2025

China Monitoring Report

www.thinkingtaiwan.net

China Monitoring Team：

Chung-Che Huang, Honorary Chairman and CEO, Financial Planning Association of Taiwan

Yi-Feng Tao, Associate Professor, Department of Political Science, National Taiwan University

Chan-Hsi Wang, Associate Research Fellow, Division of National Security Research, Institute for National Defense and Security Research

Guo-Chen Wang, Associate Research Fellow, Chung-Hua Institution for Economic Research

Translation: Ketty W. Chen

Research Assistants: Yi-Kai Chuang and Pin-Yi Huang

(Listed in Alphabetical order)

Table of Contents

Tables

Figures

Preface

In recent years, global assessments of the direction of China's political and economic development have increasingly diverged. This has prompted us to consider how to establish a more comprehensive and objective analytical framework for the long-term observation of trends in China's political economy. Over the past year, we convened a series of roundtable discussions with domestic and international scholars and experts specializing in Chinese politics, economics, and society. We also reviewed a wide range of analytical reports from leading global think tanks on China's political and economic development, and combined these perspectives with the research team's long-standing qualitative engagement with China. Through repeated discussion, refinement, and revision, we ultimately decided to structure the framework around five dimensions economy, finance, fiscal policy, society, and politics, and to develop a total of 50 monitoring indicators for long-term observation. This process culminated in the completion of our first annual report for 2025.

This report draws on an extensive compilation of statistical data related to China's political, economic, and social conditions. Data sources fall into three categories: First are open-source materials released by the Chinese government, including data from the websites of the National Bureau of Statistics, the People's Bank of China, the Ministry of Finance, the Ministry of Commerce, and the National Supervisory Commission, as well as official statistical releases and policy documents. Second are government-affiliated institutions, including the China Government Securities Depository Trust & Clearing Co., the China Foreign Exchange Trade System and National Interbank Funding Center, and the Shanghai and Shenzhen stock exchanges. Third are credible non-governmental research institutions in China and abroad, as well as reporting from news outlets and social media platforms. These data have been systematically collected and compiled by the research team over an extended period. In addition, certain indicators are calculated independently by the team based on established analytical frameworks and theoretical considerations.

This report represents an observation of current conditions and a *snapshot* of relevant trends at a specific point in time, rather than a definitive or final conclusion. These trends may continue to adjust dynamically in response to changes in domestic and external environments. Moreover, given the distinctive characteristics of China's system, comparisons with other countries require particular caution. On the one hand, bottom-up social dynamics may be more constrained; on the other, the state's capacity to suppress, defer, and transform risks may be relatively strong. When interpreting changes in these indicators, it is therefore essential to remain mindful of China's specific context and to avoid drawing conclusions based on generalized assumptions. We view this report as an exploratory analysis and welcome feedback and critique from all quarters. Such input will help us further refine the monitoring framework, enabling the production of more objective and precise annual reports in the future, to serve as references for diverse audiences and to support dialogue and exchange with think tanks around the world.

Finally, the establishment of this database and the completion of our first annual report would not have been possible without the collective efforts of many individuals. I would like to express my deepest gratitude to every member of the China Monitoring Team, who devoted the past six months to repeated meetings and discussions to refine the analytical framework. I am also sincerely thankful to the project advisors, Professors Chen Chih-Jou, Elliott Fan, and Lu Ching-Chih, who, despite their busy schedules, took the time to participate in our roundtables and provide guidance on the development of the framework. The individual sections of the report were completed by Wang Chan-Hsi, Wang Guo-Chen, Huang Chung-Che, and myself. Research assistants Huang Pin-Yi and Chuang Yi-Kai made indispensable contributions by assisting with database construction, meeting record compilation, and final editing. In the final stages of the project, the report could not have been completed on schedule without the rigorous and thorough editorial review and revision provided by Thinking Taiwan Forum Editor-in-Chief Tseng Yen-Ching and Deputy Editor-in-Chief Tien Hsi-Ju, as well as the professional and diligent translation work of Dr. Ketty W. Chen. We are also grateful to Professors Chang Hung-yuan, Chen Hua-sheng, and Tsai Wen-hsuan for reading the initial draft within a short time frame and providing detailed and constructive external feedback, which helped improve the objectivity, rigor, and readability of the report. Lastly, any remaining errors or omissions are the responsibility of the research team, and we welcome further feedback.

Yi-Feng Tao, Project Director, China Monitoring Report

Executive Summary

- Since the collapse of China's real estate sector in 2021, the Chinese economy has been undergoing a dramatic transformation. The property downturn has undermined local governments' land-based fiscal revenues, pushing local public finances and financing vehicles into distress, while private investment and consumption have contracted rapidly. Economic experts have largely converged on the view that China's economic downturn is structural rather than cyclical.

- However, facing intensifying geopolitical competition abroad, particularly the opportunities and challenges brought by the AI revolution, the Chinese central government has chosen not to directly address weak domestic demand. Instead, it plans to drive economic growth through leaps in productivity in high-technology manufacturing, concentrating resources on upgrading high-tech industries. Observing policy pronouncements from the Third Plenum in July 2024 to the Fourth Plenum in October 2025, there are no signs that China's economic policy direction will change. The emphasis remains on production over consumption, with resources concentrated on supply-side acceleration. As a result, China's economy in 2025 continues the post-pandemic pattern of being "cold at home, hot abroad."

- **Economy:** Estimated real economic growth in 2025 is 4.4 percent. Investment and consumption remain weak. Although government policy has strongly supported manufacturing upgrading to enhance productivity, the contraction of private investment has led to the first decline in overall fixed-asset investment since 1995. Consumption growth has slowed to 3.7 percent, while the consumer price index (CPI) continues to hover around zero, indicating that the economy has effectively entered deflation. Exports alone are sustaining economic growth. Weak domestic demand, combined with the shift toward supply-chain localization, has reduced imports, pushing China's overall trade surplus to over USD 1.2 trillion for the first time. This has heightened global concern over "China Shock 2.0" and the export of deflation. At the same time, the withdrawal of foreign capital has produced a new phenomenon in which the share of high-technology products in China's exports has declined, suggesting that the effectiveness of current industrial upgrading policies warrants further observation.

- **Finance:** Amid a simultaneous real estate downturn, weakening local public finances, and private-sector deleveraging, China's economy now exhibits the classic characteristics of a "balance sheet recession." Monetary policy has shifted from a growth-stimulating instrument to a defensive mechanism aimed merely at maintaining static financial system stability. In order to preserve a façade of stability, the government has relied on "Great Wall–style" measures, such as debt swaps and administrative controls, to shift the impact of falling asset prices onto the balance sheets of financial institutions, thereby suppressing the visible manifestation of risk. While this approach avoids an acute crisis, it embeds risk within the system, leading to severe resource misallocation and delaying necessary asset revaluation, ultimately becoming a major source of concern for prolonged low economic growth in the future.

- **Fiscal Policy:** In line with recent trends, the shares of both government revenue and government expenditure in China's GDP have continued to decline. Meanwhile, fiscal deficits and debt issuance have both reached historic highs and are expected to keep rising. When hidden liabilities are included, China's government debt-to-GDP ratio is already comparable to that of the United States; however, given China's relatively weak fiscal revenue base, its future debt-servicing capacity is a cause for concern. As the central government prioritizes geopolitical competition, fiscal policy has sought to relieve budgetary pressure by steadily reducing the proportion of spending related to people's livelihoods and increasing individual tax burdens, producing a "closing the umbrella when it starts to rain" effect that made things worse at the worst possible time, on the overall economy.

- **Society:** The economic downturn has translated into tangible impacts on people's lives: slower income growth accompanied by rising polarization, increasing unemployment, heavy debt burdens, and declining confidence in economic prospects. Marriage and fertility rates have fallen rapidly, while social security provision has been steadily reduced due to local fiscal crises. Social discontent is rising, manifested in a sustained increase in social protests since the pandemic. Compared with the peak under the Hu Jintao era, however, today's protests are driven less by direct economic losses and more by perceptions of systemic injustice. This suggests that the social contract, accepting authoritarian rule in exchange for improving living standards, has broken down, with some arguing that a "new class war" has emerged.

- **Politics:** The most salient political trend in 2025 is the renewed intensification of anti-corruption campaigns. Overall, the intensity during the 20th Party Congress period exceeds that of the 18th. Notably, the absence rate of Central Committee members and alternate members at the Fourth Plenum is unprecedented since the start of reform and opening, and is concentrated among senior PLA officers personally promoted by Xi Jinping. Observations of party-wide anti-corruption and disciplinary campaigns likewise show greater intensity than during the 18th Party Congress, indicating an increasingly centralized yet increasingly unstable "Stalinist logic" under Xi Jinping's leadership.

- The official readout of the "Central Economic Work Conference" held at the end of 2025 still shows no clear indication of a shift away from the imbalanced development path described above. Although *Qiushi* magazine prominently published Xi Jinping's article, *"Expanding Domestic Demand Is a Strategic Move,"* the content largely consists of excerpts from Xi's major speeches since 2015 on expanding domestic demand. This has led markets to perceive that the article's emphasis lies less on "expanding domestic demand" than on the notion of "strategy." As a result, there is a broad expectation that the Chinese government will continue to concentrate resources on accelerating technological self-reliance, using productivity gains to respond to external geopolitical competition and address internal economic challenges.

- Calculating from statistical data released by the Chinese government, export composed around 33 % of China's GDP growth in 2025.If the cycle of weak domestic demand, deflation, and deleveraging does not undergo a dramatic shift, China's economic growth is likely to remain heavily dependent on exports. Whether this reliance ultimately expands or constrains China's room for maneuver in its external relations will be an important issue to monitor going forward.

Introduction

Since the end of the COVID-19 pandemic, China's economy has shown little sign of recovery. In recent years, economists both within China and internationally have largely reached a consensus: China's economic downturn is structural rather than cyclical. Since 2008, reliance on credit expansion (borrowing) to sustain local infrastructure investment and real estate development has maintained high economic growth, but at the cost of severe structural imbalances, excessive investment and insufficient consumption, and massive debt accumulation. State-controlled financial institutions, burdened by these debts, have become an impediment rather than a driver of economic growth[1].

Although professional economic assessments, including those by the International Monetary Fund (IMF), have consistently recommended that the Chinese government address the real estate bubble through a one-time, large-scale fiscal intervention, resolving the massive debts affecting local governments, enterprises, financial institutions, and households, and substantially restructuring fiscal revenues and expenditures to expand social welfare and implement a degree of wealth redistribution so as to enable household consumption and make domestic demand the next engine of growth[2], China's leadership, facing intensifying geopolitical competition, particularly the disruptive impact of the AI-driven Fourth Industrial Revolution, appears unwilling to shift its attention toward weak domestic demand. Instead, economic policy remains focused on technological self-reliance under geopolitical competition and on controlling supply-chain "choke points," continuously channeling large-scale funding into the expansion of national strategic industries. As a result, private investment and household consumption have contracted rapidly, domestic demand has weakened, deflationary pressures have emerged, and the economy has entered what can be described as a "balance sheet recession with Chinese characteristics."

The AI-driven Fourth Industrial Revolution undoubtedly brings unprecedented shocks and uncertainty to global political and economic systems. Governments around the world are striving to seize the opportunities created by AI while managing the challenges it poses, particularly with respect to employment and income inequality. Successfully balancing these forces, capturing opportunities while mitigating risks, will be decisive and represents a shared challenge confronting governments globally. China, however, enters this phase already burdened by the economic distortions left by the collapse of its real estate sector, making the challenge substantially more difficult.

From the Third Plenum of the 20th Central Committee in July 2024 to the Fourth Plenum in October 2025, global observers closely watched whether China would heed economists' recommendations and pivot toward boosting domestic demand through large-scale central government borrowing to absorb domestic debt and expanded social welfare to stimulate consumption, thereby making the domestic market a new engine of growth. Instead, the Chinese

---

[1] George Magnus (2022), "The Chinese economy: Troubled times ahead," *Council on Geostrategy*, No. GPE09; Nichalos Lardy (2023), "How serious is China's economic slowdown," *Peterson Institute for International Economics*; Adam Posen (2023), "The end of China's economic miracle," *Foreign Affairs*; Logan Wright (2024), "China's economy has peaked. Can Beijing redefine its goals?" *China Leadership Monitor*, Issue 81.

[2] IMF (2024), "People's Republic of China: 2024 Article IV Consultation," IMF Country Report No. 24/258.

government has clearly prioritized competition in the AI-driven industrial revolution over resolving domestic economic imbalances, continuing to concentrate national resources on supply-side productivity enhancement and technological self-reliance. This has prolonged China's longstanding development bias toward production over consumption. Weak domestic demand has consequently been offset through massive exports to absorb excess capacity, generating an unprecedented trade surplus exceeding USD 1.2 trillion. This outcome has further reinforced concerns over a "China Shock 2.0" and has fueled a rise in global economic nationalism, with anti-dumping measures likely to constrain China's export growth in the period ahead[3].

Based on the indicators we have collected, this report assesses the internal risks China faces in 2025 across five dimensions: economy, finance, fiscal policy, society, and politics.

[3] David Autor and Gordon Hansen (2025), "We warned about the first China shock. The next one will be worse," *New York Times*, July 14, 2025; USCC (2025), "The 2025 Annual Report to Congress," Chapter 8: China Shock 2.0; Robin Harding (2025), "China is making trade impossible: Europe has nothing to offer and difficult decisions to make," *Financial Times*, Nov. 26, 2025.

I. Economy

Guo-Chen Wang

China's economic downturn persisted. In 2025, the economic growth rate was 5.0%, slowing for three consecutive quarters. Forecasts from 31 institutions place 2026 growth between 4.0% and 4.8%, with a weighted average of 4.4%—a downward revision of 0.4 percentage points from the previous year—and likely falling below the 5.0% policy target (see Table 1-1).

Table 1-1 China GDP Growth Forecasts

Unit: Year-on-year growth rate (%)

Institution Type	Number of Institutions	2025	2026	Revision
International Organizations	6	4.9	4.4	-0.5
Credit Rating Agencies	3	4.8	4.3	-0.5
Commercial Consultancies	3	5.0	4.6	-0.4
Financial Media	3	4.9	4.4	-0.5
Investment Banks	16	4.9	4.5	-0.4
Weighted Average	-	4.9	4.4	-0.5

Note: Latest observation as of December 20, 2025.

The underlying situation may be more fragile than headline figures suggest. In 2025, the combined total of investment, consumption, and the current account balance amounted to RMB 115 trillion, falling below the officially reported GDP figure. This discrepancy implies an overestimation of 9.1 percent and marks the eighth consecutive quarter in which an upward bias has been observed. Adjusting for this discrepancy yields an estimated actual growth rate of 4.4% (see Table 1-2).

Table 1-2 Estimated Actual GDP Growth

Unit: RMB trillion; year-on-year growth rate (%)

Period	Official GDP	Expenditure-Based GDP	Estimation Gap	Official Growth Rate	Estimated Growth Rate
2022/12	121	120	1	3.0	3.0
2023/12	126	114	12	5.2	4.7
2024/12	135	115	20	5.0	4.3
2025/12	102	115	13	5.0	4.4

Note: Expenditure-based GDP is calculated as the sum of urban fixed asset investment, real estate development investment, retail sales, property sales, and the current account balance; estimation gap equals official GDP less expenditure-based GDP.

I. Comprehensive Contraction from Consumption to Investment

Consumption momentum continued to weaken. In 2025,, retail sales of consumer goods grew by 3.7% year on year, extending a six-month deceleration trend. Commercial housing sales have now posted negative growth for 30 consecutive months, with an average contraction of 13.2%. By the end of December, cumulative unsold floor space reached 770 million square meters; based on an average housing size of 111 square meters per household, this corresponds to roughly 6.9 million vacant units.

Soft consumption has further intensified excess capacity pressures. By the end of November, finished-goods inventories held by above-scale industrial enterprises totaled RMB 6.9 trillion, twice the level recorded at the end of 2013. Capacity utilization in the fourth quarter stood at just 74.9%, remaining below the 75% warning threshold for a fourth consecutive quarter and setting a new record for duration (see Figure 1-1).

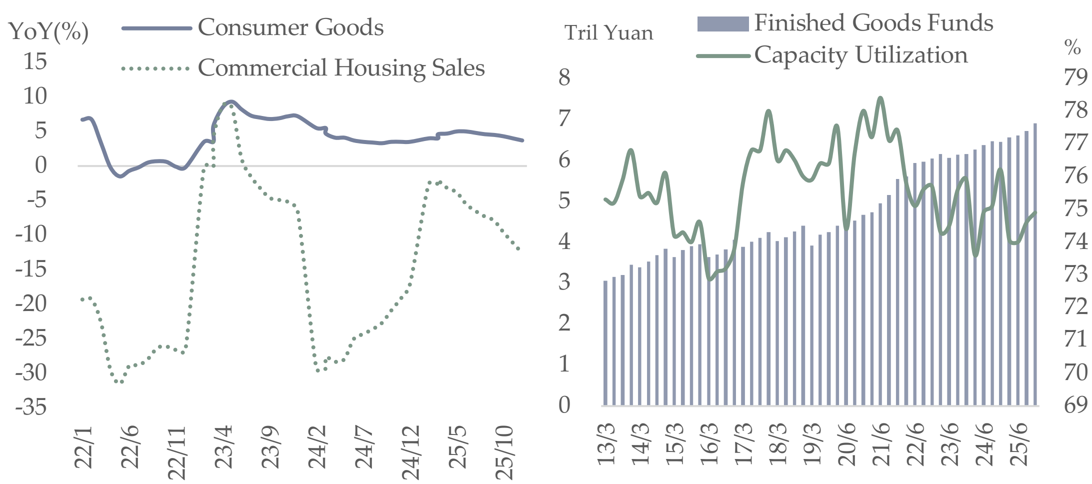

Figure 1-1 China Consumption Momentum **(Jan 2013–Dec 2025)**

Note: Latest Finished Goods Funds data as of November 2025; excludes the March 2020 outlier.

Weakness has also spread to the investment sector. In 2025, urban fixed-asset investment declined by 3.8% year on year, registering negative growth for four consecutive months and reaching a historic low; in the first 11 months, new project starts contracted for 32 consecutive months, with an average year-on-year decline of 9.9%, pointing to persistently weak investment momentum.

Aggressive industrial policy has become another driver of contraction. For the full year, real estate development investment fell by 17.2% year on year, extending a 45-month streak of negative growth. High-technology manufacturing investment is estimated to have declined by 4.2% year on year, marking its fourth consecutive month of negative growth. **Emerging sectors and new technologies have yet to replace real estate as a core economic pillar** (see Figure 1-2).

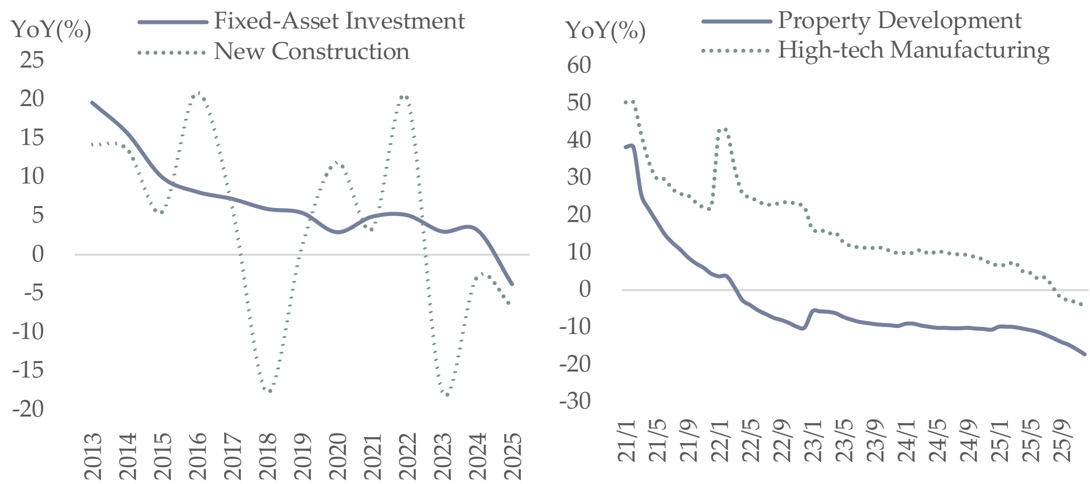

Figure 1-2 China Investment Momentum (Jan 2013–Dec 2025)

Note: Latest New Construction data as of November 2025.

Investment weakness is evident across all major actors. In 2025, private investment fell by 6.4% year on year, with growth remaining below 1% for 37 consecutive months. Investment by state-owned enterprises declined by 2.5% year on year and has slowed for 10 straight months. In the first 11 months, budgeted investment posted negative growth for three consecutive months, dropping by 23.8 percentage points from the beginning of the year.

Multinational firms have also continued to retreat from China. In the first 11 months, foreign direct investment fell by 7.5% year on year, marking 31 consecutive months of contraction. Cross-checking cross-border FDI flows suggests cumulative capital withdrawals of approximately RMB 11.1 trillion over this period (see Figure 1-3).

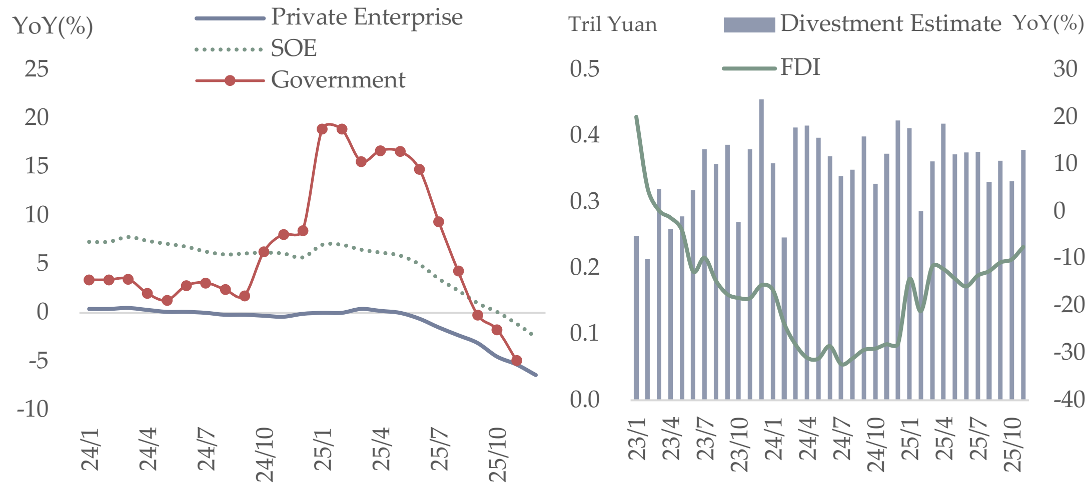

Figure 1-3 China Corporate Investment **(Jan 2013–Dec 2025)**

Note: Latest data for budgeted investment, FDI, and Divestment Estimate as of November 2025.

II. Red Supply Chains Sweep Across the Globe

China's export performance has generated global shockwaves. In 2025, goods exports grew by 5.5% year on year, extending a 24-month streak of positive growth. Imports recorded zero growth, ending an 11-month streak of contraction. Netting exports and imports, the goods trade surplus recorded double-digit growth for 15 consecutive months and reached an unprecedented US$1.2 trillion (see Figure 1-4).

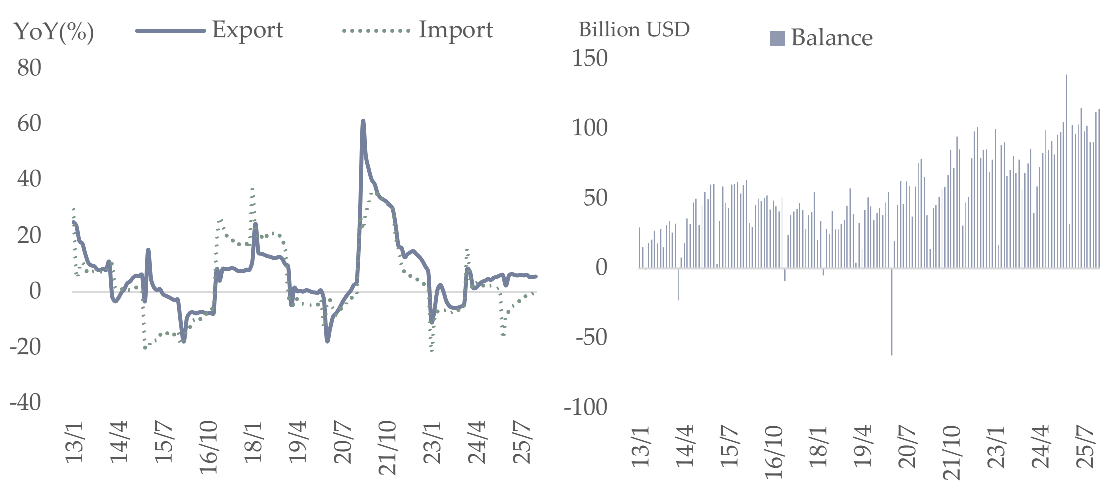

Figure 1-4 China's Goods Trade Conditions **(Jan 2013–Dec 2025)**

This headline surplus may still understate underlying distortions. As shown in Table 1-3, for 2025, China's reported imports from Taiwan totaled US$230.7 billion, $130.7 billion higher than Taiwan's recorded exports to China. Conversely, China's reported exports to Taiwan amounted to $83.6 billion, $8.1 billion lower than Taiwan's recorded imports. Cross-Strait phantom trade alone accounts for 11.6% of China's total surplus, suggesting a scale that is difficult to fully quantify.

Table 1-3 Cross-Strait Phantom Trade

Unit: US$100 million

Year	China Exports	Taiwan Imports	Underreported Exports	Taiwan Exports	China Imports	Overreported Imports	Total
2020	601	636	34	1,024	2,007	982	1,017
2021	784	825	41	1,259	2,500	1,241	1,282
2022	816	840	24	1,211	2,381	1,170	1,194
2023	685	702	17	957	1,993	1,036	1,054
2024	752	793	41	970	2,178	1,208	1,250
2025	836	917	81	1,001	2,307	1,307	1,388

China's trade shock also reflects intensified low-price dumping. The share of high-technology products in exports fell from 30.0% in 2020 to 25.1% in 2025; of which, exports from the "new three" industries, electric vehicles, solar energy, and lithium batteries, account for just 4.7%. In the first 11 months, average export prices declined by 15.9% from their peak; excluding June 2025, prices have posted negative growth for 29 consecutive months.

However, a major shift has occurred in the composition of trade actors. The share of exports by foreign-funded enterprises fell from 47.3% in 2013 to 27.1% in 2025, effectively halving and signaling the rise of red supply chains. The share of imports by foreign-funded firms likewise plunged by 12.6% due to import-substitution policies. Consequently, Chinese-funded enterprises are increasingly capturing global trade gains (see Figure 1-5).

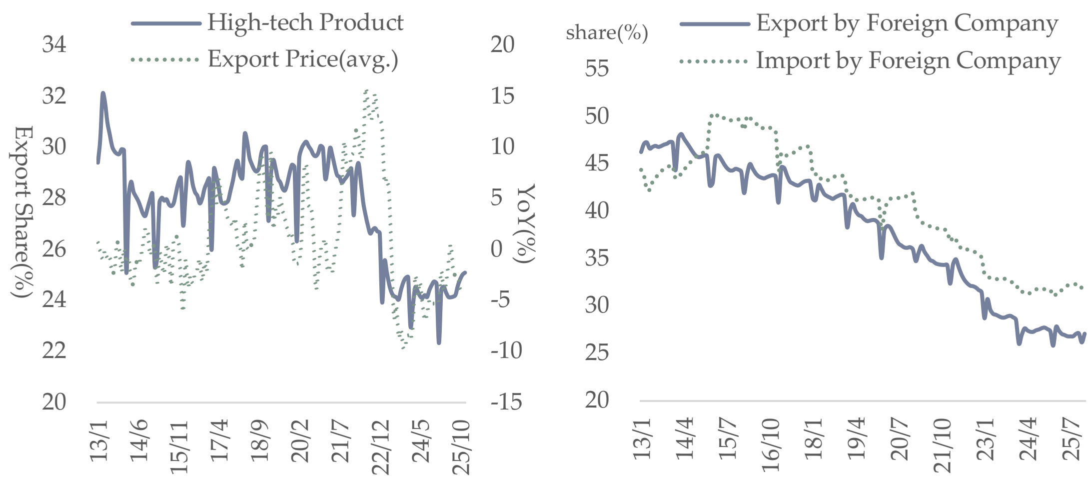

Figure 1-5 China's Goods Trade Export Structure **(Jan 2013–Dec 2025)**

Note: Latest data for Export Price as of November 2025.

III. Internal and External Pressures Severely Undermine Economic Confidence

China is deeply mired in deflation. In 2025, the Consumer Price Index (CPI) recorded zero growth; in the preceding nine months, it remained negative. The Producer Price Index (PPI) has now registered negative growth for 36 consecutive months, second only to the prolonged downturn observed between 2012 and 2016.

Deflationary dynamics have pushed up the real exchange rate. In December, CPI rose by 0.7% year on year, 1.9% below the U.S. rate, indicating rising purchasing power and contributing to an appreciation of the real effective exchange rate (REER). However, capital-account controls, combined with the renminbi's relative weakness against other currencies, have meant that nominal depreciation has outweighed deflation-driven real appreciation. As a result, the renminbi's REER remains significantly below that of the U.S. dollar and appears undervalued by roughly 20.3% (see Figure 1-6).

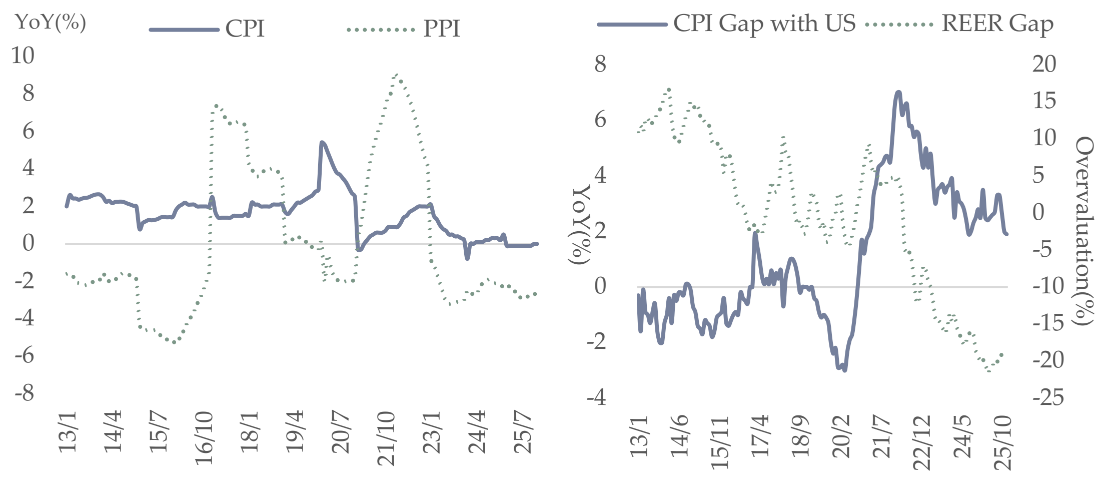

Figure 1-6 Renminbi Real Effective Exchange Rate (Jan 2013–Dec 2025)

Note: Latest data for REER as of November 2025.

Real depreciation, combined with the collapse of the housing market bubble, has weighed heavily on consumer confidence. In December, new-home prices in 70 major cities fell by 3.0% year on year, extending a 45-month streak of declines; prices are now 11.8% below their peak. In the first 11 months, the Consumer Confidence Index (CCI) contracted for 44 consecutive months, averaging 88.0—well below the warning threshold of 100.

At the same time, large volumes of foreign exchange have again been directed toward capital investment in the technology sector, further skewing industrial structure. In the first 11 months, value added by above-scale industrial enterprises grew by 6.0% year on year, far outpacing the 0.4% growth recorded by the service production index and extending a 23-month streak of positive growth. Beijing continues to advance its policy of "shifting from the virtual to the real economy" (see Figure 1-7).

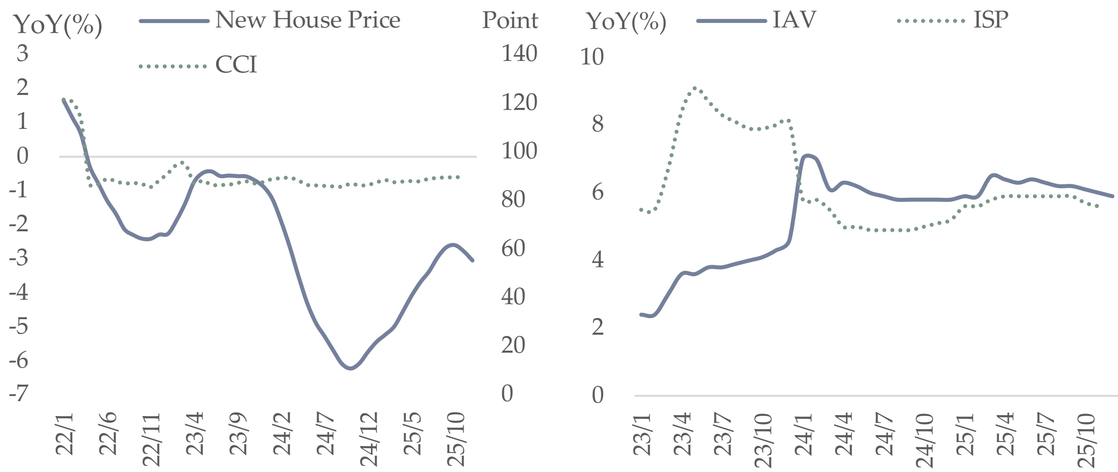

Figure 1-7 Consumer Confidence and Industrial and Commercial Output in China **(Jan 2022–Dec 2025)**

Note: Latest data for CCI and ISP as of November 2025.

Countries have increasingly moved to block export dumping. From 2023 to 2025, 36 countries launched a total of 765 trade investigations against China involving anti-dumping, countervailing, and safeguard measures. Chinese-funded firms have responded by accelerating overseas relocation. In the first 11 months, outward FDI grew by 6.9% year on year, rising for five consecutive months and nearly matching last year's pace.

International trade frictions have further undermined confidence among Chinese-funded enterprises. In December, the manufacturing PMI stood at just 50.1, having remained in contractionary territory for the preceding eight months. The non-manufacturing PMI has also hovered around the 50-point expansion–contraction threshold for 19 consecutive months (see Figure 1-8).

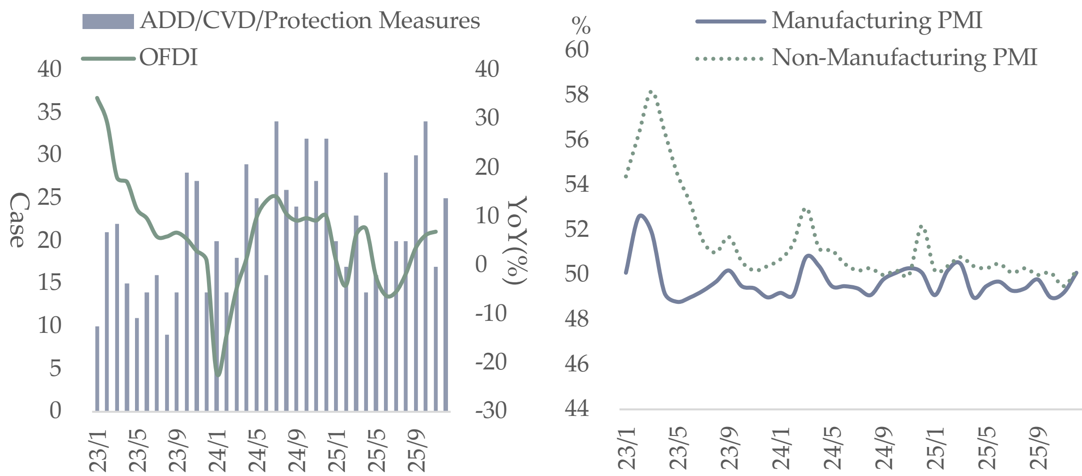

Figure 1-8 International Economic and Trade Conflicts and Confidence of Chinese-Funded Enterprises **(Jan 2023–Dec 2025)**

Note: Latest OFDI data through November 2025.

IV. Summary: Likely to Linger at the Bottom of an L-Shaped Trajectory

In 2025, China's officially reported economic growth stood at 5.0%. After adjusting for statistical discrepancies, actual growth is estimated at approximately 4.4%. Estimates from the Rhodium Group present an even more pessimistic assessment, placing growth at roughly half the official figure, in the range of 2.5 to 3.0%. In particular, the progression from weak consumption to deflation and then to broad-based investment contraction underscores a deteriorating trajectory.

Looking ahead, China's economy is likely to remain at the bottom of an L-shaped path for an extended period, with limited prospects for a strong rebound. Three key risks warrant close monitoring. First, if the goods trade surplus were to erode toward zero, investment would become increasingly unsustainable. Export growth has already slowed from 6.0% to 5.4%, while Mexico has imposed a 50% tariff on Chinese goods and other countries have tightened measures to prevent transshipment into the United States.

Second is the tightening of foreign-exchange controls, particularly constraints on overseas investment by Chinese-funded enterprises. In November 2025, the People's Bank of China issued new customer due-diligence rules requiring identity verification for single cross-border remittances of RMB 5,000, extending regulatory oversight to payment platforms.

Finally, property taxation is moving back onto the policy agenda. Shanghai and Chongqing first piloted property taxes in 2011. After a decade-long hiatus, Beijing has expanded pilot reforms, and the 2025 Central Economic Work Conference explicitly called for strengthening the local tax system—within which property tax has been designated a key local levy.

II. Finance

Chung-Che Huang

In recent years, the Chinese government has intensified efforts to maintain financial stability and contain systemic risk. Since 2020, the banking system's non-performing loan (NPL) coverage ratio has risen from approximately 179% to over 210%, while the capital adequacy ratio has remained stable at around 15%. These indicators suggest that financial institutions have continued to increase provisions against expected loan losses, thereby strengthening the banking system's overall capacity to absorb risk (see Figure 2-1, NPL Coverage Ratio, and Figure 2-2, Capital Adequacy Ratio).

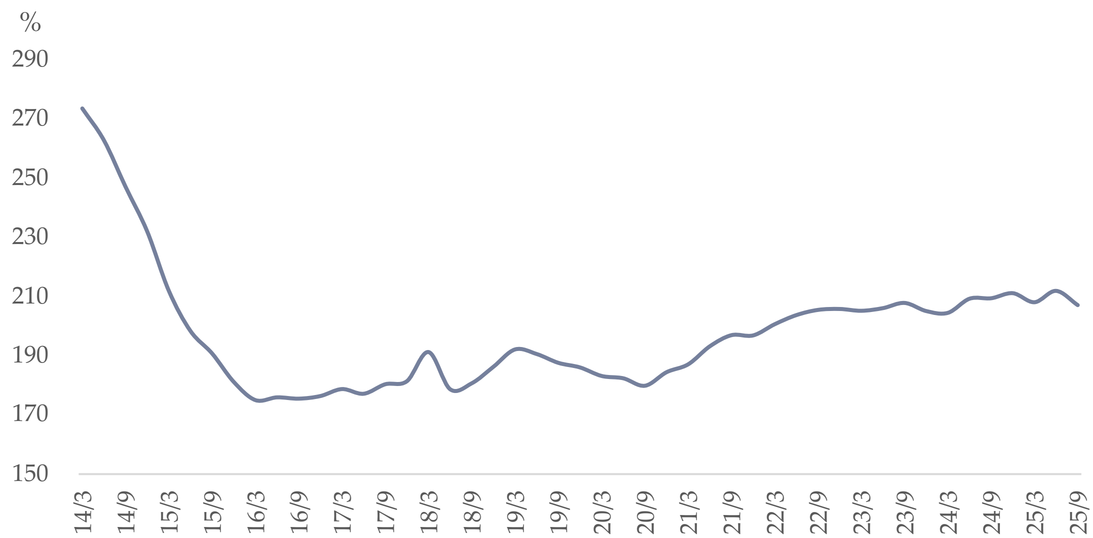

Figure 2-1 NPL Coverage Ratio (Mar 2014–Sep 2025)

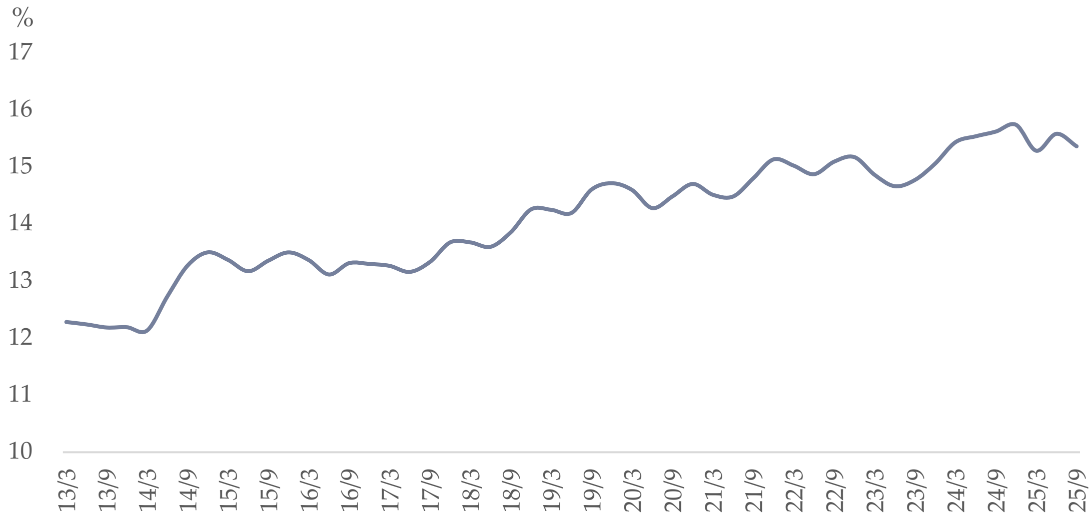

Figure 1-2 Capital Adequacy Ratio (Mar 2013–Sep 2025)

At the same time, regulatory authorities have implemented the revised Measures for the Risk Classification of Financial Assets of Commercial Banks, which require loans overdue for more than 90 days to be classified as non-performing, with the aim of ensuring that potential risks are reflected on bank balance sheets at an earlier stage. In parallel, local and policy-oriented financial institutions have gradually established stress-testing and early-warning mechanisms, improving coordination and transparency in financial supervision. Taken together, these measures indicate that the Chinese government is seeking to enhance the resilience of the financial system in line with what Xi Jinping has termed the "path of financial development with Chinese characteristics," which emphasizes the centralized and unified leadership of the Party over financial work and treats risk prevention and control as the enduring core task of financial governance. Nevertheless, despite the current appearance of temporary stability, China's financial system faces a series of high-risk challenges in the next stage of development.

I. Weak Credit Demand and the Emergence of a Liquidity Trap

Since 2013, the People's Bank of China (PBOC) has repeatedly injected liquidity through open-market operations and successive reductions in the required reserve ratio (RRR), lowering it from 19.5% in 2013 to 6.2% in 2025. Over the same period, the one-year Loan Prime Rate (LPR) declined from 6.4% to 3.0%, reflecting a sustained easing of policy interest rates (see Figure 2-3, Money Market Interest Rates).

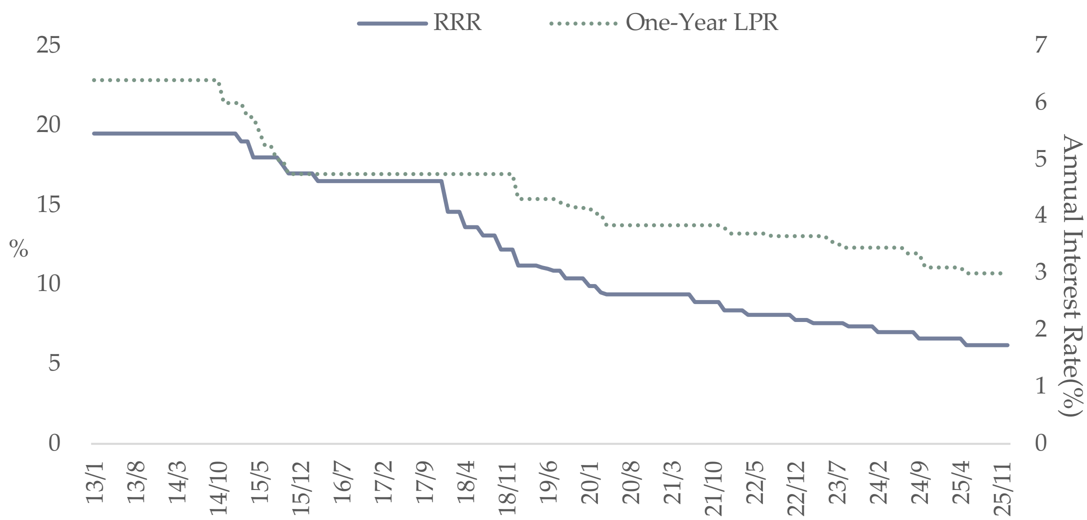

Figure 2-3 Money Market Interest Rates (Jan 2013–Dec 2025)

However, accommodative interest rates have not translated into stronger investment or consumption in the real economy. Year-on-year growth in M1 has fallen below 3%, signaling weak demand for transaction-related funds, while M2 growth has remained within the range of 8% to 9%. The widening gap between the two since 2021 has produced a pronounced "M1–M2 scissors gap," indicating that monetary expansion has flowed primarily into savings rather than into investment financing. This scissors-gap trend did not begin to narrow until the second half of 2025, largely due to renewed activity in the stock market[4].

[4] The so-called M1–M2 "scissors gap" refers to the difference between the growth rates of narrow money (M1) and broad money (M2). When M1 growth exceeds M2 growth (a positive scissors gap), it indicates ample market liquidity, optimism among firms and households about economic prospects, and strong demand for funds. By contrast, when M1 growth is lower than M2 growth (a negative scissors gap), it suggests that funds are flowing primarily into savings and that real economic activity is weak. China is currently experiencing a sustained negative scissors gap, implying that policy-injected liquidity is largely remaining within the banking system and time deposits, rather than being effectively transformed into actual investment and consumption.

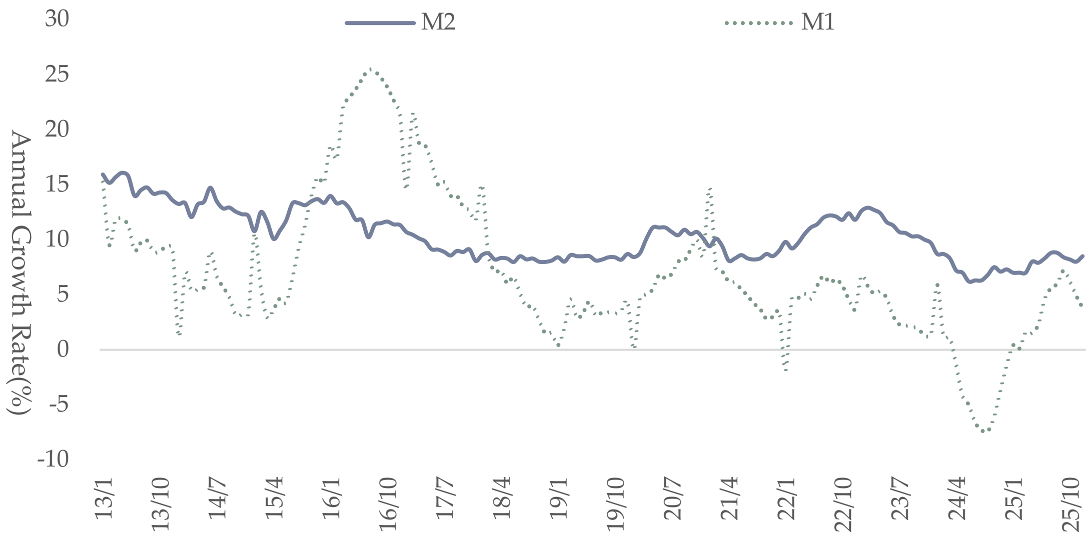

Figure 2-4 M1–M2 Scissors Gap (Jan 2013–Dec 2025)

At present, credit demand is driven mainly by government industrial policy objectives. Lending associated with government-backed projects and policy-oriented initiatives has increased significantly, while private-sector borrowing remains weak. As a result, monetary policy has gradually shifted from serving as a macroeconomic stabilization tool toward functioning as an extension of fiscal policy.

Consequently, the PBOC's liquidity injections have not led to an expansion in overall economic demand. Private investment and household consumption have continued to decline. From the perspective of monetary policy effectiveness, China now exhibits the typical characteristics of a liquidity trap: liquidity is abundant, yet investment and consumption remain stagnant; prices continue to fall due to insufficient demand, generating deflationary pressure and leaving the economy struggling to regain momentum[5].

II. Housing Market Collapse and Household Deposits as the Final Systemic Safeguard

Since 2021, prices in China's real estate market have declined, with both housing prices and transaction volumes continuing to fall. Although the central bank has repeatedly reduced mortgage interest rates to stimulate demand, home-purchase willingness has remained weak. The share of mortgages in total lending has declined markedly, while funds have increasingly shifted toward policy-based financing and local infrastructure projects. Falling housing prices have eroded collateral values, and in 2024 the nationwide non-performing mortgage ratio rose to

[5] From an economic perspective, a liquidity trap refers to a situation in which the stimulative effects of monetary policy on the real economy diminish markedly, rendering it ineffective in altering firms' and households' borrowing and spending decisions. When a liquidity trap occurs, deflationary expectations and persistently declining asset prices lead funds to remain concentrated in cash or low-risk assets, keeping effective borrowing demand subdued. Observed through the lens of current lending behavior, China already exhibits the core characteristics of a liquidity trap.

approximately 1.9%, the highest level in nearly five years. Defaults by property developers have further amplified pressures on the financial system.

However, these disclosed non-performing mortgages do not yet fully reflect the potential impact of the large number of developer defaults and funding-chain disruptions that have emerged in recent years. On the one hand, some developer financing has been temporarily shielded from formal risk recognition through policy arrangements such as the "guaranteed delivery of housing" program, debt swaps, and maturity extensions. On the other hand, both real estate development loans and mortgage loans are typically secured by property collateral, and the process from collateral disposal and judicial procedures to final recognition as non-performing assets often takes considerable time, creating a substantial lag in the on-balance-sheet manifestation of risk.

It Is therefore notable that many Chinese banks have recently accelerated the disposal and sale of real estate assets they hold, suggesting that the banking system is gradually preparing for a potential future increase in non-performing mortgages and asset-quality pressures.

Financial stress arising from the real estate downturn is particularly prone to spreading because of China's long-standing reliance on land-based local government finance. Local government financing vehicles (LGFVs) are not only the primary funding channel for urban construction but also form a large pool of local government debt through bank lending and bond issuance. For many banks, LGFV bonds and loans were once important sources of income, but the property market downturn has sharply increased their risk. Regulators have therefore required banks to raise provisioning levels and capital adequacy ratios. While overall system resilience can still be maintained, the resolution of bad loans and the rollover of bonds have eroded bank profitability, with small and medium-sized banks facing particularly acute operational pressure.

At the same time, as economic growth slows and labor-market conditions deteriorate, credit risk has spread from the real estate sector to households and firms. Overdue rates on credit cards and small and medium-sized enterprise loans have increased, while the liquidity capacity of households and businesses has weakened. This has further undermined market confidence and consumption momentum, contributing to a rapid rise in total non-performing loans since 2021. The aggregate stock of non-performing assets has now exceeded RMB 3 trillion and continues to increase (see Figure 2-5, Total Non-Performing Assets).

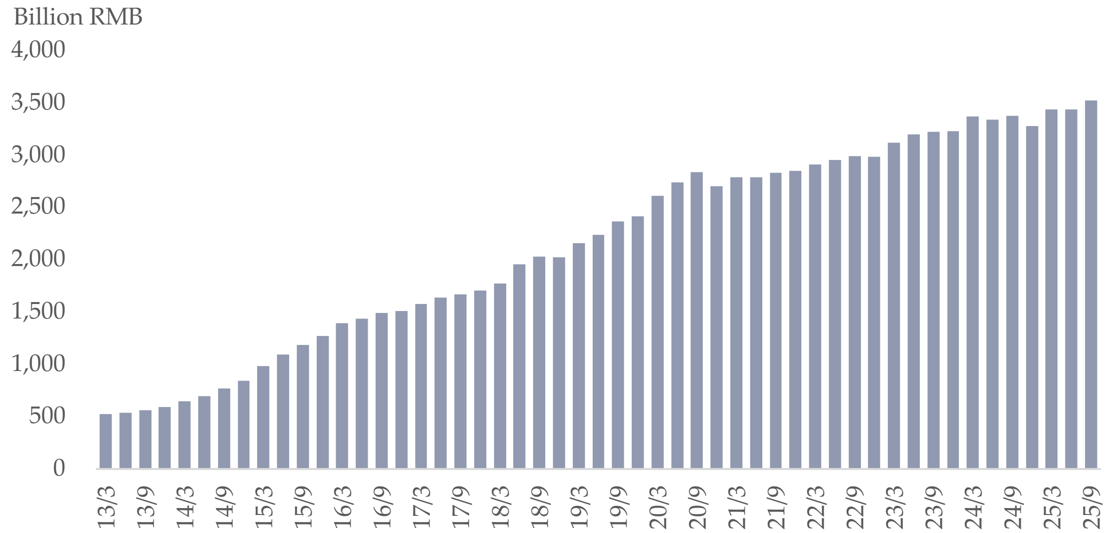

Figure 2-5 Total Non-Performing Assets **(Mar 2013–Sep 2025)**

Within this series of negative feedback loops, household deposits have instead become a key stabilizing force for the financial system. Over the past three years, total household deposits have increased by more than RMB 15 trillion, reflecting defensive saving behavior amid heightened uncertainty. While elevated savings temporarily strengthen the liability side of bank balance sheets, they also indicate a retreat in investment and consumption willingness. If economic stagnation persists, banks' asset quality and the efficiency of credit allocation will come under increasing strain (see Figure 2-6, Renminbi Deposits and Loans).

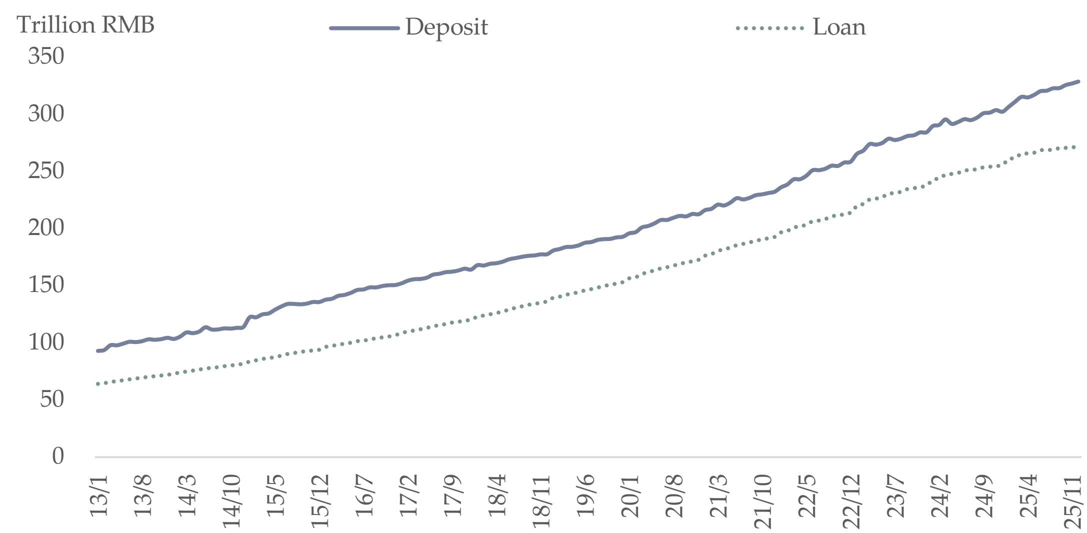

Figure 2-6 RMB Deposits and Loans **(Jan 2013–Dec 2025)**

Nevertheless, household deposits can only provide a liquidity buffer and cannot offset the deterioration in balance-sheet quality. As housing prices continue to fall, the real-estate-centered collateral system is undergoing a severe process of asset revaluation. For small and medium-sized banks and urban and rural banks with weaker risk-bearing capacity, defaults by LGFVs and property developers, combined with declining collateral values, have sharply increased the burden of non-performing asset resolution.

As these pressures heighten the risks of bank runs and institutional failure among smaller financial institutions, authorities have accelerated a wave of mergers and restructurings in order to preserve overall financial stability and prevent localized credit events from triggering systemic contagion. These government-led consolidations effectively absorb risk-laden institutions into larger provincial or state-owned banks through administrative measures. At the same time, they signal that China's financial system has entered a defensive phase in which survival increasingly depends on balance-sheet contraction and structural reorganization (see Figure 2-7, Number of Financial Institutions in China).

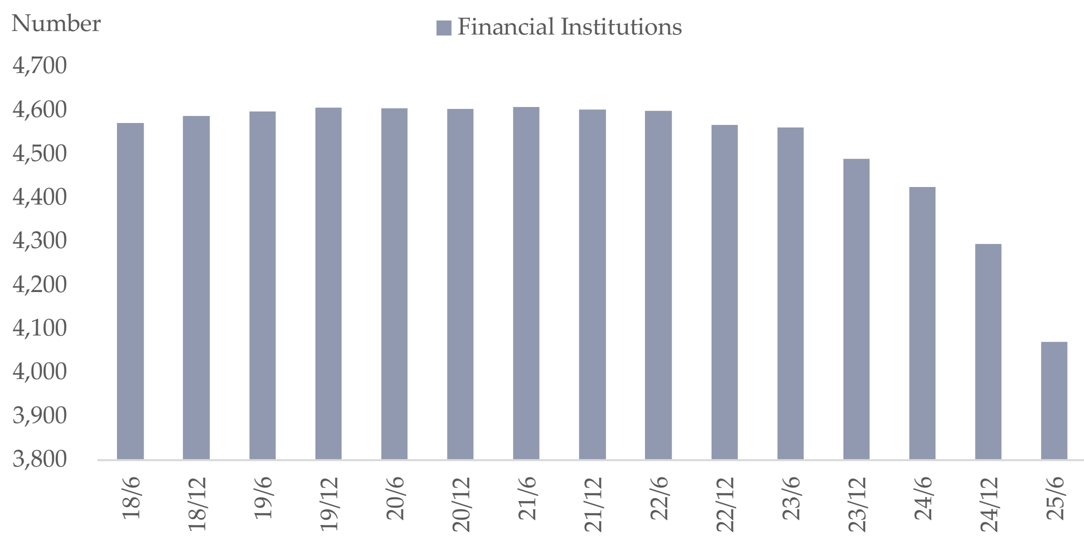

Figure 2-7 Number of Financial Institutions in China (Jun 2018–Jun 2025)

III. The Disconnect Between Stock Market Performance and Economic Growth

Over the past three years, China's stock market has experienced repeated policy-driven rebounds that have not been matched by a recovery in the real economy. Economic growth slowed from 8.4% in 2021 to approximately 4.5% in 2024, reflecting weak domestic demand and investment momentum. By contrast, major equity indices have risen under conditions of monetary easing and policy support. While abundant liquidity has lifted financial asset prices, corporate profitability and investment returns have not improved in parallel, indicating that equity performance reflects policy expectations more than underlying economic fundamentals.

To stabilize market confidence, the government has frequently deployed so-called "national team" funds and implemented administrative measures such as restrictions on short selling and encouragement of corporate share buybacks. Since 2023, large-scale buybacks have provided support for stock prices, particularly in policy-priority sectors such as semiconductors, artificial intelligence, and new energy. Although these measures may alleviate market pressure in the short term, they have also contributed to capital concentration in specific sectors, increasing the risks of valuation bubbles and capital misallocation (see Figure 2-8, Share Buyback Statistics).

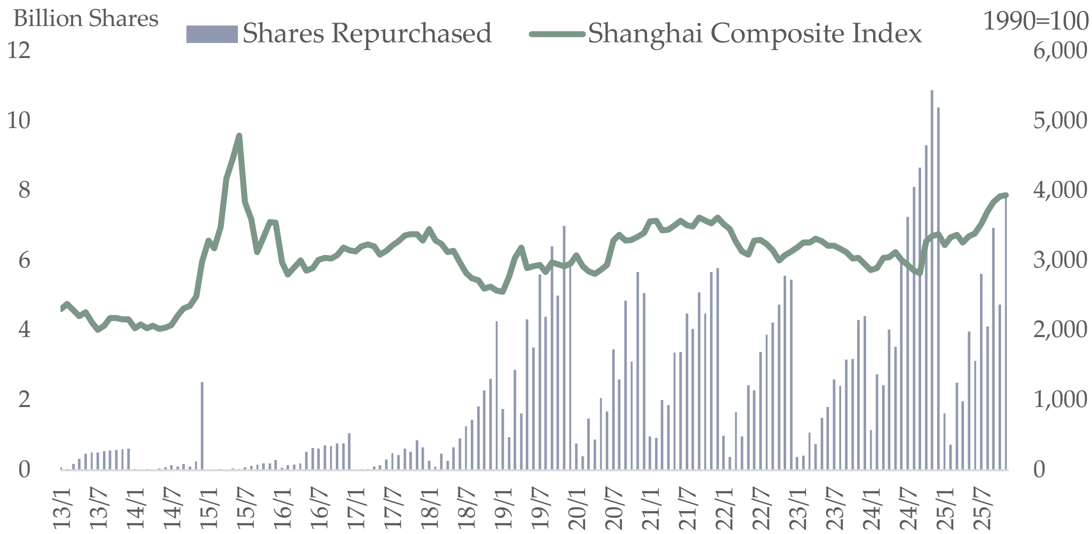

Figure 2-8 Share Buyback Statistics and SSE Composite Index (Jan 2013–Dec 2025)

Overall, when stock market stability depends primarily on policy intervention rather than corporate earnings, it comes at the expense of market-based price formation. If investors come to expect equity prices to be determined by government policy rather than firm-level competitiveness, opacity in the pricing mechanism will deepen, further weakening confidence in the functioning of China's stock market.

IV. The Futility of Building a Financial Superpower Through a "Regulatory Great Wall"

Even as financial risks continue to accumulate, China has articulated a strategic vision of "building a financial powerhouse" in its 1^{5t}h Five-Year Plan. This vision emphasizes strengthening the central banking system, monetary policy, and macroprudential management; improving policy transmission and financial stability; promoting emerging financial instruments and direct financing; and enhancing the capital market's capacity to serve the real economy. It also calls for stronger financial regulation and risk prevention, alongside the development of the Shanghai International Financial Center and the digital renminbi system, to support financial security and international competitiveness.

On the surface, this vision suggests continued confidence in financial development. In practice, however, it highlights a governance approach that substitutes administrative control for market mechanisms and maintains superficial stability by suppressing the visibility of risk. This approach resembles a nationwide "Great Wall–style" system of financial governance: risks are not resolved but contained at high cost; financial efficiency is constrained rather than enhanced; and market signals are obscured rather than corrected.

From the perspective of bank asset allocation, holdings of debt investments have expanded rapidly in recent years. As shown in Figure 9, the outstanding balance of government bonds held by commercial banks rose from RMB 5.3 trillion at the beginning of 2014 to more than RMB 60 trillion by 2024.

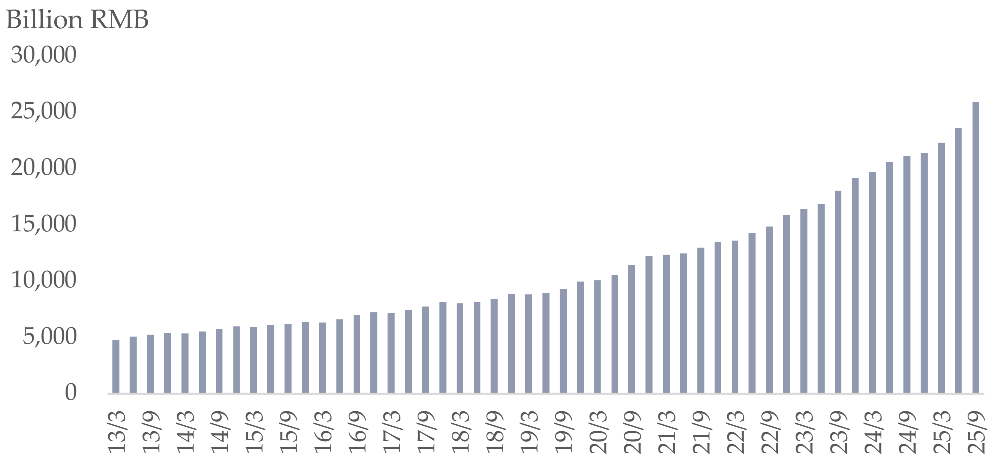

Figure 2-9 Government Bonds Held by Commercial Banks (Mar 2013–Sep 2025)

The share of government bonds in commercial banks' total assets also doubled over this period, rising from 4.2% to more than 13% (see Figure 2-10). The first peak occurred in 2018–2019, reflecting mounting stress in local government fiscal systems. In response to the risk of hidden-debt defaults, authorities expanded the issuance of local government special bonds, seeking to replace opaque non-standard debt with explicit liabilities. For banks facing a real-economy downturn, allocating assets to government bonds with zero risk weight fulfilled policy objectives while allowing balance-sheet expansion without consuming capital, making such assets a preferred refuge under regulatory constraints.

A second wave of growth began in July 2023, following the launch of a "package-style" debt resolution program that relied heavily on special refinancing bonds to address the intensifying LGFV default crisis. At this stage, bank balance sheets effectively became the final repository for plugging local fiscal shortfalls.

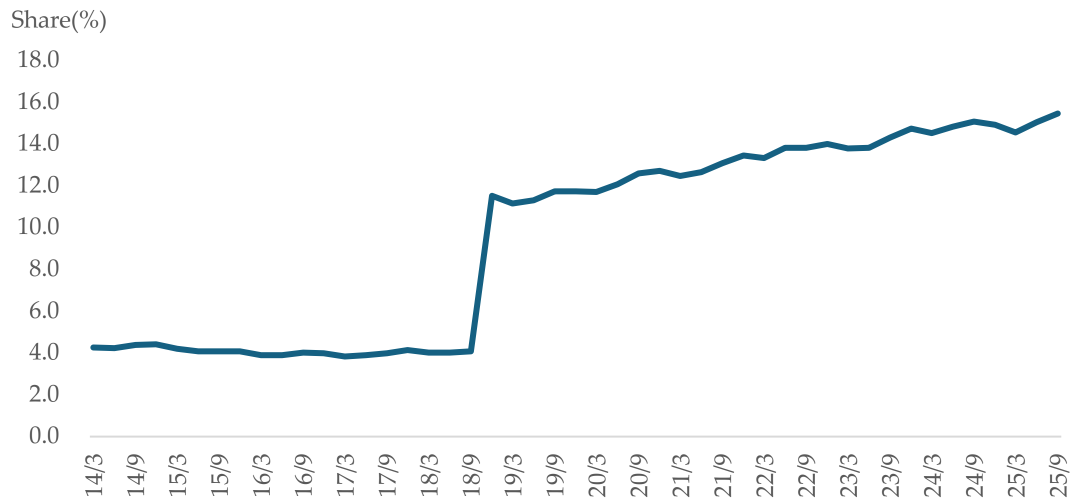

Figure 2-10 Government Bonds as a Share of Total Bank Assets **(Mar 2014–Sep 2025)**

As a result, official data continue to show capital adequacy ratios of around 15% and provision coverage ratios above 210%. What remains obscured, however, is the extent to which administrative supervision, capital controls, and policy-based financial support have insulated banks from recognizing bad debts, allowing balance sheets and asset prices to retain a low-risk appearance. Although China is therefore unlikely to experience an acute financial crisis in the near term, the costs include delayed asset revaluation, worsening resource misallocation, and impeded balance-sheet repair in the private sector, all of which prolong the recovery cycle.

V. Summary: Balance Sheet Recession as a Drag on Economic Recovery

From a macro perspective, China’s core financial risk lies not in a single collapse event, but in the prolonged process of balance-sheet contraction.

Despite continued monetary easing, weak investment and consumption demand mean that the overall scale of economic activity is likely to shift from expansion toward contraction. This dynamic closely resembles the “balance sheet recession” described by Richard Koo in the context of Japan’s lost decades, in which firms and households prioritize debt minimization over profit maximization. Under such conditions, even abundant liquidity and low interest rates fail to stimulate borrowing, as cash is used to repay debt rather than finance new investment or consumption. Monetary policy transmission weakens, and growth momentum declines.

China’s challenges, however, are more complex than Japan’s experience in the 1990s. The real estate downturn directly erodes household wealth and creates fiscal gaps in land-based local government finance; population aging and limited social safety nets encourage precautionary saving; and a deteriorating external environment heightens technological and trade uncertainty, constraining employment and income growth. These factors may deepen China’s stagnation. When compounded by additional misallocation arising from “Great Wall–style” financial governance, China may face higher adjustment costs and a longer recovery period than Japan.

Accordingly, the core of China's financial risk in 2025 is that administrative power has succeeded in preventing risk from becoming visible, sustaining short-term stability, while the government remains unwilling to resolve decisively the large debt overhang created by the real estate bubble. The economy has therefore entered a balance-sheet recession, characterized by a private sector that prioritizes debt repayment over returns, weakened monetary transmission, and a downward shift in growth potential. China's financial system is unlikely to collapse abruptly, but it will continue to advance toward the goal of becoming a financial powerhouse under conditions of low growth, low efficiency, and elevated risk.

III. Fiscal Policy

Yi-Feng Tao

As land-based fiscal revenues have been depleted in recent years and overall economic growth has slowed, fiscal revenues for both China's central and local governments have deteriorated accordingly. Governments have therefore relied on the continuous expansion of public bond issuance to meet fiscal needs, including maintaining basic government functions; managing, though not resolving, debts accumulated through local real estate bubbles; sustaining selected ongoing construction projects; and meeting the central government's substantial funding requirements for military capability expansion and strategic industry development. Although China's outstanding government debt, measured as a share of GDP, is not particularly high compared with most advanced economies burdened by extensive social welfare obligations—and thus appears to leave some room for additional borrowing—China's relatively low level of fiscal revenue raises concerns regarding its future debt-servicing capacity.

In particular, China's current use of government borrowing differs from that of economies facing weak domestic demand that rely on expanded social welfare spending to stimulate consumption. Instead, borrowing has been directed primarily toward rapidly rising military expenditures and high-technology industrial development amid geopolitical competition, making its effectiveness in supporting economic recovery or expanding the future tax base uncertain. Under these circumstances, recent fiscal adjustments have focused on expanding tax coverage and compressing expenditures. For the general public already experiencing economic downturn, these measures have produced the negative effect commonly described as "putting away the umbrella when it rains."

I. The Exhaustion of Land Finance and Record-High Fiscal Deficits

According to China's Budget Law as revised in 2014, the government budget should consist of four major components:

1. General public budget: including tax revenues, non-tax revenues, and central government transfer payments
2. Government fund budget: primarily land conveyance revenues
3. State capital operations budget: investment income and returns from state-owned enterprises under the supervision of local state-owned assets supervision and administration commissions
4. Social insurance fund budget: the operation of the five major social insurance funds, with local fiscal support required when revenues are insufficient to cover expenditures

However, the fiscal revenue and expenditure data published by the Ministry of Finance include only the first two components, namely the general public budget and the government fund budget. While government revenues fluctuate with GDP growth, the ratio of government revenue to GDP has declined steadily since 2013, falling from 22.5 percent in 2013 to 16.8 percent as of September 2025 (see Figure 3-1, lower solid line on the left). This decline has been driven primarily by the sharp contraction in the government fund budget, which is dominated by land conveyance revenues and represents the traditional form of "off-budget" income.

Alongside declining revenues, government expenditures have also fallen, and at a faster pace, decreasing from 31.6 percent in 2013 to 23.2 percent as of September 2025 (see Figure 3-1, upper dashed line on the left). As a result, the national fiscal gap ratio—the ratio of the fiscal deficit to fiscal revenue—has remained broadly stable, standing at 40.4 percent in 2013 and 38.1 percent as of September 2025 (the two lines on the left side of Figure 1 remain broadly parallel and have narrowed slightly in recent years). By contrast, the funding gap ratio of local governments, which are responsible for the majority of policy implementation, has risen from 66.7 percent in 2013 to 91.6 percent as of September 2025, indicating a continued expansion of local fiscal deficits (see Figure 3-1, where the lower solid line on the right declines gradually while the upper dashed line remains elevated).

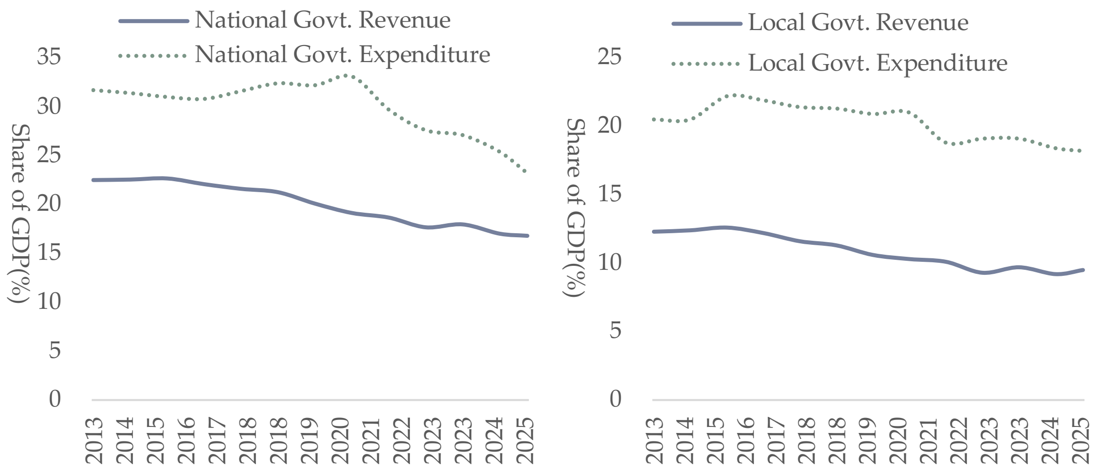

Figure 3-1 Broad Fiscal Revenues and Expenditures (Jan 2013–Sep 2025)

In the post–Covid-19 period, overall tax revenue growth has remained weak, reflecting the broader economic slowdown. Land conveyance revenues have continued to contract, while episodic increases in fiscal income have been driven largely by non-tax revenues. This pattern underscores both the severity of the land-finance shock and the growing reliance on revenue sources that risk generating social discontent and economic distortions.

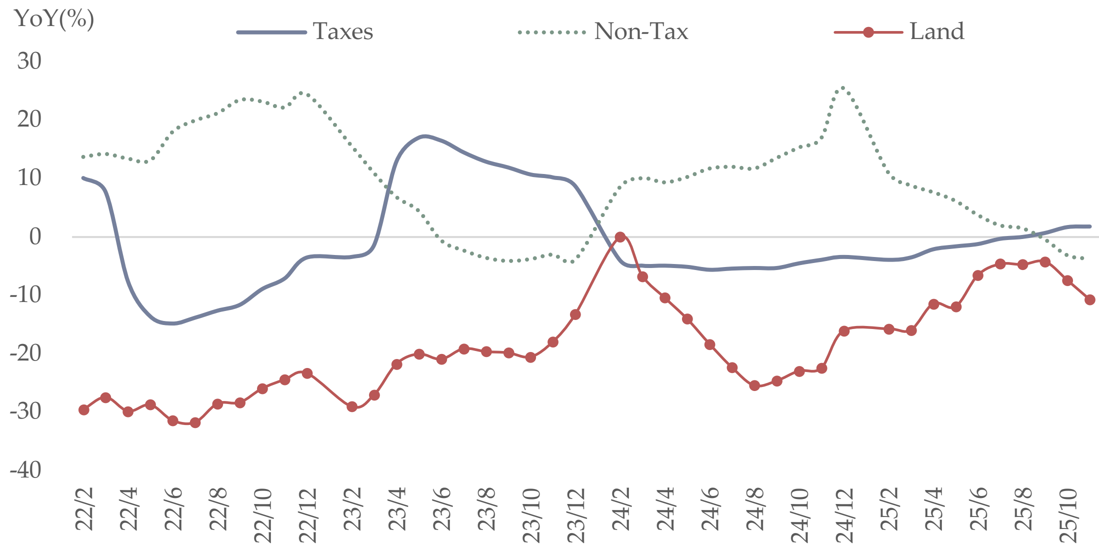

Figure 3-2 Structure of Fiscal Revenues **(Jan 2022–Nov 2025)**

II. Manageable Debt Ratios but Concerning Debt Burdens

Fiscal revenues have been insufficient to cover government expenditures. In addition, large volumes of non-performing assets generated by property developers and local government financing vehicles (LGFVs) as a result of the real estate bubble must be rolled over or addressed, while continued military expansion and the pursuit of technological self-reliance require substantial financial injections. Consequently, the volume of bonds issued by China's central and local governments in 2025 reached a historical high, with newly issued debt from January to October estimated at approximately RMB 16–17 trillion. This total includes RMB 1.3 trillion in ultra-long-term special government bonds issued by the central government to support high-technology development, infrastructure, and social expenditures; RMB 4.4 trillion in local government special-purpose bonds issued for debt swaps and local infrastructure projects; and regularly issued general government bonds, local government bonds, and urban investment bonds (chengtou bonds). In both absolute terms and as a share of total issuance, these amounts reached record levels, as shown in Figure 3, bringing cumulative outstanding government debt to RMB 102 trillion by October 2025, approaching cumulative GDP over the same period.

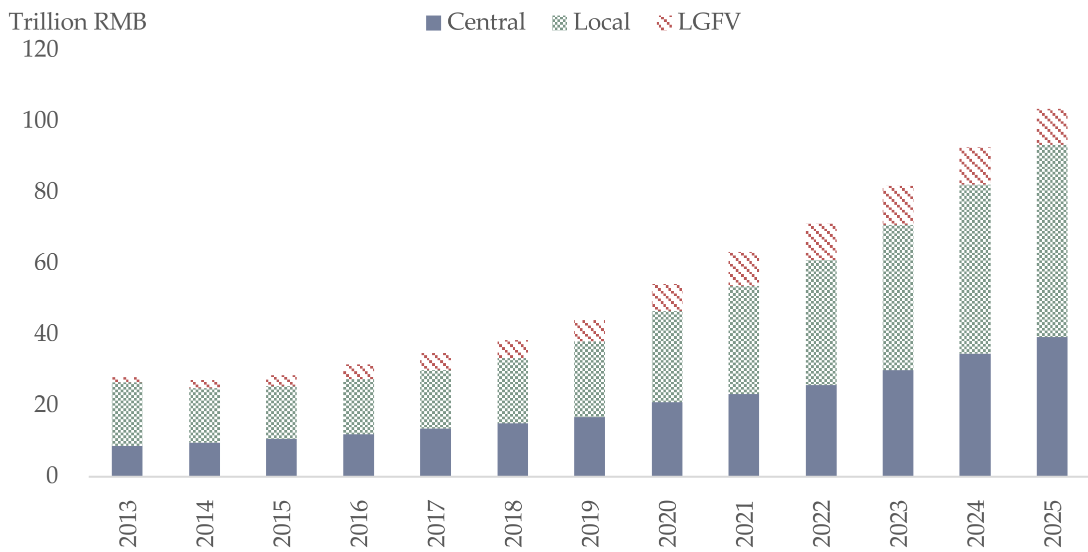

Figure 3-3 China's Government Debt Balance (Jan 2013–Oct 2025)

According to data provided by the Chinese government to the International Monetary Fund, as of 2024 the on-balance-sheet debt of China's central and local governments amounted to approximately 88 percent of GDP. This ratio is lower than that of most advanced economies with aging populations and substantial welfare obligations. Among the G7 countries, all except Germany exceed 100 percent, and Japan's ratio exceeds 200 percent. However, when compared with emerging market economies at similar income levels, China's government debt is in the upper-middle range. If hidden liabilities with implicit government guarantees—estimated at RMB 70–90 trillion and including LGFV debt, public–private partnership bonds, and other state-owned enterprise debt swaps—are taken into account, many international financial institutions estimate that China's effective government debt burden would reach around 120 percent of GDP, comparable to that of the United States.

While China's accumulated government debt appears less severe than that of most advanced economies when measured as a share of GDP, the assessment changes when debt-servicing capacity is considered—that is, the ratio of government debt to government revenue. On this measure, China's government debt-to-revenue ratio is estimated at between 350 and 450 percent, which is extremely high by international standards and ranks roughly second only to Japan. This is likely to impose increasing constraints on the government's future governance capacity[6].

III. Expenditure Compression Focused on Livelihood Spending

To slow the growth of fiscal deficits, in recent years the central government has allowed expenditures to decline in line with falling revenues, as shown in Figure 1. However, closer examination of the composition of central government spending reveals that reductions have

[6] In comparing China's government debt with that of other countries, long-standing discrepancies exist between the government debt and GDP figures that the Chinese government provides to international organizations in U.S. dollar terms and the figures published on Chinese-language websites in renminbi terms. As a result, precise estimation is not possible, and only a range can be estimated.

been concentrated in areas directly related to livelihoods, including education and science and technology, social security and healthcare, and infrastructure investment. As a result, the share of national security expenditures—including diplomacy, national defense, public security, and material reserves—rose from 47.9 percent in 2016 to 51.4 percent in 2025 (see Table 3-1).

Table 3-1 Composition of Central Government Budget Expenditures

Unit: Percentage (%)

Year	Education & Technology	Social Security & Healthcare	Infrastructure Investment	National Security
2016	15.0	3.7	18.3	47.9
2017	14.7	3.8	17.2	47.6
2018	14.9	4.3	16.6	46.3
2019	15.2	3.9	16.3	43.8
2020	14.0	4.3	17.1	46.4
2021	14.0	3.4	17.4	48.9
2022	13.3	2.8	18.0	50.9
2023	12.8	3.2	17.9	51.5
2024	12.9	3.6	16.9	50.4
2025	13.1	3.2	16.9	51.1

Note: National security expenditures include diplomacy, national defense, public security, and material reserves.

To mitigate the continued decline in revenues, the central government has also repeatedly amended regulations to expand the scope of taxation. For example, on June 20, 2025, the State Taxation Administration issued the "Notice on Several Matters Concerning the Handling of Withholding and Filing Declarations by Internet Platform Enterprises for Platform-Based Workers." Beginning October 1, online platforms are required to withhold taxes on behalf of the authorities directly from food delivery couriers, ride-hailing drivers, livestream e-commerce sellers, and online retail merchants. Even U.S.-based e-commerce platform Amazon has been required to provide data on Chinese sellers. Following implementation, these measures have increased the burden on economically vulnerable groups who already rely on the internet gig economy amid weak domestic demand and limited employment opportunities. Additional measures—including taxing interest income from government bonds, income from overseas investments, and income from gold transactions—likewise reflect efforts to identify new revenue sources. As a result, personal income tax revenue recorded year-on-year growth of 11.5 percent in January–November 2025, while corporate income tax revenue grew by only 1.7 percent.

Table 3-2 Regulations Increasing Fiscal Revenues in 2025

Date of Issuance	Policy
2025/6/20	Regulations on Tax-Related Information Reporting by Internet Platform Enterprises
2025/7/16	Housing Rental Ordinance
2025/7/17	Announcement on Adjusting the Consumption Tax Policy for Ultra-Luxury Passenger Vehicles

2025/7/31	Announcement on Value-Added Tax Policies for Interest Income from Government Bonds and Other Bonds
2025/7/31	Announcement on Matters Concerning Tax Credit Policies for Overseas Investors Reinvesting Distributed Profits
2025/8/11	Announcement on Clarifying Value-Added Tax Policies for Courier Services and Related Activities
2025/10/29	Announcement of the State Taxation Administration on Tax Administration Matters Related to Gold

At the same time, with local governments unable to achieve a near-term recovery in land conveyance revenues, they have sought alternative means to expand non-tax revenues. One of the most widely discussed terms on the Chinese internet in 2024 was “distant-water fishing,” a metaphor describing practices in which local public security authorities cross provincial boundaries to detain private entrepreneurs and impose large fines. The official term for this behavior is “irregular cross-regional profit-driven law enforcement,” and revenues generated through such practices have entered local general public budgets as confiscation and penalty income.

According to Ministry of Finance data, local non-tax revenues exceeded RMB 4 trillion in 2024, accounting for 34 percent of local public budget revenues, compared with less than RMB 1 trillion in 2010. Within this category, confiscation and penalty income peaked at RMB 428.4 billion in 2022, after which official figures were no longer disclosed. It is generally estimated that such income has remained at approximately 10–12 percent of total non-tax revenues, or RMB 400–500 billion. Following widespread public backlash in 2024, these practices became less overt in 2025, although related forms of profit-driven law enforcement have remained prevalent.

IV. Summary: Rising Debt-to-Revenue Ratios and Eroding Governance Capacity

Although in 2025 the government moved more aggressively to expand public debt issuance at both the central and local levels to meet geopolitical competition pressures and alleviate local fiscal payment stress, failure to achieve a near-term rebound in economic growth would result in local government expenditures exceeding revenues within the next three to five years. This would entrench a long-term reliance on borrowing to sustain fiscal spending.

Over the longer term, if the central government does not fundamentally reverse its current fiscal expenditure structure—which prioritizes national security over social development—and does not alter its production-focused economic strategy, the economy will struggle to return to its previous trajectory of high-speed growth. Persistent fiscal deficits may further weaken governance capacity, undermine social stability, and eventually give rise to sovereign credit risks as debt-servicing capacity deteriorates.

IV. Society

Chan-His Wang

Since the 1990s, China's sustained period of rapid economic growth led the public to tolerate authoritarian political rule. At the same time, economic expansion functioned as both a fig leaf and an anesthetic for a wide range of social problems, masking structural issues related to social development and inequality. However, the economic downturn that began after 2023 has triggered a series of changes in the social sphere. In everyday economic life, persistently high youth unemployment and income stagnation among low- and middle-income groups have intensified trends toward income polarization. In terms of confidence in the future, public pessimism regarding economic prospects has remained entrenched and has extended into personal life choices, including declining willingness to marry and have children and reluctance to participate in social insurance schemes. With respect to social stability, this pessimistic sentiment has contributed to the spread of social discontent. Even as the authorities continue to strengthen "stability maintenance" efforts, the number of social protests has risen markedly, and the targets of such protests have increasingly shifted toward abuses of power by political and business elites as well as systemic inequality.

I. Worsening Unemployment and Widening Income Gaps

Against the backdrop of economic weakness, China's youth unemployment rate (ages 16–24) has continued to rise since 2019. In mid-2023, the Chinese government suspended the publication of youth unemployment data and resumed regular releases at the end of the year after revising the statistical methodology, an effort widely seen as downplaying the severity of employment difficulties faced by university graduates. Even under the revised methodology, however, youth unemployment has continued to exhibit intermittent upward trends, particularly during the annual graduation job-seeking season from June to August, reaching a new high of 18.9 percent in August 2025. By contrast, the overall unemployment rate for the urban labor force has remained relatively stable at 5.2–5.3 percent.

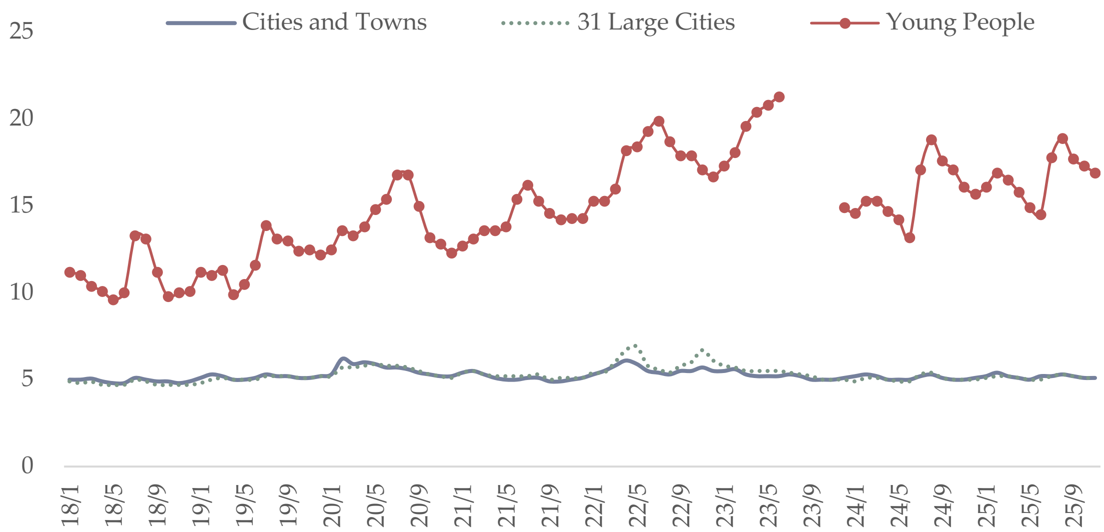

Figure 4-1 Unemployment Rate of China's Labor Force (Jan 2018–Dec 2025)

Supplementary Data: According to a survey by the Ant Research Institute, in the first quarter of 2025 the unemployment rate among the working-age population (ages 16–59), including both job seekers and those without the intention to work, reached 28 percent. Among this group, 19.7 percent were engaged in "flexible employment" with unstable working conditions, while only 52.4 percent met the traditional definition of employment.

The economic downturn has primarily affected low- and middle-income groups, further deepening income inequality. Among the five income quintiles, the gap between the average incomes of the highest- and lowest-income groups expanded from RMB 430.54 million in 2013 and RMB 724.25 million in 2020 to RMB 892.66 million in 2024. At the same time, income growth among low- and lower-middle-income groups has remained extremely limited, bordering on stagnation, contributing to a growing sense of relative deprivation among the general public.

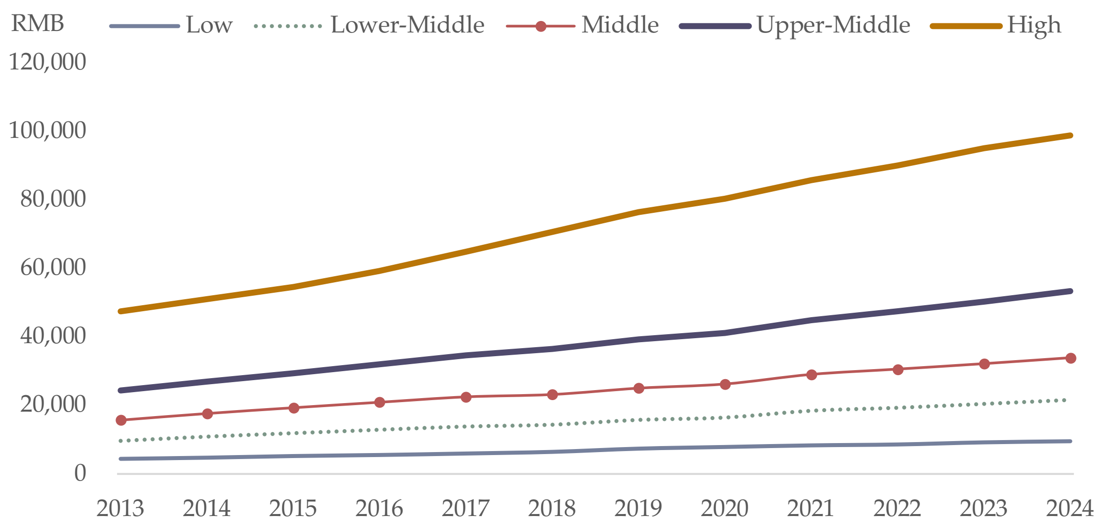

Figure 4-2 Changes in the Five Income Quintiles (2013–2024)

Supplementary Data:

1. Individual income tax data show that in 2023, approximately 600 million people in China's labor force earned monthly incomes below RMB 3,500, accounting for 81 percent of the 740 million-strong workforce. An additional 100 million earned between RMB 3,500 and RMB 5,000, and 45 million earned between RMB 5,000 and RMB 10,000. Those with annual incomes exceeding RMB 100,000 numbered only 20 million, or roughly 2.7 percent of the labor force. Meanwhile, 90 percent of individual income tax revenue was contributed by the top 10 percent of income earners.
2. In 2025, the annual growth rate of average wages in the private sector was below 2 percent in more than 14 provinces and municipalities, with six registering growth below 1 percent.

II. Erosion of Public Confidence in Economic Prospects

Public sentiment indicators related to income and confidence fell to post-pandemic lows in 2025. Only 46.5 percent of respondents reported satisfaction with their current income levels, and just 45.9 percent expressed expectations of future income growth. Meanwhile, satisfaction with current employment conditions has continued to decline since September 2023, reaching a record low of 25.8 percent in September 2025. Confidence that employment conditions would improve in the future also fell to a new low of 42.1 percent.

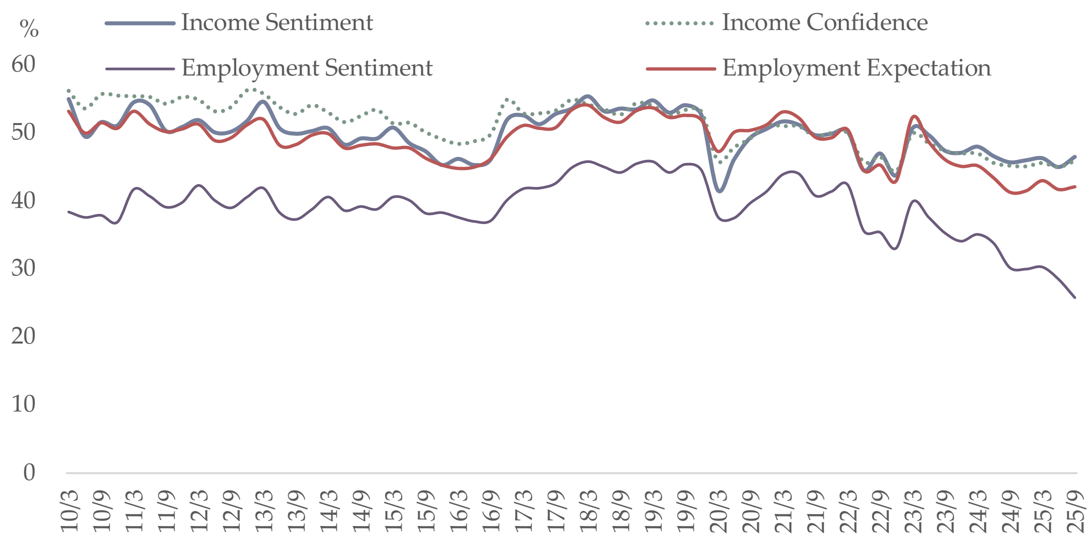

Figure 4-3 Income Confidence and Employment Expectations (Mar 2010–Sep 2025)

With limited income growth for the majority of households and a prolonged downturn in the real estate market, consumer willingness has weakened, accompanied by a growing tendency toward early debt repayment to reduce financial burdens. Personal mortgage balances began to decline in 2023. Although they rebounded modestly between late 2024 and early 2025 due to housing market stimulus measures, they subsequently fell again to their lowest level in nearly four years. At the same time, despite repeated policy efforts to stimulate consumption—including channeling credit toward consumer sectors and accelerating consumer loan programs—the growth of consumer loans has remained well below pre-2022 levels and shifted from stagnation to contraction in 2025.

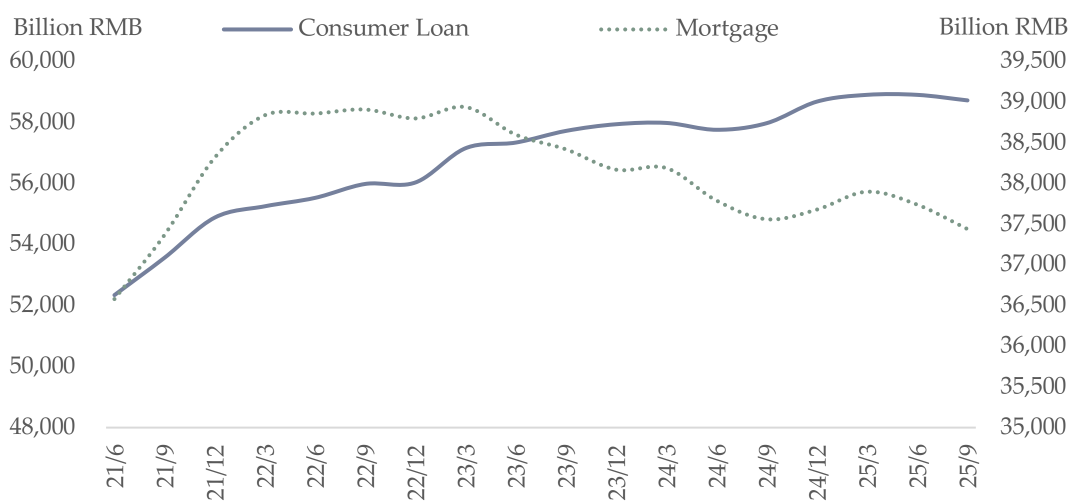

Figure 4-4 Consumer Loans and Personal Mortgages **(Jun 2021–Sep 2025)**

III. Demographic Structure and Social Security Pressures

The sense of powerlessness felt by Chinese youth regarding their livelihoods and future prospects is also reflected in life choices such as a declining willingness to marry and have children, accelerating China's downward birthrate trend. Since 2017, the birth rate, number of newborns, and number of marriages have all exhibited a sustained decline. Although the number of births rebounded slightly to 9.54 million in 2024—attributable to the Year of the Dragon and post-pandemic "compensatory fertility"—the number of marriages fell to a new low of 6.11 million. This caused the number of births in 2025 to drop to a new low of 7.92 million, with the fertility rate falling below 1 for the first time (see Figure 4-5). In 2024, the Chinese government began introducing various subsidy policies to encourage marriage and childbirth, expanding them in 2025, yet these measures failed to effectively improve youth willingness to marry and have children. This trend not only exacerbates pressures on the demographic structure but also reflects a collective atmosphere of lacking confidence in development prospects.

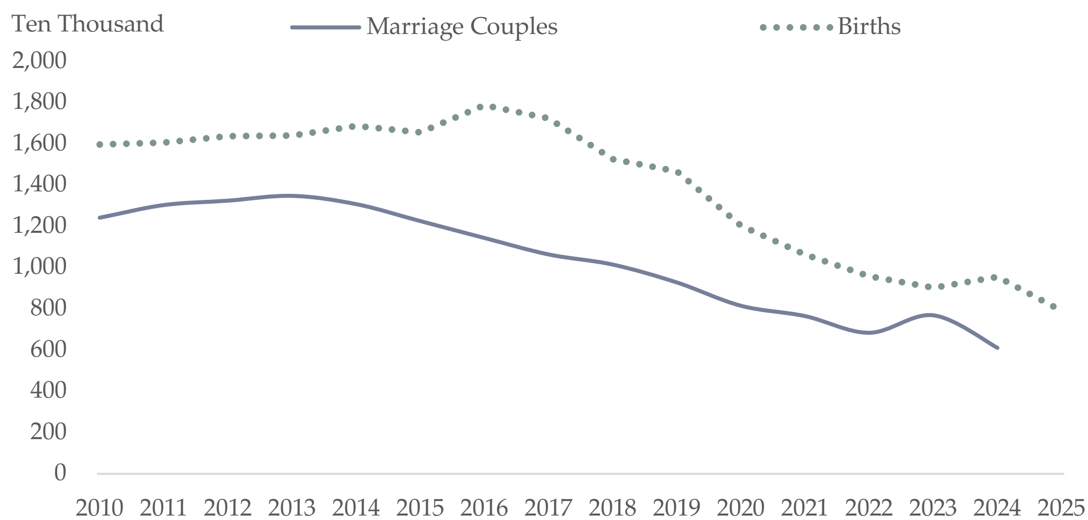

Figure 4-5 Number of Marriages and Number of Newborns (2020–2025)

From a medium- to long-term perspective, low fertility constitutes an irreversible structural constraint on China's development. The decline in births that began in 2018 has already had a pronounced impact on the maternal and child industry and the education sector. Obstetrics and gynecology services, early childhood education, and infant product businesses have all contracted sharply. In 2024 alone, 21,100 kindergartens closed, accounting for 7.7 percent of the total at the beginning of the year; primary schools decreased by 7,500; and the number of preschool and primary school teachers fell by 300,000. Over the next decade, the effects of low fertility will continue to propagate through the education system and are expected to reach higher education and the labor market around 2035.

Population aging represents another major demographic challenge. In 2025, the population aged 60 and above reached 22 percent (310 million people), while those aged 65 and above accounted for 15.6 percent (220 million). Over the next decade, the elderly population is expected to grow by more than 10 million annually, steadily increasing the social dependency burden. By 2035, the elderly dependency ratio is projected to rise from 22.5 percent in 2023 to over 30 percent, meaning that every 100 working-age individuals will need to support more than 30 retirees. At the same time, insufficient public provision of eldercare services and subsidies means that most caregiving responsibilities continue to fall on families, further constraining labor supply.

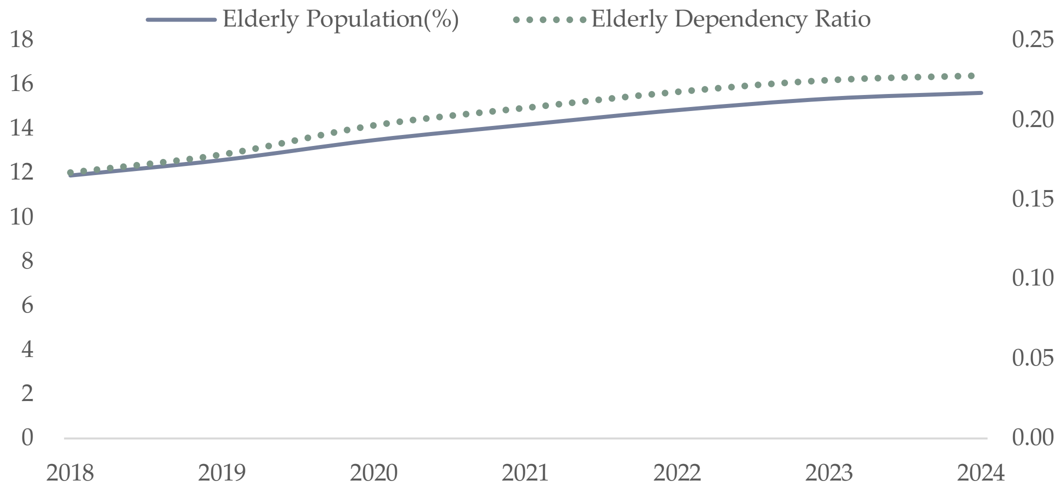

Figure 4-6 Elderly Population Proportion and Elderly Dependency Ratio (2018–2024)

Population aging poses a direct challenge to the sustainability of the pension system and erodes public confidence in social welfare. Although the government has announced measures such as gradually delaying the retirement age, accelerating national pooling, and promoting supplementary systems including occupational annuities and commercial insurance, the latest estimates in 2025 still suggest that pension fund reserves could be exhausted by 2044.

In addition, the social security system—centered on pension and medical insurance—has become a heavy burden for the working population. China's pay-as-you-go model means that rising numbers of retirees and higher pension payouts place increasing pressure on current contributors. Enterprises and individuals together are required to contribute around 40 percent of wages, a rate higher than in most advanced welfare states. For individual workers, contribution rates range from 10 to 22.5 percent, combined with high minimum contribution bases. For low- and middle-income earners with monthly incomes below RMB 5,000, social security contributions may even exceed take-home pay.

High contribution burdens, structural flaws in the pension system, and low confidence in long-term sustainability have reduced participation incentives among low- and middle-income workers and those in flexible employment. At the same time, roughly 70 percent of enterprises underpay or avoid contributions altogether to reduce labor costs. Declining participation further weakens the financial foundation of the social security system. By September 2025, although the pension fund still recorded a surplus, the gap between revenues and expenditures had narrowed to its lowest level since 2023.

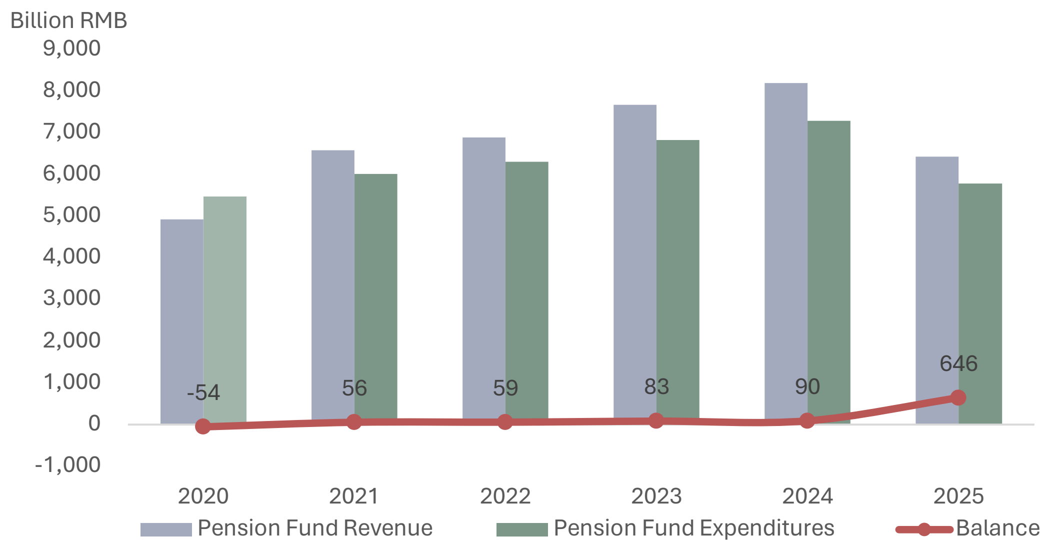

Figure 4-7 Pension Insurance Fund Income, Expenditure, and Balance (2020–Sep 2025)

Under mounting financial pressure, the increase in pension payments in 2025 fell to a historical low of 2 percent. In August, the Supreme People's Court ruled in favor of compulsory collection of social security contributions in an effort to alleviate fiscal stress caused by refusals and withdrawals. However, amid economic slowdown, compulsory enforcement triggered widespread backlash among small and micro-enterprises and low- and middle-income households, prompting local governments to introduce mitigation measures. Whereas contribution base adjustments ranged from 4 to 23 percent in 2024, they were reduced to 0.9–8 percent in 2025, and more than 15 provinces introduced policies in early October to subsidize 25 percent of individual contributions. These developments reflect the structural dilemma facing the social security system: expenditures continue to rise, while revenue expansion remains constrained.

IV. Accumulating Discontent and Diverse Forms of Social Conflict

Declining living standards and persistent social injustices have continued to fuel public dissatisfaction. Even under intensified social control, protest incidents have continued to increase. From January to November 2025, the number of protests nationwide already exceeded the annual totals recorded between 2022 and 2024 (see Figure 4-8). At the same time, public resistance has increasingly taken alternative forms under heightened surveillance and repression.

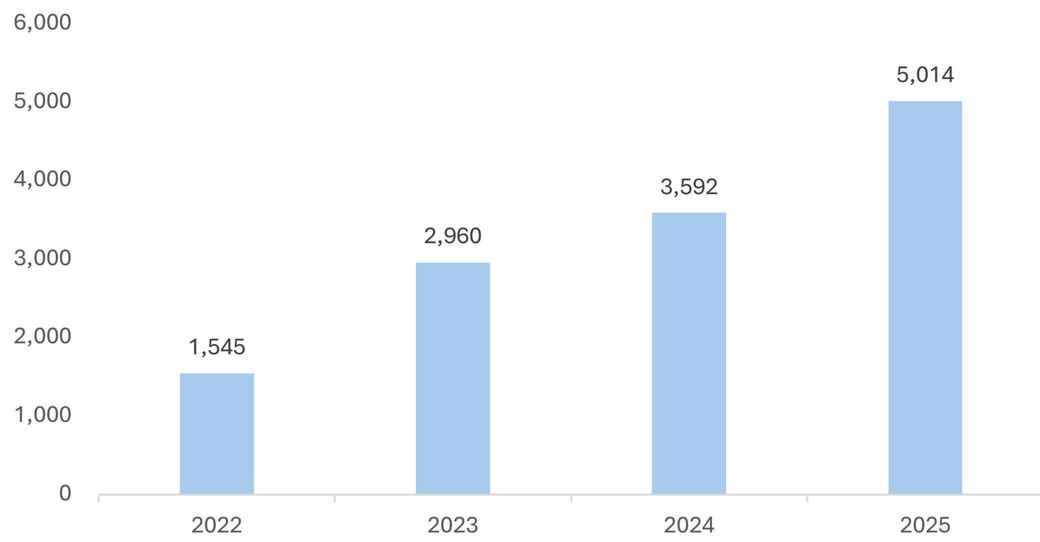

Figure 4-8 Protest Incident Statistics (2022– 2025)

(i) Sudden Collective Protests

In July 2025, a school bullying incident in Jiangyou, Sichuan, sparked demonstrations involving tens of thousands of people demanding transparency and severe punishment of those responsible, leading to violent clashes between police and civilians. The Jiangyou case was not isolated. In January 2025, the death of a vocational school student in Pucheng, Shaanxi—suspected to have fallen from a building after being bullied—also triggered protests involving around 10,000 participants. Similar large-scale incidents occurred in Lianyungang, Jiangsu in 2024 and Ningling, Henan in 2023. In addition, numerous protests involving thousands of participants have been triggered by the improper treatment of street vendors or delivery workers by urban management authorities. Over the 15 years prior to the pandemic, only five sudden collective protests exceeded 10,000 participants; since 2023, such incidents have occurred annually, including two in 2025 (see Figure 4-9).

Figure 4-9 Sudden Collective Protest Incidents of Over 10,000 People **(2004–2025)**

These protests differ from conventional economically motivated demonstrations and typically occur in third- and fourth-tier county-level cities. Participants are usually driven by outrage over perceived cover-ups by local authorities or unexplained deaths, demanding fair investigations and accountability. Beyond immediate grievances, these incidents reflect deeper public frustration with unchecked power, elite impunity, and pessimism about long-term social development.

(ii) Lone-Wolf Political Protests

While the CCP has long suppressed organized political opposition, it has been less able to prevent individual acts of protest driven by anti-communist sentiment, often referred to as “lone-wolf” political protests. These actions typically involve clear and direct political slogans that attract attention and occasional imitation following media exposure, with the 2022 Sitong Bridge incident serving as a prominent example. Despite extensive censorship efforts, such incidents continued in 2025. In April, a young man named Mei Shilin hung anti-communist banners on an overpass in Chengdu; in August, Qi Hong projected large-scale anti-communist messages in Chongqing University Town. The proliferation of anti-communist graffiti in residential areas, public toilets, and on utility poles points to a diffuse but persistent undercurrent of opposition sentiment.

(iii) Violent Incidents as Emotional Venting

Beginning in the second half of 2024, China experienced a surge in previously rare incidents of indiscriminate attacks. In 2025, despite heightened monitoring and information controls, more than 10 such incidents still entered the public domain. These attacks reflect individual frustration with shrinking opportunities and perceived injustice, though they do not articulate explicit political demands. A related phenomenon has been the rise in targeted killings of officials, which also increased significantly in 2024 and persisted into 2025. Both indiscriminate violence and retaliatory attacks underscore how accumulated grievances at the grassroots level, lacking institutional channels for expression, are seeking alternative outlets.

(iv) Online Public Opinion and Perceptions of Inequality

In the broader online sphere, cases involving systemic injustice, government–business collusion, and elite abuse of power frequently attract intense scrutiny and criticism. One of the most prominent cases was the sudden death of actor Yu Menglong in early September 2025. Police announced within 12 hours that Yu's death resulted from an accidental fall after drinking and ruled out criminal involvement. Subsequent recordings and videos circulating online, however, fueled speculation regarding industry exploitation and elite involvement. Despite strict censorship, related discussions accumulated more than 10 billion views, triggering "charging the tower" behavior, such as posting comments on state media platforms or demanding official explanations. Many participants emphasized that their concern was not fandom but dissatisfaction with elite impunity and perceived judicial injustice. Even after a "Clean Internet" campaign was launched in late September, public attention and criticism persisted.

The Yu Menglong case was not isolated. Similar waves of criticism emerged following the suspected involvement of a Beijing court assistant in the theft of hundreds of millions of yuan in enforcement funds and the controversial handling of the death of intern doctor Luo Shuaiyu. Public anger has also been directed at perceived advantages enjoyed by the children of elites through privileged access to education and career opportunities, reinforcing perceptions of unequal mobility and intergenerational power reproduction.

V. Summary: The Gradual Breakdown of the Reform-Era Social Contract

In 2025, continued economic weakness further eroded income growth and employment opportunities for ordinary citizens. Public dissatisfaction has increasingly extended beyond economic pessimism to encompass systemic injustices, including welfare bias toward those within the CCP system and the concentration of resources and unchecked authority among elites. The implicit social contract established during the reform era—exchanging economic growth and rising living standards for political acquiescence—is gradually unraveling, with the public expressing dissatisfaction and disengagement through diverse channels. Rigid social mobility and uneven distribution of economic gains are intensifying structural tensions between ordinary citizens and political and business elites. In this context, The Economist described China's emerging risks as a "new class struggle" in 2024, while Nikkei argued in 2025 that China has entered a "new class war" as conceptualized by American political scientist Michael Lind.

In response, the CCP's "15th Five-Year Plan" continues to emphasize goals such as promoting full employment, improving income distribution, strengthening social security, and advancing population development, while introducing the concept of "unblocking channels for social mobility." These formulations indicate official awareness of rising social risks. At the same time, the leadership reiterates the principle of "doing one's best while acting within one's means," suggesting that livelihood issues have not been elevated in political priority.

Although fragmented social discontent remains unable to coalesce into a direct challenge to CCP rule under extensive repression, the underlying atmosphere of instability is likely to persist. Rapid demographic shifts and a fragile social security system further constrain long-term development prospects. Without new engines of growth and comprehensive reform of public resource allocation, the authorities may struggle to contain the diffusion and transformation of social risks and to sustain public support for the regime.

V. Politics

Chan-His Wang

The operation of power at the top levels of the Chinese Communist Party (CCP) has long been characterized by a high degree of opacity. Among the limited sources of publicly available information that offer meaningful insight into political trends are the annual plenary sessions of the CCP Central Committee (with the Fourth Plenary Session of the 20th Central Committee held in 2025) and the scope and direction of anti-corruption campaigns. Trends observed in 2025 indicate that, for party and government officials, the primary source of pressure does not stem from external or internal structural challenges, but rather from the political purge initiated by top leader Xi Jinping.

I. Fourth Plenary Session of the 20th CCP Central Committee: A New Peak in Political Purges

The most striking feature of the Fourth Plenary Session in 2025 was the large number of absences among Central Committee members and the downfall of multiple senior People's Liberation Army (PLA) generals, indicating instability within the CCP's top leadership.

The Central Committee, composed of full and alternate members, referred to as the "CCP Central Committee" or the "Party Center." Its annual plenary sessions serve as the most critical political venues within the Party. Members rarely miss these meetings unless assigned tasks of exceptional importance. In 2025, of the 205 members of the Central Committee, 37 were absent (including the late Yu Jianhua), representing an absence rate of 18%. Among the 171 alternate members, 24 were absent, or 14%. The combined absence rate of 16.2% marks the highest level since the beginning of the reform and opening-up era (see Figure 5-1).

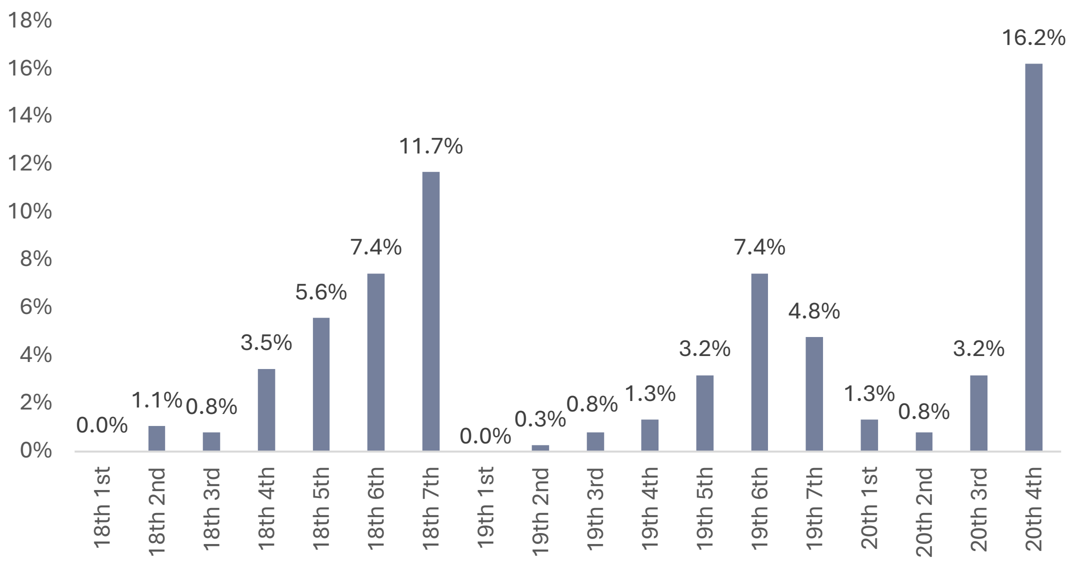

Figure 5-1 Absence Rates of Central Committee Members and Alternate Members during Plenary Sessions (the 18th to 20th Party Congresses)

The number of officials removed from office during the Fourth Plenary Session not only significantly exceeded the figures from last year but also reached a new record under Xi Jinping's tenure (see Table 1). In 2025, of the 57 absent officials (another four had already fallen during the Third Plenum), 23 party, government, and military leaders have been confirmed as having "fallen"（落馬） due to investigations, including 14 who were formally expelled from the Party, 6 whose cases are still pending final procedures and 3 removed Central Committee members are currently missing. Furthermore, 7 high-ranking alternate members might have failed to elevate to full membership due to ongoing investigations; for instance, Fang Hongwei was officially placed under investigation shortly after the Fourth Plenum.

Table 5-1 Personnel Removed or Investigated at the Third and Fourth Plenary Sessions of the CCP 20th Central Committee

Category	Third Plenum	Fourth Plenum
Central Committee members expelled from the Party	Li Shangfu; Li Yuchao	Tang Renjian; Jin Xiangjun; Miao Hua; Wang Chunning; He Weidong; He Hongjun; Wang Xiubin; Lin Xiangyang; Qin Shutong; Yuan Huazhi
Central Committee members placed under investigation	-	Lan Tianli; Wang Lixia; Yi Huiman; Zhang Lin

Central Committee members resigned / removed / disappeared	Qin Gang	Liu Jianchao; Jin Zhuanglong; Lei Fanpei
Alternate Central Committee members expelled from the Party	Sun Jinming	Yang Fasen; Zhu Zhishong; Zhang Fengzhong; Li Shisong
Alternate Central Committee members placed under investigation	Li Shisong	Fei Dongbin; Wu Shenghua
Alternate Central Committee members resigned / disappeared	-	-
Alternate members eligible for elevation but not elevated	Ding Xingnong	Wang Liyan; Wang Kangping; Wang Jiayi; Fang Yongxiang; Fang Hongwei; Shi Yugang; Shi Zhenglu

Source: Compiled by the author.

During the period of the 18th Party Congress, when Xi Jinping had only recently consolidated power, the leadership was already actively dismantling potential anti-Xi factions led by figures such as Ling Jihua, Xu Caihou, and Guo Boxiong. Even so, over the five-year term, a total of just 35 incumbent Central Committee members and alternate members were removed, including eight PLA generals. The single meeting that recorded the highest number of removals was the Seventh Plenum of the 18th Central Committee in 2017, when 15 officials fell, including two full PLA generals. During the subsequent five-year term of the 19th Central Committee, the total number of Central Committee and alternate members removed declined further, to only six. Moreover, across these two Party Congresses and their combined ten-year span, no incumbent Politburo member was removed.

In contrast, at the Fourth Plenum of the 20th Party Congress alone, the number of Central Committee members and alternate members removed reached 23, including one Politburo member and ten PLA generals (See Figure 5-2).

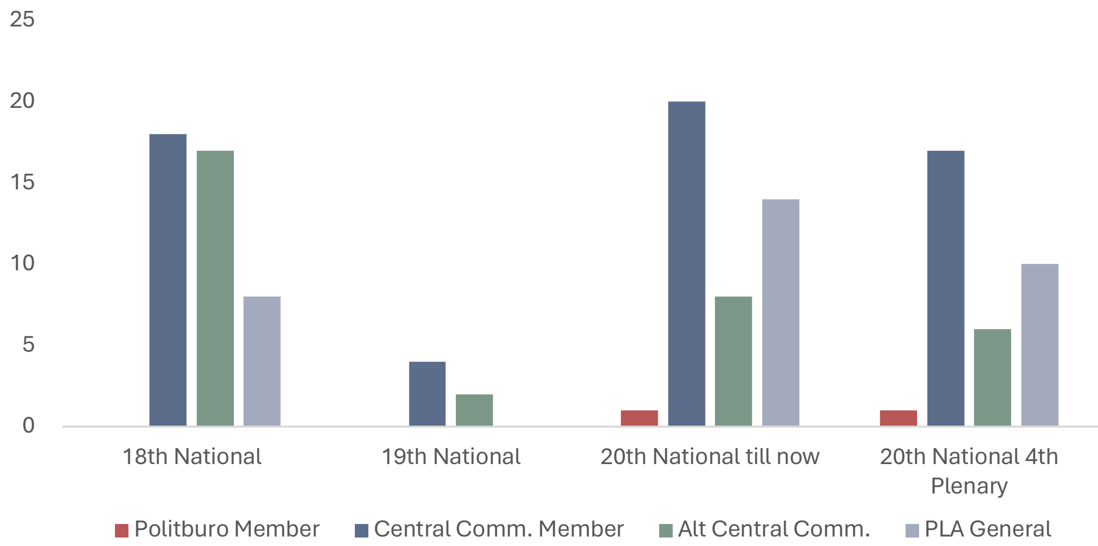

Figure 5-2 Number of Central Committee and Alternate Members Dismissed during Their Term (18th to 20th Party Congresses)

The People's Liberation Army (PLA) emerged as the most heavily affected sector in this round of purges. Of the 32 active-duty full generals （上將）, only 11 attended the Fourth Plenary Session. 9 had been expelled prior to the session, including Central Military Commission (CMC) Vice Chairman He Weidong and CMC member Miao Hua. He Weidong also marked the first sitting Politburo member to fall since the 18th Party Congress. Additionally, 14 generals and 5 lieutenant generals were absent from the session. Of the 42 military representatives, 27 failed to attend, bringing the overall attendance rate to a mere 36%. These absent generals were likely already under investigation. Among the 21 full-general-level commanders and political commissars of the Joint Operations Command Center, the five Theater Commands, four military branches, and the People's Armed Police, 14 were absent, suggesting severe disruption within the PLA's operational command system. More importantly, the Fourth Plenum did not mark the end of this purge; the political rectification within the PLA is expected to persist into 2026.

In the party and government apparatus, the intensity of political purges has in fact been no less severe than within the PLA. At this plenum, as many as 30 party and government officials were absent, of whom 14 have been confirmed to have fallen from office. This figure exceeds the 13 officials removed at the Seventh Plenum of the 18th Central Committee (in that year, an additional two PLA full generals were also removed), indicating that by 2025 the scale of political cleansing targeting senior party and government officials has likewise reached a new peak since Xi Jinping assumed power.

Among the 30 absent civilian officials were several prominent provincial leaders, including Wang Lixia of Inner Mongolia, Lan Tianli of Guangxi and Jin Xiangjun of Shanxi. In addition, Liu Jianchao, head of the CCP's International Liaison Department, has been absent from public view since July, while Politburo member Ma Xingrui has repeatedly missed major meetings, raising speculation that he may be under investigation. If Ma Xingrui is also confirmed to have been removed from office, this would set a new precedent since the 18th Party Congress, marking the first time that two incumbent Politburo members have been dismissed during the same period.

II. Anti-Corruption and Party Discipline Campaigns Targeting the Entire Party

In addition to central leadership, the scope of anti-corruption investigations among officials at all levels expanded more significantly in 2025 than in previous years. According to the Central Commission for Discipline Inspection (CCDI), the number of cases in 2025 reached 1.6 times that of 2023, with an average annual growth rate exceeding 20%, reflecting three clear trends: upward, downward, and outward expansion.

"Upward expansion" refers to the growing scale of disciplinary action directed at officials at the provincial–ministerial level and above. In 2025, 69 provincial–ministerial–level CCP officials were disciplined, the second-highest total in the past nine years, exceeded only in 2024. At the same time, the number of officials formally placed under investigation rose to 115, surpassing the 87 cases recorded in 2023 and the 73 cases in 2024, and marking a new high since the 20th Party Congress.

More broadly, the overall scale of disciplinary actions since the 20th Party Congress has been markedly higher than during Xi Jinping's previous term. During the five-year period of the 19th Party Congress (2018–2022), approximately 208 officials at the provincial–ministerial level and above were disciplined. By contrast, in just the three years since 2023, the total has already reached 191 (see Figure 5-3).

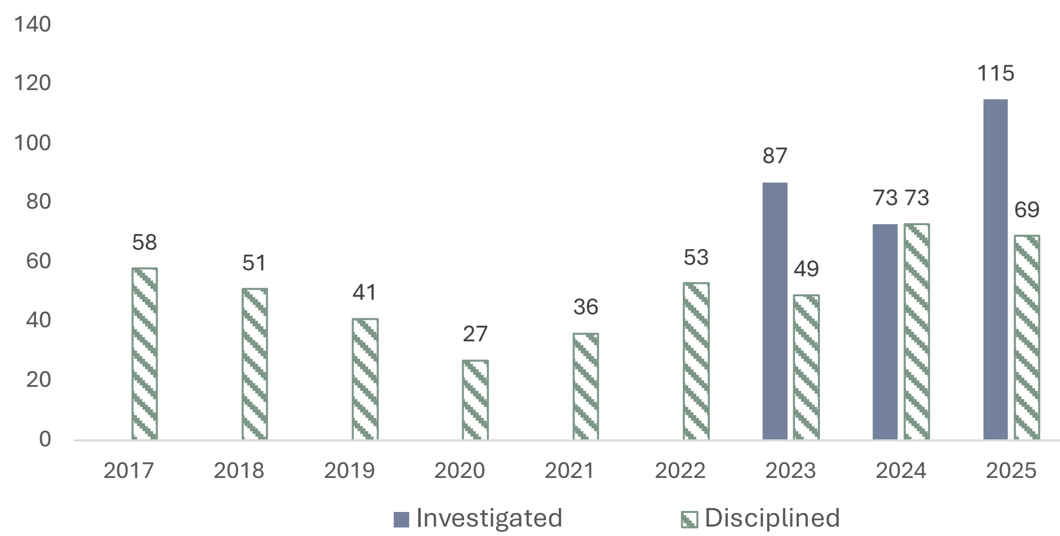

Figure 5-3 Number of officials at the provincial and ministerial level and above Investigated and Disciplined (2017–2025)

Broadly, anti-corruption campaigns are expanding toward the grassroots-level and non-Party sectors. The "downward" trend signifies that lower administrative levels face a faster pace of purges, particularly among "other personnel" in rural collective and state-owned enterprises who lack formal official posts. Over the past three years, this group has seen a rapid average annual growth of 23.9% (see Figure 5-4).

The trend of "outward expansion" is reflected in the widening scope of investigations from party and government officials to include grassroots personnel and a broader range of individuals within the institutional system. Under this framework, CCP members who are investigated are subject to both Party disciplinary sanctions and administrative penalties, while officials without CCP membership are subject only to administrative sanctions. In 2023, cases involving Party disciplinary sanctions accounted for 82% of the total; this share declined to 76% in 2024 and further to 74% in 2025. The year-on-year decline in the proportion of Party disciplinary cases suggests that, in recent years, anti-corruption enforcement has increasingly extended to non–CCP-affiliated personnel within the broader grassroots institutional workforce.

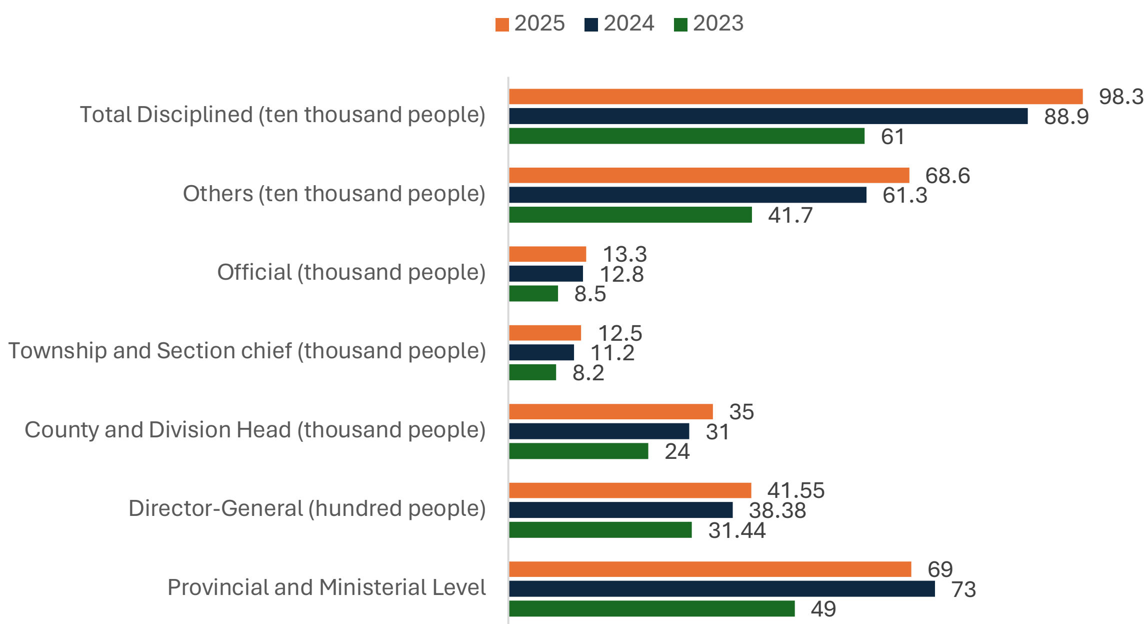

Figure 5-4 Personnel Disciplined by Disciplinary Inspection and Supervision Organs Nationwide (2023-2025)

III. Summary: Waves of Purges and the Formation of Collective Insecurity within the Ruling Elite

Based on the foregoing analysis, the scale and seniority of political purges and routine anti-corruption enforcement in 2025 reached their highest levels since Xi Jinping assumed power. This underscores the extent to which political loyalty has become a central organizing principle in the current operation of the Chinese Communist Party. Beyond signaling Xi's heightened concerns over intra-party loyalty, this dynamic has also contributed to a climate of collective political insecurity. Such conditions are likely to increase uncertainty among party officials regarding their future prospects, potentially weakening governance capacity within the political system.

Xi Jinping's enduring concerns over intra-party loyalty represent a fundamental driver of the large-scale anti-corruption purges. Against this backdrop, some observers have speculated that, as Xi grows older and greater attention is paid to his health, and as questions of political succession increasingly move onto the internal party agenda, he has become more vigilant, and more concerned, about the potential resurgence of opposing forces. As a result, following the 20th Party Congress, large-scale political purges have continued, aimed at ensuring absolute loyalty among officials at all levels to his governing authority and policy direction.

At the same time, the "15th Five-Year Plan" adopted at the Fourth Plenum largely reflects Xi Jinping's policy orientation, indicating that he continues to exercise decisive control over major political and economic decision-making. This suggests that his leadership position remains firmly consolidated.

A key characteristic of the current purge of senior party officials is that those targeted are drawn largely from within Xi Jinping's own political network. This includes a number of senior PLA officers from the former 31st Group Army in Fujian, many of whom were personally promoted by Xi after he assumed power, as well as senior party and government officials selected at the 20th Party Congress in 2022 through a process Xi himself described as being "personally arranged and strictly vetted at every level." This pattern suggests that Xi has raised the standards applied to political loyalty. At the same time, the expanding scale of routine anti-corruption enforcement, together with its accelerated extension to grassroots personnel and non–CCP-affiliated groups, also reflects an underlying impulse to consolidate authority and suppress potential challenges. This sense of insecurity at the apex of power, often described as the "loneliness at the top", has been a recurring feature in the political decision-making of leaders exercising highly concentrated authority across historical and political contexts. Stanford University Professor Wu Guoguang, drawing comparisons among the late-stage political purges of Stalin, Mao Zedong, and Xi Jinping, has argued that the highly centralized nature of communist systems reinforces authoritarian leaders' incentives to rely on political purges to consolidate personal authority, a pattern he characterizes as the "Stalinist logic."

For officials at all levels of the CCP, the intensification of political purges has generated a widespread sense of insecurity. In daily governance, the overriding priority has increasingly become the continuous demonstration of political loyalty, while considerations of rational and professional problem-solving are pushed into a secondary role. Under such conditions, few officials are willing to question or challenge policy directions set by higher authorities. Moreover, large-scale purges inevitably create vacancies in key party, government, and military positions, requiring officials with more limited experience to step in. This dynamic raises decisionmaking risks across sectors and administrative levels, weakens governance effectiveness, and makes cross-agency and cross-level policy coordination more difficult.

While more frequent political purges may reinforce political loyalty, they also impose costs in terms of professional capacity and the transmission of institutional experience. At a time when China faces increasingly severe domestic and external challenges, how the CCP leadership balances political loyalty with governance capability will constitute a significant test for the party's senior leadership.

Conclusion

The Central Economic Work Conference convened at the end of 2025 emphasized the need to "continuously expand domestic demand, optimize supply, improve incremental growth, revitalize existing stock, develop new quality productive forces according to local conditions, and deepen the construction of a unified national market." For economic work in 2026, the meeting identified eight key tasks, with the first being to "adhere to domestic demand as the main driver and build a strong domestic market." In terms of policy implementation, however, the emphasis remains on "expanding the supply of high-quality goods and services" and optimizing the "Two New" policies—large-scale equipment renewal and consumer goods trade-ins. This approach continues to frame the expansion of domestic demand primarily from the supply side and does not represent a departure from China's long-standing development bias toward production over consumption. Notably, "stabilizing the real estate market" was relegated to the eighth and final task, signaling diminished priority and disregarding the repeated recommendations of Chinese and international economists that resolving real estate debt is a necessary structural precondition for expanding domestic demand.

On December 15, 2025, official media prominently promoted the announcement that the CCP's flagship journal *Qiushi*would publish Xi Jinping's article, "Expanding Domestic Demand Is a Strategic Move." The article itself, however, consisted largely of compiled excerpts from Xi's speeches since 2015 addressing domestic demand. Rather than signaling a substantive policy shift, the publication reinforced market perceptions that the emphasis lay less on "expanding domestic demand" than on "strategy." As a result, it is widely expected that the Chinese government will continue—much as it has since the launch of the "Made in China 2025" policy—to concentrate resources on accelerating technological self-reliance and boosting productivity as a means of responding to external geopolitical competition while managing internal economic challenges.

Following the Fourth Plenum, the State Council's first consumption-promotion initiative was the *Implementation Plan on Enhancing the Alignment Between Supply and Demand of Consumer Goods and Further Promoting Consumption*, jointly issued by six ministries, including the Ministry of Industry and Information Technology, in late November 2025. The plan set a preliminary target for 2027 of creating three "trillion-yuan consumption sectors" and ten "hundred-billion-yuan consumption hotspots." In substance, however, the document largely outlines a broad range of measures aimed at aligning various industries with green energy and AI-related industrial upgrading. Once again, "consumption enhancement" is approached primarily from the production and supply side, rather than through addressing local real estate debt or expanding social welfare—measures that economists have consistently argued are necessary to raise household purchasing power from the demand side.

Taken together, these developments suggest that a near-term policy shift toward addressing China's structural economic imbalances, long anticipated by many observers, is unlikely to materialize. The Chinese Communist Party is expected to continue prioritizing support for high-technology industries, while a meaningful recovery in domestic demand remains improbable in the short term. As a result, excess domestic capacity is likely to be absorbed through increasingly intense "involuted" price-cutting competition and continued reliance on exports. Under these conditions, concerns that “China Shock 2.0” may further intensify deindustrialization pressures on manufacturing sectors in other countries are likely to deepen, exacerbating trade tensions between China and its trading partners.

At the same time, prolonged domestic economic weakness is likely to fuel rising social discontent, erode public confidence in future economic prospects, and further undermine the social contract that has underpinned reform and opening. Protests demanding greater public welfare are therefore expected to continue increasing, giving rise to what has been described as a “new class war.” Meanwhile, the CCP’s ruling elite appears to be undergoing increasingly centralized yet increasingly anxious, Stalin-style purges, weakening state governance capacity. In the absence of any dramatic reversal in the cycle of weak domestic demand, deflation, and deleveraging, China’s economic growth in 2026 is expected to remain dependent on exports. Whether this trajectory ultimately expands or constrains China’s room for maneuver in its external relations remains an open question that warrants continued observation.

Appendix: China Monitoring Indicators

1. Projected GDP growth rate
2. Estimated realized GDP growth rate
3. Retail sales of consumer goods
4. Commercial residential property sales (value)
5. Finished goods inventories and capacity utilization (above-scale industrial firms)
6. Urban fixed-asset investment
7. High-tech manufacturing investment
8. Foreign direct investment inflows and estimates of firm exits/relocations
9. Merchandise trade imports and exports
10. Trade remedy investigations against China
11. Export share and average unit values of high-tech products
12. Consumer Price Index (CPI)
13. Producer Price Index (PPI)
14. Consumer Confidence Index
15. Purchasing Managers' Index (PMI)
16. Value added of above-scale industrial enterprises
17. Services production index
18. Loan loss provision coverage ratio
19. Capital adequacy ratio
20. Money market interest rates
21. M2–M1 growth differential ("scissors gap")
22. Total non-performing loans
23. RMB deposits and loans
24. Number of financial institutions in China
25. Share Repurchase Volume Statistics and SSE Composite Index
26. Outstanding government debt held by commercial banks
27. Government bond holdings as a share of commercial banks' total assets
28. General government revenue and expenditure (nationwide)
29. Local government revenue and expenditure (general public budget)
30. Composition of fiscal revenue
31. Composition of fiscal expenditure
32. Outstanding government debt (central government, local government, and LGFV debt)
33. Estimates of contingent and off-balance-sheet government liabilities
34. Government debt outstanding, debt-to-GDP ratios, and debt-to-fiscal-revenue ratios of G20 countries
35. New debt instruments and gross issuance
36. Newly introduced fiscal policy–related laws and regulations
37. Unemployment rate: total labor force and youth unemployment
38. Income inequality: quintile income distribution
39. Economic sentiment: income and employment perceptions and confidence indices
40. Household debt: consumer loans and residential mortgages
41. Households: number of marriages and number of live births
42. Demographic structure: share of elderly population and old-age dependency ratio
43. Social security: pension fund revenues, expenditures, and balances

44. Social stability: incidence of collective action and protest events
45. Social stability: large-scale mass incidents (10,000+ participants)
46. Party elite politics: attendance and absence rates of full and alternate CCP Central Committee members at plenums
47. Party elite politics: number of CCP Central Committee full and alternate members dismissed or removed from office during their terms (18th–20th Party Congresses)
48. Military personnel: number of CCP Central Committee full and alternate members who are PLA generals dismissed or removed from office during their terms
49. High-level anti-corruption: officials at the provincial and ministerial level under investigation or discipline
50. Grassroots anti-corruption: officials disciplined by national discipline inspection and supervision authorities