KPMG

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Issue: 2026 Q3



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Key takeaways

- China's real GDP grew 4.7% year on year (YoY) in H1 2026, remaining within the government's 4.5%–5.0% annual growth target. However, growth lost momentum in Q2. Real GDP growth eased to 4.3%, down 0.7 percentage points from Q1, while seasonally adjusted quarter-on-quarter growth slowed to 0.9%, the second-lowest reading for the same period in the past decade. While real activity softened, nominal growth improved. Nominal GDP growth accelerated to 5.9% in Q2, up 1.0 percentage point from Q1.
- On the consumption side, retail sales of consumer goods grew 1.3% YoY in H1, down 3.7 percentage points from a year earlier. Growth slowed to just 0.2% in Q2. This reflected both a high comparison base created by last year's large-scale consumer goods trade-in programme, together with the gradual phase-out of subsidies this year. In addition, although household employment and income have improved, consumer confidence remains subdued and household willingness to spend remains weak.
- Exports remained the strongest growth driver. Exports rose 17.6% YoY in H1, up 11.7 percentage points from a year earlier, with Q2 export growth accelerating to 20.1%. Growth was increasingly supported by two engines: the AI computing supply chain and the new energy supply chain. At the same time, export performance became more polarised, as traditional labour-intensive industries continued to face production relocation with intensifying overseas competition.
- Industrial production moderated in Q2. Growth in industrial value added slowed from 6.1% in Q1 to 5.4% in H1, while capacity utilisation fell to its lowest level for the same period on record. Four factors weighed on production: weaker imports of petrochemical feedstocks following the Middle East conflict; temporary disruptions to coal and copper output and tax enforcement measures; continued weakness in the property sector; and softer consumer demand, which weighed on downstream consumer goods manufacturing.
- Fixed asset investment contracted 5.7% YoY in H1, compared with -3.8% in 2025, while Q2 investment fell 9.7%, nearly 10 percentage points weaker than in Q1. Property investment continued to decline, manufacturing investment softened amid energy supply disruptions and imported inflation pressures, and slower fiscal spending caused infrastructure investment growth to fall sharply from 9.2% in Q1 to -8.6% in Q2.
- Looking ahead, the July Politburo meeting reaffirmed that expanding domestic demand will remain the government's top policy priority in H2. Fiscal policy is expected to accelerate spending and advance investment on the "Six Networks". On consumption, the 15th Five-Year Plan for Expanding Consumption, for the first time, sets a target of around RMB 60 trillion in total retail sales of consumer goods by 2030, suggesting that consumption policies will be implemented more pragmatically.

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Economic growth increasingly reflects a widening K-shaped divergence

Growth rate of major economic indicators, YoY, %

	2020-23 Average	2025 Q1	2025 Q2	2025 Q3	2025 Q4	2026 Q1	2026 Q2
GDP	4.8%	5.4%	5.2%	4.8%	4.5%	5.0%	4.3%
Industrial production	5.1%	6.5%	6.4%	6.2%	5.9%	6.1%	5.4%
Retail sales	3.7%	4.6%	5.4%	3.5%	1.6%	2.4%	0.2%
Fixed asset investment	4.0%	4.2%	2.1%	-6.2%	-12.8%	1.7%	-9.7%
Exports	7.8%	5.7%	6.2%	6.5%	3.8%	14.7%	20.1%
Imports	5.3%	-7.0%	-0.8%	4.6%	3.1%	22.7%	29.6%
Income per capita	4.8%	5.6%	5.3%	5.1%	5.0%	4.9%	5.2%
Fiscal revenue	4.6%	-1.1%	0.6%	2.5%	-7.9%	2.4%	7.3%
Fiscal expenditures	3.7%	4.2%	2.6%	2.4%	-4.2%	2.6%	0.2%

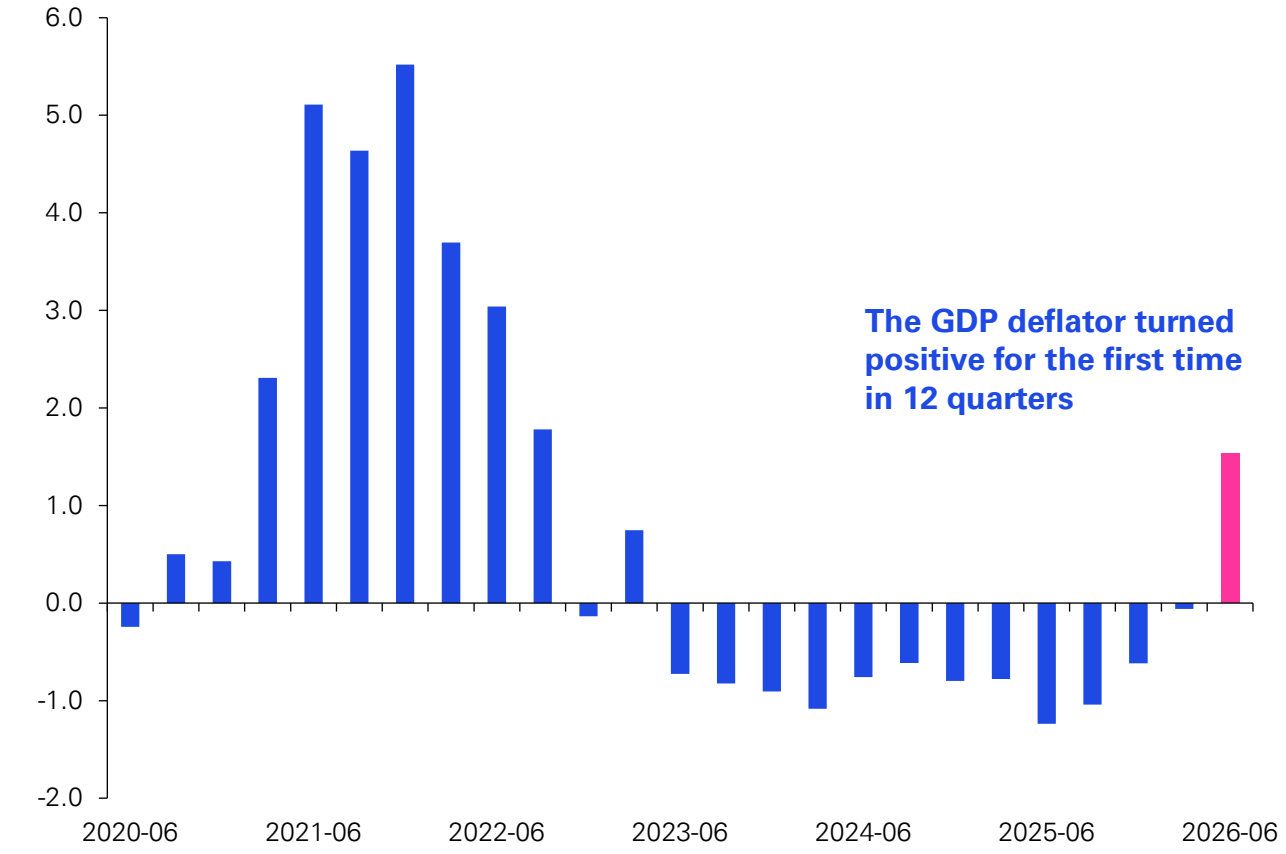
Source: Wind, KPMG analysis
Note: GDP growth and industrial production are in real terms, other indicators are in nominal terms.

- China's GDP growth slowed to 4.3% year on year in Q2, down 0.7 percentage points from Q1, mainly due to two factors. First, the Middle East conflict disrupted commodity supply chains, weighing on upstream production and raising input costs for manufacturers. Second, domestic demand recovery remained weaker than expected.
- The economy also showed a widening K-shaped divergence across four areas: External demand outperforms domestic demand; emerging industries outperform traditional sectors; services outperform industry; and higher-tier cities outperform lower-tier cities. This was particularly evident in property markets, where ~~in~~ tier-one cities show early signs of stabilisation, while lower-tier cities remain under pressure.
- Overall, China's economy remains in a structural transition. Rapid growth in emerging industries is not yet sufficient to offset the contraction of traditional growth drivers, leaving weak domestic demand and the property downturn as key constraints.

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Nominal growth improves despite pressure on real activity

GDP deflator, YoY, %



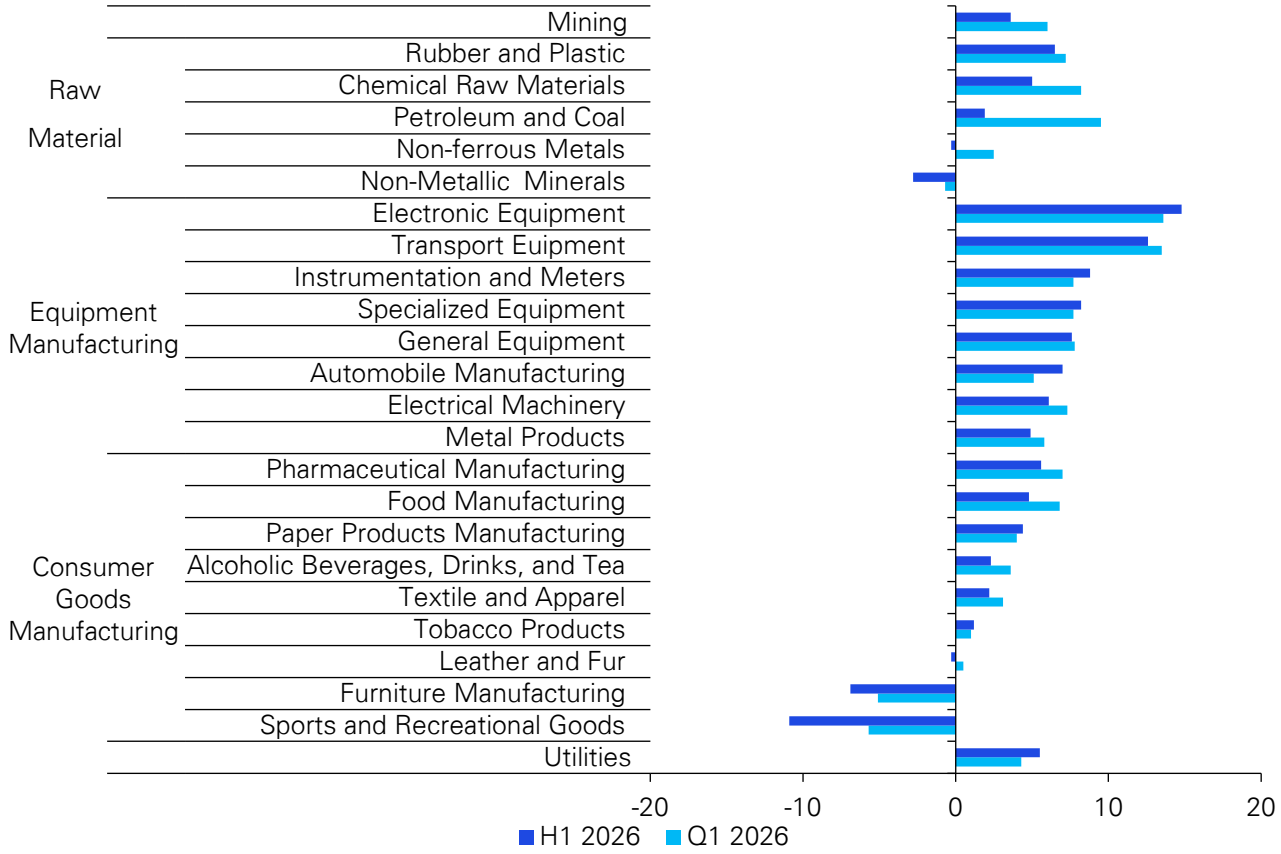
Source: Wind, KPMG analysis

- While real GDP growth has slowed, nominal growth has shown signs of improvement. Nominal GDP growth accelerated to 5.9% in Q2, up from 4.9% in Q1, supported by higher industrial prices amid energy supply disruptions and stronger AI-related demand. The GDP deflator turned positive for the first time in 12 quarters, rising to 1.53% in Q2 2026, 1.6 percentage points higher than in Q1. Economic momentum remained soft in early Q3 amid extreme weather disruptions, weaker domestic demand, and moderating external demand.
- Expanding domestic demand remains the government's key policy priority for H2. On investment, fiscal policy is expected to accelerate spending, speed up special-purpose bond issuance, deploy RMB 800 billion in policy-based financial instruments, and advance investment on the "Six Networks". On consumption, the government will continue to strengthen social spending and expand the supply of high-quality consumer services.

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Industrial activity slows amid supply shocks, while high-tech manufacturing remains resilient

Growth rates of industrial production, by sector, cumulative YoY, %



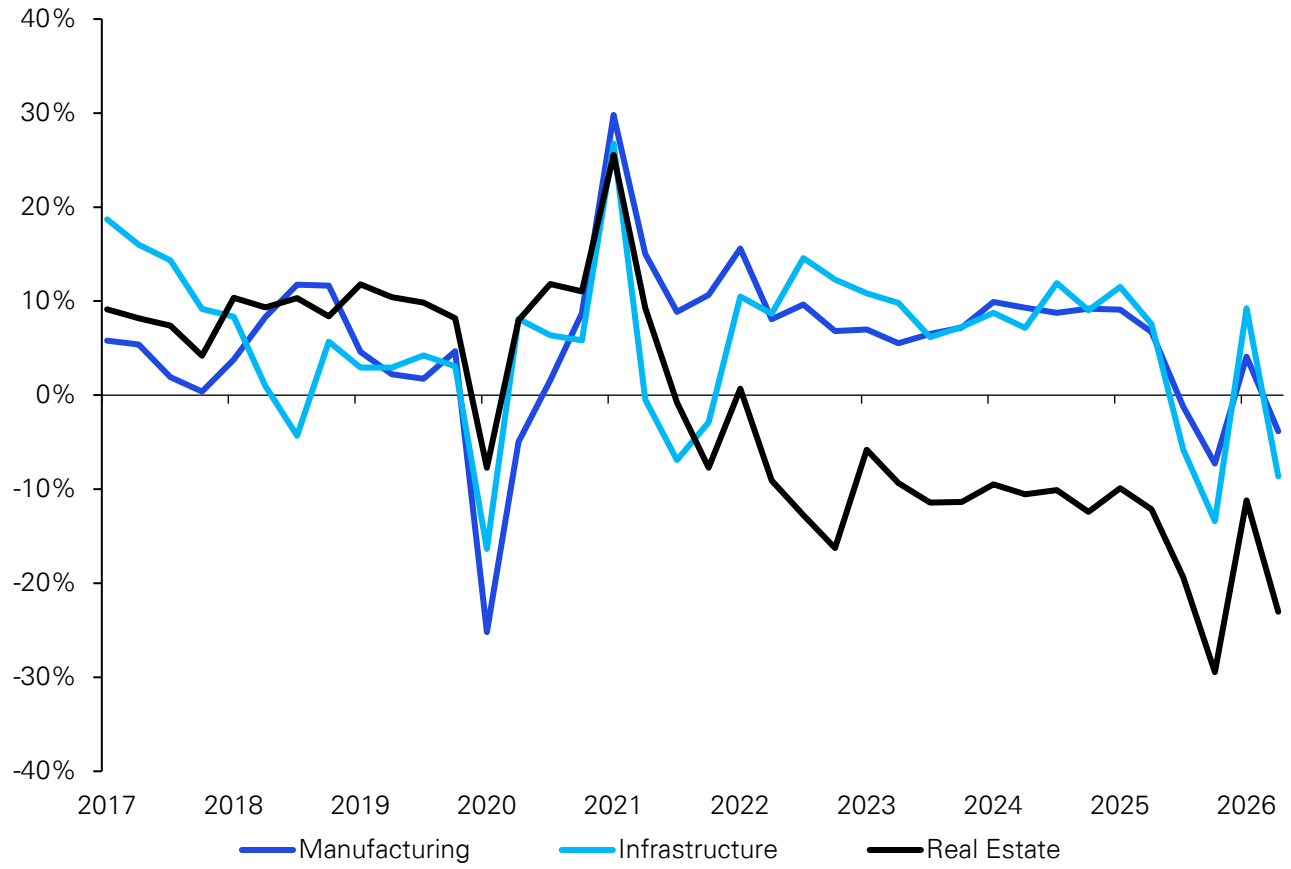
Source: Wind, KPMG analysis

- Industrial activity slowed in Q2, with growth easing from 6.1% in Q1 to 5.4% in H1. The slowdown reflected multiple factors. First, the Middle East conflict disrupted imports of petrochemical raw materials, and growth in petroleum and coal, chemical raw materials, and rubber and plastics slowed in H1. Second, coal and copper production weakened by more than typical seasonal trends due to the Shanxi coal mine accident and the tax authority's crackdown on irregular invoicing practices. Third, weak property market conditions continued to weigh on upstream industries. Finally, weaker household demand cooled production in downstream consumer goods industries.
- However, equipment manufacturing remained resilient, supported by strong external demand for AI-related hardware and new energy products.
- Looking ahead, industrial activity is expected to recover gradually, supported by-a lower base in H2 2025, fading supply-side disruptions, and continued strength in equipment manufacturing.

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Investment slows as policy support fades and confidence weakens

Growth rate of fixed asset investment by sector, quarterly YoY, %



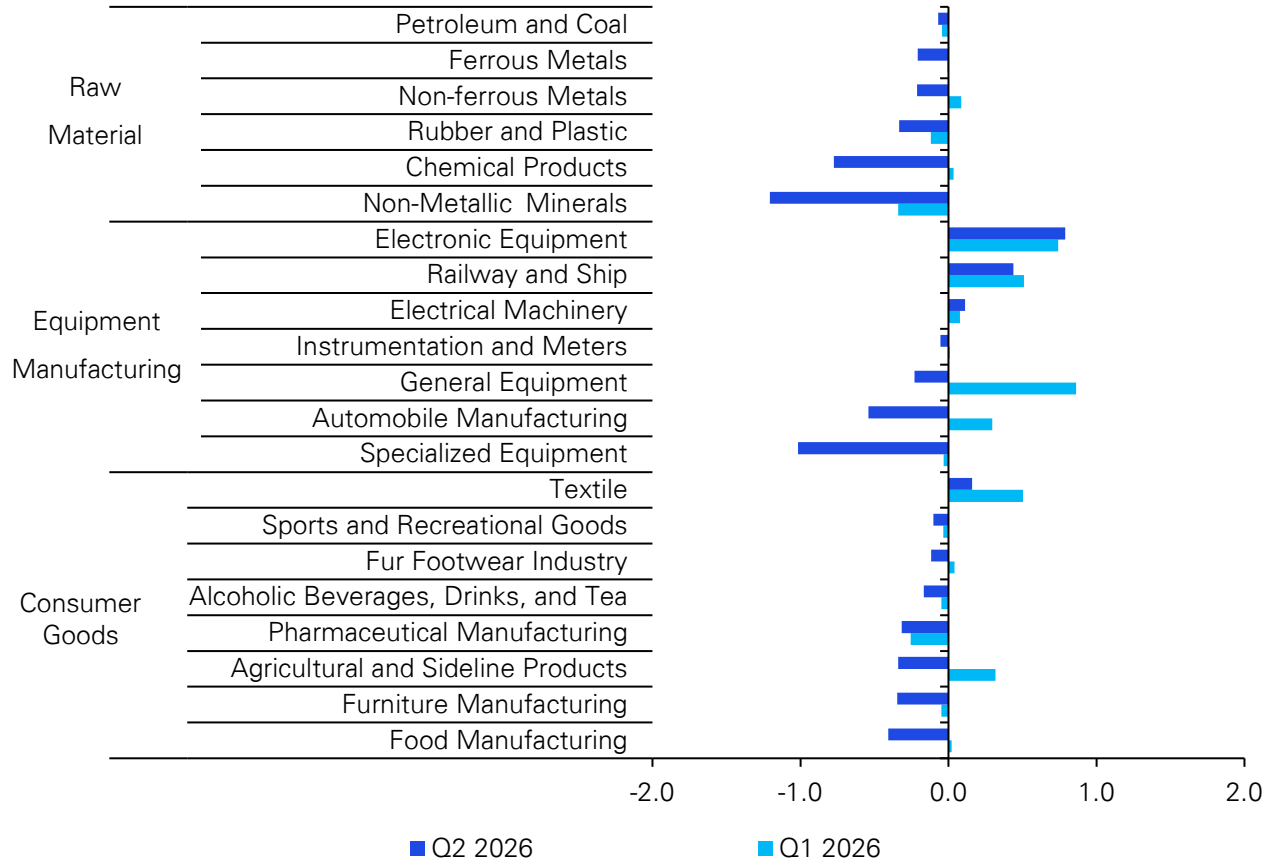
- Fixed asset investment growth slowed sharply in H1 2026, declining 5.7% YoY. Q2 investment growth fell to -9.7%, down nearly 10 percentage points from Q1.
- Property investment continued to contract as developers focused on controlling new investment, with growth declining from -11.2% in Q1 to -23.0% in Q2. Manufacturing investment weakened amid energy supply disruptions and imported cost pressures, with growth slowing from 4.1% in Q1 to -3.8% in Q2. Weaker fiscal spending weighed heavily on infrastructure investment, with growth falling from 9.2% in Q1 to -8.6% in Q2.
- Despite the broader slowdown, high-tech investment continued to outperform, supported by strong exports and rapid AI development. H1 high-tech investment grew 4.6%, outperforming overall investment by 10.3 percentage points. However, given the relatively small scale of high-tech industries, their investment expansion remains insufficient to offset the broader contraction in traditional sectors.

Source: Wind, KPMG analysis

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Rising cost pressures weigh on manufacturing investment

Contributions to manufacturing investment growth by sector, percentage points



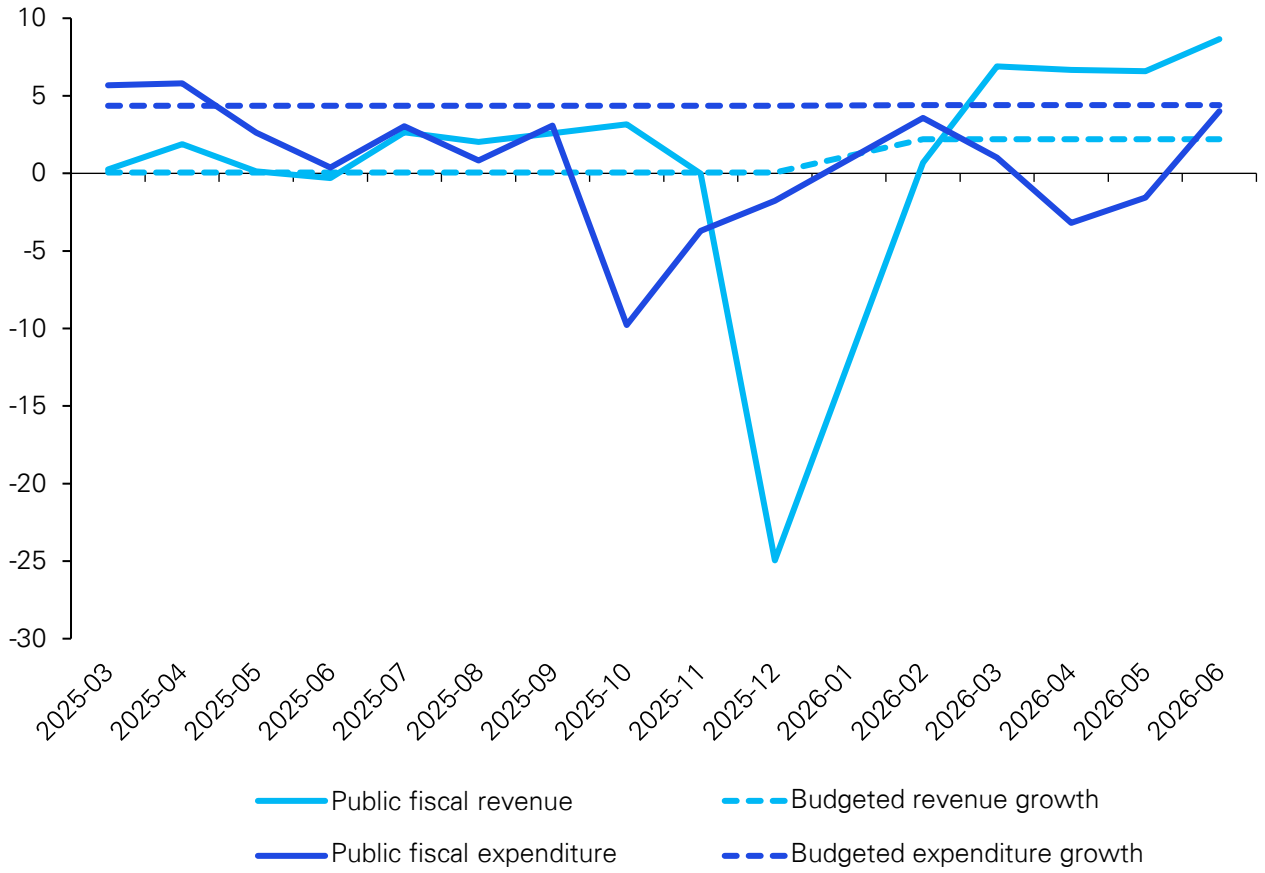
Source: Wind, KPMG analysis

- Manufacturing investment momentum weakened significantly in Q2, with growth slowing from 4.1% in Q1 to -3.8%.
- Upstream industries were under pressure as supply disruptions and higher energy prices squeezed margins. Investment growth in chemical products, petroleum processing, and rubber and plastics slowed, while weaker property and infrastructure activity further weighed on building materials investment. Investment on downstream consumer goods also slowed under sluggish consumption and higher raw material costs.
- By contrast, equipment manufacturing remained resilient, supported by external demand and domestic investment in emerging industries.
- Looking ahead, manufacturing investment may stabilise at low levels, supported by a lower base and sustained demand for AI and new energy products. However, margin pressures from higher input costs may continue to constrain the recovery.

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Fiscal spending slowdown weighs on infrastructure investment

Growth of public fiscal revenue and expenditure, cumulative YoY, %



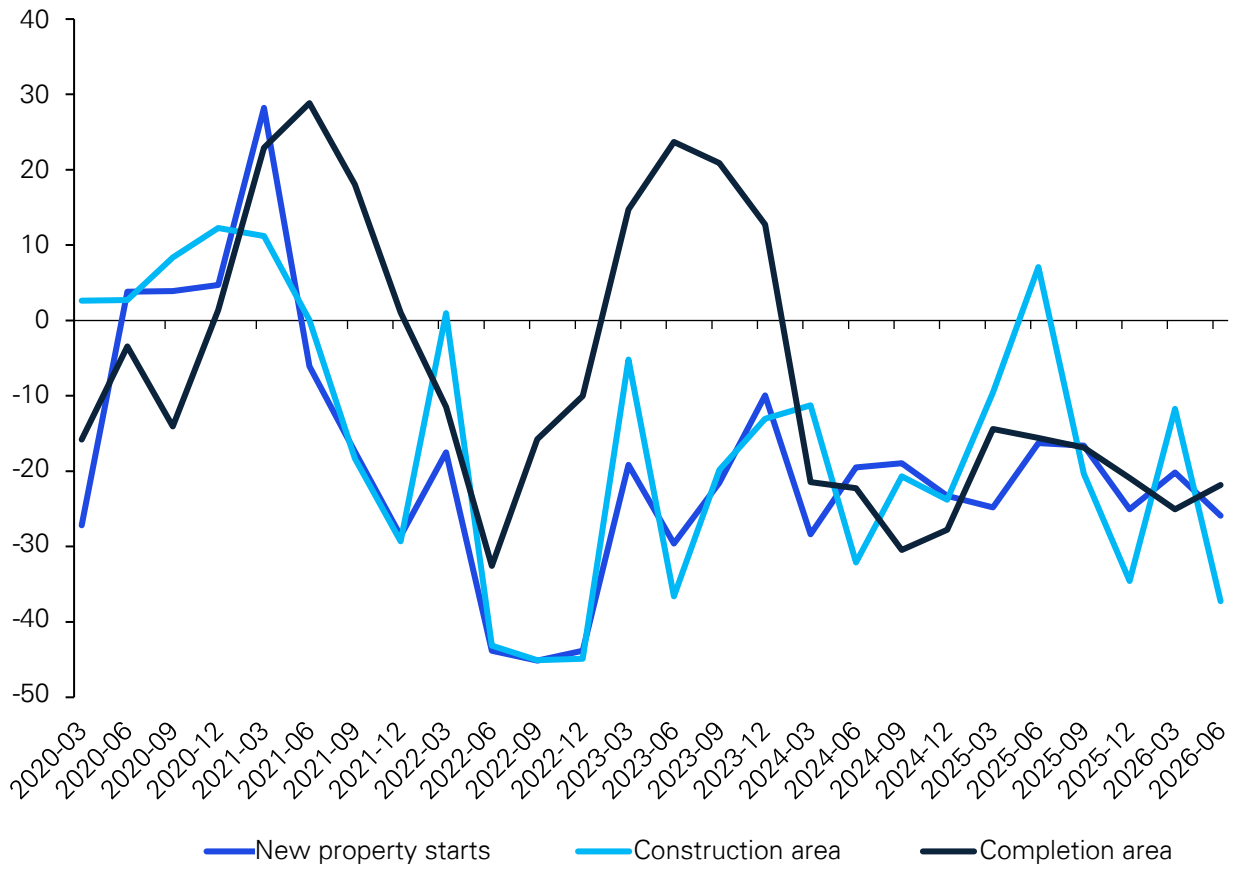
Source: Wind, KPMG analysis

- Infrastructure investment growth slowed sharply in Q2, falling to -8.6% from 9.2% in Q1, bringing H1 growth to -2.4%.
- The decline mainly reflected slower fiscal spending. Despite stronger-than-expected fiscal revenue growth, public fiscal expenditure growth slowed from 2.6% in Q1 to 0.2% in Q2, with infrastructure-related spending falling 9.0% YoY. Fiscal expenditure remained concentrated on public wellbeing. Meanwhile, infrastructure investment was constrained by tighter project approval processes and slower local government fiscal spending.
- Looking ahead, infrastructure investment is expected to recover gradually. Fiscal resources remain supportive, with an estimated RMB 5.3 trillion of broad fiscal funds available for infrastructure-related investment in H2, alongside RMB 800 billion of policy-backed financial instruments. Faster implementation of major projects, including investment on the "Six Networks", should provide additional support.

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Property investment continues to contract amid controlled supply expansion

Real estate development investment by project stage, quarterly YoY, %



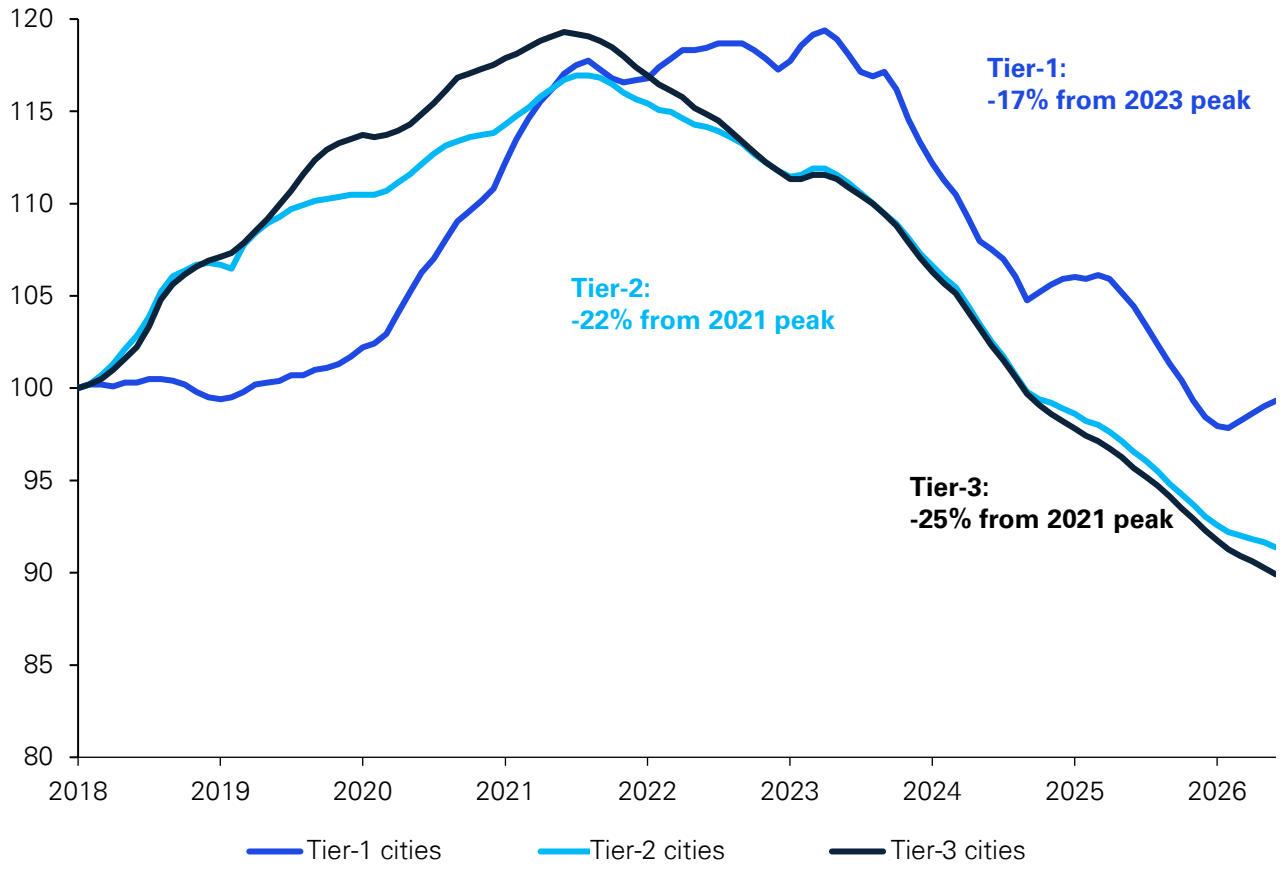
Source: Wind, KPMG analysis

- Real estate investment declined 18.4% YoY in H1 2026, with the contraction widening from -11.2% in Q1 to -23.0% in Q2, subtracting 2.5 percentage points from overall investment growth.
- The deeper decline was mainly driven by continued supply-side adjustment. Under the policy focus of "controlling new supply and reducing inventories", local governments have reduced land supply, limiting new construction activity. Meanwhile, developers have increasingly adopted a sales-driven investment strategy amid weak housing demand. New home sales growth slowed further in Q2, pushing new starts growth down to -25.9%.
- Looking ahead, urban renewal projects are expected to gradually replace traditional real estate development as a new investment driver. Property developers may increasingly shift toward urban renewal, rental housing, and property operation services.

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Housing market recovery remains uneven, with higher-tier cities outperforming

Existing home price index in 70 major cities, 2018=100



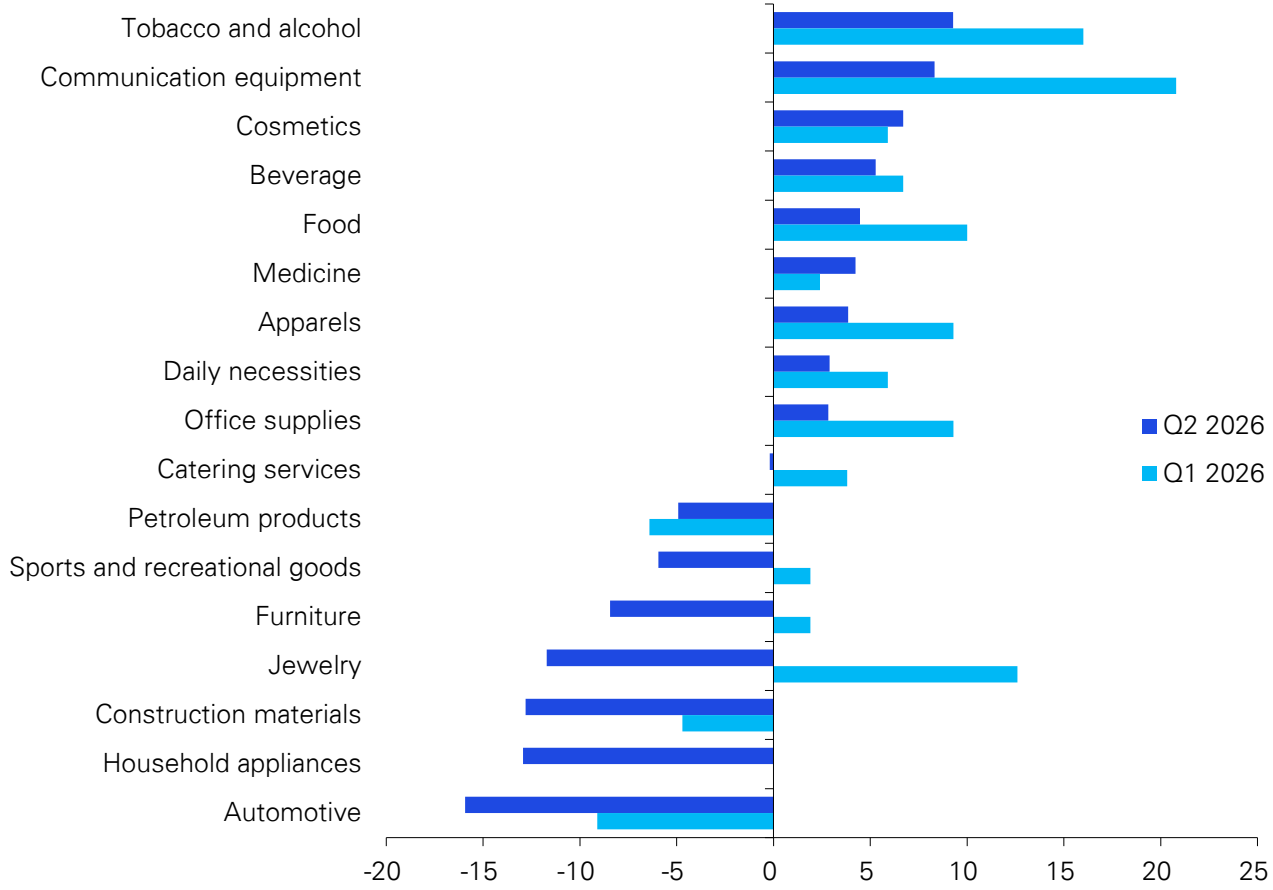
Source: Wind, KPMG analysis

- Following continued declines in new housing supply and gradual inventory reduction, housing markets in higher-tier cities have stabilised earlier, while lower-tier cities remain under pressure, showing a K-shaped recovery.
- Higher-tier cities benefit from stronger industrial clusters, population inflows and policy support. Both new and second-hand housing markets have shown signs of recovery. In Q2, new and second-hand home transactions in tier-1 cities increased by 8.3% and 10.7% YoY, respectively. Meanwhile, new and second-hand home prices in tier-1 cities returned to month-on-month growth in February and March, respectively, and continued to rise thereafter.
- By contrast, lower-tier cities continue to face weak demand amid limited population inflows and slower development of emerging industries. Second- and third-tier cities recorded year-on-year declines in housing sales in Q2, while high inventories continued to weigh on market recovery.

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Consumption remains under pressure, while services consumption provide resilience

Growth rate of goods sales by category, quarterly YoY, %



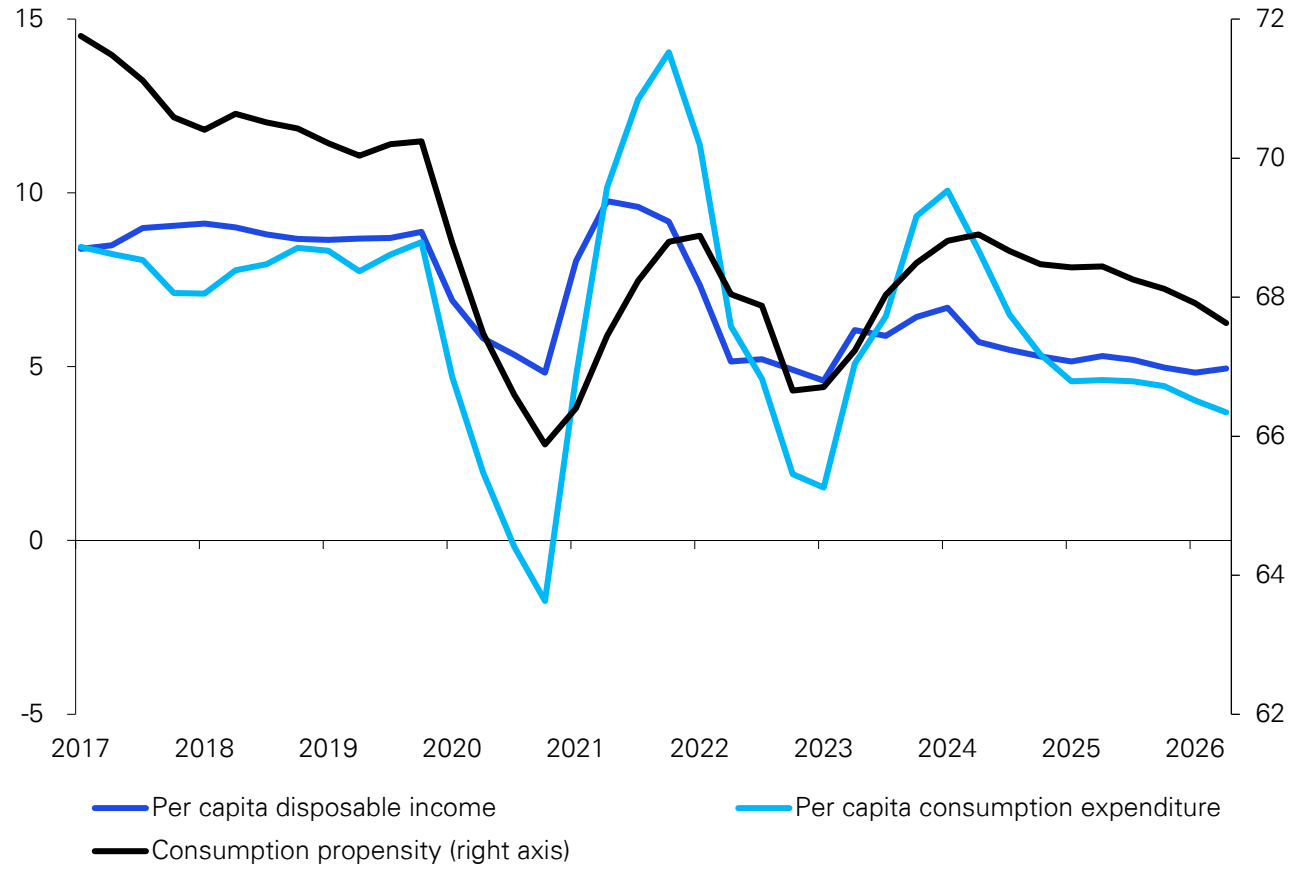
Source: Wind, KPMG analysis.
Note: Goods sales data are for above-size retail enterprises

- Retail sales grew by 1.3% YoY in H1 2026, down 3.7 percentage points from a year earlier. Growth slowed further to 0.2% in Q2, reflecting fading support from consumer subsidies and a high base effect from large-scale trade-in programmes in 2025. Weak confidence also continued to weigh on households' willingness to spend.
- The National Bureau of Statistics introduced a new indicator, "total retail sales of goods and services", which increased 2.7% YoY in H1. Services consumption rose 5.3%, with its share of household expenditure reaching 45.7%, up 0.2 percentage points from a year earlier, highlighting a gradual shift toward experience-based consumption. Goods consumption trends remained divergent, with essential goods holding up better while durable goods weakened as earlier subsidies brought forward replacement demand. Overall, consumption is undergoing structural adjustment and is expected to recover gradually as base effects fade.

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Household confidence remains weak despite improving income growth

Growth rate of per capita disposable income and consumption expenditure, 4QMA, %



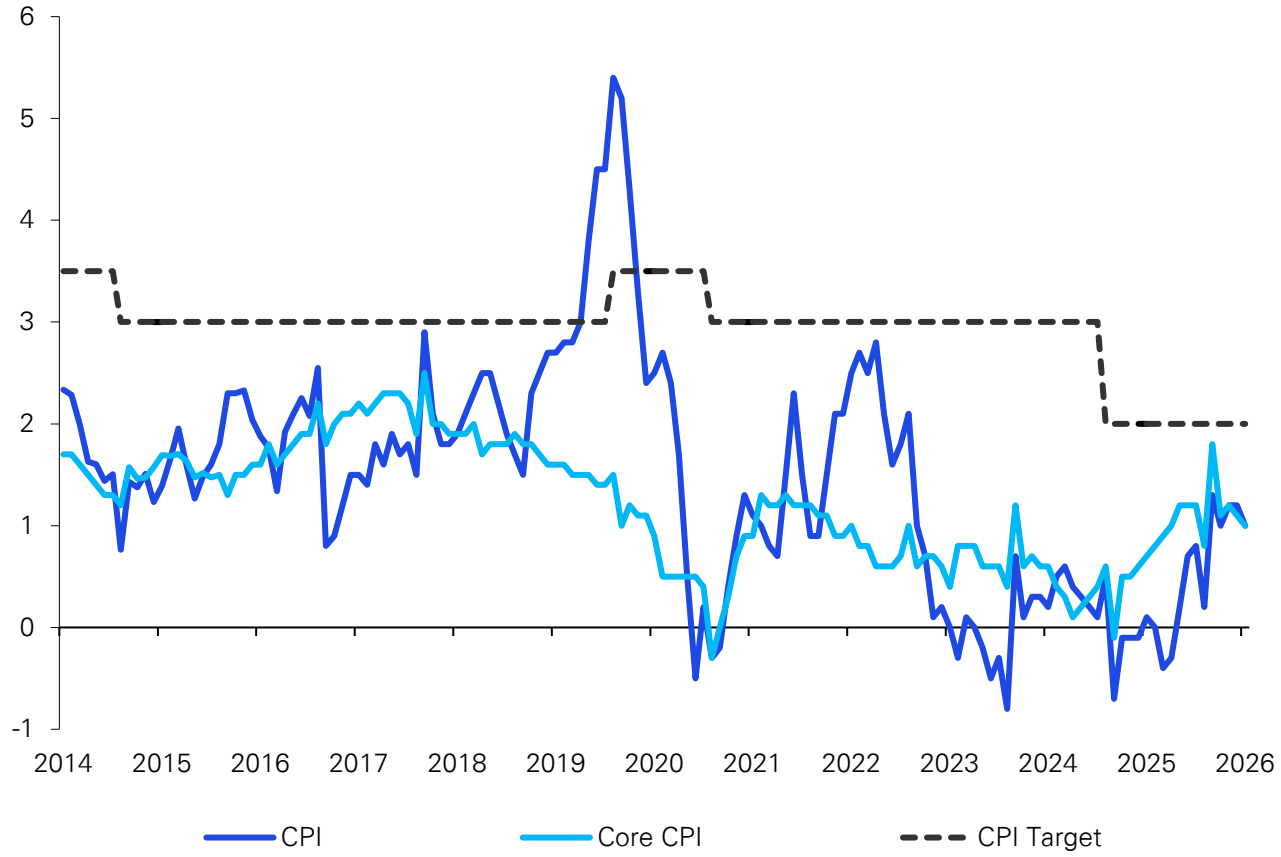
- Household income growth has stabilised, while consumption recovery remains relatively weak. In H1 2026, per capita disposable income reached RMB 22,981, rising 5.2% YoY in nominal terms and 4.2% in real terms, both slightly higher than in Q1. Per capita consumption expenditure grew 3.7% YoY in nominal terms and 2.7% in real terms, showing only marginal improvement.
- Despite better income conditions, households remain cautious, with precautionary savings elevated and consumption propensity below historical levels. The national unemployment rate declined to 5.0% in June, down 0.4 percentage points from March. To support employment, the State Council's Plan on Implementing the Employment-first Strategy during the 15th Five-Year Plan Period (2026-2030) emphasises the expansion of jobs through digital transformation and emerging industries, which could help improve employment quality and strengthen household confidence.

Source: Wind, KPMG analysis
Note: Consumption propensity = per capita disposable income / per capita consumption expenditure

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Inflation recovery strengthens but remains fragile

China consumer price index (CPI), YoY, %



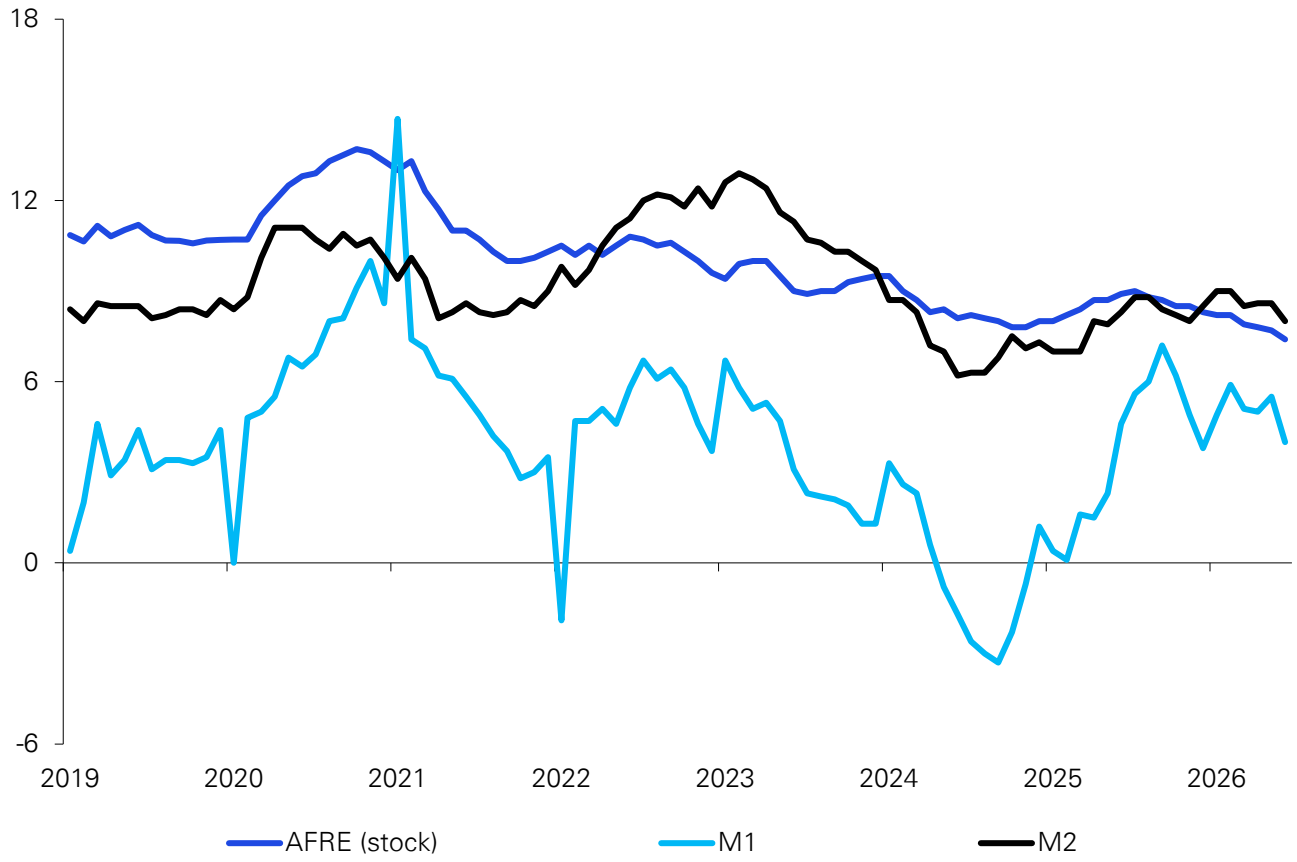
- Consumer prices continued to recover in H1 2026. CPI rose 1.0% YoY in H1 2026, while core CPI increased 1.2%, marking a gradual shift from deflationary pressure toward mild inflation. Improving industrial prices and recovering consumer prices supported the overall price level, in the right direction to achieving the government's goal of turning price growth positive.
- PPI increased 1.5% YoY in H1 and accelerated to 4.1% in June, driven by low base effects, higher commodity prices and stronger demand for equipment manufacturing. The recovery in H1 was mainly driven by industrial upgrading, reduced price competition in key sectors, and higher upstream input costs.
- Looking ahead, inflation is expected to continue recovering in H2, but the foundation remains weak. Further improvement will depend on the strength of domestic demand recovery and policy coordination to strengthen the employment–income–consumption–investment cycle.

Source: Wind, KPMG analysis

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Financial conditions shift toward more targeted policy support

Growth rate of AFRE (stock), M1, and M2, YoY, %



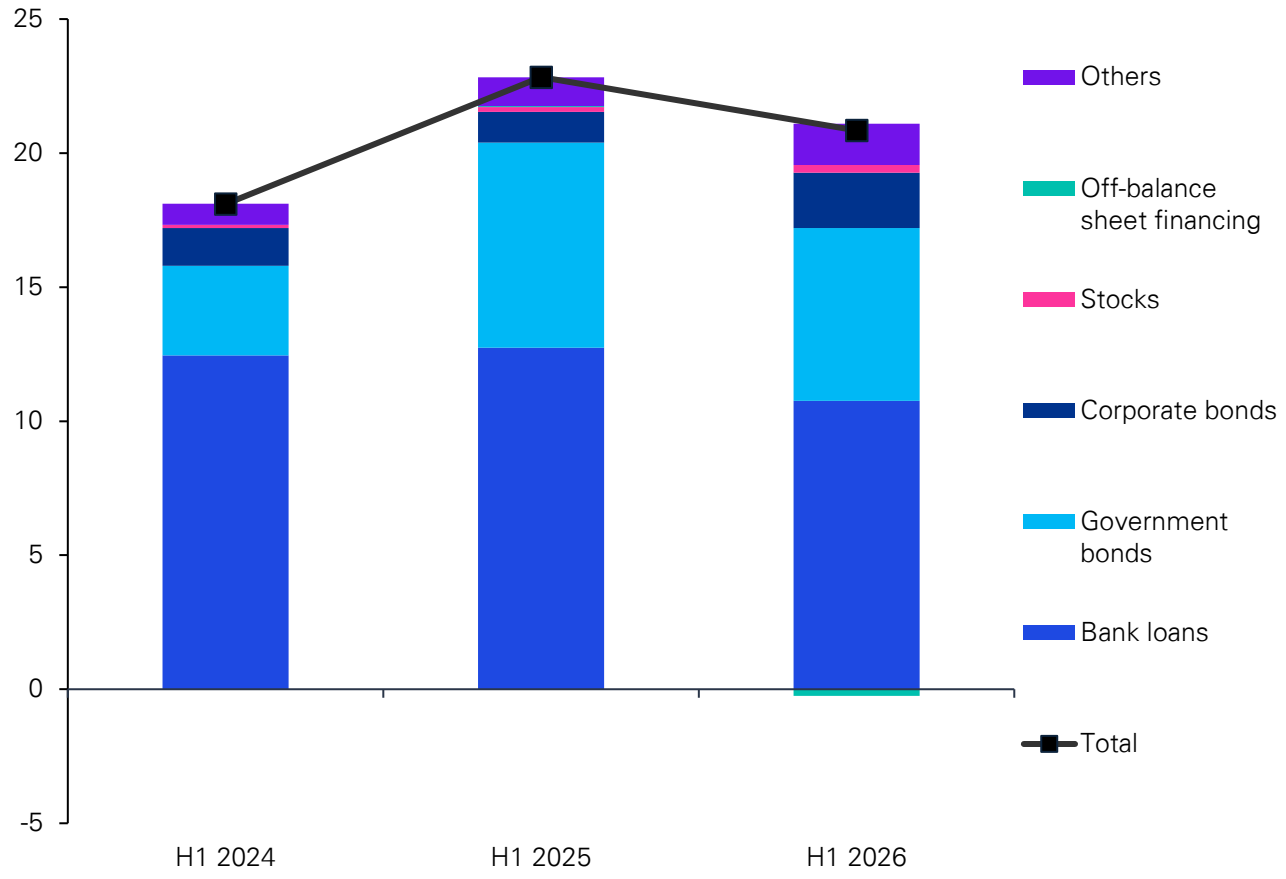
Source: Wind, KPMG analysis

- Financial activity slowed in H1 2026 amid weaker financing demand, changing financing structures, and slower fiscal policy implementation. Aggregate financing reached RMB 20.8 trillion, RMB 2.0 trillion lower than a year earlier. By the end of June, growth of aggregate financing slowed to 7.4%, down 0.5 percentage points from Q1. Money supply growth also moderated. M1 growth slowed to 4.0% YoY and M2 growth to 8.0% YoY in June, as weaker credit expansion and slower government bond issuance constrained liquidity creation. The widening M2–M1 growth gap reflects weaker money circulation, with households increasing savings and debt repayment while corporates remained cautious on investment.
- The slowdown in financial expansion reflects structural transformation. As the economy shifts toward new growth drivers, monetary policy is moving from broad-based support toward more targeted measures—maintaining overall stability while directing financial resources toward emerging sectors.

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Credit growth slows while direct financing gains momentum

Growth of total social financing (TSF) by sector, RMB trillion



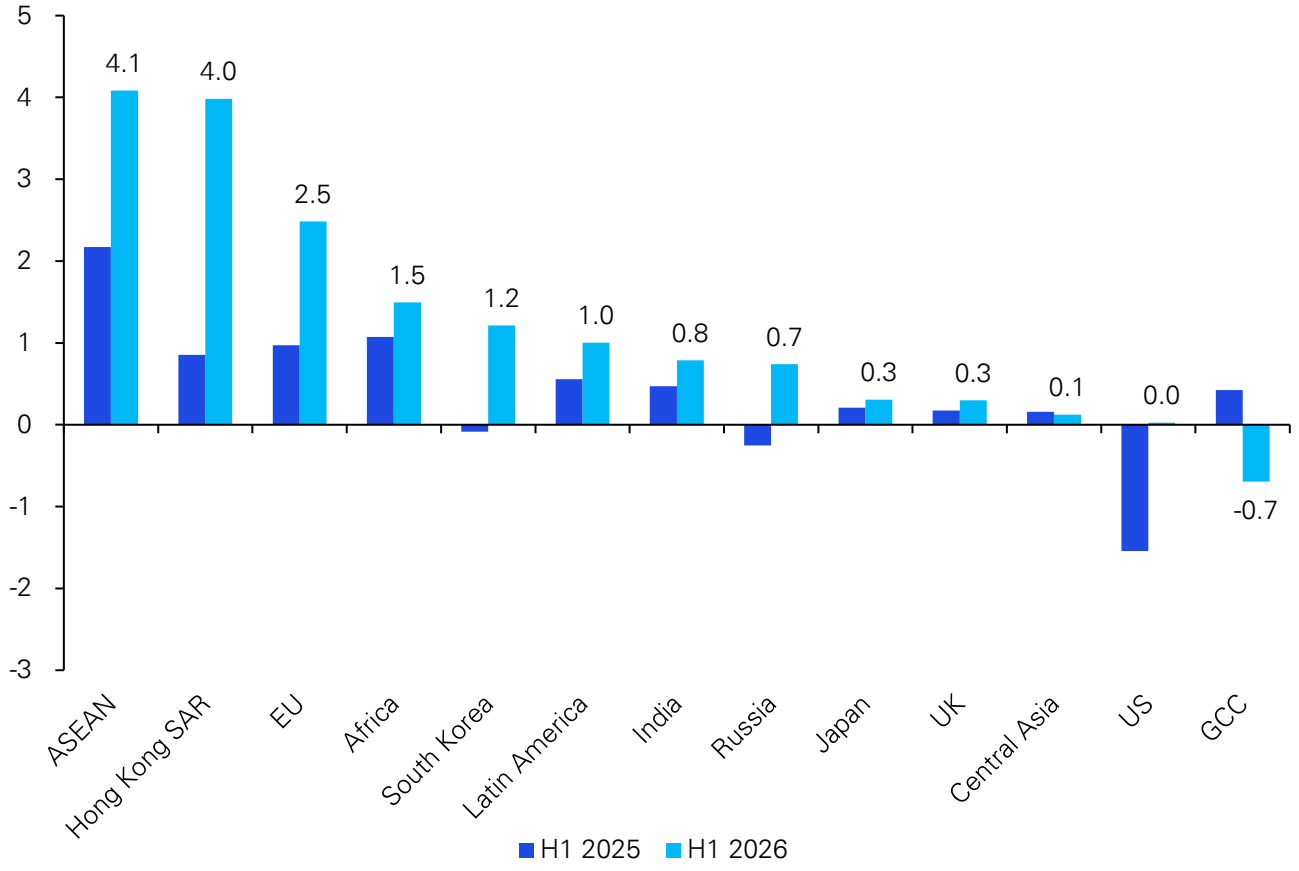
Source: Wind, KPMG analysis

- The composition of social financing continued to shift in H1 2026. Government bond financing increased by RMB 6.4 trillion, RMB 1.2 trillion less than a year earlier. In Q2, government bond financing declined further amid stronger-than-expected exports and tighter project management. Bank loans remained the largest drag, with lending growth of RMB 10.8 trillion, RMB 2.0 trillion less than a year earlier.
- Meanwhile, direct financing gained momentum. Corporate bond financing increased by RMB 2.1 trillion, RMB 0.9 trillion more than a year earlier, supported by lower issuance costs, accelerated investment in major projects, and improved financing mechanisms for technology companies. Stock financing also increased by RMB 293 billion. The rising share of direct financing aligns with financial sector reform by reducing reliance on bank lending. However, it has yet to fully offset weaker credit expansion and remains concentrated among larger and technology firms, highlighting a potential K-shaped financing recovery.

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Trade momentum strengthens amid improving trade structure

Contributions to China's exports growth, by major trading partners, percentage points



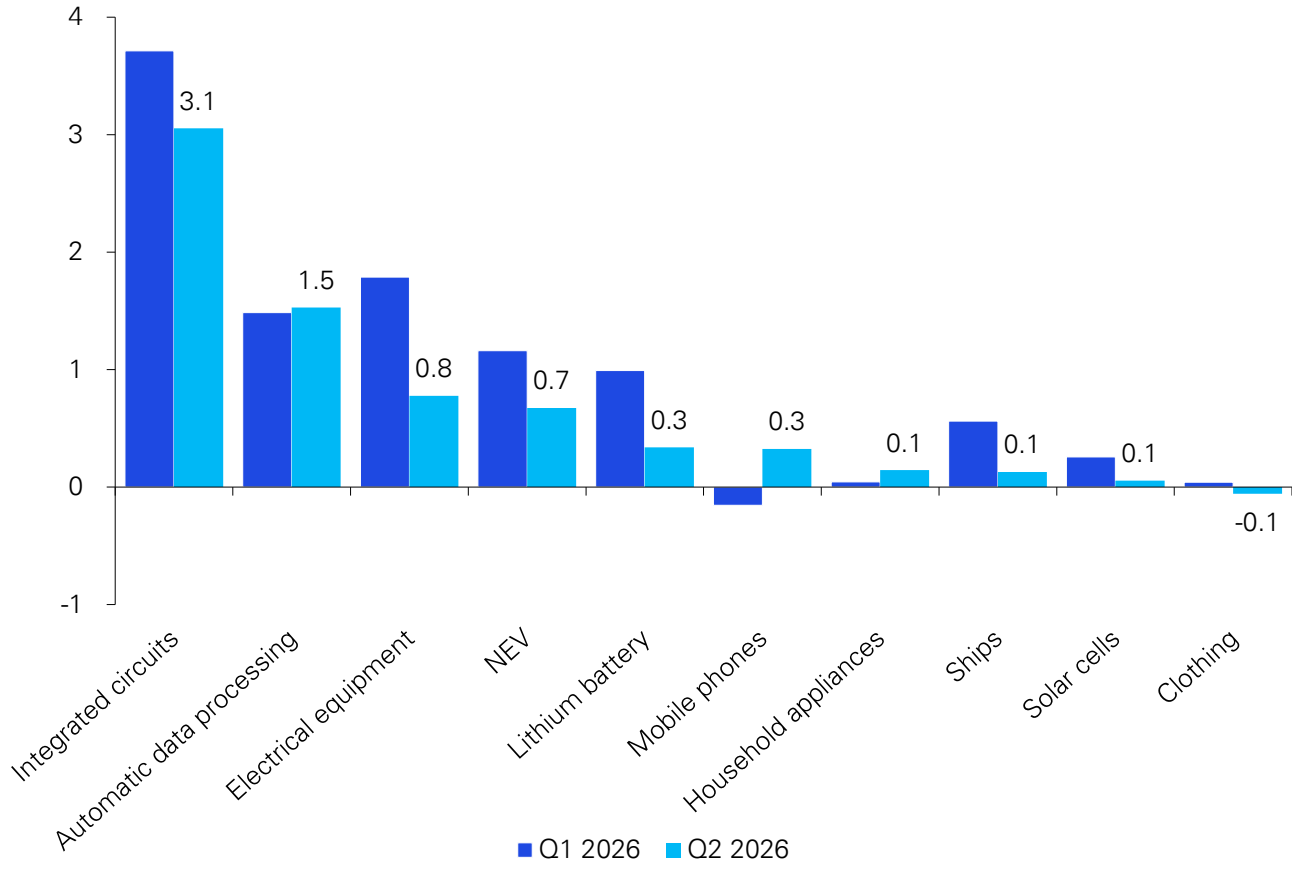
- Exports remained a key growth driver in H1 2026, rising 17.6% YoY in US dollar terms. Growth was supported by China's supply chain advantages and strong demand for AI-related electronics and new energy products. Exports accelerated to 20.1% YoY growth in Q2, while imports increased 26.6% in H1, supporting a more balanced trade recovery.
- By trading partners, exports to Hong Kong SAR and ASEAN contributed 4.0 and 4.1 percentage points to overall export growth, respectively, driven by AI demand and deeper supply chain integration. Emerging markets, including Africa, Latin America, India and Central Asia, contributed 3.4 percentage points, while traditional markets such as the EU, South Korea, the UK and Japan also provided strong support.
- Looking ahead, global AI expansion and energy transition remain key long-term drivers supporting export resilience. China is also expected to further expand imports and optimise trade structures to promote more balanced and sustainable trade growth.

Source: Wind, KPMG analysis
Note: The GCC economies include the United Arab Emirates, Saudi Arabia, Oman, Kuwait, Qatar, and Bahrain; the Central Asia economies include Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan.

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AI drives export growth through technology-intensive products

Contributions to export growth by category, percentage points



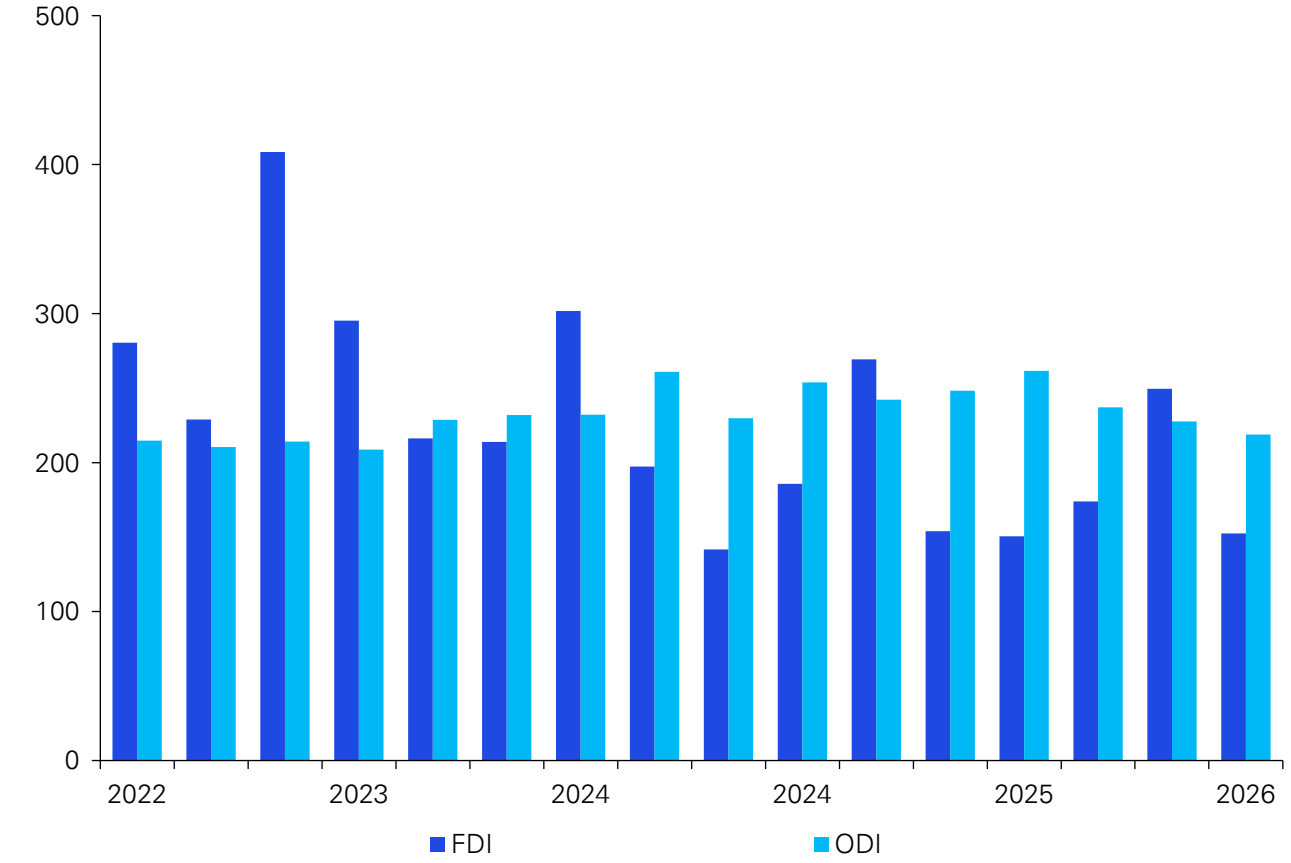
Source: Wind, KPMG analysis

- Mechanical and electrical products remained the key pillar of China's exports in Q2 2026, growing 27.3% YoY in Q2 and contributing 8.7 percentage points to overall export growth. AI-related products were the main growth engine, with integrated circuit exports rising 111.3% YoY and automatic data processing equipment exports increasing 55.2%. Meanwhile, new energy products, including electric vehicles, lithium batteries and solar cells, continued to support exports amid accelerating global energy transition.
- However, export divergence became more evident, as labour-intensive products, such as clothing, faced rising competition and supply chain relocation pressures.
- Looking ahead, global AI investment and green transition will continue to support China's technology-intensive exports, while helping offset external uncertainties.

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Foreign investment shifts toward services and high-tech sectors

China's foreign direct investment (FDI) and outbound direct investment (ODI), RMB billion



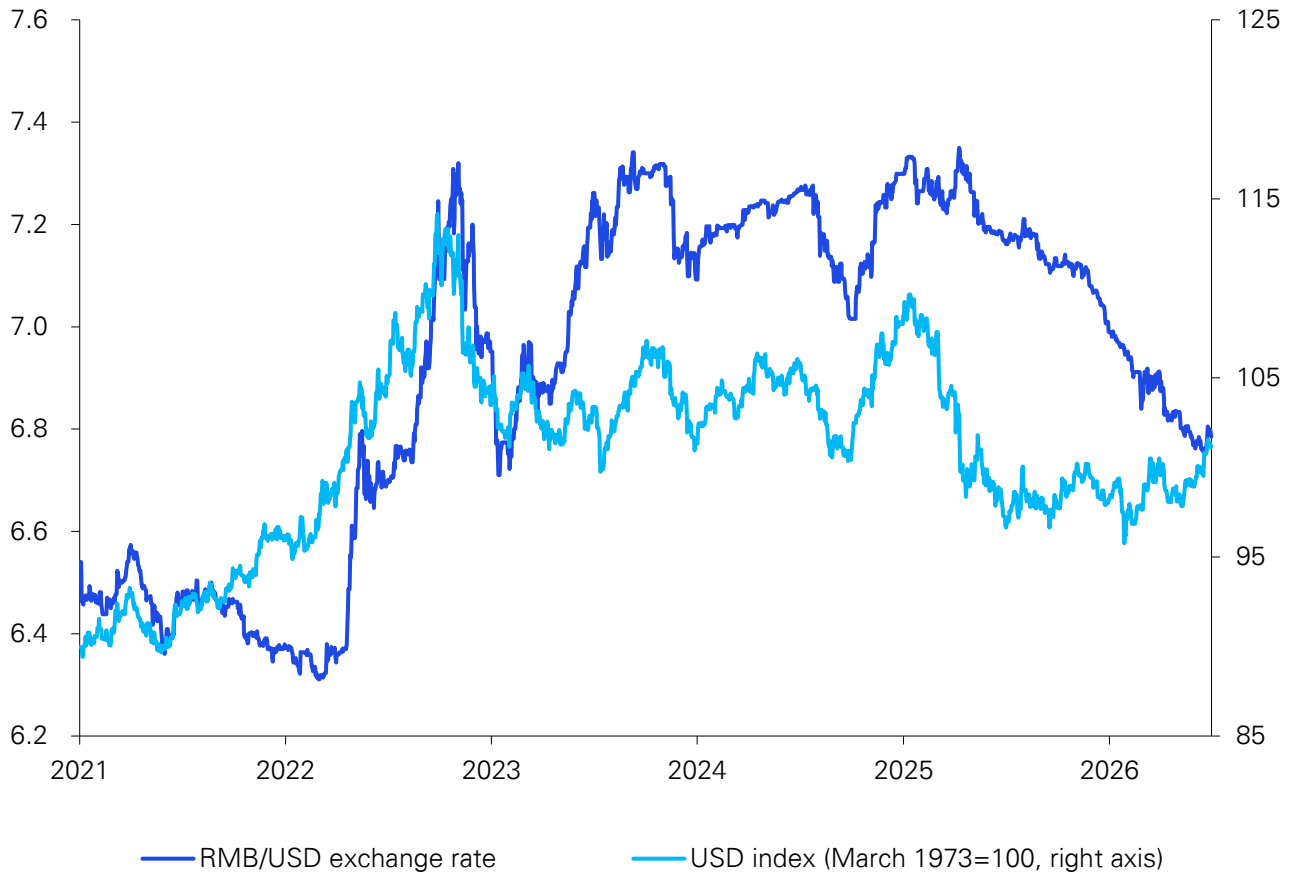
Source: Wind, KPMG analysis

- China's foreign investment landscape showed signs of stabilisation in H1 2026. FDI into China declined 5.0% YoY to RMB 402.1 billion. The number of newly established foreign-invested enterprises increased 5.3% to 31,600. Compared with Q1, the decline in FDI narrowed, indicating improving investor sentiment and continued long-term commitment to the Chinese market.
- Investment continued to shift toward higher value-added sectors. Services accounted for 72% of total FDI, highlighting the growing role of services sector. High-tech industries attracted RMB 170.3 billion, accounting for 42.4% of total FDI, up 12.2 percentage points YoY.
- Overall, supported by rapid AI development, expanding application scenarios and a stronger innovation ecosystem, China continues to attract multinational companies to deepen their technology and innovation investment.

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RMB appreciates moderately amid greater two-way fluctuations

USD index and RMB/USD exchange rate



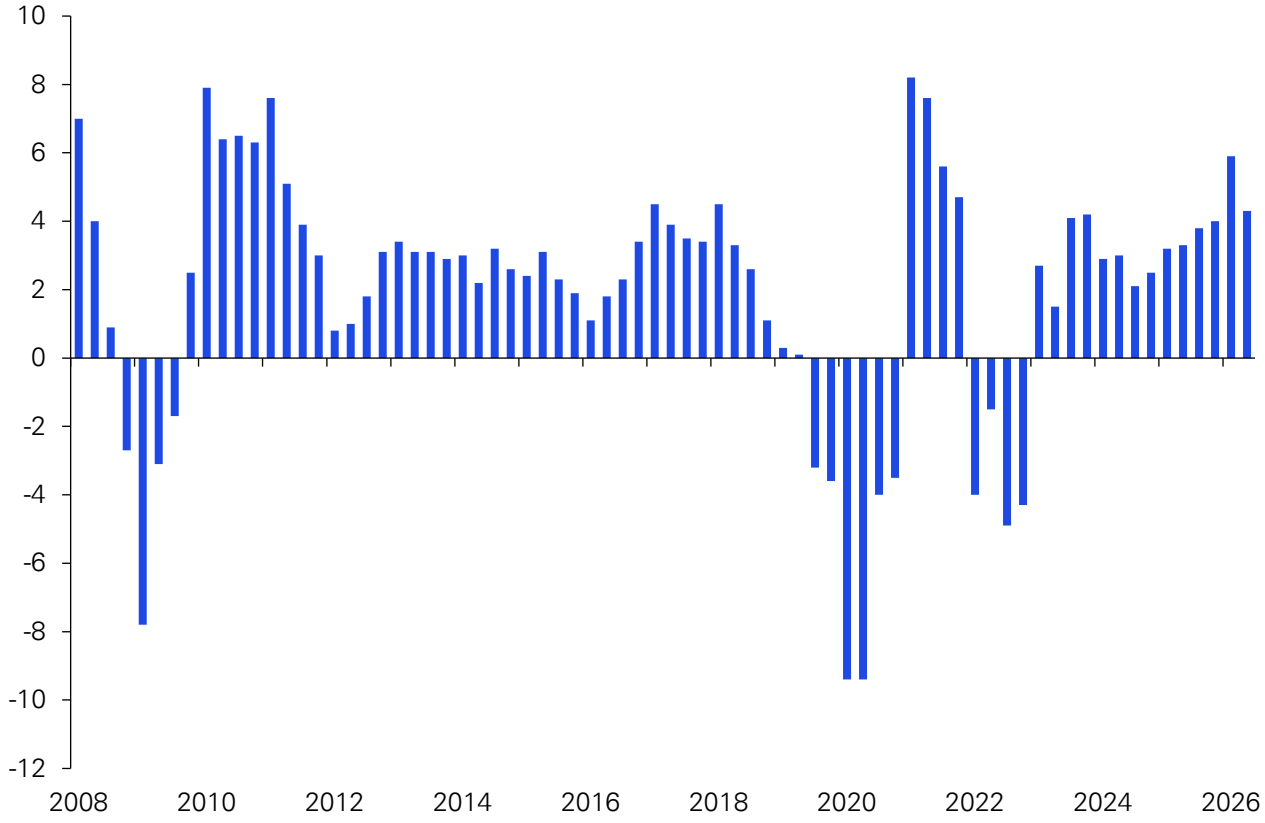
Source: Wind, KPMG analysis

- The RMB demonstrated resilience in H1 2026, appreciating moderately despite volatility in global markets. While the US dollar index strengthened in Q2 amid changing Fed policy expectations, the RMB moved independently from the dollar and appreciated 1.8% against the US dollar to 6.79 by the end of June. The CFETS RMB exchange rate index also rose 1.7%, reflecting broad-based strength against a basket of currencies.
- Looking ahead, the RMB is likely to move from one-way appreciation toward greater two-way fluctuations as supportive factors and external pressures rebalance. On the downside, a stronger US dollar amid reduced Fed easing expectations, moderating export growth after temporary boosts fade, and geopolitical uncertainties could weigh on the RMB. However, export resilience provides fundamental support, while foreign investment continues to flows into RMB assets. The PBOC retains sufficient policy tools to stabilise expectations and manage exchange rate volatility.

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Hong Kong SAR's economy maintains steady expansion

Hong Kong SAR's real GDP growth rate, quarterly YoY, %



- Hong Kong SAR's economy continued to expand in Q2 2026, although growth momentum moderated from Q1. GDP grew 4.3% YoY, down from 5.9% in Q1, with growth driven mainly by strong external demand and resilient domestic activity.
- Exports remained the key growth engine, with goods exports rising 28.8% YoY, supported by global AI supply chain expansion and strong electronics demand. Services exports increased 3.4% YoY, benefiting from continued tourism recovery and stable cross-border financial and business service activity. Visitor arrivals reached 12.4 million in Q2, up 8.7% YoY.
- Domestic demand remained supportive but moderated. Private consumption growth slowed to 2.9%, while government consumption growth eased to 0.5%. Fixed investment rose 4.6%, but growth slowed as temporary Q1 factors faded. Nevertheless, technology investment and stronger financial market activity continue to support private investment resilience.

Source: Wind, KPMG analysis

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