

CHINA

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A CONFIRMED EXPORT POWERHOUSE WITH AN UNBALANCED GROWTH MODEL

After a solid start to the year, Chinese economic growth has gradually slowed. Thanks to a rapid reorientation, exports have weathered the US tariff shock well. They are the main driver of economic activity, while domestic demand remains stubbornly fragile. The authorities have launched an “anti-involution” campaign, but adjusting demand policy in order to boost domestic investment and consumption, at a time when exports may begin to run out of steam, is also becoming urgent. Despite the deterioration in public finances in recent years, the central government and local governments still have some room for manoeuvre to act.

GROWTH: DRIVEN BY EXPORTS

China's real GDP growth stood at +5.4% year-on-year (y/y) in Q1 2025, followed by +5.2% in Q2 and +4.8% in Q3. It is expected to continue slowing in the short term, reaching 5% for 2025 as a whole and 4.5% in 2026.

In the industrial sector, growth was stronger than expected (*Chart 1*). It reached +6.2% y/y in the first nine months of 2025 (after +5.8% in 2024), largely supported by exports of manufactured goods. On the other hand, manufacturing investment growth slowed steadily this year (+4% in value year-on-year over the first nine months, compared with +9.2% in 2024). This significant slowdown is due to the uncertainties that weigh on export prospects, as well as weak domestic consumption and the anti-involution campaign (*see below*).

In services, the acceleration in growth recorded in H1 2025 (+5.9% y/y, after +5.2% in 2024) came to a halt in Q3 (+5.7%). The recovery in domestic demand remains fragile and fiscal support measures are proving insufficient. Government-subsidised consumer-goods-replacement programmes have encouraged household spending, but retail sales growth slowed again during the summer (from more than 5% y/y in volume terms in H1 to +3.8% in Q3). In the property market, the crisis has not yet bottomed out. In the first nine months of 2025, transaction volumes continued to fall; they were half of what they were in the same period in 2021. The correction in housing prices is continuing gradually.

Household sentiment is not improving, undermined by the property crisis and labour market conditions that have deteriorated compared to pre-COVID levels (high youth unemployment and more modest income growth). This explains their preference for deleveraging, despite monetary policy easing and measures to support consumer credit. Household debt has fallen very slightly over the past two years (estimated at 60.4% of GDP in Q3 2025 and just under 100% of disposable income, which is a relatively high level). While significant measures would be needed to boost household confidence, the authorities have not yet made this issue a priority. However, in the official statement of 22 October on the broad outlines of the 15th Five-Year Plan for 2026–2030, the need to stimulate private consumption is reiterated.

A NEW OBJECTIVE FOR THE AUTHORITIES: COMBATING “INVOLUTION”

The authorities have adjusted their industrial policy since the summer. They are paying more attention to the problem of deflation and “involution”. This term refers to the intense and destructive competition affecting many sectors (from steel and pharmaceuticals to green technologies and delivery) and is characterised by overcapacity, price wars and declining profits. The authorities are encouraging companies to raise their selling prices and limit their production, and promoting consolidation in some sectors. The anti-involution campaign should reduce deflationary pressures and boost corporate profits, while maintaining the capacity of the strongest players to innovate.

FORECASTS

	2022	2023	2024	2025e	2026e
Real GDP growth, %	3.1	5.4	5.0	5.0	4.5
Inflation, CPI, year average, %	2.0	0.2	0.2	0.0	1.0
Official budget balance / GDP, %	-2.7	-3.8	-3.0	-4.0	-3.8
Official general government debt / GDP, %	49.4	54.7	60.9	68.5	74.3
Current account balance / GDP, %	2.4	1.4	2.3	3.1	2.9
External debt / GDP, %	13.4	13.4	12.9	12.5	11.9
Forex reserves, USD bn	3 307	3 450	3 456	3 686	3 856
Forex reserves, in months of imports	12.6	13.3	12.7	13.5	13.5

e: ESTIMATES & FORECASTS

SOURCE: BNP PARIBAS ECONOMIC RESEARCH

TABLE 1

CHINA: ACTIVITY IN INDUSTRY AND SERVICES

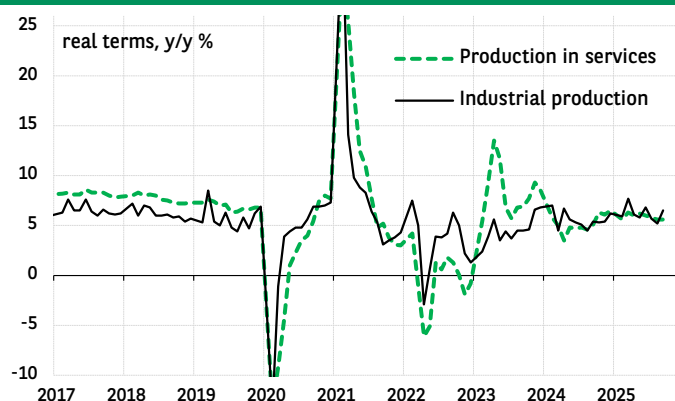


CHART 1

SOURCE: NBS, BNP PARIBAS

The first visible effects are still weak. Core inflation accelerated slightly (+1% y/y in September) and producer price deflation eased (-2.3%). However, consumer price inflation remained negative (-0.3%) due to lower food prices (-4.4%) and fuel prices (-6%). The anti-involution policy has probably also contributed to the recent slowdown in activity and investment in the manufacturing sector. This shows that, in order not to slow economic growth or penalise employment, anti-involution measures will have to be accompanied by strong export growth and/or a sustained increase in private consumption.



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➡ A CURRENT ACCOUNT SURPLUS OVER 3% OF GDP

In 2025, the export base strengthened further, and the trade and current account surpluses increased to their highest level (as a percentage of GDP) in more than a decade.

Due to the tariff shock, exports to the United States fell by 15.8% y/y in USD terms over the first nine months of the year. However, this loss was more than offset by gains in other regions (ASEAN: +14.5%, EU: +7.9%, Latin America: +7.3% and Africa: +27.8%). This was possible thanks to rerouting export flows via third countries in order to circumvent tariffs, and diversifying markets in order to offset market share losses in the US. The success of Chinese companies was underpinned by the strong price and non-price competitiveness of their products, aided by the weakness of the yuan (Chart 2). Over the first nine months of 2025, the trade surplus increased by 26% y/y to USD 876 billion (customs administration data). Over 2025 as a whole, it is expected to be close to 5% of GDP, and the current account surplus is expected to exceed 3% of GDP for the first time since 2010 (it averaged +1.7% of GDP over the 2011–2024 period).

The increase in the current account surplus in 2025 was partly offset by an increase in net capital outflows, largely related to residents' investments and credit abroad. And China's already very comfortable liquidity and external solvency position strengthened slightly. The country has significant foreign exchange reserves (which rose in 2025). It is not very dependent on foreign financing, and its external debt is low (less than 15% of GDP). Therefore, the macroeconomic stability is not particularly vulnerable to changes in external financial conditions.

These strengths will persist in the medium term. Exports will remain a powerful driver of China's external accounts, especially as they are a strategic lever for Beijing in its rivalry with the United States and in its quest for global leadership. Innovation, strengthening the manufacturing sector, and technological autonomy remain objectives for the next five-year plan.

However, in the short term, export growth momentum could slow. Firstly, competitive pressure from Chinese products on foreign markets could ease somewhat. Indeed, the yuan has reappreciated slightly since last May (against the USD, the euro and in real effective terms) and the decline in the average dollar price of Chinese exports appears to be moderating (-1.2% y/y over the May–August period, after -4.1% in the previous six months). Anti-involution measures could also cause selling prices in the manufacturing sector to rise slightly. In addition, Chinese exporters could face new protectionist barriers, which could be imposed by the United States, but also by other trade partners. The last month saw renewed tensions between Beijing and Washington following the announcement on 10 October of tighter controls on China's exports of rare earths. Tensions have since eased significantly. Reciprocal port duties have been in effect since mid-October, but the truce has not been broken and negotiations have made progress.

🏦 FISCAL ROOM FOR MANOEUVRE PRESERVED IN THE SHORT TERM

Public finance metrics have continued to deteriorate in 2025. The official budget deficit (consolidated general government balance adjusted for various transfers between public accounts) is expected to reach 4% of GDP this year, up from 3% in 2024. The total general government (GG) deficit is expected to exceed 8% of GDP (IMF estimate).

It has increased since 2020, rising from an average of 3.9% in 2015–2019 to 7.4% in 2020–2024, due to the health crisis, the property crisis, the slowdown in GDP growth, and stimulus measures.

CHINA: TRADE SURPLUS AND EXCHANGE RATE

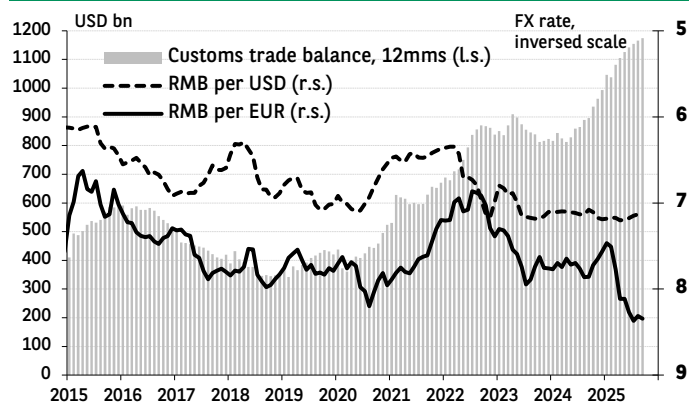


CHART 2

SOURCE: GENERAL ADMINISTRATION OF CUSTOMS, BNP PARIBAS

In the meantime, the GG's official debt increased from 38% of GDP at the end of 2019 to 66% in mid-2025. On the one hand, the central government's (CG) solvency remains very strong, and liquidity risks are very low: its debt is moderate (28% of GDP), consisting mainly of securities issued at low rates on local bond markets. Less than 1% of the debt is denominated in foreign currency and foreign investors hold less than 10% of the total. In the medium term, the CG's debt dynamics will continue to benefit from a favourable spread between GDP growth and interest rates, despite the expected slowdown in economic growth and the (moderate) increase in the average interest rate paid on the debt.

On the other hand, local governments (LGs) have significant vulnerabilities: i/ structurally high expenditure and insufficient revenue, which has been depressed by the contraction in land sales proceeds, and ii/ while LGs' direct (bond) debt is moderately high (38% of GDP) and easily refinanced on local markets, their indirect debt, contracted by their "financing vehicles" (FVs), is high (estimated at 50% of GDP in 2024). This debt is a significant source of credit risk for creditors (which are mainly banks) and contingent risk for LGs.

Despite the fragility of local government finance, the authorities still have room for manoeuvre to support economic activity (LGs are responsible for a large part of the implementation of fiscal policy).

Firstly, the financial strength of the CG enables it to introduce stimulus measures. Second, monetary easing facilitates bond issuance by LGs. Finally, the liquidity risks faced by FVs have been gradually reduced over the past two years by debt swap programmes, with LGs issuing bonds directly in their own name to refinance the debt of the most troubled FVs. This programme does nothing to resolve the medium-term solvency problem of local governments, but it does ease their liquidity constraints in the short term. With exports likely to slow in the short term, it is becoming urgent for the authorities to use all the leeway at their disposal to implement ambitious measures to boost household incomes and stimulate domestic demand.

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Christine Peltier

christine.peltier@bnpparibas.com



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