection–AI model iteration–industry-specific scenario implementation".
- Multiple efforts to promote balanced trade development: On the policy front, emerging business forms such as digital and green trade have been designated as priority development areas. Authorities are ramping up the supply of high-quality services through fiscal and financial tools, trade facilitation reforms and innovation incentives. Meanwhile, the government will gradually ease market access restrictions in telecommunications, education, culture, health care, finance and other fields. By proactively aligning with high-standard international economic and trade rules, China will lift foreign equity caps in service industries, attracting global resources into the market.
- Real estate enters a new policy cycle: After years of deep adjustment, the real estate market has transitioned into a new phase featuring regular risk management, stock-based transformation and household balance sheet repair. Policy priorities have shifted from targeted risk mitigation toward stabilizing the market, boosting domestic demand and lifting consumption. The real estate market is expected to see notable K-shaped divergence in H2. First- and second-tier cities will see a resilient recovery, while third- and fourth-tier cities will focus on stabilization and speed up inventory destocking.
- Multi-tiered capital markets bolster technological innovation: A series of institutional reforms have steadily broadened IPO access for hard-tech enterprises. The STAR Market has expanded its fifth set of listing criteria, the ChiNext Board has rolled out a fourth listing standard for tech innovators, and the Hong Kong Stock Exchange has launched its dedicated Technology Enterprise Channel. These initiatives have transformed capital markets from a traditional financing tool into a core platform underpinning the innovation-driven development strategy, supporting the development of AI, quantum computing and commercial aerospace, etc. As the direct financing system matures, more capital will flow into R&D and advanced manufacturing sectors to fuel industrial upgrading.

China’s H1 growth holds steady as new engines emerge

- GDP posts five-year high incremental growth amid a pronounced K-shaped economic pattern: China’s GDP totaled RMB69.57 trillion in H1, growing 4.7% YoY[7] and registering its biggest incremental increase over the past five years for the same period. Soft momentum in investment and consumption resulted in a pattern of weak real output amid rising prices in Q2. Real GDP growth moderated from 5.0% in the first quarter (Q1) to 4.3% in Q2, while improved price indicators pushed nominal GDP growth up from 4.9% to 5.9%.[8] The GDP deflator swung back to positive growth for the first time in 12 quarters, rising from -0.06% to 1.53%. A K-shaped landscape was evident across the economy – emerging growth engines such as high-end manufacturing, the digital economy and modern services contributed more than 40% of total GDP growth, signaling a policy pivot from stabilizing aggregate output to improving operational efficiency. Though improved price dynamics have lent support to corporate earnings for now, domestic demand stays under pressure and uncertainty remains over whether deflationary pressures will ease in a sustainable manner.

Figure 1. Exports remain a key growth driver of H1 economic expansion

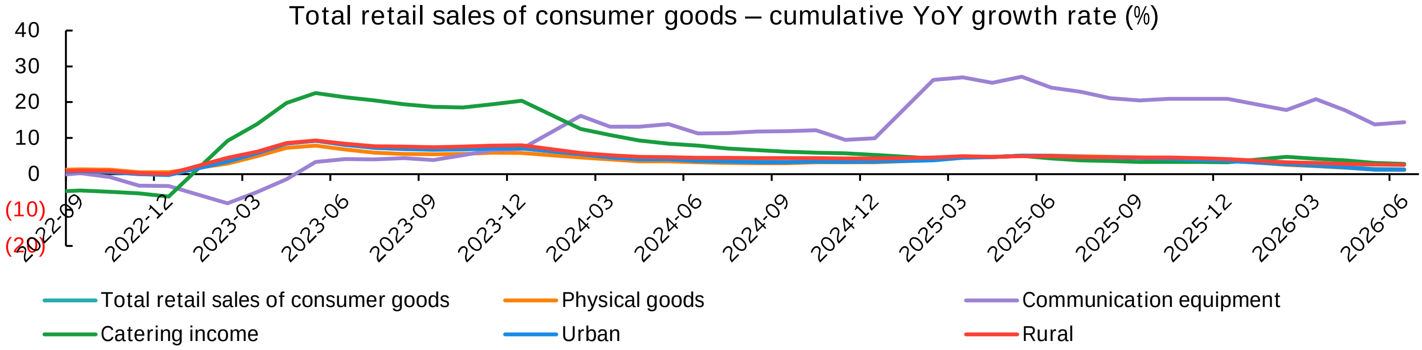


Source: NBS

- Consumption divergence accelerates with new drivers gaining momentum: China’s total retail sales of consumer goods hit RMB24.87 trillion, up 1.3% YoY. June consumption swung back to positive growth with a mild month-on-month increase of 0.38%. As trade-in subsidies faded and manufacturers’ price competition cooled off, households turned more conservative on big-ticket spending, dragging down overall durable goods consumption. From January to June, sales of automobiles, home appliances and furniture dropped 12.6%, 7.4% and 3.7% YoY[9], respectively. On the other hand, demand for services and smart consumption expanded at a steady pace. Cultural tourism-related spending, including transportation and catering, grew 6.1% and 4.9% YoY, while sales of electronic products surged 9.5%.[10] Markets showed clear divergence across distribution channels and geographic tiers. Online retail sales rose 4.8% YoY in H1, continuously outpacing offline brick-and-mortar consumption. Rural consumption growth outpaced that in urban areas continuously, with the gap widening to 1.3 percentage points. Backed by smart logistics networks, digital supply chains and integrated online-and-offline omnichannel services, lower-tier markets have become a key driver of new consumption growth, underpinning domestic demand expansion and urban-rural integrated development.

7. NBS, https://www.stats.gov.cn/sj/zxfb/202607/t20260716_1964142.html
8. The State Council of the PRC, https://www.gov.cn/lianbo/202607/content_7075685.htm
9. NBS, https://www.stats.gov.cn/sj/zxfb/202607/t20260715_1964127.html
10. The State Council of the PRC, https://www.gov.cn/lianbo/202607/content_7075145.htm

Figure 2. Total retail sales rebounded in June amid persistent market divergence

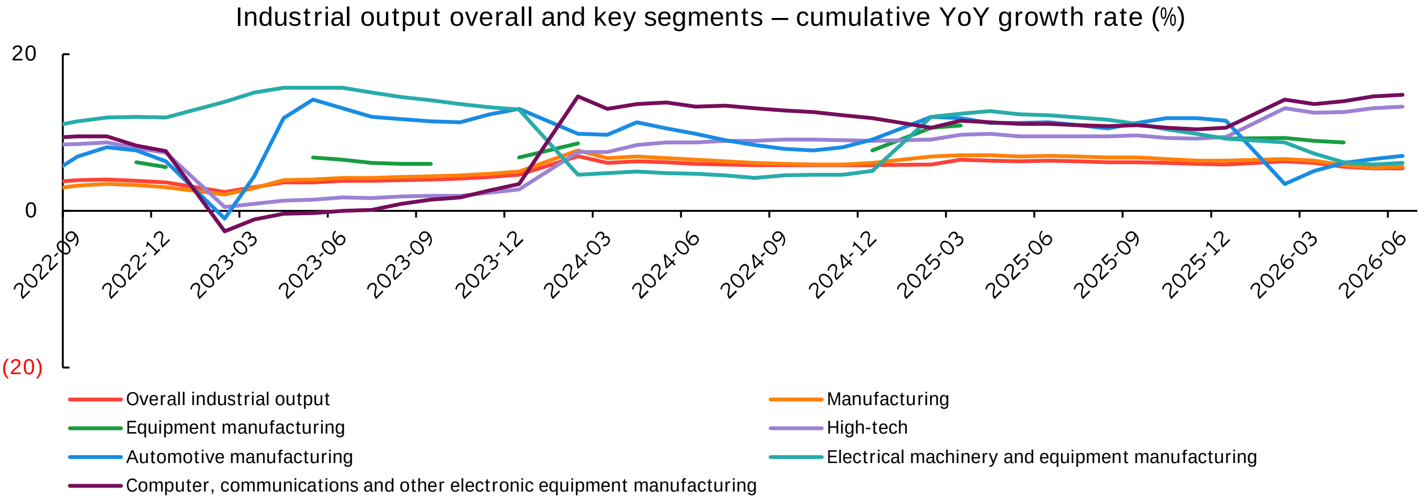


Source: NBS

- Industrial production lacked strong momentum, yet profit improvements persisted: The value-added of industrial enterprises above designated size rose 5.4% YoY[11] in H1. While overall growth moderated in Q2, new drivers strengthened further. Value added in high-tech manufacturing and equipment manufacturing increased by 14% and 9.7% YoY, picking up 1.5 and 0.8 percentage points respectively from Q1. On the profit side, industrial enterprises above designated size generated total profits of RMB3,947.99 billion, up 18.7% YoY.[12]

Buoyant AI and semiconductor sectors further lifted profit growth of the computer, communications and electronics industry to 96.9% YoY. Looking ahead, industrial profits remain on a recovery path. However, dragged by high base effects and pressures on both domestic and external demand, profit growth is set to moderate from current high levels. Profit divergence across industries will continue to widen. Sectors such as automobiles and electrical machinery may face margin compression amid elevated costs and limited room for price hikes.

Figure 3. Industrial production showed periodic cooling alongside structural divergence



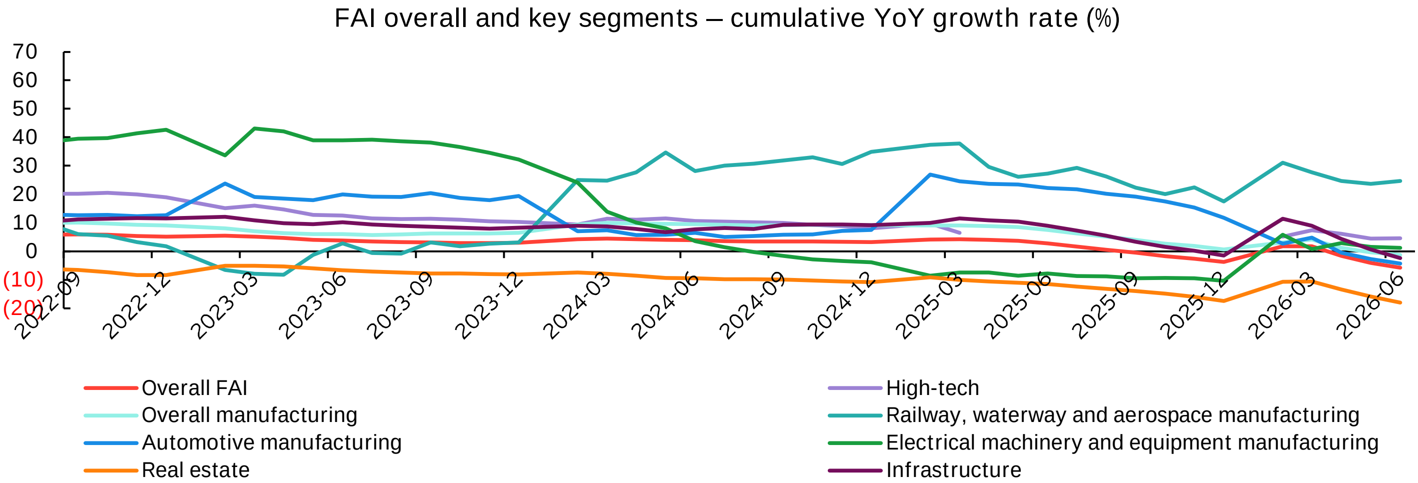
Source: NBS

11. NBS, https://www.stats.gov.cn/sj/zxfb/202607/t20260715_1964123.html
12. NBS, https://www.stats.gov.cn/sj/zxfb/202607/t20260727_1964194.html

- FAI records deepening declines amid periodic headwinds: FAI fell 5.7% YoY[13] in H1, with downward momentum accelerating markedly in Q2. By sector, FAI in infrastructure and manufacturing weakened concurrently, down 2.4 and 1.2 percentage points respectively. Most traditional infrastructure projects saw delayed progress due to slower issuance of local special bonds, however, FAI in new infrastructure such as computing power and next-generation communication networks defied the broader downturn. FAI in internet-related services and fiber-optic manufacturing increased by 39.9% and 26.5%[14], respectively. Manufacturing investment cooled mainly due to sluggish domestic demand and rising raw material costs.

Nevertheless, industrial upgrading and supply chain self-reliance continued to underpin investment in the niche segments. Looking ahead to H2, FAI in high-end manufacturing and infrastructure is set for a steady recovery, with the implementation of major infrastructure and manufacturing projects and the gradual deployment of RMB800 billion new policy financial instruments. The construction of the “six networks” will serve as a critical lever to mobilize private capital and expand four key industrial chains: power and new energy, computing and communications, construction machinery and modern logistics. Over the medium- to long-term, industrial synergy and corporate earnings improvement will remain the fundamental anchors for a sustainable investment rebound.

Figure 4. Investment in infrastructure and manufacturing needs to be bolstered



Source: NBS

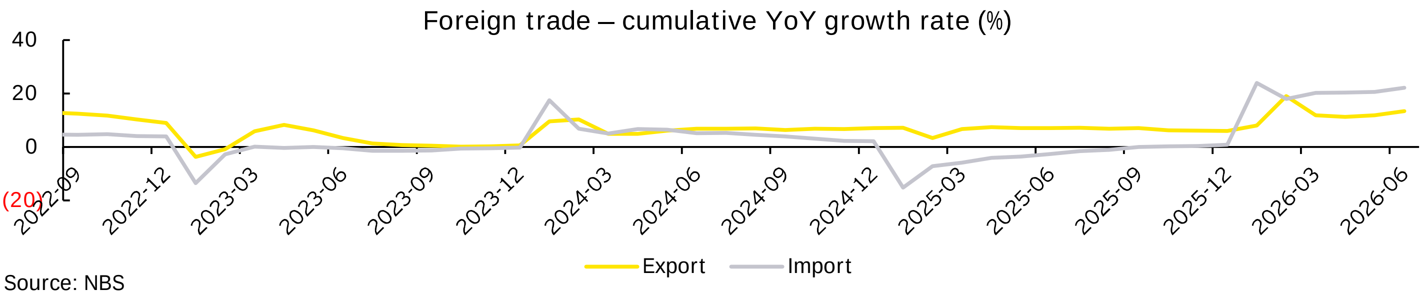
- Foreign trade remains resilient amid a narrowing surplus: China’s total goods trade reached RMB25.47 trillion in H1, rising 16.9% YoY[15] with a moderate narrowing in the accumulated trade surplus. Robust AI industry expansion and global low-carbon transition served as core growth drivers for outbound shipments, with exports of integrated circuits and new energy vehicles surging by 88.7%[16] and 120% YoY[17] in H1. Exports from the private segment kept rising, with new materials, electronic information products and high-end equipment increasing by 44.5%, 43.1% and 29.8%[18], respectively.

13. NBS, https://www.stats.gov.cn/sj/zxfb/202607/t20260715_1964124.html
14. NBS, https://www.stats.gov.cn/sj/sjjd/202607/t20260716_1964145.html
15. GAC, http://www.customs.gov.cn/customs/2026-07/14/article_2026071409284053539.html
16. GAC, http://www.customs.gov.cn/customs/2026-07/14/article_2026071409284169645.html
17. The State Council of the PRC, https://www.gov.cn/yaowen/liebiao/202607/content_7074898.htm
18. The State Council of the PRC, https://www.gov.cn/lianbo/fabu/202607/content_7075392.htm

On the import side, strong growth was again boosted by expanding AI computing capacity and proactive inventory restocking across the electronics industrial chain. Imports of automatic data processing equipment and components jumped 72.2% YoY[19], driving a notable expansion in overall volumes.

Looking ahead to H2, Section 301 may accelerate the structure divergence of exports, but upward trends from overseas computing power investment deployment, server capacity expansion and semiconductor inventory restocking will continue to materialize. Nevertheless, price volatility will remain a persistent downside risk to trade volumes.

Figure 5. Exports continue to remain robust on global tech cycle upswing

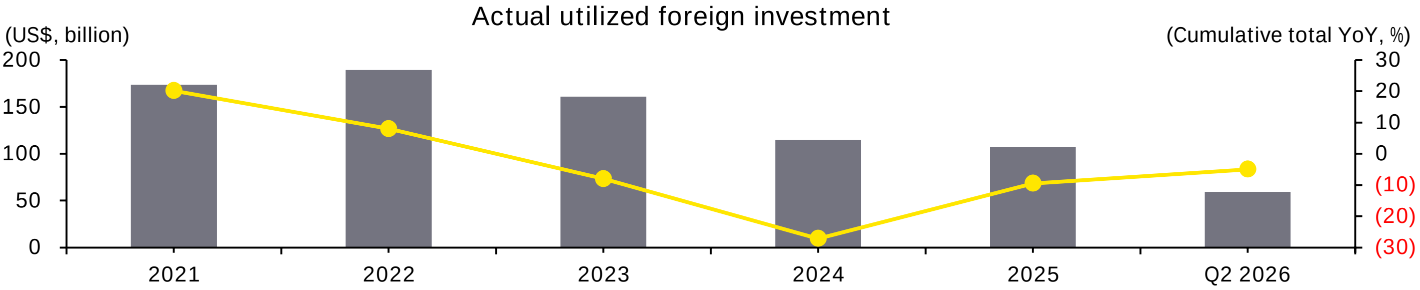


Source: NBS

- Inbound foreign direct investment (FDI) shows further signs of stabilization: In H1, actual utilized foreign investment reached RMB402.1 billion, marking two straight months of positive YoY growth and the overall decline narrowing further to 5%. FDI in R&D and design services, as well as electronics and communications equipment manufacturing, surged markedly by 82% and 52% YoY[20], respectively. In late June, China unveiled a 15-point action plan[21] to stabilize and upgrade support for foreign investment. With manufacturing access restrictions now fully lifted, the plan prioritizes expanding market access in services, finance and pharmaceuticals, while streamlining processes for cross-border mergers and acquisitions (M&As), data flows and domestic reinvestment by foreign firms.

To further open the services sector, the plan adds pilot programs in vocational training, schools and high-level universities, while allowing more foreign financial institutions to manage risks via treasury bond futures and conduct fund investment advisory services. For the pharmaceutical sector, the plan carves out new space with cross-border segmented production of biologics and chemical drugs, allowing drug production stages to span different countries. It also expands pilot zones for wholly foreign-owned hospitals and encourages insurers to cover more innovative drugs and devices. Fueled by this set of initiatives, hidden barriers within the service industry and beyond will likely be removed rapidly, creating new opportunities for foreign investors.

Figure 6. High-tech industries and services strengthen their ability to attract foreign investment



Source: Ministry of Commerce

19. GAC, http://www.customs.gov.cn/customs/2026-07/14/article_2026071409284233760.html
20. Ministry of Commerce, https://www.mofcom.gov.cn/xwfb/rcxwfb/art/2026/art_ea6d68fe5ee74367a2be1ca271765033.html
21. The State Council of the PRC, https://www.gov.cn/zhengce/zhengceku/202606/content_7072838.htm

Strengthening counter-cyclical adjustment in H2 to stabilize growth and advance industrial transformation

- Accelerating fiscal spending and doubling down on hard tech: Against sustained K-shaped economic divergence, the July Politburo meeting set the core policy tone of "fully leveraging the existing policies and rolling out incremental measures in a timely manner"[22] and reiterated the need to strengthen counter-cyclical adjustment. On the fiscal side, authorities will speed up the issuance and deployment of proceeds from local special bonds and ultra-long-term special treasury bonds, with government bond supply set to peak in the third quarter. "Six networks" will act as key levers to bolster investment in H2 and more capital expenditures are poised to shift toward hard tech such as AI and advanced manufacturing. From a monetary perspective, the central bank will maintain a moderately accommodative stance while enhancing policy adjustments and a targeted approach. It will guard against fund idling in the financial system and curb financial risks, keeping a close watch on vulnerabilities at small and medium-sized financial institutions, the property sector and operational debt of local government financing platforms. Reserve requirement ratio cuts and interest rate reductions will be implemented on a discretionary basis.
- Services and innovative consumption usher in a new era of high-quality development: Services consumption is expected to sustain robust growth in H2, with structural divergence further intensifying across sub-sectors. On one hand, the integrated "culture, sports and tourism IP + digitalization" model nurtures a high-stickiness yet volatile traffic-driven economy. The core breakthrough hinges on converting ephemeral online traffic into long-term, sustainable digital assets. The in-depth penetration of AI, extended reality (XR), blockchain and other digital technologies will expand the boundaries of immersive experience consumption, solidifying the layout of the digital ecosystem.

  On the other hand, the recently unveiled 17 new measures[23] for AI-enabled consumption drive coordinated advancement across five key dimensions: supply, demand, infrastructure, business models and regulatory governance. These efforts empower the intelligent transformation of consumer service sectors, smart elderly care and large language models in education, accelerating product iteration and the large-scale commercialization of high-value scenarios. Smart home devices, lightweight wearables and service robots are expected to see explosive industrial growth.
- Policy tailwinds fuel scaled AI commercialization: Since the start of the year, integration between domestic AI agents and the real economy has deepened substantially. The industry is rapidly shifting its focus from foundational computing infrastructure construction toward high-value, large-scale commercial rollout. Jointly launched by the Ministry of Industry and Information Technology and the National Data Administration, the 2026 Digital-Physical Synergy Initiative addresses core bottlenecks in industrial transformation, covering 20 pillar industries including steel, automotive manufacturing, aerospace, advanced equipment manufacturing and new materials. The initiative aims to build a mature industrial AI application ecosystem by year-end and to form a virtuous closed loop of "data collection–AI model iteration–industry-specific scenario implementation". Meanwhile, as computing power becomes more affordable and accessible, the AI industry is undergoing structural reshuffling and market consolidation. Leveraging technological strengths, computing resources and ecosystems, leading enterprises dominate the high-barrier upstream segments such as computing infrastructure and general-purpose large language models. Small and medium-sized enterprises (SMEs) have withdrawn from homogeneous competition in mainstream segments and adopted differentiated layouts focused on industrial fine-tuned models and edge intelligent services.

22. The State Council of the PRC, https://www.gov.cn/yaowen/liebiao/202607/content_7077056.htm
23. The State Council of the PRC, https://www.gov.cn/zhengce/zhengceku/202606/content_7072672.htm?use_xbridge3=true&loader_name=forest&need_sec_link=1&sec_link_scene=im&theme=light

To streamline collaborative innovation among large enterprises, SMEs and micro firms, seven authorities have jointly issued an *Action Plan for Promoting Collaborative Development among Large, Medium and Enterprises in the Platform Economy (2026-2028)*.[24] The policy requires leading platforms to open core assets including technologies, datasets and computing power to smaller market participants. By 2028, authorities plan to release three batches of platform openness catalogues and support at least 100 pilot projects focused on sharing platform resources, accelerating AI's evolution from isolated pilots to full-scale industrial commercialization.

- Multiple efforts to promote balanced trade development: On the policy front, emerging business forms such as digital and green trade have been designated as priority development areas. Authorities are ramping up the supply of high-quality services through fiscal and financial tools, trade facilitation reforms and innovation incentives. Meanwhile, China's trade in services is shifting from scale expansion to quality upgrading. The international competitiveness of knowledge-intensive and high value-added services continues to rise, with travel services serving as a critical pillar supporting the narrowing services trade deficit. To deepen institutional opening-up, the government will gradually ease market access restrictions in telecommunications, education, culture, health care, finance and other fields. By proactively aligning with high-standard international economic and trade rules, China will lift foreign equity caps in service industries, attracting global resources and boosting domestic market vitality.

- Real estate enters a new policy cycle: After years of deep adjustment, the real estate market has transitioned into a new phase featuring regular risk management, stock-based transformation and household balance sheet repair. Policy priorities have shifted from targeted risk mitigation toward stabilizing the market, boosting domestic demand and lifting consumption. Coordinated measures including inventory housing destocking by state-owned enterprises, credit easing, guaranteed project handovers and improved secondary housing circulation focus on revitalizing existing housing stock and supporting rigid housing demand. These measures will help house prices stabilize amid modest fluctuations, restore household asset values and shore up consumer confidence. *The 15th Five-Year Plan for Urban Renewal*[25] is set to attract more than RMB15 trillion and create a steady, predictable track with multiple benefits: stabilizing investment, expanding domestic demand and enhancing public services. The real estate market is expected to see notable K-shaped divergence in H2. First- and second-tier cities will see a resilient recovery, while third- and fourth-tier cities will prioritize stabilization and accelerate inventory destocking.

- Multi-tiered capital markets bolster technological innovation: A series of institutional reforms have steadily broadened IPO access for hard-tech enterprises. The STAR Market has expanded its fifth set of listing criteria, the ChiNext Board has rolled out a fourth listing standard for tech innovators, and the Hong Kong Stock Exchange has launched its dedicated Technology Enterprise Channel. These initiatives have transformed capital markets from a traditional financing tool into a core platform underpinning the innovation-driven development strategy, supporting the development of AI, quantum computing and commercial aerospace, etc. Meanwhile, private equity and venture capital (VC) act as early-stage incubators, forming a tiered development ecosystem featuring "VC incubation + BSE nurturing + growth on the STAR Market or ChiNext". Capital markets have further refined rules for equity incentives and M&As, enabling tech enterprises to retain core talent and consolidate industrial chain resources. As the direct financing system matures, more capital will flow into R&D and advanced manufacturing sectors to accelerate the commercialization of scientific and technological achievements, establishing a virtuous cycle connecting technology, industry and capital.

24. The State Council of the PRC, https://www.gov.cn/zhengce/zhengceku/202606/content_7072741.htm
25. The State Council of the PRC, https://www.gov.cn/zhengce/content/202605/content_7070539.htm

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