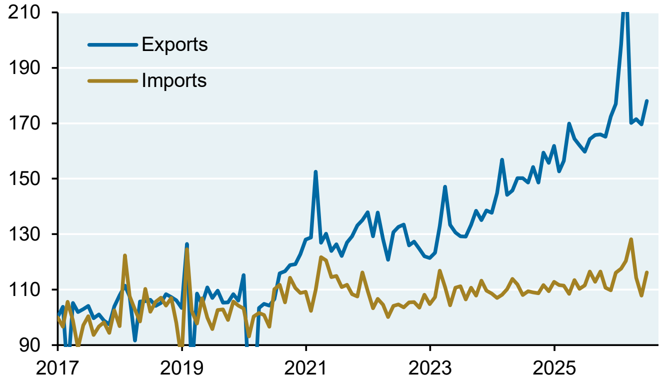
The Year of the Trojan Fire Horse: China's imbalanced economy and unrelenting mercantilism

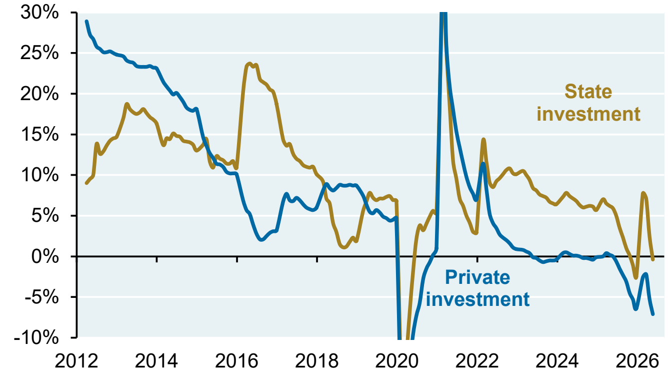
I read an article[1] in the FT recently regarding China's economy from Stephen Roach, currently of the Yale China Center and formerly Morgan Stanley's Chief Asia Economist. Roach argues that China's reliance on a production based, export-driven model is unsustainable, that weak Chinese domestic demand forces excess manufacturing supply onto global markets, thereby creating risks that resemble past financial crises. The main pillars of Roach's argument are clearly visible in China: soaring exports, weak private and state-driven investment, weak retail sales, a housing collapse and high levels of precautionary household savings due to an insufficient safety net.

China exports and imports
Index (100 = 2017)



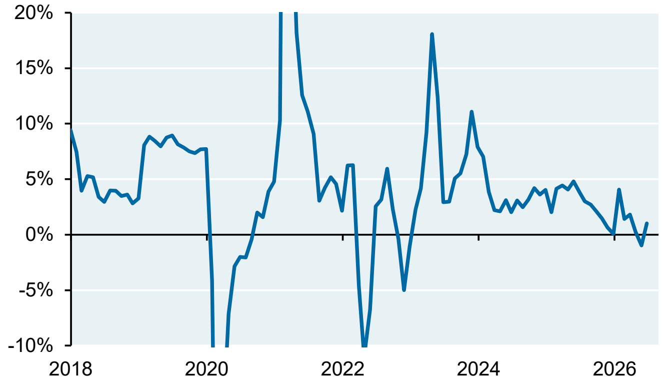
Source: Haver, General Administration of Customs, JPMAM, June 2026

China state vs private investment in fixed assets
y/y % change



Source: China National Bureau of Statistics, JPMAM, May 2026

China retail sales
y/y % change

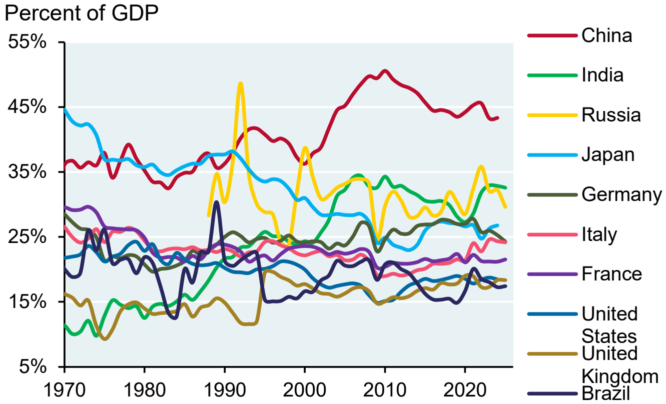


Source: Haver, China Customs, Bloomberg, JPMAM, July 2026

China real estate development investment
Index (100 = 2017)

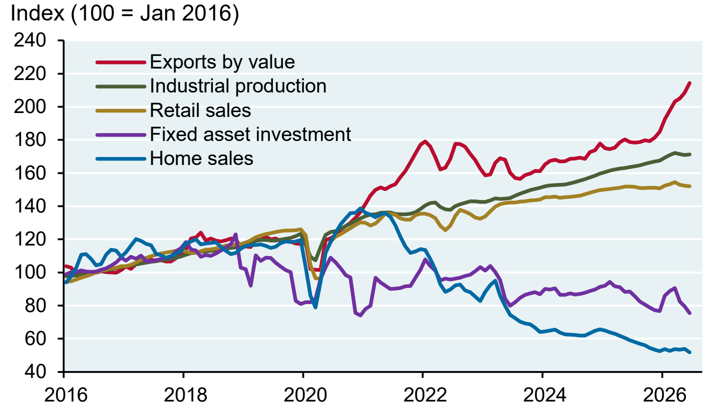
Source: Haver, China Customs, Bloomberg, JPMAM, July 2026

Gross domestic savings rate of the top 10 economies
Percent of GDP



Source: World Bank, JPMAM, 2025

China activity indicators
Index (100 = Jan 2016)

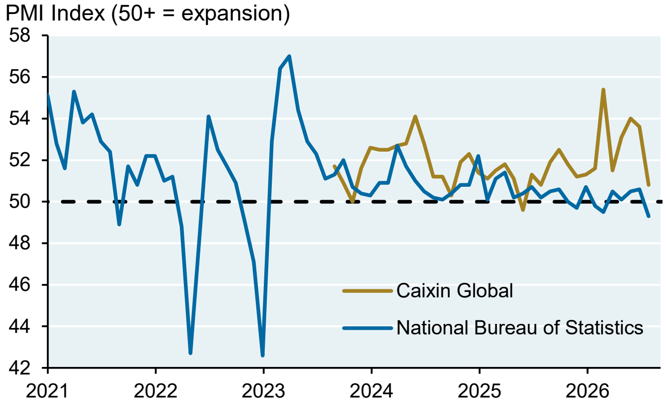


Source: China National Bureau of Statistics, GACC, JPMAM, June 2026

[1] "*How long can China defy history and logic with its imbalances?*", Stephen Roach, FT, July 22, 2026

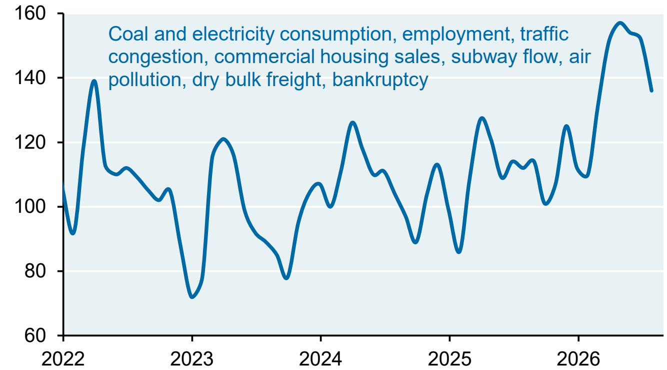
That said, higher frequency indicators we track in China are mostly stable. The charts below show some ups and downs in services/manufacturing surveys and different activity monitors, but nothing exceptionally weak. Also, China's GDP deflator is rising after a period of deflation. I don't sense an imminent crisis on tap for China's economy given the indicators below, even if there is no big-bang stimulus package this fall to revive domestic demand. **Unfortunately for equity investors, these trends are not enough to offset concerns about China's imbalanced economy, leading to yet another year in 2026 of Chinese equity underperformance after a very poor five year stretch.**

China composite services / manufacturing survey
PMI Index (50+ = expansion)



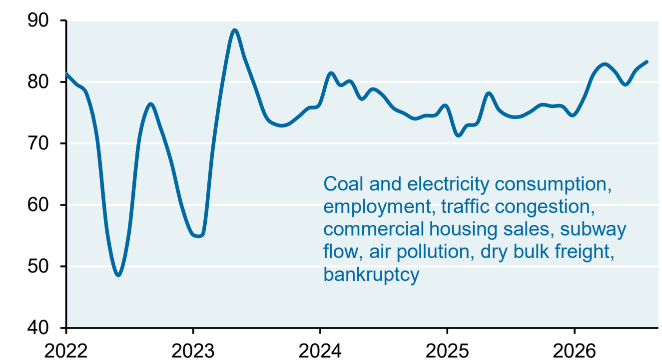
Source: Bloomberg, JPMAM, July 2026

China economic activity monitor (Yicai Index)
Index (100 = Jan 2020)



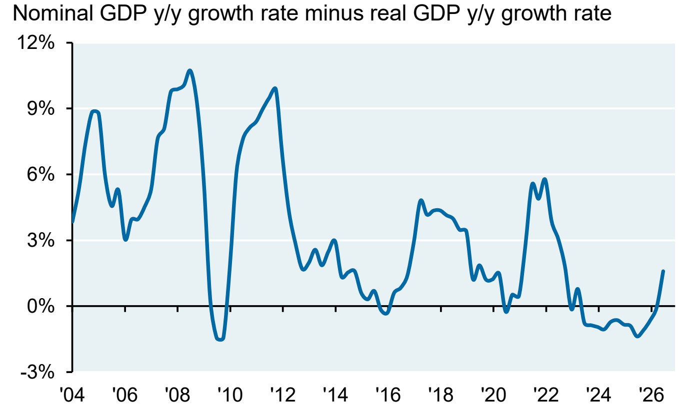
Source: Yicai Research Institute, JPMAM, July 2026

China economic activity monitor (Now Casting Index)
Index (100 = Mar 2000)



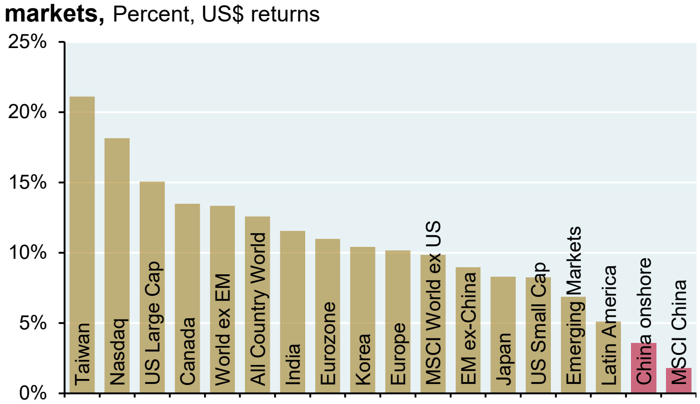
Source: Now-Casting Economics, JPMAM, July 2026

China GDP deflator
Nominal GDP y/y growth rate minus real GDP y/y growth rate



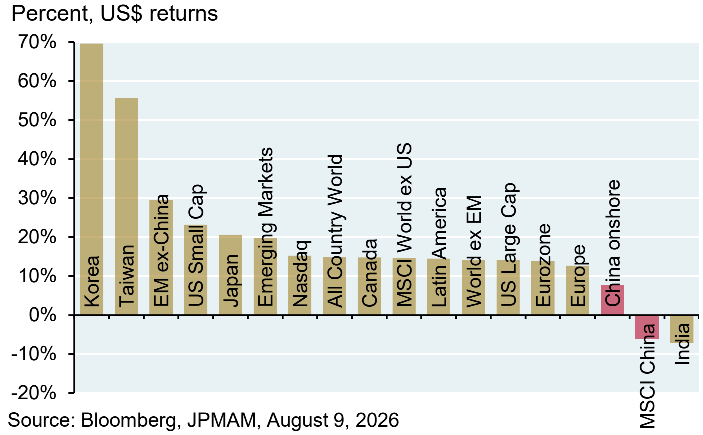
Source: Bloomberg, JPMAM, Q2 2026

2020-2025 annualized total returns for major equity markets, Percent, US$ returns



Source: Bloomberg, JPMAM, December 31, 2025

2026 ytd total returns for major equity markets
Percent, US$ returns



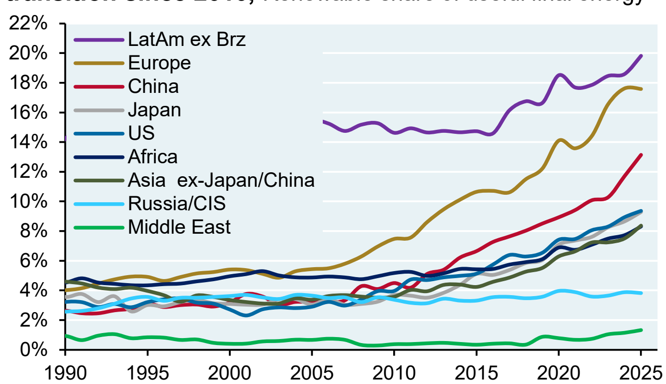
Source: Bloomberg, JPMAM, August 9, 2026

Despite ample evidence of China's malaise[2], China is living up to anthropomorphic characteristics of this year's zodiac, the Fire Horse, in at least one regard: bold moves, self-reliance, speed, action and innovation in energy.

Let's start with three energy barometers: the renewable share of useful final energy, a topic we discussed at length in the 2026 energy paper; the share of useful final energy that is electrified; and the self-sufficiency of energy consumption. On the first two, the rate of change in China is the fastest of all major countries, particularly vs the US. These two factors contributed to China's improved energy self-sufficiency which rose from 66% in 2019 to 81% in 2025.

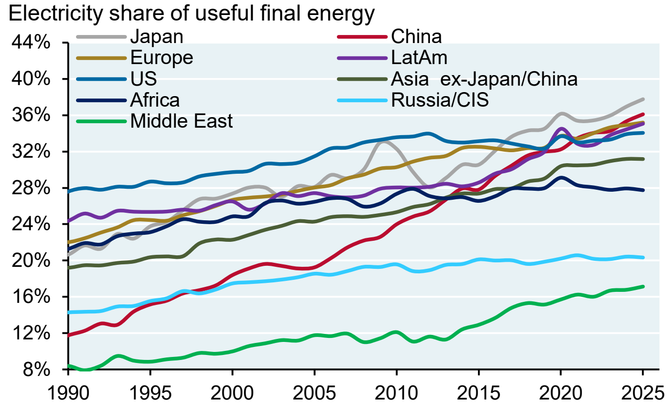
China's energy self-sufficiency is even higher in 2026. China has cut its oil imports by 30%-35% this year by some combination of (a) drawing down on strategic and commercial reserves that reportedly exceed 1 billion barrels, (b) increased gasification of domestic coal reserves to make petrochemicals (coal-to-olefins) and (c) increased electrification. The exact attributions are hard to derive since some figures are opaque. According to Michal Meidan, head of China Energy Research at the Oxford Institute for Energy Studies, the question of exactly how China slashed oil imports this year is the million dollar question: "there's a massive level of uncertainty because we don't fully understand what has happened".

Decarbonization has been a mostly linear industrial transition since 2010, Renewable share of useful final energy



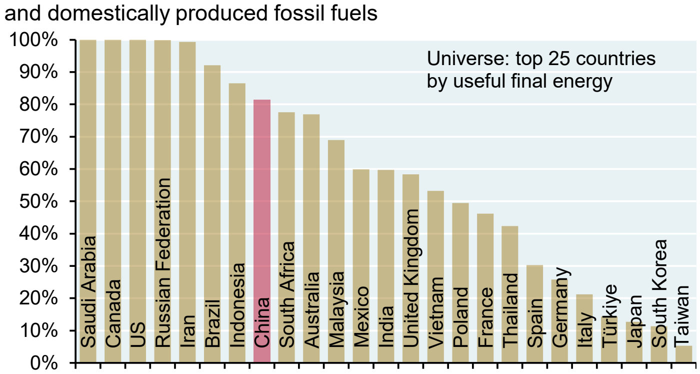
Source: Energy Institute, IEA, JPMAM, 2025

Electrification: China and Japan power ahead
Electricity share of useful final energy



Source: Energy Institute, IEA, JPMAM, 2025

Useful final energy self sufficiency
Percent of useful final energy consumption from renewables, nuclear and domestically produced fossil fuels

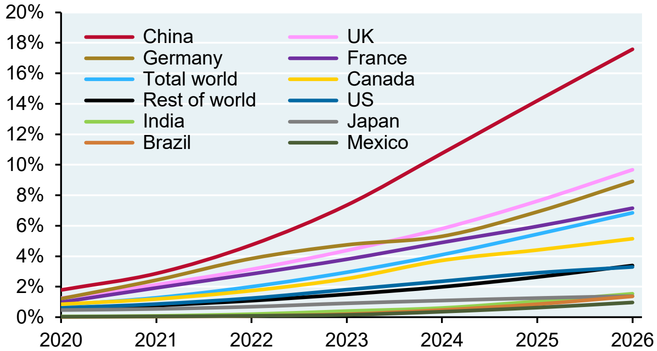


Source: Energy Institute, IEA, JPMAM, 2025

[2] While China official data shows 4.6% real GDP growth from 2022 – 2025, the Rhodium Group estimates that the more plausible range is 1.5% - 2.0%

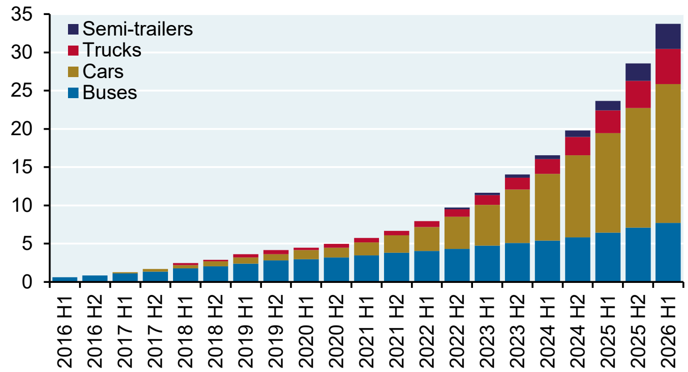
On electrification of transport, China is arguably the only major car market whose EV share of the existing fleet has reached escape velocity. As shown on the right, China's EV adoption has started to reshape global oil demand; EV's displaced 6% of China's oil imports in the first half of 2026[3].

EV share of passenger vehicle FLEET, largest car markets
Percent, BEV + PHEV + EREV



Source: BloombergNEF, JPMAM, June 2026. The top 10 countries above make up ~70% of global passenger vehicle sales

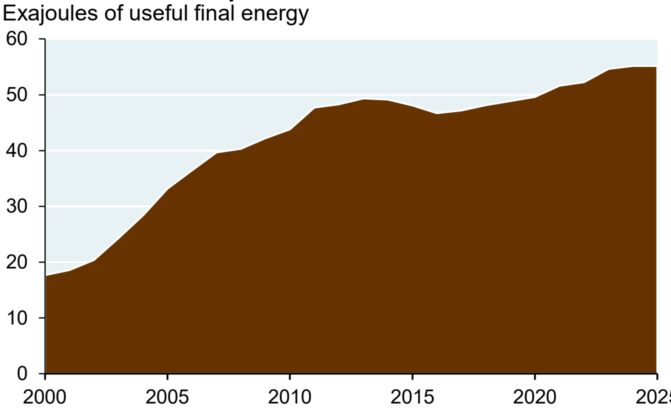
Chinese oil demand displaced by EVs
Million tonnes of oil equivalent



Source: Center for Research on Energy and Clean Air, July 2026

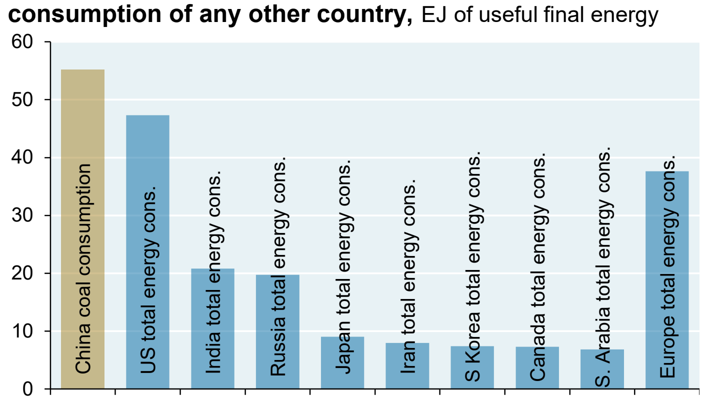
While China renewable and electrification *shares* of energy are rising, so is China's energy consumption and consumption of fossil fuels in absolute terms. As a result, Chinese CO_2 emissions are still on the rise. One pair of striking charts below. First, China's coal consumption is not declining yet despite China installing roughly half of the entire world's wind and solar power. A lot of energy commentary I read obsesses over China's use of coal for power generation, but that only represents ~55% of coal consumption; the rest is for thermal heat and feedstocks for petrochemicals and plastics. Second: China's consumption of coal actually exceeds the ENTIRE energy consumption of the countries/regions shown on the right (!!). But on a rate-of-change basis, China is the among the world leaders on deployment of renewable energy and electrification of transport.

China coal consumption
Exajoules of useful final energy



Source: Energy Institute, JPMAM, 2025

China COAL consumption exceeds TOTAL energy consumption of any other country, EJ of useful final energy



Source: Energy Institute, JPMAM, 2025

Note: these energy charts are all part of a broader midyear energy update slide deck that you can access **here**.

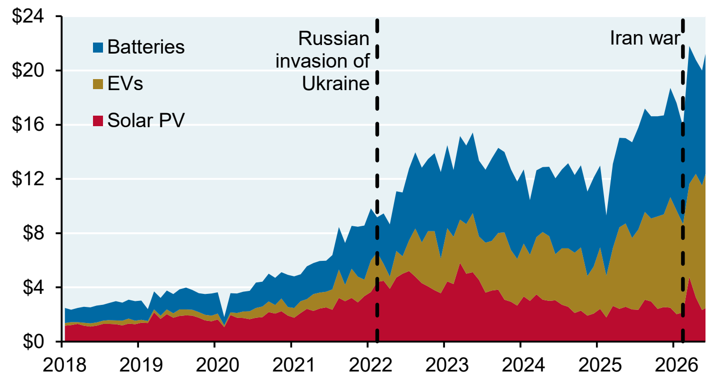
[3] "*EV-related oil cuts emerge as a new driver for China's clean air progress*", Center for Research on Energy and Clean Air, July 14, 2026

***The Year of the Trojan Fire Horse*. Like the Trojan Horse in the Odyssey, the gift of inexpensive Chinese exports is not always as beneficial as it seems; many come with supply chain dependencies and deindustrialization risks for countries receiving them**.

As shown below, Chinese exports of clean technology (batteries, solar PV and EVs) rose sharply after Russia's invasion of Ukraine, and rose again after the US invasion of Iran earlier this year. These exports are helping many countries increase their energy independence, reducing demand for imported oil and gas whose prices are linked to security conditions in the Gulf. **But Chinese EV imports come with a price for countries with their own auto industries**: Chinese competition could threaten 350,000 jobs in Europe by 2030 due to a 35% European cost disadvantage which is driven by rising European material, labor and energy costs[4]. Even the imposition of duties has not stopped the onslaught of EVs into Europe, as shown in the second chart[5]. These projected 350k job losses would follow on 104k European automotive jobs already eliminated in 2024 and 2025 by ZF Friedrichshafen, Bosch, Continental, Schaeffler and others. Around 50% of European automotive suppliers now indicate that they will reduce investments in Western Europe over the next 5 years.

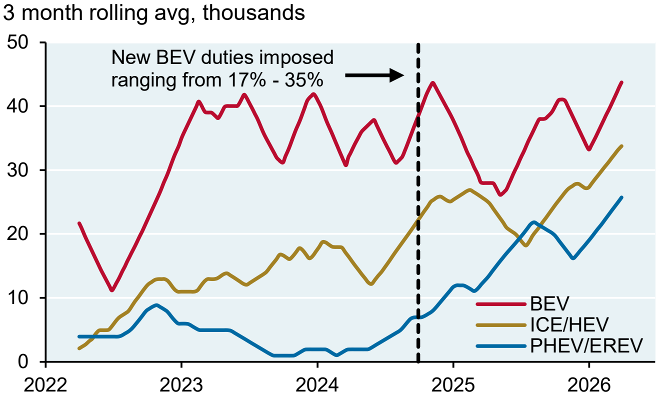
Europe has also struggled to build a homegrown battery industry, with 11 out of 16 planned battery factories delayed or canceled, making European automakers more dependent on Chinese and Korean alternatives.

China clean technology exports: batteries, EVs & solar PV
US$, billions



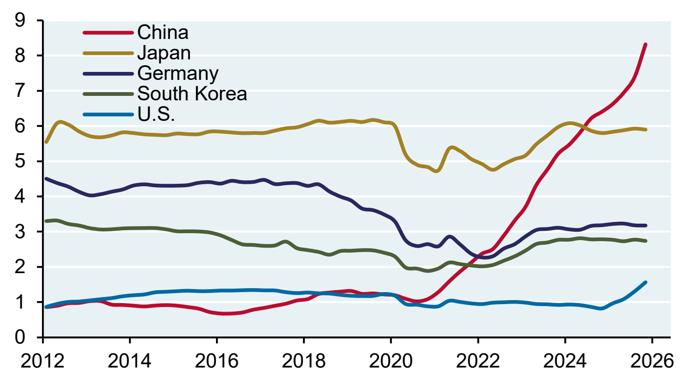
Source: EMBER, JPMAM, June 2026

Chinese car exports to EU
3 month rolling avg, thousands



Source: Rhodium Group, April 2026

Global auto exports
Units, millions



Source: Japan Ministry of Finance, BEA, GAC China, VDA Germany, Q2 2026

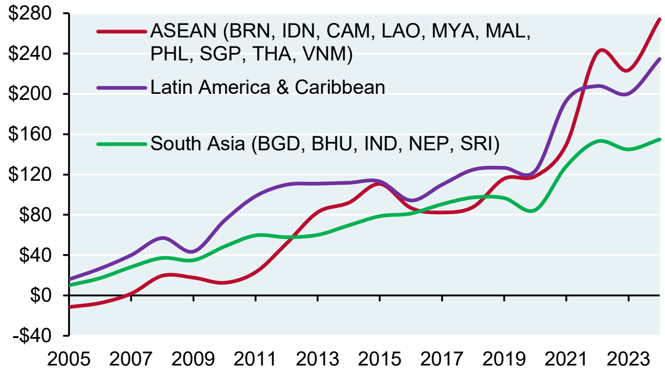
[4] "*Competitiveness gap: manufacturing in EU threatened by displacement*", CLEPA/Roland Berger, Nov 24, 2025

[5] Exports of EVs from China have increased much faster than sales of those imported EVs. According to the IEA, over 1 million electric car exports from China have not yet been registered as sales in importing countries. While it can take months for car-carrying vessels from China to reach destinations, it is likely that inventories of electric cars from China are building up in various export markets. Europe is debating policies that would restrict EV incentives to vehicles with 70% domestic content; no passage yet.

Europe is not the only region struggling with Chinese excess production. As shown on the left, China runs massive trade surpluses with developing countries as well. When sourcing critical raw materials, chemicals and electronic component inputs, firms in developing countries are increasingly left with few options other than Chinese suppliers. Overcapacity is essentially the hallmark of China's impact on the global economy. As shown on the right, China's manufacturing *capacity* is often 2x or more than its current *production*, setting the stage for years of low-cost exports whether the rest of the world is prepared for it or not.

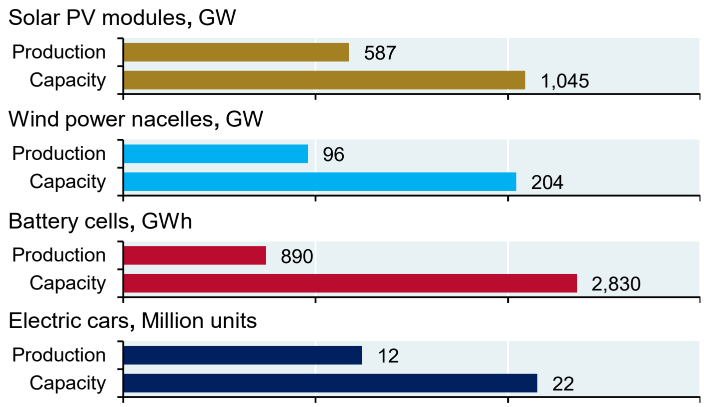
The third chart is also very telling: at the beginning of the 21st century, China's share of value added in global apparel, textiles, footwear and leather exports was ~35% of the low- and middle-income (LMI) country total. At the time, that figure was around the same as China's LMI population share. Today China's value added share is two thirds of the LMI total even as its population share has gone down.

China's manufactured goods trade surplus by region
US$, billions



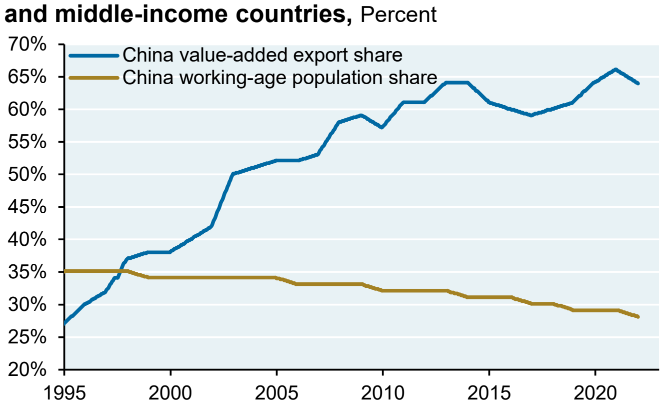
Source: World Bank WITS, UN Comtrade, JPMAM, 2024

China manufacturing capacity vs production, 2024



Source: IEA, 2025

Apparel, textiles, footwear and leather exports from low- and middle-income countries, Percent



Source: OECD, Foreign Affairs, June 18, 2026

What about Chinese FDI?

Chinese firms have used FDI to try and avoid targeted trade restrictions in Asia, the Middle East, Africa and other emerging manufacturing hubs. However: the presence of Chinese firms often fails to transfer significant benefits to local communities in areas like upskilling and technology transfer since Chinese firms typically prioritize vertical integration and rely on inputs made by other Chinese suppliers. Also: Chinese firms often bring in skilled labor and managers from China rather than hiring local workers, and encourage Chinese subsidiaries to continue producing key components in China and instead focus just on assembly and packaging in overseas facilities. Bottom line: fewer benefits for host countries.

Source: US-China Economic and Security Review Commission 2025 annual report to Congress; Part IV Exposure to China's Economic Distortions and Coercion; Chapter 8 China Shock 2.0

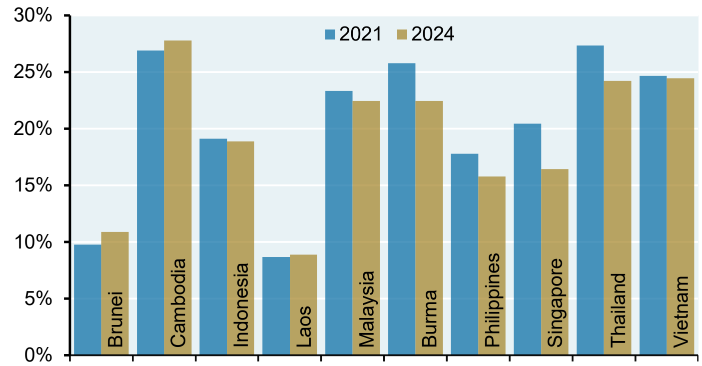
While China strenuously objects[6] to such descriptions of its mercantile approach, the story is pretty clear. Normally, a prolonged period of negative industrial producer prices would lead to competition and reduced capacity. Not in China, however; instead, **~30% of Chinese industrial companies are unprofitable zombies that survive due to a broad-based subsidy approach that dwarfs the rest of the world as shown below.**

To complete the picture, countries that experienced large increases in manufactured imports from China also experienced slowdowns in domestic manufacturing. From 2021 to 2024, as Chinese imports to the ASEAN region increased, every ASEAN country except for Brunei, Cambodia and Laos experienced a decline in their manufacturing share of GDP. Some consequences were outlined in the US-China Economic and Security Review Commission 2025 report to Congress: dozens of Indonesian textile and garment firms shuttered with 250,000 jobs lost in 2023 and 2024 with another 280,000 jobs at risk; and the closure of 4,000 small household appliance, furniture, electronics, garment, auto and steel factories in Thailand in 2023 and 2024.

China industrial producer prices & entities operating at a loss, y/y % change

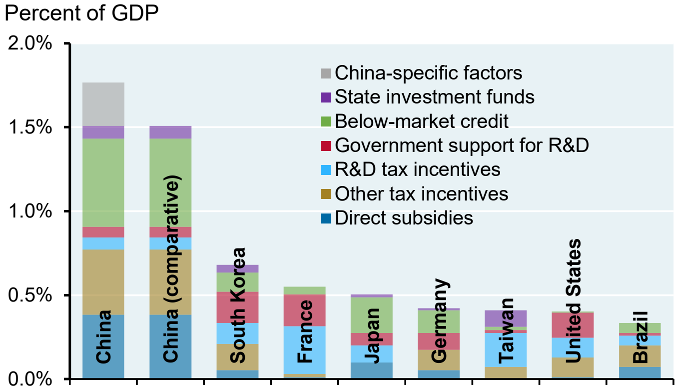
Source: China National Bureau of Statistics, Haver, JPMAM, June 2026

Manufacturing value added by ASEAN countries
Percent of GDP



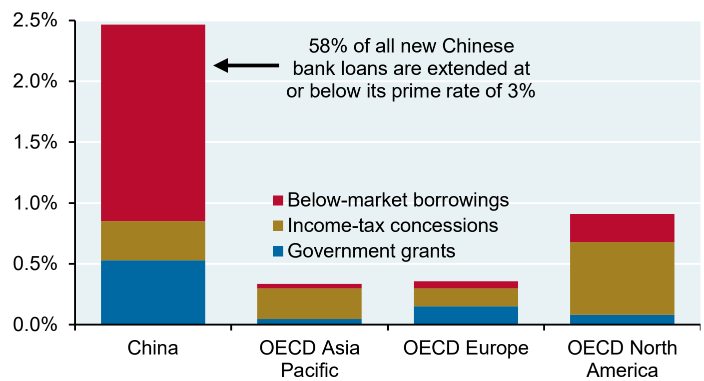
Source: World Bank, 2024

Industrial policy spending in key economies, 2022
Percent of GDP



Source: CSIS, 2022

Industrial subsidies, 2005 - 2024
Percent of annual firm revenue



Source: OECD MAGIC database, June 1, 2026

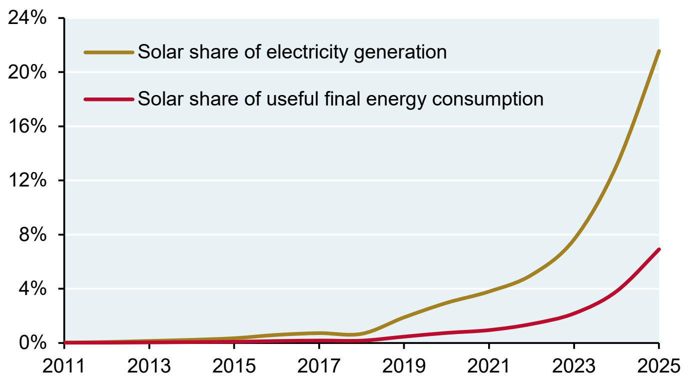
"China is pulling up the ladder behind it", Foreign Affairs, June 18, 2026
Many poorer countries fear that China's economic rise will not leave room for them to industrialize. Unlike the US and Europe, which in the past helped facilitate the industrialization of poorer countries (including China), Beijing is currently on track to have the opposite effect. China is not merely climbing the technological ladder; it is pulling up the ladder behind it. It dominates the new commanding heights of manufacturing (electric vehicles, solar panels, batteries, drones) but it has not vacated the older, labor-intensive sectors through which it and other rich and middle-income countries escaped poverty. In effect, China is trying to do what economic theory says no country should be able to do: retain comparative advantage in almost everything. [Shoumitro Chatterjee, Johns Hopkins and Arvind Subramanian, Peterson Institute]

[6] China's rebuttal is encapsulated in an article submitted to the World Trade Organization in July 2026: "*China's position on the So-called Excess Capacity Issue*". I read all of it and was convinced by none of it

As stated earlier, China's renewable energy exports contribute to decarbonization on a global scale. Countries like Pakistan are seeing rapid uptake of solar power in large part to cheap imports from China. But like the one-eyed Odyssey character Polyphemus, having a singular point of focus misses the big picture: **energy is just one sector of the economy, so cheap solar power and greater energy independence has to co-exist with a flood of Chinese imports across multiple sectors, not just energy**. Countries trying to navigate China's unprecedented global production surplus face a huge challenge, energy independence dividends notwithstanding. That may explain the surge in anti-dumping and countervailing duty investigations targeting China filed since 2023[7].

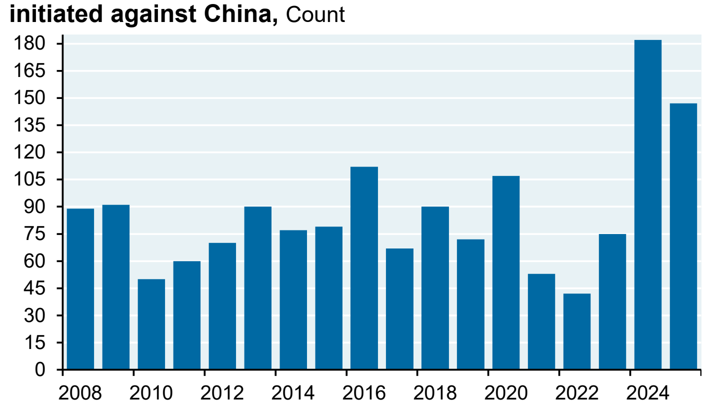
China is fighting back: after Europe announced the Industrial Accelerator Act to create incentives for EU-based procurement and production, Beijing threatened countermeasures against Europe. China also issued decrees authorizing retaliatory measures against foreign laws seen as "discriminatory" against China, and introduced new controls on outbound direct investments to provide the legal basis for punishing countries that restrict Chinese corporate investments. I'm not sure how that is going to work out: "an economy like China's that is so dependent on global demand for growth cannot remain in perpetual conflict with its customers" [8].

Solar shares of Pakistan electricity and useful final energy
Percent



Source: Energy Institute, IEA, JPMAM, 2025

Anti-dumping and countervailing duty investigations initiated against China, Count



Source: World Trade Organization, JPMAM, 2025

Michael Cembalest
JP Morgan Asset Management

The other Odyssey
So far, Nolan's Odyssey film has been criticized for unconventional casting choices, American accents, insufficient attention to details regarding interventions by Greek gods that were present in the original Homeric text, anachronistic themes of character introspection in the ancient world, filming in territorially disputed parts of Morocco, the insufficient depth of female characters, costume inaccuracies and the use of Norse longships instead of Bronze Age Greek vessels. As the film crosses $1 billion in worldwide box office revenues, most audiences are simply ignoring them. Two recent films I also recommend seeing: "The Tuner" and "It Was Just an Accident"

[7] On US tariffs: the US is moving toward a more diversified tariff regime. Section 301 will replace the expiring Section 122 levy, Section 338 has been invoked or threatened and further Section 232/301 actions are still in progress. This points to higher barriers alongside EU trade-defense actions, ASEAN transshipment scrutiny, etc

[8] "*China's moment of weakness*", Logan Wright, Foreign Affairs, July 23, 2026

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