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EDITORIAL

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WHY CHINA RESISTS REBALANCING ITS GROWTH MODEL?

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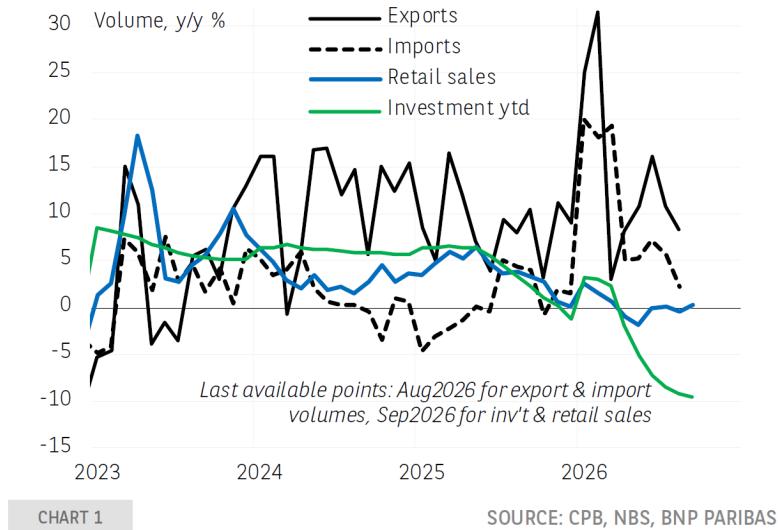
China has never exported as much as it does now, and its trade surplus has never been higher. At the same time, its economic growth is slowing, held back by weak domestic demand. The imbalances in China's growth model, and the external imbalances they give rise to, are therefore continuing to worsen. With Europe taking a tougher line and the United States, with which China shares nothing more than 'strategic stability', the standoff looks set to continue. However, the European Union and China would have a great deal to lose from a lasting deterioration in their relationship. It is in the interests of both parties to seek to restore the balance. To this end, it is important to understand Beijing's objectives and the constraints facing China. Why does the country resist adjusting its growth model? Whilst exports are a vital asset for sustaining economic activity and asserting China's technological and industrial power, this strategy also comes at a cost.

Imbalances are worsening

A K-shaped economy. China's economic growth slowed to 4.6% year-on-year (y/y) over the first three quarters of 2026, from 5.0% in 2025. More worryingly, the gap is widening between weak domestic demand and the very strong performance of exports, driven by artificial intelligence equipment and green technologies. Furthermore, the dynamism of export-oriented industries has not, so far, had any positive knock-on effects on other sectors or on households.

Domestic demand is struggling. The property crisis, now in its sixth year, and a sluggish labour market are weighing on household confidence and consumption. Since the start of 2026, households have been prioritising debt reduction (bank loans to households have fallen by 1% y/y), house sales have continued to fall, and retail sales have been stagnating (Chart 1). On the investment front, the decline is becoming more pronounced and widespread: it is affecting not only the property sector but also infrastructure and many manufacturing sectors (with the exception of the textile industry, transport and communications, and electronic and electrical equipment).

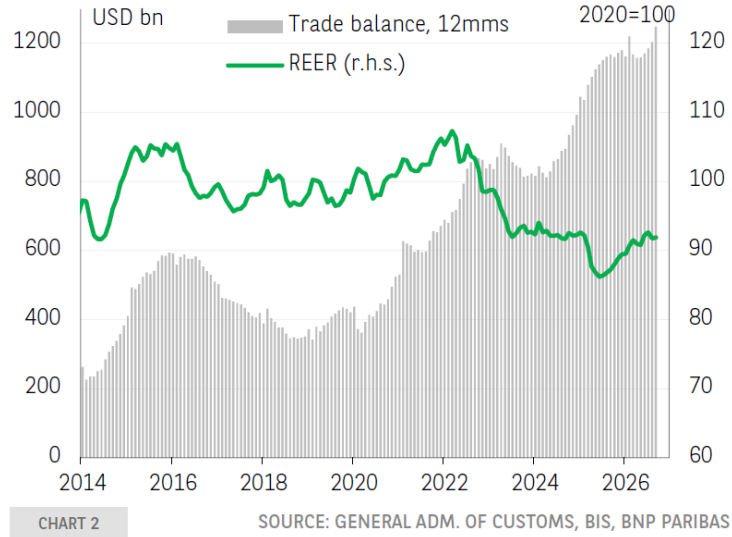
Chinese growth: solid exports, sluggish domestic demand



Exports remain very buoyant. Exports continue to be the main driver of growth (their net contribution is expected to account for around a third of real GDP growth in 2026, as it did in 2024–2025). Against a backdrop of rebound in global trade, Chinese companies maintained their market share at 14.6% of total exports (measured in US dollars) in the first half of 2026, as they had in 2025. Growth in goods exports accelerated (21.9% y/y in USD over the first nine months, compared with 5.2% in 2025), driven by both volumes and prices. These have rebounded after three years of decline, driven by rising costs of raw materials and the prices of goods required for AI, but they have increased at a slower rate than the global price average. Exports from high-tech sectors (batteries, electric vehicles, robots and AI equipment) are posting the highest growth rates (+55.8% y/y for all AI-related goods over the first nine months of 2026).

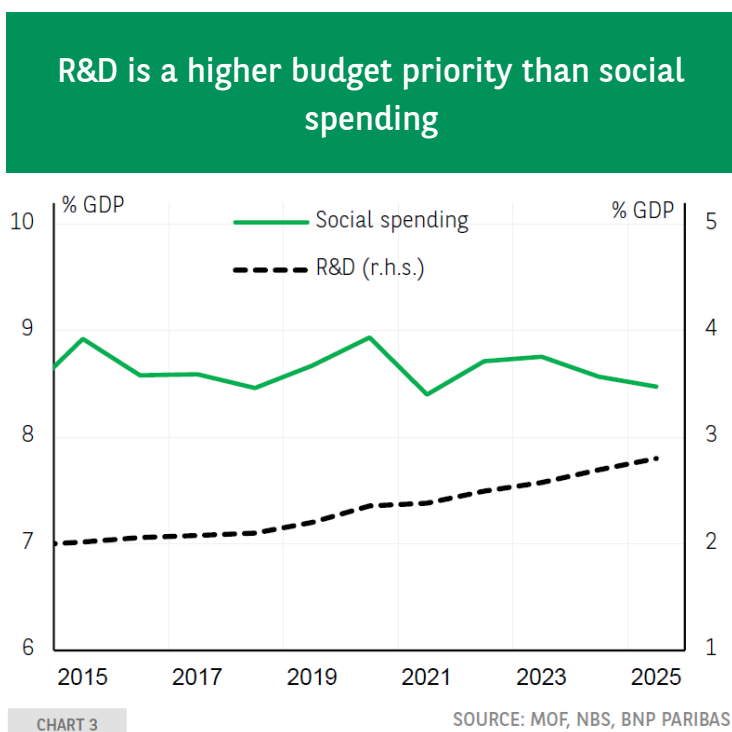
Record external surpluses. Imports, which had been stagnating since 2022, have been recovering since the start of the year (up 27.2% y/y over the first nine months), also driven by both volumes and prices. The countries benefiting from this rebound in the Chinese market are commodity exporters and Asian producers integrated into AI value chains (South Korea in particular). Otherwise, China has significantly reduced its reliance on imports over the past few years. Overall, the trade surplus has grown at a slower rate in 2026 than in previous years. Nevertheless, it has still reached a record high: USD1,249 billion over the twelve months to September 2026, which is three times its 2019 level (see Chart 2). Meanwhile, the current account surplus is expected to approach a record level of USD 800 billion in 2026, representing nearly 4% of China's GDP (a ratio already seen in the late 2000s). As a proportion of global GDP, this is unprecedented (at 0.6%).

Record-high trade surpluses and a still relatively weak yuan



Imbalances set to persist. The imbalances inherent in the growth model are likely to persist, fuelled notably by the strong price and non-price competitiveness of Chinese goods. This competitiveness remains underpinned by: i/ innovation efforts and the move up the value chain in high-tech sectors and the low-carbon transition; ii/ low production costs (labour, low-cost credit, land and energy, tax benefits[1]); iii/ the yuan's exchange rate. Its slow appreciation since mid-2025 has not offset the cumulative depreciation from 2022 to 2025 (nominal and real depreciation due to low inflation), and its real effective exchange rate (REER) remains 10% below its 2021 average. At the end of 2025, the IMF estimated that the REER was undervalued by between 12% and 20%.

Beijing's economic strategy is exacerbating imbalances. The 15th Five-Year Plan[2], launched this year, prioritises innovation, high-tech (export-oriented) sectors and technological self-reliance above all else, whilst reforms to the social security system and private consumption remain on the back burner (see Chart 3). Furthermore, fiscal policy, which had provided moderate support for household spending for a time in 2025, was tightened in 2026 (until the recent announcements of new measures for the final quarter).



Why Beijing is digging its heels in

Beijing is not giving ground on any key issues. Faced with trading partners calling on China to rebalance its economic model, reduce industrial subsidies and strengthen the yuan, Beijing responds that the trade surplus reflects the competitiveness of its goods, points to the United States' insufficient savings, and uses critical materials as a bargaining chip in negotiations.

The need for growth. Exports are a key driver of growth at a time when the Chinese economy is undergoing a period of transition. The country has moved away from its pre-2022 model, which was based on investment in property and traditional industries and financed by debt. Growth is now driven by 'new productive forces', and exports must provide producers with the market that domestic demand does not. Furthermore, innovation and the roll-out of AI must stimulate productivity gains and offset the impact of the shrinking labour force on economic growth. It is essential to limit the slowdown of growth in order to support job creation and absorb the economy's excess debt.

The strategic argument. Exports are a means of asserting China's industrial and technological supremacy, weakening its competitors, and strengthening 'national security'. They place China at the heart of value chains in the most strategic industries, such as AI and the low-carbon transition. Furthermore, the pursuit of self-sufficiency and import substitution — which exacerbate external imbalances — also help to build national sovereignty by reducing dependencies.

A political and fiscal choice. Expanding the social safety net is seen as a solution for providing long-term support for household consumption[3] by reducing their savings rate (estimated at 35.7% of disposable income in 2025, which is more than double the average rate for the euro area). However, this is not a priority for Beijing, certainly due to 'ideological' mistrust of the welfare state and a desire for fiscal prudence. A major reform of the healthcare or pension systems would place a strain on public finances in both the short and long term, particularly as the population ages. Whilst the central government remains in a sound financial position, local governments are already under strain following several years of falling land sales proceeds, high deficits and rising debt. The authorities do not have a large fiscal room for manoeuvre and wish to preserve it in anticipation of future shocks.

Limitations and possible adjustments

In China, a society gripped by anxiety... Economic imbalances are taking their toll on households. The emphasis placed on manufacturing rather than services is having a negative impact on employment and wages (the share of value added allocated to employees' pay is estimated at 50% in the services sector and 41% in manufacturing). The downturn in the property market is eroding households' wealth, and their savings are mainly held in low-yield bank accounts. Finally, social spending is rising slowly (by 5.2% a year since 2020, compared with 9.7% over the previous five years).

... and enterprises under pressure. The low prices of Chinese goods, both for export and on the domestic market — resulting from excess production capacity and 'involution' — are eroding corporate profit margins. Total profits for industrial enterprises have recovered this year but they are highly concentrated, particularly in AI-related sectors, while the proportion of industrial companies reporting losses has continued to rise (30%, compared with 26% in 2022). These vulnerabilities are having increasing contagion effects on the rest of the economy, notably through worsening payment delays and rising pressure on the profitability of financial institutions.

Abroad, trading partners are becoming increasingly intolerant. This is particularly the case of the United States and the European Union[4], which have absorbed 24% and 28% respectively of China's trade

surplus over the last twelve months (data from China's General Administration of Customs). Tensions between the US and China could rise again in 2027 when the current truce (which has mainly led to a reduction in tariffs following the peak in H1 2025) comes to an end. Against a backdrop of competition for technological supremacy and industrial sovereignty, the trend towards decoupling between China and the US could continue, thereby reducing market opportunities for Chinese producers. Europe, for its part, is reinforcing its strategic approach and expanding its toolkit of measures, moving towards more targeted restrictions and stricter market access conditions, especially in case of serious market distortions). Rather than pursuing a strategy of decoupling, the EU is seeking to reduce risks and provide greater protection for critical sectors (including the automotive and chemical industries) without closing its market and whilst continuing to attract Chinese investment. This strategy will also lead to tensions. With imbalances becoming increasingly unsustainable, what course of action would make it possible to avoid a sudden adjustment precipitated by episodes of crises?

A 'concerted' adjustment is difficult to envisage. A negotiated adjustment, along the lines of the 1985 Plaza agreements, seems unlikely in the current international and military context. Furthermore, China and its trading partners largely disagree on the diagnosis and the causes of the imbalances. Moreover, a simple revaluation of the yuan would, on its own, have only a limited effect on China's competitiveness.

A gradual adjustment may be possible... in the long term. However, the reduction of imbalances will need to come both from partner countries (through increased savings) and from China. In the short term, China can ease trade tensions by investing more abroad, which is all the easier given that it has huge current account surpluses. This would enable it to maintain its access to foreign markets and support the production capacity of its trading partners. More structural changes (a more flexible exchange rate regime, less fiscal support for industries and more support for households) will only be feasible once Beijing considers that the costs of its export-led model will outweigh the strategic gains. A key challenge for trading partners will be to work out how to shift this cost-benefit balance.

[1] According to the IMF, the cost of China's industrial policy amounts to about 4% of GDP. See IMF, 'Industrial Policy in China: Quantification and Impact on Misallocation', August 2025: <https://doi.org/10.5089/9798229017855.001>

[2] See BNP Paribas, EcoWeek, [China's 15th Five-Year Plan: prioritising power over addressing imbalances](#)

[3] The IMF estimates, for example, that doubling social expenditure (health, education, social services and basic pensions) in rural areas could reduce savings and raise the ratio of private consumption to GDP by 1.8 pp in the medium term, at an annual fiscal cost of 1% of GDP. See IMF, People's Republic of China 2025 Article IV, February 2026: <https://doi.org/10.5089/9798229038911.002>

[4] See BNP Paribas, EcoWeek, [When it comes to China, Europe should focus less on its trade deficits and more on its investments](#)

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