PART I

THE YEAR IN REVIEW

CHAPTER 1: U.S.-CHINA ECONOMIC AND TRADE RELATIONS (YEAR IN REVIEW)

Executive Summary

In 2026, China's two-speed economy continues. The country's structural economic weaknesses became more apparent, even as the Chinese Communist Party (CCP) doubled down on its strategy to promote production and innovation in targeted industries and rely on exports to absorb the excess. Rather than address persistent weak domestic demand and deflationary pressures, China allowed its consumption support programs to expire and continues to funnel credit and investment toward its oversaturated manufacturing sector. The conflict in Iran has introduced a cyclical element to these challenges as global energy supplies tighten, raising costs for China's manufacturers and leading to economic hardship for many of China's trade partners.

China's export of its excess production means it is well on its way to a trade surplus of over $1 trillion for the second year in a row. This "China Shock 2.0"—a flood of low-cost exports—is hurting economies all over the world that fail to put up barriers to China's market distortions as their manufacturing sectors are undercut by cheaper products. Many of China's trade partners have introduced more measures to protect domestic manufacturing sectors, including traditional WTO remedies as well as non-tariff barriers. At the same time, China has sought to use concerns about U.S. trade policy to enhance its market access, ironically, claiming to be a more reliable trading partner that supports the rules-based trading system.

Instead of addressing these growing issues, China's 15th Five-Year Plan (FYP) released in 2026 showcases its continued focus on technological dominance. Beijing hopes its efforts to dominate technology supply chains and innovate at the frontier—combined with its own de-risking measures—will allow it to weather the broader economic slowdown, achieve self-sufficiency, and enhance its geopolitical power. China has also deepened and expanded its toolkit to exert economic leverage on global markets as well as resist foreign sanctions and export controls.

Key Findings

- China's two-speed economy persisted in 2026. Weak domestic demand and shrinking profit margins weighed on businesses at home, even as General Secretary of the CCP Xi Jinping pressed ahead with efforts to dominate global manufacturing supply chains and advanced technology sectors while strengthening Beijing's ability to exert economic leverage and withstand pressure from abroad.
- China still has not lived up to its repeated promises to spur greater consumption. Continued malaise in the property market has kept domestic demand muted, contributing to excess supply in the manufacturing sector. An estimated 87 percent of Chinese urban households own property; with average home prices having declined 20–25 percent since their peak in 2021, the average Chinese household's wealth has been reduced significantly.
- Weak labor demand and technological displacement are pushing more workers into "flexible" employment in the "gig" economy, leading to lower and less stable earnings, limited career advancement, and weaker social protections. As of 2026, 320 million people worked flexible jobs, including workers from traditionally professional occupations, such as software engineers, financial analysts, and healthcare workers, placing constraints on China's ability to boost consumption.
- Beijing implicitly acknowledged the problem of excess production through its "anti-involution" campaign targeting harmful price competition, as Chinese companies repeatedly slash prices to unload surplus output. The campaign remains limited in 2026, however, and Beijing is unlikely to move more aggressively to curb supply; doing so would undercut exports, a core growth driver, and eliminate many firms' sole pressure release valve, in addition to putting greater pressure on the labor market.
- China Shock 2.0 shows no signs of abating: China's exports accelerated in the first half of 2026 after a record trade surplus in 2025. The resulting flood of exports is hurting manufacturers in developed and developing economies alike, while Beijing has used a range of tactics to forestall a coordinated response.
- Despite the current détente with the United States, China continues to expand its ability to wield supply chain leverage, withstand U.S. and allied sanctions and export controls, and retaliate against foreign measures the CCP deems "unjustifiable." These efforts are setting up a clash between competing regulatory systems that could leave foreign companies operating in China caught between conflicting demands while raising the costs the United States and its partners must weigh when using economic statecraft.

- The 15th FYP confirmed that China remains committed to mobilizing the full weight of the state to advance its technology sector. Beijing treats artificial intelligence (AI) as a general-purpose technology—the connective layer driving other priorities, including biotechnology, robotics, and quantum—believing that mastering these foundational technologies will secure a durable, economy-wide advantage and overcome its economic challenges.
- China continues to face significant compute constraints due to U.S. export controls, yet its frontier AI capabilities have largely kept pace with advances in the United States. Chinese developers are using techniques such as distillation to steal the methods and outputs of top U.S. models to develop capable, lower-cost Chinese alternatives. By releasing these models with open weights and encouraging their adoption abroad, China aims to make its AI systems the global default. U.S. leadership in frontier AI remains real, but China's strategy for spreading its models could make that lead less secure than it appears.
- As China's technologies advance, Beijing is refining its economic toolkit to keep capital, technology, data, and talent at home: screening outbound investment, blocking foreign acquisitions of Chinese firms, restricting AI researchers at frontier labs (and their families) from leaving the country, and limiting the types of foreign investment permitted in its AI companies.

Introduction

On many levels, the story of 2026 for U.S.-China economic relations is continued détente. The two presidents have met twice as of the date this report was completed and were slated to meet two more times during the year. Little new was sought or accomplished at these meetings, with the main focus being modest purchases of certain U.S. goods by China and professed stability on economic issues. Each country exercised restraint around areas of leverage while actively seeking to de-risk in ways that did not undermine the détente.

China Awards Itself Top Marks, Strives for Continuity in Its Management of the Economy

The Party's high level of confidence in its handling of the economy was palpable during the Commission's trip to China in July 2026. In early 2025, the prospect of tariff and trade uncertainty loomed.[1] Yet rather than addressing longstanding domestic economic imbalances, the Party doubled down on its traditional economic playbook of export-driven growth. Even as the United States and China began a new phase of trade tensions, China's exports hit a new record as global markets absorbed its manufacturing surplus.[2] Additionally, in retaliation for U.S. tariffs on China, Beijing imposed rare earth export controls on the United States.[3] This move ultimately contributed to the two countries coming to the negotiating table, and

it demonstrated to the world China's geo-economic leverage around rare earths and critical minerals.

China released its 15th FYP in March 2026, indicating continuity in China's core economic policies. The FYP calls for accelerating breakthroughs in a range of frontier technologies, including AI, quantum technology, nuclear fusion, life sciences and biotechnology, brain science, clinical medicine, and deep-sea and deep-space exploration.[4] The plan signals China's intent to continue pursuing manufacturing dominance and technological self-reliance rather than rebalancing growth toward greater domestic consumption, which outside observers have long insisted China needs to support more sustainable long-term growth.[5] Just months after China released its national-level plan, several provinces unveiled their own FYPs that echoed the national plan.[6]

The CCP's unwillingness to rebalance its economy toward greater domestic consumption may seem irrational to free market observers, but it is entirely consistent with the CCP's belief in its model. For China, household consumption is a byproduct of industrial and technological development rather than a goal in its own right. Two recent articles in China's state-run publications *Qiushi* and *Economic Daily* argue that manufacturing and diffusion of advanced technologies should be the primary drivers of future productivity growth and will ultimately resolve the country's economic slowdown.[7] Even the 15th FYP's consumption measures are framed as an "investment in human capital" serving industrial ends.[8]

China's successes have reinforced its leaders' confidence in their management of the economy, despite an erosion in profitability, high debt levels, glacial wage growth, low returns on investment, and significant economic weakness outside of favored sectors. Viewed through the lens of geopolitical competition, market inefficiency is a feature of the CCP economic system, not a bug. Beijing appears willing to bear the near-term economic costs of expanding manufacturing capacity to undercut foreign industry, capture global market share, and gain the power to wield critical supply chains as geopolitical leverage.

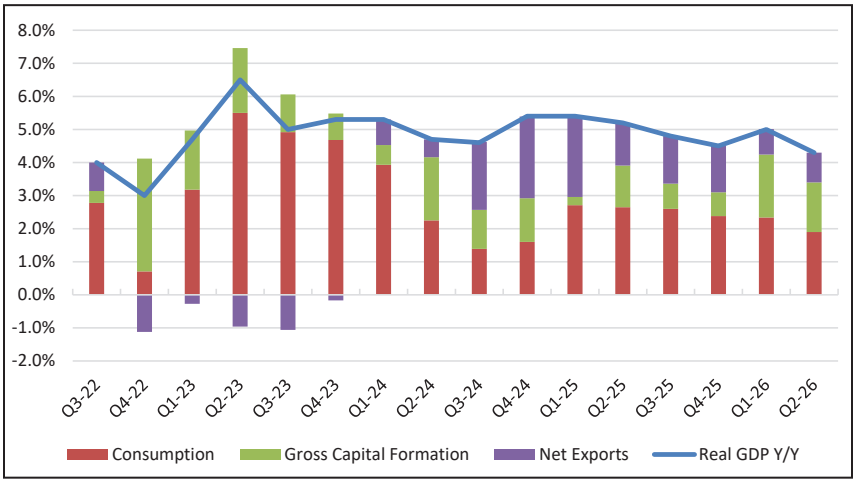
GDP Growth Dips, Investment Plummets Despite Strong Exports

China's year-on-year GDP growth was 4.7 percent* in the first half of 2026, but further examination of this fairly strong topline figure's composition reveals a deteriorating outlook. First quarter GDP growth of 5.0 percent exceeded expectations, buoyed by 14.7 percent first quarter export growth and frontloaded infrastructure

*China often pauses or modifies the methodology of economic datasets, raising questions around the reliability of official data. Independent estimates by prominent outside organizations posit that actual growth in China's economy is likely far lower than reported. Rhodium Group estimates 0–1 percent topline GDP growth in Q2 2026 compared to the official 4.3 percent. Rhodium Group derives alternative estimates of China's GDP growth by reconstructing expenditure-side GDP from a range of underlying economic indicators, and it adjusts official national accounts where they diverge from observable economic activity. For more, see U.S.-China Economic and Security Review Commission, Chapter 1, "U.S.-China Economic and Trade Relations (Year in Review)," in *2025 Annual Report to Congress*, November 2025, 52–53. Thomas Hale, Joe Leahy, and Haohsiang Ko, "Five Things to Watch When China Reports Economic Growth," *Financial Times*, July 14, 2026; Daniel H. Rosen et al., "China's Economy: Rightsizing 2025, Looking Ahead to 2026," *Rhodium Group*, December 22, 2025; Logan Wright, "The Strategic Logic of China's Economic Data," *Rhodium Group*, September 11, 2025.

investment.[9] After solid growth in Q1, topline growth in Q2 fell sharply to 4.3 percent, the lowest quarterly figure since 2022.[10] Weakening investment and consumption, exacerbated by global uncertainty and fluctuating energy prices from the Iran conflict, contributed to the dropoff.[11] However, manufacturing output remained resilient. Industrial value-added output increased 5.4 percent year-on-year from January to June. High-tech manufacturing value added increased 13.3 percent year-on-year during this period, including a 28 percent increase for industrial robotics and a 39.3 percent increase for lithium-ion batteries.[12] Exports grew 13.4 percent in the period while imports were up 22.1 percent, driven by demand for AI gear, tightening a goods trade surplus that reached $576 billion halfway through the year.[13] Integrated circuits and automated data processing equipment exports accounted for 40.1 percent of year-on-year export growth through June.[14] The precipitous growth in exports was driven primarily by AI-related demand. While China does not currently export advanced semiconductors for AI, the AI boom drove up prices for memory chips and other lower-value semiconductors as well, which China does export.[15] In June, China's exports of integrated circuits were up 120 percent year-on-year by value, but only 5.1 percent by volume (in other words, China sold slightly more semiconductors, but at significantly higher average prices).* [16]

Figure 1: Year-to-Date Contributions to Real GDP Growth
Q3 2022–Q2 2026



Source: China's National Bureau of Statistics, via Haver Analytics.

Despite resilient industrial output and exports, China's relatively strong GDP growth is not translating into more high-quality jobs. Export growth is increasingly driven by capital- and technology-intensive manufacturers rather than labor-intensive processes, de-

*The increase in export values did not indicate China is exporting advanced semiconductors. Market conditions, in part driven by global AI infrastructure demand, led to higher prices for the less advanced semiconductors China exports.

creasing headcount on factory floors.[17] Industrial profits were under pressure entering 2026 from "involution"—fierce price competition among firms resulting from excess capacity. Such factors contributed to stagnant wage growth and shifting composition of the labor force, as jobs in traditional growth sectors like manufacturing and construction dissipate and more workers take flexible employment opportunities in the "gig" economy.[18] Negative consumer sentiment continues to be reflected in low retail sales growth, which in the first half of 2026 reached its weakest point since 2022 under zero-COVID policies.[19]

Falling fixed asset investment (FAI) is also notable for an economy that relied upon investment to fuel growth for decades, especially since consumption is not rising as would be necessary for a genuine rebalancing of the economy.[20] In 2025, overall FAI declined for the first time since the late 1980s; it had only registered similar drops during the Great Leap Forward and subsequent famine (1961) and the Cultural Revolution (1967).[21] After starting 2026 in the black, FAI turned negative in April and was down 7.2 percent year-to-date through August.[22] Official FAI statistics show a rapid decline, reflecting both a structural slowdown and a likelihood that China's investment figures have been overstated for years.*[23] (For more on China's overstatement of FAI and other economic metrics, see U.S.-China Economic and Security Review Commission, Chapter 1, "U.S.-China Economic and Trade Relations (Year in Review)," in *2025 Annual Report to Congress*, November 2025, 52–53.) The drawback of investment across the board comes despite significant policy signals from Beijing at the end of 2025 indicating it was prioritizing investment as a driver of growth.[24] On December 31, 2025, the National Development and Reform Commission (NDRC) announced $42 billion for infrastructure projects.[25] However, this has proven insufficient to offset falling investment in the aggregate. By sector, real estate FAI declined 18 percent, infrastructure investment dropped 2.4 percent, and investment across manufacturing fell 1.2 percent (see Table 1).[26] In one bright spot for FAI, manufacturing of computers and information and communications technology (ICT) equipment was up 7.8 percent year-to-date through July 2026 after finishing last year in the red.[27] China's manufacturers are therefore facing a challenge on two fronts: not only compressed margins from higher costs but also weak domestic demand, made all the more difficult amid deflationary pressures from continuing excess supply-fueled price wars and mounting trade tensions globally.[28]

*The credibility of China's FAI figures has been questioned by commentators such as Derek Scissors at the American Enterprise Institute, who points to backward revisions as evidence that official GDP growth statistics have been overstated. Separately but related, following a change in methodology, the infrastructure portion of FAI grew 8.9 percent year-on-year during Q1 2026 after declining 2.2 percent in all of 2025. The sharp increase was driven partly by the National Bureau of Statistics adding power investment into the figure, which had previously been tracked separately by the National Energy Administration. Allen Feng, "Apples to Oranges in Infrastructure Investment Data," *Rhodium Group*, April 20, 2026; Derek Scissors, "When Does China Stop Growing (Entirely)?" *American Enterprise Institute*, March 2026; China's National Bureau of Statistics, via Haver Analytics.

Table 1: Key Economic Metrics (Year-on-Year Growth)

	Q1 and Q2 2026	2025	2023–2025 avg.	2015–2019 avg.
Retail Sales	**1.4%**	**3.7%**	**4.8%**	**9.6%**
Total FAI	**-5.7%**	**-3.8%**	**0.8%**	**7.3%**
real estate	*-18.0%*	*-17.5%*	*-12.1%*	*6.1%*
infrastructure	*-2.4%*	*0.7%*	*6.2%*	*10.9%*
manufacturing	*-1.2%*	*0.6%*	*5.4%*	*5.9%*
Exports	**18.1%**	**5.2%**	**2.1%**	**1.7%**

Source: China's National Bureau of Statistics and General Administration of Customs, via Haver Analytics.

Beijing's Anti-Involution Campaign Is Implicit Acknowledgment of Overcapacity

Excess industrial capacity remains one of the defining distortions in China's economy, and Beijing has had little success in curbing destructive price wars without sacrificing the production and exports supporting economic growth. Although there is not a single measurement for overcapacity, it is reflected in persistently low industrial capacity utilization rates, suppressed producer prices, weak corporate profitability, and a rising share of loss-making firms.* Outside of chipmakers experiencing a windfall from AI-related demand, firm profitability continues to decline, and industrial capacity utilization in Q2 dropped to 73.0 percent, a tenth of a percent shy of an all-time low outside the pandemic.[29] About a quarter (23.8 percent) of Chinese industrial enterprises were loss-making in 2025, compared to 11.9 percent a decade earlier, according to official statistics.[30] Under free market conditions, unprofitable firms would exit the market, bringing supply and demand back into equilibrium. But heavily subsidized loss-making "zombie firms" in China's state-guided economic system continue operating and even increase production despite insufficient demand.†[31] Though China generally does not admit that its economic model leads to overcapacity, conditions have become severe enough that Beijing now describes the fierce price competition that results as "involution" and has launched a campaign to—in Xi Jinping's words—rectify the "chaotic situation of disorderly competition among enterprises."[32]

After setting the tone for curbing excess supply, Beijing has stepped up scrutiny of disorderly competition cases. But in the face of the rising price pressure on manufacturers, slowing growth, and increasing trade tensions, it has stopped short of stronger enforce-

*For more on indicators of China's overcapacity, see U.S.-China Economic and Security Review Commission, Chapter 1, "U.S.-China Economic and Trade Relations (Year in Review)," in *2025 Annual Report to Congress*, November 2025, 41–42.

†The total value of subsidies under China's industrial policy is estimated to be equivalent to 4 percent of GDP, according to a 2025 working paper from the International Monetary Fund. These include cash subsidies, tax benefits, subsidized credit, and subsidized land. The Organisation for Economic Co-operation and Development (OECD) estimated that between 2005 and 2024, industrial firms in China received on average three to eight times more government support than competitors based in OECD countries. "OECD Magic Database of Industrial Subsidies," *Organisation for Economic Co-operation and Development*, June 2026; Daniel Garcia-Macia, Siddharth Kothari, and Yifan Tao, "Industrial Policy in China: Quantification and Impact on Misallocation," *International Monetary Fund*, August 8, 2025.

ment measures. The anti-involution campaign has included regulatory pressure to rein in price wars. In February, the State Administration for Market Regulation (SAMR) issued price guidance for the auto industry as subsidies for trade-ins were phased out to steer consumers toward higher-end models.[33] In May, SAMR vowed to increase investigations of "unfair competition" in certain industries and is rolling out measures to implement central government guidance on standardizing local government regulation, decreasing local protectionism, reducing excessive local government support for the same sectors, and creating a more integrated national market to facilitate industry consolidation.[34]

The anti-involution campaign has thus far yielded limited results. Meaningfully curbing overcapacity would run counter to Beijing's reliance on manufacturing and exports to boost growth, while allowing more firms to fail would put additional pressure on the labor market. Another structural inhibitor is local government subsidies. Local governments rely heavily on value-added tax and corporate tax revenue derived from production and manufacturing within their jurisdiction, creating a strong incentive to prop up provincial champions even if they are unprofitable or redundant on a national level.[35] The unwinding housing market has intensified this fiscal dynamic for local governments as they can no longer rely on income from land sales, which had provided roughly one-third of revenue during the boom years.*[36]

Iran Price Shock Adds Further Stress

China's ability to weather energy disruptions and rising prices from the Iran conflict reflects its gains in energy security, but the conflict has also added economic strain. Despite nearly half of its oil imports traveling through the Strait of Hormuz, China has managed to largely insulate itself from severe energy price shocks due to its large oil stockpiles, shift to renewable energy, substantial domestic coal reserves, and other policy responses that afforded it more flexibility than many other countries.[37] Nevertheless, the energy price spike from the Iran conflict serves as a natural experiment for China's state-supported industrial production and export-driven growth model. Tellingly, 2026 has seen a decline in investment in manufacturing segments most exposed to the price shock.[38] For instance, in the first half of 2026, year-on-year FAI fell in resource-intensive industries and those with high exposure to energy input costs, including petroleum processing (-5.7 percent), chemical fibers (-13 percent), and automotive manufacturing (-4.2 percent).[39] Pressure from the Iran conflict has also exacerbated the structural slowdown in traditional growth segments of the economy, such as the property sector, as developers confronted with higher material costs put projects on pause.[40]

China's Flexible Sourcing Cushioned Oil Shock

China has used a variety of methods to insulate its economy from an energy shock. As crude oil futures doubled from $57 per barrel at

*For more on local government fiscal dynamics, see U.S.-China Economic and Security Review Commission, Chapter 3, Section 2, "Fiscal, Financial, and Debt Problems Weigh Down Beijing's Ambitions," in *2023 Annual Report to Congress*, November 2023, 340–393.

the beginning of 2026 to a peak of $112 per barrel in April, China reduced the volume of its imports by 23 percent month-on-month in April and 14 percent in May.[41] China exercised several levers concurrently to compensate for the fall in available crude. First, it tapped into its nearly 1.4-billion-barrel stockpile,* withdrawing an estimated one million barrels per day starting in May, primarily from its commercial reserves.[42] Next, it drew on meaningful volumes of floating, sanctioned oil from Russia and Iran.[43] China also restricted exports of processed petroleum products between March and June, causing refiners to reduce processing to a four-year low and helping ensure supply for domestic buyers.[44] Finally, manufacturers relied on renewable energy, which accounted for a third of China's total electricity consumption in 2025, and coal, which it uses as a substitute for oil and gas to produce fertilizer and plastics.[45]

By cutting back on crude oil purchases and consumption, China has dampened Hormuz-related stress on its manufacturing sector. Its producer price index for producer goods spiked in March and April but appeared to level out at around 4 percent year-on-year since June.[46] By reducing its oil purchases during a time of compressed global supply, China hoped to slow the rise of oil prices so energy prices did not dissuade its trade partners from buying trillions of dollars of exports.†[47]

The global energy price spike ostensibly reversed years of deflation in China, but supply shock inflation should not be mistaken for a healthy return of demand. After hovering around zero since April 2023, the consumer price index rose from 0.2 percent growth year-on-year in January to 1 percent in June.[48] The producer price index rose from a 1.4 percent year-on-year decline in January to a 4.1 percent increase in June.[49] Though impact on consumption is negligible, higher input prices for producers compress already razor-thin margins for China's manufacturers.

Structural Challenges Continue to Suppress Domestic Demand

Business and consumer confidence remained subdued in 2026 as mutually reinforcing structural challenges ossified within China's increasingly imbalanced economy. Despite some positive signs, the property sector continues to weigh heavily on the broader economy. Credit expansion has slowed dramatically as the financial sector struggles to remain profitable under pressure from the central government to service poor-quality debt on longer time horizons. Another key indicator is the struggling labor market. Official unemployment figures from China's National Bureau of Statistics, including the headline "surveyed urban unemployed" rate, have remained stable around 5 percent.[50] But this figure excludes large segments of the population such as rural and migrant workers, and independent analysis estimates are often much higher, including one from Tsin-

*China's national stockpiles consist of roughly 360 million barrels of government-held inventories and an additional one billion barrels held by national oil companies, blurring the lines between commercial and strategic reserves. U.S. Energy Information Administration, *China, the United States, and Japan Hold Most Strategic Oil Inventories in 2025*, April 20, 2026.

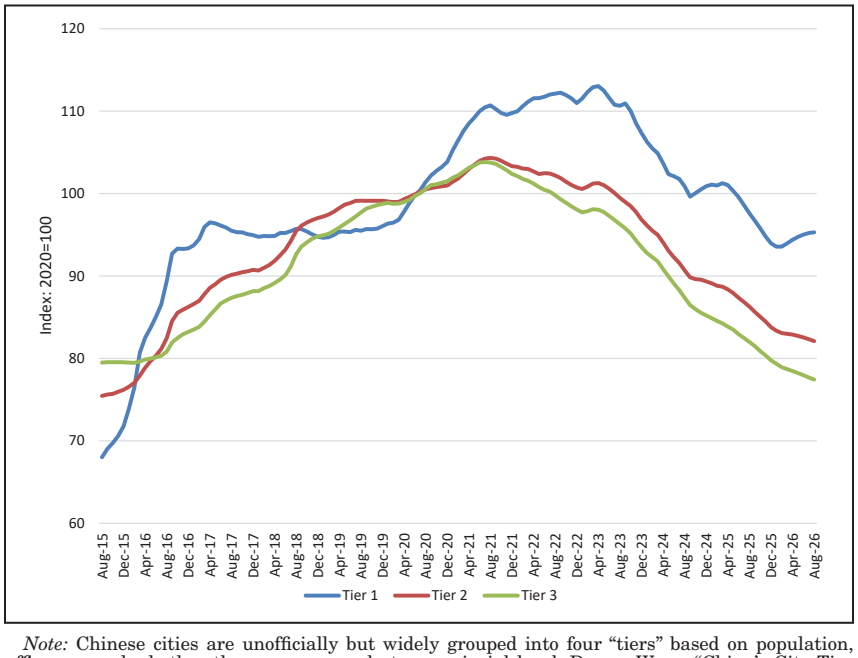
†It is also possible that China is using the experience from the Strait of Hormuz as a "live experiment" on ways to reduce its vulnerability and enhance its resiliency to a disruption in seaborne oil imports in the case of a Taiwan contingency. China has demonstrated that it can reduce oil imports abruptly by about 30 percent with a negligible impact on its economic activity.

ghua University that calculated 10.2 percent unemployment in July 2026.[51] Wages have stagnated and the rise of more tenuous flexible employment coincides with growing anxiety around displacement from AI and automation. Diminished asset values and precarious wage growth prospects all contribute to anemic household spending and demand.

Slow Unwinding of Property Sector Continues to Be a Drag on Economy Five Years On

China's massive property sector continues to weigh heavily on consumer sentiment and the broader financial system five years on from the 2021 peak. FAI in real estate has been negative since 2022, and in 2026 the decline accelerated to -21.5 percent year-on-year for the eight months through August.[52] While reduced investment is necessary to bring supply back in line with demand, in the interim the continued drop puts pressure on developers, local governments, and the banking system.[53] Prices in Tier 1 cities (i.e., Beijing, Shanghai, Guangzhou, and Shenzhen) showed signs of recovery, rising 1.9 percent year-to-date through August.[54] However, prices more broadly in cities across the country continue to decline, albeit at a slowing rate (see Figure 2). In August, prices for new housing in 65 of the 70 largest cities in China were lower than a year before, and prices for existing real estate were down in every city compared to the year prior, even those in Tier 1.[55]

Figure 2: Property Price Index for 70 Cities, Existing Residential Buildings (2020=100), August 2015–August 2026



Note: Chinese cities are unofficially but widely grouped into four "tiers" based on population, affluence, and whether they are governed at a provincial level. Dorcas Wong, "China's City-Tier Classification: How Does It Work?" *China Briefing*, February 27, 2019.
Source: China's National Bureau of Statistics, via Haver Analytics.

Real estate still comprises as much as 70 percent of wealth held by Chinese households, with over 20 percent owning multiple properties due to low returns on savings and limited alternative investment options.*[56] A study from 2021 estimated 87 percent of Chinese urban households owned property, among the highest rates of home ownership in the world.[57] With average home prices declining 20–25 percent since the 2021 peak, the average Chinese household's wealth has been reduced significantly, leading indirectly to a pullback in broader spending. The consumer confidence index dropped from 121.5 to 88.3 in 2022 under zero-COVID and has flatlined since, signaling that most Chinese consumers remain pessimistic about their economic prospects.†[58]

Existing debt burdens and local government fiscal conditions further complicate Beijing's effort to stabilize the housing market. Banks are directing credit to roll over property-related debt on longer time horizons at the expense of more efficient deployment of capital.[59] Local state-owned enterprises (SOEs) are buying unsold housing from developers for conversion into "affordable housing" and are borrowing from banks to do so, often with the support of local governments.[60] The drag on real estate continues to lower revenue for fiscally constrained local governments. Moreover, local governments are using bonds traditionally earmarked for infrastructure to clean up hidden debt‡ and buy back land from property developers, contributing to the previously mentioned decline in infrastructure investment.[61]

A number of policy moves in August 2026 indicate Beijing may feel the need to shore up the property sector in the days and months ahead.[62] On the demand side, regulators raised the maximum debt-service-to-income ratio for homebuyers from 55 percent to 60 percent and extended the maximum mortgage term from 30 to 40 years, measures intended to expand access to mortgages and lower monthly payments.[63] The rule changes shift lending decisions toward individual projects rather than developers' overall credit profiles and allow loan terms to vary according to project type.[64] Perhaps most importantly, new rules seek to move the property sector away from the pre-sale model that fueled the sector's debt-driven expansion.[65] Going forward, developers will generally be required to complete a building's main structure before beginning pre-sales, while mortgage proceeds from pre-sold units will not be disbursed until completion filings.[66] These measures may improve project completion and help restore the confidence of buyers. However, tighter restrictions on pre-sale financing could lengthen developers' working-capital cycles and further constrain new construction and property investment.[67]

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*Despite efforts in recent years to boost the role of equity markets in funding high-tech sectors, returns for investors in China's stock markets have been flat for years, compared to large gains in U.S. equity markets. Shanghai Stock Exchange, via Haver Analytics.

†Scores greater than 100 indicate optimistic consumer confidence. China's National Bureau of Statistics, via Haver Analytics.

‡"Hidden" or "implicit" debt refers to borrowing by local government financing vehicles (LGFVs) and other entities acting on behalf of local governments to finance infrastructure, public services, or other government expenditures outside the formal budget. Although these liabilities are legally corporate rather than government obligations, investors have often treated them as implicitly backed by local governments, creating moral hazard. As part of efforts to "clean up" hidden debt, China's Ministry of Finance has authorized provincial governments to issue explicit local government refinancing bonds to replace qualifying LGFV liabilities, converting implicit obligations into explicit government debt. "Why China Is Hoping $1.6 Trillion Can Fix Its Hidden Debt Problem," *Bloomberg*, April 16, 2025; Cheng Siwei et al., "China's Economy Hostage to Local Governments' Hidden Debts," *Nikkei Asia*, August 23, 2023.

Falling Credit Demand Despite Low Rates Sends a Warning Signal

In 2026, China's sizable debt burden continued to weigh on the financial system. Bank profitability remained historically compressed and credit demand weakened significantly, despite exceptionally low interest rates.[68] Lending dropped precipitously in the first half of 2026. New renminbi (RMB) loans totaled 10.7 trillion ($1.6 trillion), a 17 percent drop from the same period in 2025.*[69] Total social financing (TSF),† a broad measure of credit in China's economy, grew just 7.4 percent in June, its slowest pace on record and well below the 12 percent average in the five years before COVID.[70] These declines come even though the People's Bank of China (PBOC) has held benchmark rates at record lows for more than a year, with the one- and five-year loan prime rates at 3.0 and 3.5 percent, respectively.[71] China announced it would inject RMB 290 billion ($42.8 billion) into three state banks to shore up capital levels, following similar moves last year.[72]

Competition over shrinking credit demand, combined with central government direction to roll over bad loans on longer time horizons, has squeezed bank profit margins such that roughly 90 percent of listed banks now fall below the industry standard profitability threshold.[73] Official figures likely understate the problem. Chinese authorities reported a nonperforming loan ratio of 1.5 percent, but some independent estimates put the real figure closer to 10 percent.[74] Thin margins leave banks less able to absorb bad loans and build capital to lend. While heavy state control substantially reduces the risk of an immediate liquidity crisis, the deeper problem is a persistent drag on growth as banks devote more capital to rolling over existing debt rather than financing new, productive activity.

Chinese officials have cast slower credit growth as a deliberate transition from bank lending toward "direct financing" through stocks and bonds—suggesting credit is being allocated in the economy via more market-based mechanisms.[75] This claim does not hold up under scrutiny. Government bonds comprise about 85 percent of direct financing, and 70 percent of those are held by commercial banks; equity financing accounts for a mere 3 percent.[76] In other words, under this supposed transition of the financial system, credit is held and distributed largely by the same state-controlled or influenced lenders and it goes largely to the same government destinations.[77]

Stable Employment Figures Mask Slowing Wage Growth and Rising Job Insecurity

China's headline urban unemployment rate changed little through 2025, but beneath this apparent stability, job quality deteriorated and structural strains intensified. The reported urban unemployment rate, which surveys only a narrow subcomponent of overall unemployment, continues to hover around 5 percent, remaining conveniently below Beijing's official target of around 5.5 percent, while

*Unless otherwise noted, this section uses the following exchange rate throughout: $1 = RMB 6.78.

†Measured since 2011, TSF, or "aggregate financing to the real economy" is a broad measure of credit and liquidity that reflects fundraising by Chinese non-state entities. "FACTBOX-What Is China's Total Social Financing Indicator?" *Reuters*, November 13, 2012.

authorities claimed to exceed their target of creating 12 million new urban jobs in 2025 by more than half a million.[78] Despite these supposed gains, average nominal wages rose just 4.3 percent from 2024 to 2025—well below the 6 to 10 percent annual growth common earlier in the decade—as intense price competition and shrinking profit margins limited firms' ability to raise pay.[79]

Youth unemployment also remains elevated. Despite a 2024 methodological revision excluding students from the official measure, the unemployment rate for urban 16- to 24-year-olds reached 18.9 percent in August 2026, roughly three times the headline unemployment rate.[80] At the same time, China's transition toward advanced manufacturing, AI, and other high-technology industries has reshaped labor demand faster than many workers can adapt.[81] Rapid adoption of automation and AI is reducing demand for routine manufacturing, administrative, and other white-collar jobs while increasing demand for specialized technical skills, widening labor market mismatches.[82] Although these sectors are intended to generate higher-value employment, they have failed to absorb the country's growing pool of educated workers, including the 12.2 million higher education graduates entering the labor market in 2025.[83]

Beijing portrays automation as compatible with long-term productivity gains and job creation (see textbox below); however, weak labor demand and technological displacement are pushing more workers into "flexible" employment in the "gig" economy. This includes white-collar workers from traditionally professional occupations, such as software engineers, financial analysts, and healthcare workers.[84] In 2025, more than 200 million people worked flexible jobs, including roughly 84 million platform workers,* according to Chinese government estimates.[85] In 2026, that number is expected to reach approximately 320 million, roughly 44 percent of the workforce.[86] While flexible employment helped absorb displaced workers, its lower and less stable earnings, limited career advancement, and weaker social protections have contributed to underemployment and labor insecurity, potentially undermining Beijing's efforts to boost household consumption by encouraging precautionary saving.†[87]

China's View on AI Productivity and Labor Displacement

China treats AI as a "general-purpose technology" that will boost total factor productivity (TFP) and enhance industrial competitiveness. (For more on China's strategy to deploy AI as a general-purpose technology, see "China's 15th FYP: Technology Dominance and Security Priorities and Trajectory" below.) At the same time, Beijing acknowledges short-term frictions around unemployment. A study by Chinese scholars at Capital University

*Platform workers are individuals who obtain employment through digital platforms that connect service providers with customers. In China, this category includes ride-hailing drivers for DiDi Chuxing, food delivery couriers for Meituan and Ele.me, and workers engaged in other app-based delivery, logistics, and on-demand service occupations.

†Many gig workers are rural-to-urban migrants employed outside the locality of their registered household (hukou). Because China's hukou system ties many social benefits (pensions, healthcare, unemployment insurance, and other public services) to local registration, migrant platform workers often have weaker access to social protections than local residents, contributing to greater income insecurity and precautionary saving. Yizhi Xu et al., "Reforms to Reduce China's High Household Savings," *International Monetary Fund*, December 2025, 4.

China's View on AI Productivity and Labor Displacement—*Continued*

of Economics and Business and Wuhan University found that "AI serves as a crucial TFP driver in China and may help mitigate the risks associated with the country's aging population and the potential middle-income trap."[88] However, in a 2019 study, Chinese researchers raised concerns that roughly one-third of Chinese workers (around 278 million people) could be displaced by automation by 2049, with agriculture, manufacturing, construction, and transport most affected.[89] A separate survey by Tencent Research Institute also found that 40 percent of its respondents are concerned about their roles being replaced by AI.[90]

The Chinese government has pursued a number of policies to balance AI's pains with its gains. In 2025, the NDRC issued guidance framing AI as a net positive for employment, as the state builds training, matching, and safety net infrastructure alongside China's AI industrial growth.[91] An August 2025 "AI+ Initiative"—a national strategy to integrate AI across various sectors—also seeks to "actively exploit AI's role in creating new jobs and empowering traditional job positions."[92]

These policy frames are beginning to show up in practice. Chinese courts have ruled against companies that dismissed workers citing AI automation. A Hangzhou court ordered $38,000 in compensation for an unlawful AI-related firing, while a Beijing arbitration court ruled that companies must retrain displaced staff for new roles rather than simply cut them.[93] State media framed these rulings as a warning that businesses benefiting from AI must also bear responsibility for protecting workers' jobs.[94]

Anti-Corruption Campaign Picks Up Steam

While Xi Jinping's military purges have received much attention, Beijing is also engaged in a widening purge of senior financial officials. Court records indicate extensive and longstanding corruption allegations among various senior financial regulators and executives at state-affiliated banks who have been dismissed since 2022 (see Table 2). Yet many of the purges also involve allegations of violating Party discipline, failing to implement Central Committee directives, and undermining efforts to control financial risk.[95] (For more on China's military purges, see Chapter 2, "U.S.-China Security and Foreign Affairs (Year in Review).") For example, authorities accused former Bank of China Chairman Liu Liange of implementing Central Committee decisions "half-heartedly" and neglecting his responsibility to prevent financial risks before detailing allegations that he accepted bribes.[96] The campaign therefore appears to be serving two objectives at once: (1) rooting out entrenched corruption in China's state-dominated financial system, and (2) enforcing Party discipline over how regulators and bankers direct capital and manage financial risk. This convergence has become particularly salient since Beijing's 2023 financial sector restructuring strengthened direct Party oversight of financial policymaking.[97]

Table 2: High-Level Officials in Financial Sector Charged

Year	Name	Position	Criminal Charge	Sentence
2022	He Xingxiang	Former Vice President, China Development Bank (CDB)	Bribery; illegally issuing financial instruments; illegally granting loans; concealing overseas deposits	20 years imprisonment
2022	Cai Esheng	Former Vice Chairman, China Banking Regulatory Commission (CBRC)	Bribery; accepting bribes through abuse of influence; abuse of power	Death with two-year reprieve
2022	Tian Huiyu	Former Party Secretary and President, China Merchants Bank	Bribery; abuse of power by personnel of a state-owned company; trading on undisclosed information; insider trading and divulging insider information	Death with two-year reprieve
2023	Fan Yifei	Former Deputy Governor, PBOC	Bribery	Death with two-year reprieve, subsequently life imprisonment without commutation or parole; property confiscated
2023	Liu Liange	Former Party Secretary and Chairman, Bank of China	Bribery; illegally issuing loans	Death with two-year reprieve; also ten years for illegal lending; political rights revoked for life and property confiscated
2023	Li Xiaopeng	Former Party Secretary and Chairman, China Everbright Group	Bribery	15 years imprisonment
2023	Zhou Qingyu	Former Vice President and former Discipline Inspection Secretary, China Development Bank	Bribery	15 years imprisonment
2024	Zhang Hongli	Former Executive Vice President, Industrial and Commercial Bank of China (ICBC)	Bribery	Death with two-year reprieve; political rights revoked for life and property confiscated

Table 2: High-Level Officials in Financial Sector Charged—*Continued*

Year	Name	Position	Criminal Charge	Sentence
2024	Lou Wenlong	Former Vice President, Agricultural Bank of China; previously senior CBRC regulator	Bribery	Life imprisonment; political rights revoked for life and property confiscated
2025	Lin Jingzhen	Former Executive Vice President, Bank of China	Bribery	No final sentence; expelled from Party, benefits revoked, and referred for prosecution
2025	Wang Jianjun	Former Vice Chairman, China Securities Regulatory Commission (CSRC)	Bribery	Life imprisonment; political rights revoked for life and property confiscated
2026	Xu Yiding	Former Vice President, Agricultural Development Bank of China	Bribery	No final sentence; expelled from Party, dismissed, and referred for prosecution
2026	Fang Xinghai	Former Vice Chairman, CSRC	Bribery	No final sentence; under investigation
2026	Zhou Liang	Former Deputy Director, National Financial Regulatory Administration (NFRA)	Bribery	No final sentence; under investigation
2026	Yi Huiman	Former Chairman, CSRC; former Chairman, ICBC; later Deputy Director, CPPCC Economic Committee	Bribery	Expelled from Party and public office and referred for prosecution

Source: China's Central Commission for Discipline Inspection.

China's External Economic Relations

In 2026, China has sharpened and broadened its economic statecraft toolkit, even as it softened the impact of its critical minerals and rare earth export controls. The CCP has long believed that global economic conditions would eventually shift into a more unfavorable and uncertain environment for Chinese exports and investment.[98] Xi perceives that period is well underway as countries begin to erect barriers designed to protect their domestic manufacturing from China's overcapacity.[99] Beijing has been working to expand the range of policies, legal tools, points of economic leverage, and capacity for retaliation available to China to address geo-economic tensions.[100] China's extra-territorial critical mineral and rare earth controls in

2025 were a watershed development, demonstrating its ability to effectively wield export controls and supply chain dependencies as global economic leverage.[101] Developments in 2026 indicate that China plans to continue expanding its tools for economic statecraft, economic coercion, and technology self-reliance while retaining its traditional toolkit involving access to its home market.

China Shock 2.0 Deepens

Discussed at length in the Commission's 2025 Annual Report to Congress, China's domestic economic imbalances, fueled by substantial government intervention in favor of targeted industries, generate excess production far beyond domestic demand, which flows outward as cheap goods that undercut competitors. According to a 2026 report, between 2005 and 2024, Chinese firms received from three to eight times more government support than those in Organisation for Economic Co-operation and Development countries.[102] Furthermore, these subsidies are linked to 60 percent of Chinese firms' gains in global market share.[103] In 2026, this export flood—often referred to as "China Shock 2.0"—continued to undermine the manufacturing sectors in both developed and emerging economies. The resulting harm has prompted alarm and protective measures from China's trade partners. Beijing has calibrated its response: it has retaliated aggressively against many developed economies while granting concessions and exercising greater restraint toward countries that supply its commodities, offer geopolitical value, or represent opportunities for future export growth.

China Shock 2.0 Threatens Both Emerging and Developed Economies

China's flood of low-cost, subsidized exports has continued unabated. With domestic demand too weak to absorb its excess production, China posted a record $1.2 trillion trade surplus in 2025.[104] In 2026, China's total exports increased 19.3 percent over the first eight months of the year, to $2.9 trillion.[105] Chinese exports to Southeast Asia, Latin America, and Africa grew 25.8 percent, 13.6 percent, and 25.7 percent year-on-year, respectively, through August on top of already enormous trade surpluses (see Table 3).

Table 3: China's Trade Surplus Swamps Emerging Markets, Year-to-Date August 2026

	ASEAN	Latin America	Africa
China's Total Exports	$546.0 billion	$221.4 billion	$177.0 billion
China's Trade Surplus	$230.0 billion	$22.2 billion	$80.6 billion
China's Year-on-Year Export Growth	25.8%	13.6%	25.7%

Source: China's General Administration of Customs, via Haver Analytics.

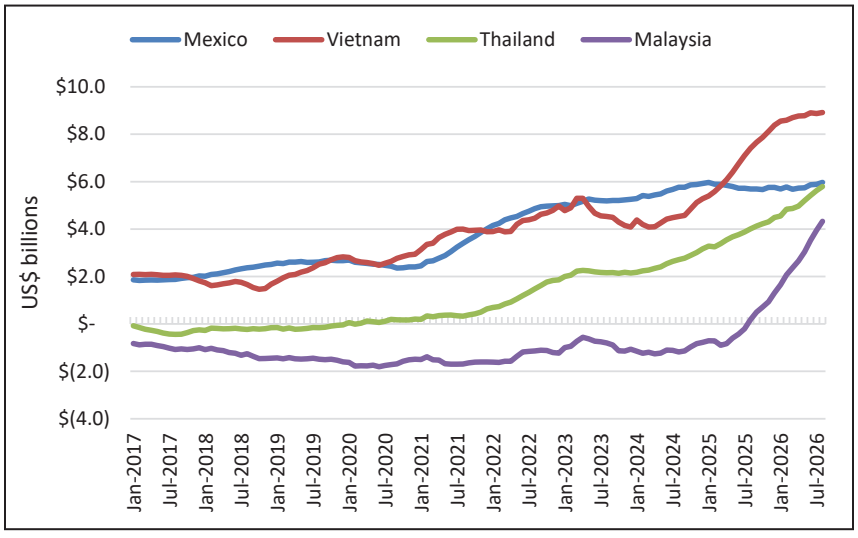
This flood of exports is threatening emerging economies' ability to move up the value chain and increasingly bringing China into direct competition with developed economies both at home and in third country markets.

Emerging Economies: Fewer Opportunities to Advance Beyond Low-Level Assembly

In the past few years, emerging economies have begun to absorb the brunt of China's exports, limiting domestic development opportunities. As China moved up the value chain into manufacturing higher-end goods, it has held onto production of low-end and intermediate goods as well. These goods are flooding into emerging economies, causing local factories to shut down and displacing workers. Thailand's trade deficit with China grew 59 percent year-on-year through July 2026 as imports of machinery and components grew rapidly (see Figure 3).[106] Factory closures in Thailand outnumbered new openings in the first quarter of the year, with the trends especially apparent among small and medium-sized enterprises.[107] Manufacturing employment in Indonesia and Vietnam was growing at a healthy pace prior to the COVID-19 pandemic.[108] Since then, growth has slowed or stalled as China has ramped up exports to these markets.[109] Labor-intensive industries—including furniture, footwear, and plastics—have experienced the worst slowdowns, compounded by rising energy costs.[110] Factories in the Philippines laid off 217,000 workers in March 2026, while over 100 furniture factories in Malaysia closed in recent months.[111] Mexico's national textile chamber estimates that seven of every ten fabrics and garments sold in its street markets are illicit and have cost the industry $8.8 billion, connecting the figure to Chinese products illegally rerouted through Vietnam and other countries to evade tariffs.[112] Chinese exports, having already devastated Mexico's textile industry, are now threatening its steel and automobile industries.[113] Manufacturing employment in Mexico declined 2 percent in 2025 as automobile factories closed under pressure from imported Chinese vehicles.[114] Chinese car brands' share of new vehicle sales in Mexico rose from 14 percent in the first half of 2025 to 17 percent in the first half of 2026.[115] Mexico imposed a sweeping set of tariffs at the beginning of 2026, including 50 percent tariffs on Chinese autos, but Chinese car brand sales continued to grow nearly 30 percent through June.*[116] (For more on the impact of Chinese exports to Latin America, see Chapter 4, "China's Predatory Diplomacy in Latin America: Broken Promises, Harmful Practices.")

*Chinese automakers appear to have front-loaded shipments ahead of the new tariffs, but imports fell by 43 percent year-on-year from January to May 2026, so Chinese vehicle sales may start to decline. In September, Chinese regulators issued new rules for its automakers, instructing them to avoid unfair price competition and misleading advertising and protect the reputation of Chinese brands in their operations abroad. The move likely reflects Beijing's awareness of growing pushback on Chinese auto exports and a desire to avoid more stringent restrictions and tariffs. "China Issues Guidelines for Automakers' Overseas Operations," *Reuters*, September 1, 2026; Emily Green, "Chinese Car Sales in Mexico Surge Despite New Tariffs," *Reuters*, July 20, 2026.

Figure 3: China's Trade Surplus with Manufacturing Competitors Grows, January 2017–August 2026, Trailing 12-Month Average

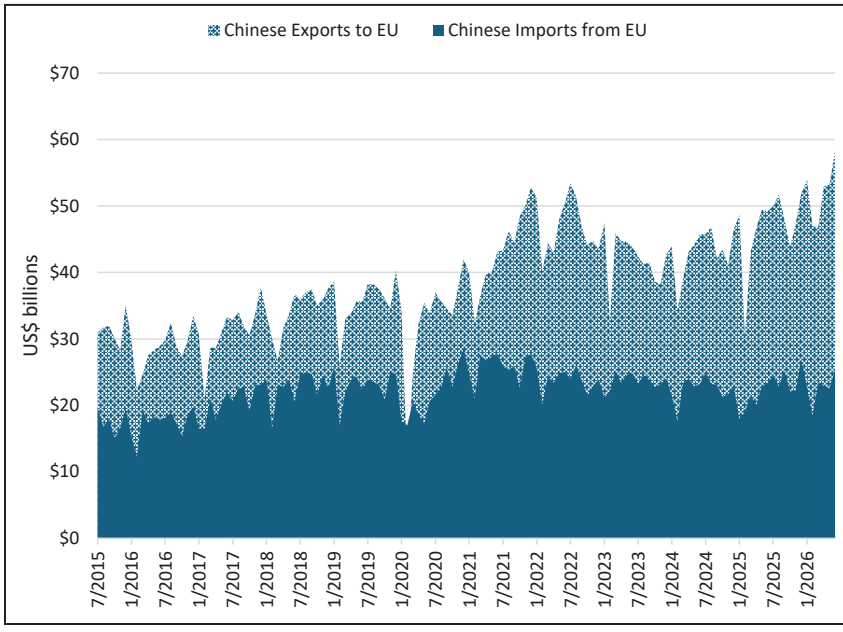


Source: China's General Administration of Customs, via Haver Analytics.

Developed Economies: Direct Competition Eroding Profit Margins and Taking Market Share

China Shock 2.0 is simultaneously hitting developed countries, eroding market share away from high-tech manufacturing industries at home and contributing to job losses. The Export Similarity Index (ESI), a measurement of how much two economies' export baskets overlap, shows how China's export basket now resembles that of developed economies much more than during the first China Shock, a reflection of how China has moved into higher-value-added manufacturing.[117] China's high-tech exports present the greatest challenge to countries including Germany, Japan, and South Korea in sectors like chemicals, machinery, and equipment.[118] In each of these countries, manufacturing capabilities in a few highly specialized sectors and firms contribute a relatively high share of economic output and exports, making them even more vulnerable to disruption from China Shock 2.0.[119] Developed economies are hit on multiple fronts. At home, firms must contend with greater competition from subsidized Chinese goods if tariffs are still too low to constitute a meaningful barrier to imports.[120] They also risk losing their traditional export markets (including China), as end customers purchase "good enough" Chinese goods, sold at lower costs due to China's market distortions. Rhodium Group estimated that 12 percent of G7 manufacturing exports could be exposed to China's growing market share by 2030.[121] The EU lost almost one million manufacturing jobs between 2019 and 2023.[122] Competition from Chinese firms is causing layoffs among Germany's Mittelstand, its high-tech manufacturing base made up of specialized, medium-sized firms.[123] One report estimated that the country is losing over 10,000 industrial jobs per month.[124]

Figure 4: China's Trade Surplus with the EU Grows, 2015–2026



Source: China's General Administration of Customs, via Haver Analytics.

China's Managed Currency Helps Perpetuate Flood of Exports

China's currency controls limit the appreciation of the RMB and contribute to its persistent and outsized trade surpluses. China manages the value of the RMB within a fixed trading band, ostensibly to a basket of currencies. The PBOC announces the midpoint of the trading band and maintains the peg by buying and selling currency either directly or through instructions to state-owned commercial banks.[125] By definition, countries that save more than they invest must run a current account surplus, the largest component of which is typically a country's trade balance.*[126] However, a country with a persistent trade surplus like China should see its currency appreciate as foreign buyers purchase the currency needed to pay for imports. Currency appreciation can cause exports to become relatively more expensive compared to trading partners' exports, and the trade surplus falls as a result. Despite China's trade surplus reaching $575 billion for H1 2026 and on track to exceed $1.2 trillion in 2026, the RMB is undervalued relative to the currencies of its trading partners.[127]

*China's present-day trade surplus is often compared to Japan's situation in the 1980s as the country became a leading exporter of electronics and other manufactured goods. China's high savings rate has persisted for longer due to a poor social safety net, weak wage growth, and negative wealth effects from the property market downturn. This has the added effect of depressing Chinese demand for imports, exacerbating the trade surplus. Erik Green and Olivia Parker, "China's Consumption Problem," *International Institute for Strategic Studies*, February 19, 2026; Alicia García-Herrero and Jianwei Xu, "Will China's Economy Follow the Same Path as Japan's?" *Bruegel*, February 27, 2025.

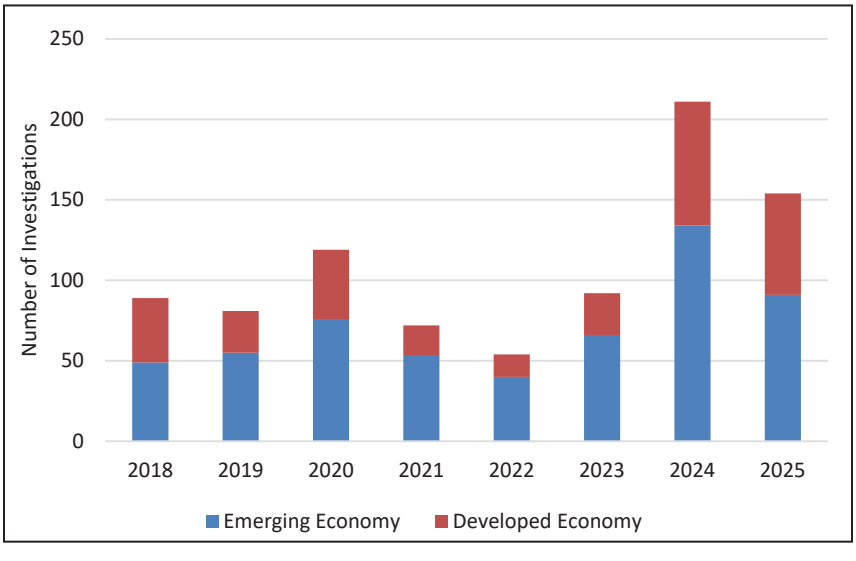
China's Managed Currency Helps Perpetuate Flood of Exports—*Continued*

The International Monetary Fund estimated the RMB's real exchange rate to be undervalued by around 16 percent, while Brad Setser at the Council on Foreign Relations estimated the RMB is up to 35 percent undervalued after adjusting for rising gold imports and understated investment income.[128] In July 2026, the U.S. Department of the Treasury declined to designate China as a currency manipulator, although China remains on a watchlist with nine other U.S. trading partners due to a lack of transparency around its currency management policies.[129]

Pushback on China Shock 2.0 Grows

Countries are intensifying efforts to protect their manufacturing bases from China's export flood. At a meeting of G20 finance ministers in August 2026, U.S. Treasury Secretary Scott Bessent's chair statement called on countries to address global imbalances for their impact on global growth, supply chain security, and economic resiliency.[130] All G20 members present except China agreed with the statement.[131] WTO members across emerging and developed economies initiated 154 antidumping and countervailing duty (AD/CVD) investigations against China in 2025 (see Figure 5).[132] India accounted for 30, the greatest number of any individual economy.[133] Even Russia, a staunch Chinese ally, initiated two antidumping cases.[134]

Figure 5: New AD/CVD Investigations Initiated Against China by Type of Reporting Economy, 2018–2025



Source: World Trade Organization, "Trade Remedies Data Portal."

China's trade partners are also exploring new response pathways, including regulations, tariffs, and quotas. EU measures have sought to protect its advanced manufacturers from Chinese exports. The EU has investigated Chinese rail, wind turbine, security scanning, and e-commerce companies under its Foreign Subsidies Regulation, introduced in 2023 to prevent third-party country subsidies from distorting domestic competition.*[135] In 2025, following an investigation of China's own preferential procurement policies for its domestic companies, the European Commission excluded Chinese medical device firms from public procurement for tenders over 5 million euros ($5.68 million).[136] Emerging economies have also employed a variety of targeted quotas and tariff barriers. Mexico introduced heightened tariffs effective January 2026 on apparel, automobiles, steel, and other products, impacting only those countries with which it does not maintain a free trade agreement, including China.[137] Other countries in Southeast Asia have implemented or are exploring similar tariffs targeting Chinese exports.[138] Thailand imposed a new tariff in 2026 on low-value packages in an effort to slow the flow of imports from Chinese e-commerce platforms.[139] In the Western Hemisphere, Brazil, Canada, and Chile have also extended tariff-rate quotas or implemented tariffs on steel imports.[140]

EU leaders have begun to consider more widespread measures to protect its manufacturing sector. The EU trade remedy tariffs of 17 to 35.3 percent on Chinese EV imports, instituted in 2024, have not protected Europe's auto sector from bearing the brunt of China's industrial policy.[141] Chinese car exports to Europe rose 26 percent in 2025 despite the tariffs; imports of Chinese hybrid vehicles, which the EU tariffs excluded, rose 155 percent.[142] This trend has continued in 2026. Through July, the value of China's total passenger vehicle exports to the EU rose 90 percent year-on-year, nearly reaching the 2025 total of $19.1 billion.[143] Initially reluctant to impose more widespread tariff measures due to concerns of retaliation from China, EU leaders have begun to reconsider.[144] At a meeting between EU Trade Commissioner Maros Sefcovic and Chinese Commerce Minister Wang Wentao in June 2026, the EU and China agreed to a joint monitoring mechanism for bilateral trade.[145] However, the EU has yet to implement some of its more aggressive proposals, including an instrument that would allow it to address systemic distortions from Chinese overcapacity rather than requiring industry-by-industry investigations.[146] In an October 2026 letter to the European Commission, France and Germany proposed new tools for diversifying supply chains, combating third country-induced systemic distortions, and addressing foreign non-tariff barriers as well as

*While the WTO specifically allows countervailing duties against subsidies, the EU determined that these rules do not cover subsidies provided by third-party countries: "existing WTO rules . . . are limited in scope, for reasons such as their focus on trade in goods, and face some challenges in view of transparency shortcomings and enforcement constraints. In the absence of comprehensive and effective multilateral rules capable of addressing the full range of distortions observed in the internal market, the EU considered it necessary to equip itself with an autonomous instrument to address distortions caused by foreign subsidies, while remaining open to future multilateral solutions." European Commission, *Commission Staff Working Document Accompanying the Document: Report from the Commission to the European Parliament and the Council on the Implementation and Enforcement of Regulation (EU) 2022/2560 of 14 December 2022 on Foreign Subsidies Distorting the Internal Market, in Accordance with Article 52(2) Thereof*, July 14, 2026, 4; U.S. Department of Commerce, International Trade Administration, "Regulations Improving and Strengthening the Enforcement of Trade Remedies Through the Administration of the Antidumping and Countervailing Duty Laws," 89 Fed. Reg. 20766 (March 25, 2024).

undervalued exchange rates—though not specifically naming China, clearly aimed at China.[147] While the details of the proposal and the likelihood of approval from the rest of the EU were unclear as of early October 2026, such a toolkit would enhance European countries' ability to respond quickly to market distortions caused by China's exports.

China's Counteractions: Tough on Developed Economies, More Calibrated on Others

China's responses to its trade partners' efforts to protect domestic manufacturing and achieve other strategic aims have varied by target. Beijing retaliates most aggressively where it sees little prospect of shifting a country or bloc's alignment, as is the case for the United States and the EU. In those cases, Beijing has demonstrated its willingness to escalate with sanctions, investigations targeted at companies from those jurisdictions, and export controls.[148] For instance, China responded to the United States' imposition of additional 20 percent tariffs in March 2025 with antidumping investigations of U.S. exports, export and import controls, and tariffs of its own.[149]

By contrast, Beijing has shown greater flexibility toward emerging economies, often absorbing product-level measures and offering concessions. It expanded zero-tariff treatment to 53 African countries in 2026 and did not retaliate after South Africa imposed 74.98 percent tariffs on its structural steel exports in March.[150] Less than two months later, the Chinese Embassy in Pretoria hosted a seminar highlighting economic cooperation and China's zero-tariff policy for Africa.*[151] Manufacturing powerhouses in Southeast Asia have imposed a number of protective measures targeting imports of low-value goods, electronics, and automobiles, but China's response has been muted so far.[152] China upgraded its free trade agreement with ASEAN in October 2025, and state-run media have also touted the benefits of the Regional Comprehensive Economic Partnership, a separate free trade agreement that includes all ASEAN countries except Timor Leste.[153] Turkey imposed additional tariffs of 40 percent on Chinese EVs in 2024, and China's primary response to date has been a WTO challenge.[154] The WTO adjudicated in China's favor in July 2026, and Turkey and China jointly requested an extension on next steps to October 27, 2026.[155] If Turkey appeals, the decision will be largely unenforceable given the stalled WTO appellate system, and as of the "pens down" date for this publication, China has not taken any other retaliatory actions.[156]

Three sometimes overlapping motives appear to drive China's varied responses. First, geopolitical positioning: for smaller markets, China seems more interested in bilateral goodwill, "Global South" alignment, and positive regional dynamics than marginal export revenue.[157]

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*Chinese state media contrasted the temporary lapse of the U.S. African Growth and Opportunity Act (AGOA) with China's newly announced zero-tariff policy, calling AGOA "self-serving" while presenting China's zero-tariff policy as offering "hope" to Africa's industries. The United States extended AGOA for two more years in September 2026. Witney Schneidman, "AGOA Was Extended for Two Years—Now the Real Work Begins," *Brookings Institution*, September 17, 2026; "Interview: AGOA Hampers Africa's Industrialization amid Political Motives, Says Kenyan Scholar," *Xinhua*, March 18, 2026.

Second, Beijing has taken a lighter touch with many of the economies that supply China's critical inputs like Brazilian iron ore and soybeans, Indonesian nickel, and South African ores and metals.[158] Africa's exports to China are primarily commodities, including crude oil and minerals.[159] Aggressive retaliation could threaten Beijing's diversification and economic resilience goals as well as its access to key inputs for the manufacturing sector.

Third, muted retaliation discourages emerging economies from joining a coordinated response as they weigh China's ability to retaliate. China has responded to many countries' restrictions on Chinese imports through tariff concessions, market access offers, and diplomatic engagement. By contrast, it escalates against the United States and the EU to demonstrate that neither the world's largest economy nor a bloc of 27 can establish escalation dominance in a tit-for-tat confrontation.[160] Emerging economies see the potential costs of escalation and realize they must choose their battles carefully.* In this way, China hopes to keep its aggregate access to global markets open given the importance of exports to its economic model.

China Seeks to Exploit U.S. Trade Tensions to Expand Relationships with Third Countries

Beijing is seeking to exploit concerns about uncertainty caused by U.S. trade policy to promote itself as the upholder of the international economic order. Ironically, China has trumpeted its support for multilateralism and the rules-based trading system, free trade, and win-win cooperation. Over the past 18 months, China's senior leaders, including General Secretary Xi, Premier Li Qiang, and Vice Premier He Lifeng, have repeated these themes in meetings at the World Economic Forum and other regional meetings.[161] At the World Economic Forum's annual summer forum in Dalian in June 2026, Premier Li notably dismissed the threat of China Shock 2.0 as overblown and instead said that domestic investment and new market creation presented a "China Opportunity 2.0."[162] State-run newspaper *Global Times* noted that China's imports grew 22 percent in the first half of 2026.†[163]

Whether China's rhetoric has been persuasive is not clear, but China has received many high-level engagements with other countries, including U.S. allies and partners, to promote trade and investment cooperation (see Table 4). China signed new agreements that included trade and investment with the UK and Spain.[164] Canadian Prime Minister Mark Carney's visit to Beijing—the first by a Canadian Prime Minister to China since 2017—yielded a trade agreement and several memoranda of understanding (MOUs) on other areas of cooperation.[165] Beijing also hosted leader-level visits from Ireland, Finland, and South Korea.[166]

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*Some developed countries have reached agreements with China when beneficial to their own economies. Canada slashed its EV surtax to a managed quota in exchange for China cutting canola tariffs. Its exports to China, which are dominated by commodities like crude oil, liquified propane, and metals, grew 30 percent year-on-year through June 2026. Lisa Xing, "Amid Trump Trade War, Canada's Exports to China up 30% in First Half of 2026," *CBC*, September 14, 2026; Maria Cheng, "Canada, China Slash EV, Canola Tariffs in Reset of Ties," *Reuters*, January 16, 2026.

†Notably, China's total imports grew less than 1 percent in 2025. China's General Administration of Customs, via Haver Analytics.

Table 4: China's Recent High-Level Trade and Investment Negotiations

Date	Country	Officials	Outcomes
January 5, 2026	South Korea	Xi Jinping and President Lee Jae Myung	Over 15 MOUs on environmental cooperation, technology partnerships, and export promotion. Agreed to conclude negotiations on investment aspects of Korea-China Free Trade Agreement this year.
January 14–17, 2026	Canada	Xi Jinping and Prime Minister Mark Carney	Agreement to collaborate on new energy technology and expand Chinese investment in Canadian auto industry, and preliminary measures for China to lower tariffs on Canadian agricultural goods.
January 27, 2026	Finland	Xi Jinping and Prime Minister Petteri Orpo	11 commercial agreements between Finnish firms and Chinese counterparts. Additional MOUs signed on new energy cooperation and other sectors.
January 29, 2026	UK	Xi Jinping and Prime Minister Keir Starmer	Commitments to deepen bilateral trade in services, expand UK access to the Chinese market, and invite additional Chinese direct investment in the UK.
February 25, 2026	Germany	Xi Jinping and Chancellor Friedrich Merz	Soft commitments for bilateral investment and trade in high-tech goods and agreements, including agricultural protocols.
April 11–15, 2026	Spain	Xi Jinping and Prime Minister Pedro Sanchez	Limited Chinese concessions on agricultural imports and MOUs on technology transfers, joint ventures, and capacity building.
April 15, 2026	Vietnam	Xi Jinping and General Secretary To Lam	32 cooperation documents including for a cross-border economic cooperation zone, working group on supply chain cooperation, and phytosanitary requirements for agricultural exports.
May 25, 2026	Serbia	Xi Jinping and President Alexandar Vucic	Agreements for cooperation, including in AI, digital economy, technological development, and food exports.

Table 4: China's Recent High-Level Trade and Investment Negotiations—*Continued*

Date	Country	Officials	Outcomes
June 25, 2026	Bangladesh	Xi Jinping and Prime Minister Tarique Rahman	13 MOUs, including increased Chinese support for Bangladeshi infrastructure projects and other investment priorities.
July 17, 2026	Thailand	Xi Jinping and Prime Minister Anutin Charnvirakul	Five MOUs on science and innovation cooperation in nuclear energy, education exchange, space, and other joint research initiatives.
August 18–19, 2026	Ecuador	Xi Jinping and President Daniel Noboa	Agreements on promoting cooperation in trade and investment, ensuring effective implementation of the bilateral free trade agreement, and refraining from taking unfair or discriminatory economic and trade measures against each other.
August 24, 2026	Jordan	Xi Jinping and King Abdullah II	Agreements for cooperation in trade and supply chains.
August 31, 2026	Kyrgyzstan	Xi Jinping and President Sadyr Zhaparov	More than 20 cooperation documents in science and technology, education, people-to-people exchanges, and media.
September 2, 2026	Egypt	Xi Jinping and President Abdel Fattah El-Sisi	Agreements on BRI cooperation, expanding a joint economic zone, increasing bilateral local currency trade, promoting people-to-people exchanges, and increasing technology cooperation.
September 12, 2026	India	Xi Jinping and Prime Minister Narendra Modi	General statements on expanding trade, resolving economic issues, increasing the number of people-to-people exchanges, and strengthening both sides' support for multilateral organizations like BRICS.

Note: Xi Jinping met with leaders from Uzbekistan and Mongolia on the sidelines of the Shanghai Cooperation Organization in August.
Source: Various.[167]

U.S.-China Economic Relations: A Trade Détente Masks Continued De-Risking

Over the past year, U.S.-China trade relations stabilized after a contentious 2025, when both sides imposed escalating tariffs on each other and China effectively froze soybean purchases from U.S. suppliers for several months.[168] Beijing then ratcheted up export controls on rare earth elements and related products, claiming that broad international controls on commodities were justified by "national security" concerns.[169]

Still, both countries indicated an interest in stability. The United States and China reached an agreement in May 2025 to unwind a portion of their retaliatory tariffs.[170] President Donald Trump and General Secretary Xi agreed to reset the tariff truce at a meeting in Busan, South Korea, in October 2025.[171] According to the U.S. readout of the meeting, China made a number of other pledges, including:*

- To stem fentanyl precursor exports in exchange for lowering the United States' fentanyl-related tariffs from 20 to 10 percent.[172]
- To resume soybean shipments from the United States with specific goals through the end of 2025 and for 2026–2028.† [173]
- To suspend implementation of a subset of rare earth export controls and issue licenses to restart the flow of critical minerals, rare earths, and related products to U.S. purchasers.‡ [174]

As of October 2026, these data indicate less than full compliance with the terms of the existing presidential agreements. U.S. buyers have continued to experience difficulties in purchasing critical minerals from China due to licensing delays and export controls that have made some rare earths "nearly unobtainable."[175] China's total exports of dysprosium, lutetium, scandium, terbium, and yttrium to the United States fell to zero in May 2026. Average monthly exports from January to May 2026 were only 20 metric tons, compared with a monthly average of 75 metric tons for the full year in 2024.[176] In September 2026, U.S. Ambassador to China David Perdue warned that China has "weaponized" its dominance over critical minerals while also expanding domestic regulations that could criminalize actions taken by foreign entities to diversify away from Chinese supply

*The Chinese Ministry of Commerce's readout of the meeting was far less detailed than the United States'. For example, China only noted its commitment to increase purchases of agricultural products rather than giving hard purchase targets. China's Ministry of Commerce, 商务部新闻发言人就中美吉隆坡经贸磋商联合安排答记者问 [Ministry of Commerce Spokesperson Response to Reporter Questions Regarding the U.S.-Kuala Lumpur Trade Arrangements], October 30, 2025; China's Ministry of Foreign Affairs, *President Xi Jinping Meets with U.S. President Donald J. Trump in Busan*, October 30, 2025.

†Notably, China's soybean purchase commitments further strengthen South American suppliers' share of its market. The agreement commits China to purchase at least 25 million metric tons of U.S. soybeans each year through 2028; this is below both the preceding five-year (29 million metric tons) and ten-year (27 million metric tons) average annual purchases by China, skewed by very low imports in 2018 at the start of the first trade war. Joana Colussi and Michael Langemeier, "U.S.–China Soybean Deal: Comparing Past Export Levels and Global Market Impacts," *Purdue University Center for Commercial Agriculture*, November 14, 2025.

‡China did not agree to roll back these export controls. The approach allows China to leave the legal framework in place and to continue to build up its experience with and capacity for continued imposition of its broad critical minerals export control regime and elements of its rare earth export controls. Aidan Powers-Riggs, Brian Hart, and Matthew P. Funaiole, "The U.S.-China Trade Truce Has Not Solved the Gallium Problem," *Center for Strategic and International Studies*, May 11, 2026; "China Rolls Back, Suspends Retaliatory Measures Against Some US Entities," *Reuters*, November 5, 2025.

chains.[177] China has not fulfilled a promise to increase its purchases of U.S. agricultural products, which the White House claimed included a commitment of at least $17 billion annually, not including soybeans.[178] While it has met its soybean purchase commitments so far, China's other agricultural imports have barely risen through July 2026.[179] An airplane deal has also reportedly stalled as China made new requests for assurances that the United States would not restrict its access to servicing and spare parts in the future.[180]

The United States likewise reversed or paused various measures it had imposed on China, including the so-called "Affiliates Rule," a measure that would have substantially expanded Commerce Department Entity List controls by covering subsidiaries owned 50 percent or more by listed entities.[181] Separately, President Trump decided to allow licenses for sales of certain advanced semiconductors to China that had previously been prohibited.[182] Penn Wharton's latest customs-based estimate puts the effective U.S. tariff rate on Chinese goods at 22.8 percent in July 2026, down from 33.9 percent in January.[183] These figures measure customs duties as a share of actual import value.

The efforts to maintain stability and establish guardrails for economic tensions continued in 2026. The two presidents are set to meet four times in 2026.*[184] In May 2026, President Trump met General Secretary Xi in Beijing for a two-day summit.† Under the rubric of "constructive strategic stability based on fairness and reciprocity," the United States and China agreed to establish a U.S.-China Board of Investment to discuss investment-related issues and a U.S.-China Board of Trade to discuss bilateral trade in non-sensitive goods and work to resolve trade tensions.‡[185] China made additional commitments to resume purchases of U.S. agricultural products and airplanes and to address supply chain concerns related to exports of rare earth-related products.[186]

In September 2026, Xi made his first official state visit to the White House since 2015, meeting with President Trump and setting the stage for two additional meetings later this year. The United States and China agreed to extend last year's tariff truce two months from its original November 2026 expiration date and moved forward on operationalizing the Boards of Trade and Investment.[187] Each side pledged to review a list of non-sensitive imports from the other worth $30 billion for potential tariff reductions.[188] U.S. exports under review include agricultural goods, fish and seafood, logs and wood products, cosmetics, and medical devices, while U.S. imports under review include consumer products such as small ap-

*As was evident during the Commission's trip to China in July 2026, while both U.S. and Chinese sources include the phrasing "constructive strategic stability," the United States also emphasizes the underlying need for "fairness and reciprocity," while China instead focuses on cooperation. Edward Wong, "Trump's Sharp Turn on China: Embracing It as a Peer Power," *New York Times*, June 9, 2026.

†The summit covered a range of topics beyond economics and trade. For a discussion of outcomes surrounding issues of security and foreign affairs, see Chapter 2, "U.S.-China Security and Foreign Affairs (Year in Review)."

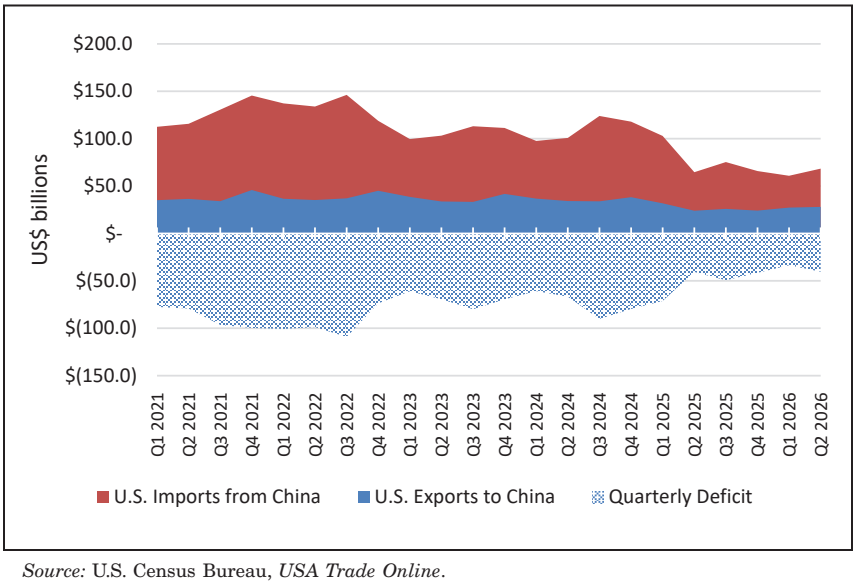
‡The 2026 Supreme Court decision striking down the president's authority to level tariffs under the International Emergency Economic Powers Act did not fundamentally alter the U.S.-China trade dynamic. The decision did not affect existing Section 301 tariffs covering a broad array of Chinese imports. The Administration has pursued tariff authority under other statutes, including for balance of payment imbalances under Section 122 of the Trade Act of 1974 and various other Section 301 investigations. William F. Burkhart, "Active Presidential Tariff Actions in 2026: Fact Sheet," *Congressional Research Service* (Report No. R49481), October 8, 2026.

pliances, toys, holiday decorations, and children's car seats.[189] China also agreed to purchase 10 million metric tons of coal from the United States in both 2027 and 2028.*[190] The two countries also established a new forum to discuss risks and benefits related to AI and a bilateral channel to report certain AI-related incidents.[191]

U.S.-China Trade Trends Show Immediate Response to Tariffs

U.S.-China bilateral trade slowed dramatically in 2025, as high tariffs accelerated some combination of supply chain diversification, transshipment, or diversion. Bilateral trade between the two countries fell nearly 30 percent in 2025 from $584 billion to $415 billion (see Figure 6). The slowdown continued in the first half of 2026; total trade with China fell 17 percent through June.[192] Compared with full year 2025 when trade in both directions dropped dramatically, declining imports from China contributed almost all of the decrease in the first half of 2026, while exports to China held steady.[193] As a result, the U.S.-China trade deficit declined 34 percent year-on-year.[194] Notably, semiconductor exports to China grew by over $600 million during this time frame, comprising 11 percent of all U.S. exports to China.[195] For the first time in recent history, Taiwan is set to overtake China in total bilateral goods trade with the United States, driven by rising demand for Taiwan's export of advanced AI hardware.[196]

Figure 6: Quarterly U.S.-China Bilateral Trade and Deficit, Q1 2021–Q2 2026



Source: U.S. Census Bureau, *USA Trade Online*.

However, bilateral figures alone paint only one component of the overall picture. U.S. trade statistics understate the real value of goods

*In 2025, the United States exported just below 1 million short tons of coal to China, a decline of 92 percent from 2024 exports of 13.1 million short tons. U.S. Energy Information Agency, *Quarterly Coal Report October–December 2025*, April 2026.

produced in China and transshipped through third countries as well as the persistence of Chinese-origin inputs in global supply chains. Illegal transshipment, whereby a product's country of origin is relabeled despite no substantial transformation to the product, contributes to lost tariff revenue and displaced domestic production.[197] Countries including Vietnam, Taiwan, and Mexico saw large increases in exports to the United States at the same time their imports of similar products from China grew.[198] A White House report released in August 2026 noted that estimates of transshipment range from $34.2 billion to $303 billion, reflecting both the variety of methodologies available and the opaque nature of the problem.[199] The White House Council of Economic Advisers estimated a midpoint figure of around $60 billion for 2025 data.[200] On the upper end, detailed supply chain data tracking facility-level product movements produce a figure as high as $303 billion.[201] This estimate likely incorporates both unlawful transshipment and tariff-avoidance strategies whereby Chinese firms move factories and production abroad.[202] This latter phenomenon is qualitatively different than transshipment but still gives the appearance of more diversified supply chains, even as the origin of much of value added remains under Chinese control.

While both countries continue to take measures to promote de-risking and reduce reliance on each other, their economies remain intertwined. Import statistics suggest that U.S. importers continue to prefer Chinese sourcing across many categories of imports. Out of 4,463 six-digit harmonized tariff schedule (HTS) codes the United States imported from China between January and June 2026, China accounted for over 50 percent of total imports for 385 of these products; it accounted for over 25 percent of total imports for 944.*[203] The products where total import value is both large and highly reliant on China include household and consumer goods, smartphones and printed circuits, and lithium-ion batteries.[204] And, as noted above, these metrics only account for final goods imported into the United States and do not include Chinese-manufactured components earlier on in the value chain. For example, India became the largest supplier of smartphones, including iPhones, to the United States in 2025, but upstream supply chains for electronic components, including semiconductors and printed circuit boards, still trace back to China-based manufacturers.[205]

U.S. Government Initiatives to Protect Supply Chains See Progress

The U.S. government has undertaken a concerted effort over the past several years to reduce reliance on Chinese critical minerals while proactively addressing supply chain risks in other sectors with new initiatives. These initiatives aim to encourage

*In comparison, the United States only has a similar level of dependence on Canada among its top trading partners. Of the five economies—Mexico, Canada, China, Taiwan, and Vietnam—with exports to the United States over $100 billion in the first half of 2026, Canada had 531 products that accounted for over 50 percent of total U.S. imports of that good. Mexico had 233, Vietnam had 45, and Taiwan had 33. In 2019, China was the world's dominant producer (defined as producing more than 50 percent of global exports within a six-digit product category) of six times as many products as the United States, Japan, or any other country. Sebastien Jean et al., "Dominance on World Markets: The China Conundrum," *CEPII*, December 2023; UN Comtrade.

U.S. Government Initiatives to Protect Supply Chains See Progress—*Continued*

manufacturing capabilities outside of China for connected devices or other critical components.

Critical Minerals and Rare Earth Elements: The U.S. Department of Energy announced $134 million in available funding for projects that aim to recycle rare earth elements from mine tailings, e-waste, and other waste materials.[206] The Export-Import Bank approved $10 billion to Project Vault, a new critical minerals strategic stockpiling initiative, and the U.S. International Development Finance Corporation has invested in multiple overseas mines and critical mineral cooperation initiatives.[207] The Office of the U.S. Trade Representative has signed action plans with Mexico and the EU agreeing to explore critical mineral price floors, regulatory and technical cooperation, and joint research and development.[208] The U.S. Department of Defense (DOD) continued its support for rare earth miner and refiner MP Materials with price floors after its $400 million equity investment in 2025.[209]

AI Technologies: The U.S. Department of State has convinced 24 countries to sign onto its Pax Silica initiative to build a secure global AI supply chain.[210]

Robotics and Autonomous Systems: The U.S. Federal Communications Commission (FCC) added multiple technologies to its Secure Networks Act covered list for communications equipment, banning imports of foreign-produced humanoid robots, quadruped robots, and uncrewed aircraft systems and their critical components. The FCC has been building on the standards for connected vehicles established in 2025 by the U.S. Department of Commerce's Office of Information and Communications Technology and Services.[211]

Telecommunications: The FCC added foreign-manufactured routers to the Secure Networks Act covered list, banning the sale of new router models in the United States without explicit approval.[212]

Electrical Grid: Executive Order 14420 banned the purchase, sale, and installation of critical power grid components produced in countries of concern that pose an unmitigable risk to the United States.[213] The U.S. Department of Energy plans to implement a $375 million program to upgrade domestic refurbishment capacity and invest in next-generation manufacturing for critical equipment in the grid such as transformers and circuit breakers.[214] The FCC also banned imports of foreign-produced power inverters.[215]

China Continues to Sharpen Its Economic Statecraft Toolkit

While Beijing pulled back from its most aggressive threat of export control enforcement in 2025 as part of the trade détente with the United States, it deployed its toolkit in more targeted ways. China has continued to block exports of critical minerals to Japan since January 2026 after Prime Minister Sanae Takaichi commented on the impact of a hypothetical Taiwan contingency on Japan's

security.[216] In May and June 2026, China detained multiple Japanese executives of companies with operations in China over alleged violations of dual-use export controls, escalating tensions between the two countries.*[217] China also imposed company-specific export controls for dual-use items in June 2026, targeting Japanese heavy industry firms.[218] China has also targeted the EU; in response to new EU sanctions on Chinese and Hong Kong entities for enabling Russia's war in Ukraine, China restricted dual-use exports to European entities.[219]

China Expands and Hones Its Legal Framework to Hinder Effectiveness of Sanctions

In addition to sharpening its export control regime, the CCP created several new tools to blunt the effectiveness of U.S. and allied sanctions, export controls, and supply chain de-risking efforts, which will create significant new legal risks for foreign companies operating in China (see Table 5). In March and April 2026, the State Council introduced two regulations that expand Beijing's legal authorities to counter foreign economic statecraft efforts.[220] Decree No. 834, the Provisions on Industrial and Supply Chain Security, broadens Beijing's authority to punish foreign entities deemed to threaten China's industrial or supply chain security and allows Chinese authorities to restrict supply chain due diligence efforts by foreign organizations.†[221]

Decree No. 835, the Regulations on Countering Foreign Improper Extraterritorial Jurisdiction, focuses on countering U.S. and allied sanctions and export controls. The decree enables Chinese authorities to deem a foreign measure that harms Chinese security, interests, or entities an application of "improper extraterritorial jurisdiction."[222] If Chinese authorities issue an associated blocking announcement, entities and individuals within China (including foreign subsidiaries of U.S. companies) may not comply with the foreign measures identified as such unless they receive express approval from Beijing.[223] Chinese entities may bring civil lawsuits against companies implementing unjustifiable measures, potentially even those with no operations in China.[224] In addition, Chinese authorities may designate "Malicious Entities"—foreign entities and individuals that "promote" or help implement unjustifiable measures—potentially triggering sanctions including limits on imports or exports, restrictions on visas, deportation, asset freezes, and fines; violating a prohibition could result in criminal liability.[225] The scope of "promote" is vague, giving Beijing broad discretion to determine what types of actions might be implicated.[226] Decree 835 also gives the

*The detentions came just before China's Ministry of Commerce published implementation guidance for its supply chain security measures outlining various offenses, setting up a whistleblower hotline for suspected violations, and detailing investigative procedures. China's Ministry of Commerce, 商务部公告2026年第26号 公布关于进一步完善战略矿产两用物项出口管制违法违规行为举报处理工作有关事项 [Ministry of Commerce Announcement No. 26 of 2026: Matters Concerning Further Improving the Handling of Reports of Violations of Export Controls of Strategic Mineral Dual-Use Items], June 24, 2026.

†The CCP has been steadily chilling due diligence efforts within China since at least 2021, when Chinese officials closed the Shenzhen office affiliated with well-known U.S. labor auditing firm Verite, followed in 2023 by significant actions against U.S. due diligence firm Mintz Group and Bain & Company. A. Launder, "Due Diligence in China Is Over," *Fintel Brief*, May 14, 2023; Lingling Wei et al., "China Closes U.S. Auditor as Tensions Mount over Forced Labor Allegations," *Wall Street Journal*, August 19, 2021.

Chinese government the power to exercise its own extraterritorial jurisdiction over foreign conduct with an "appropriate connection" to China that harms Chinese interests, and it may extend liability across multinational corporate structures to controlled or affiliated entities.[227]

While the two decrees overlap in many ways with existing provisions of Chinese law and regulation, they indicate that "China has transitioned from ad hoc countermeasures to a comprehensive, multiagency countersanctions legal framework capable of addressing commercial conduct, regulatory compliance decisions and cross-border legal conflicts."[228] In practice, these provisions could allow Chinese authorities to pursue liability against foreign parent companies or affiliated entities when overseas conduct by a subsidiary is deemed to harm China's interests.

Chinese firms have already been making use of China's anti-coercion toolkit—as shown by two legal disputes resolved in 2026. In the first, a Chinese shipbuilding company sued a Swiss company under Article 12 of the 2021 Anti-Foreign Sanctions Law (AFSL) for withholding $12 million in outstanding payments when the Chinese company was placed under U.S. sanctions.[229] A Chinese court ultimately mediated a resolution that resulted in the Swiss company paying the outstanding amount.[230] In a separate case, a Singaporean company refused to deliver electronic goods to a Hong Kong buyer on the U.S. entity list.[231] Chinese courts ordered the Singaporean company to pay damages to the Hong Kong firm in the first court ruling to establish the mandatory application of the AFSL.[232] In June 2026, China's Supreme People's Court highlighted the case as a representative use case for the law.[233] China's Ministry of Commerce also invoked a 2021 blocking law for the first time to protect Hengli Petrochemical, a large private Chinese refiner, after the United States sanctioned it for purchasing Iranian crude oil.[234] The blocking order puts entities between conflicting systems: Chinese law bars them from complying with or enforcing the sanctions, while continued transactions with Hengli could expose them to U.S. secondary sanctions.*[235]

China has also already deployed its new Regulations on Countering Foreign Improper Extraterritorial Jurisdiction to counter EU investigations into its companies. Under its Foreign Subsidies Regulation, the European Commission has opened two investigations into activities of Chinese companies in European markets—one in December 2025 relating to Nuctech's involvement in the threat detection systems market and a separate one in August 2026 involving Chinese e-commerce firm JD.com's pending acquisition of a German electronics retailer.[236] In both cases, the EU alleges that Chinese companies may have received state subsidies that could distort competition in the EU market.[237] In May 2026 and August 2026, respectively, China invoked its rules on improper extraterritorial jurisdiction to prohibit Chinese firms from fully assisting with the investigations, including by providing certain China-based informa-

*China's NFRA reportedly asked large Chinese banks under its supervision to suspend new loans to Hengli and review their exposures to the company despite the blocking order, indicating that China's regulators are still weighing the risks of secondary sanctions for its largest financial institutions. "China Asks Banks to Pause New Loans to US-Sanctioned Refiner," *Bloomberg*, May 7, 2026.

tion.*[238] Similar to the use of the Blocking Law in the Hengli case, opposing directives from Beijing and the EU force the companies into selective compliance.[239]

Table 5: China's Growing Economic Statecraft Toolkit Pushes Back Against the United States' Supply Chain Diversification Efforts

Effective Date	Instrument	Authority	Purpose and Key Milestone
September 19, 2020	Unreliable Entity List	Ministry of Commerce	Creates authority for China to place restrictions on foreign entities that endanger China's national security, apply discriminatory measures, or otherwise cut off market relations with Chinese entities. First use in February 2023.
December 1, 2020	Export Control Law	National People's Congress Standing Committee	Regulates dual-use technology and codifies license regime for sensitive products, services, and other transfers. First cited use in January 2021.
January 9, 2021	Measures for Blocking Improper Extraterritorial Application of Foreign Laws and Measures	Ministry of Commerce	Creates authority for China's government to block implementation of secondary sanctions and prohibit compliance with some foreign laws and measures. First use in May 2026.
January 18, 2021	Measures for Security Review of Foreign Investment	Ministry of Commerce, National Development and Reform Commission	Establishes security review process for inbound foreign investment in certain sectors.
June 10, 2021	Anti-Foreign Sanctions Law (AFSL)	National People's Congress Standing Committee	Creates legal tool for reciprocating against foreign sanctions and authority to impose retaliatory sanctions on a wide variety of targets, along with family members and affiliates. First use in July 2021.
March 23, 2025	AFSL Implementation Provisions (State Council Decree No. 803)	State Council	Broadens explicit scope of AFSL trigger actions and clarifies countermeasures.

*It is notable that China invoked its extraterritorial jurisdiction authority over cases involving the EU's foreign subsidies regulation regime. While this EU regime is focused on competition policy-type impacts of foreign subsidies and is separate from its CVD regime, the underlying logic of China's position would suggest it could impose blocking orders on requests for information in China related to a CVD or AD case. Were China to impose a blocking order in an AD or CVD case, that would add further tension to its membership in the WTO.

Table 5: China's Growing Economic Statecraft Toolkit Pushes Back Against the United States' Supply Chain Diversification Efforts—*Continued*

Effective Date	Instrument	Authority	Purpose and Key Milestone
March 31, 2026	Provisions on Industrial and Supply Chain Security (State Council Decree No. 834)	State Council	Unifies a national system for monitoring and responding to threats to supply chains. Targets foreign due diligence and information collecting in China.
April 7, 2026	Regulations on Countering Improper Extraterritorial Jurisdiction by Foreign States (State Council Decree No. 835)	State Council	Targets foreign measures deemed extraterritorial and unjustified. Creates a Malicious Entity List of companies that participate in implementing the foreign measures. First use in May 2026.
June 15, 2026	Regulations on the Implementation of the Mineral Resources Law (State Council Decree No. 839)	State Council	Expands state authority over the granting of mining rights and clarifies process for determining national list of strategic minerals.
July 1, 2026	Regulations on Outbound Investment (State Council Decree No. 837)	State Council	Restricts outflow of technology, services, goods, or other information.

Source: Various.[240]

Even as China has suspended and relaxed its export controls under the presidential agreements, it continues to grow the capacity to enforce and expand its regime in the future. China's issuance of export licenses for rare earths remains volatile, and companies have flagged repeated delays in receiving approvals.[241] Companies requesting licenses must provide extensive detail on the intended use and end user, providing China with more visibility into supply chain dependence at the firm level.[242] Given that China is targeting sales to U.S. defense manufacturers, it is likely gaining insights into these companies' supplier networks and import dependencies. China has also used its licensing regime to restrict rare earths and dual-use exports to defense-related U.S., Japanese, and European companies, such as U.S. firms MP Materials and USA Rare Earth, which are developing alternative rare earth supply chains.[243] As noted above, China's exports of key rare earths to the United States remain significantly below pre-export control levels despite Xi's commitment to Trump in Beijing. As noted above, in 2026 China expanded its economic statecraft policy toolkit, providing new authorities and mechanisms to punish compliance with U.S. sanctions and export controls and protect its supply chains. New regulations effective as of June 2026, for example, expanded state authority over the critical mineral and rare earth elements industries to reinforce China's leverage against foreign de-risking efforts.[244] As discussed in the section below on "China's 15th FYP: Technology Dominance and Security Priorities and Trajectory," China is working to preserve

its control over domestically produced technology by tightening controls over outbound investment, limiting access to foreign capital, and preventing domestic technology companies, talent, data, and knowhow from moving overseas.

China is also cognizant of other sources of leverage or potential leverage over the United States. In addition to its growing global exports of foundational semiconductors, China has sought to preserve its role as a major buyer of U.S. soybeans, using purchases as leverage during trade negotiations.[245] The United States' share of Chinese soybean imports has fallen from 35 percent in 2017 to 15 percent in 2025.[246] However, China accounted for an average of 45 percent of U.S. soybean exports over the last five years, making U.S. soybean farmers asymmetrically dependent on the Chinese market.[247] (For more on China's efforts to diversify soybean supplies, see Chapter 6, "The Price of Everything: China's Bid to Reshape Global Commodities Markets.")

China's 15th FYP: Technology Dominance and Security Priorities and Trajectory

China has laid out a comprehensive state-led strategy to compete with the United States and other countries across key emerging and critical technologies, including AI, biotechnology, and robotics. The essence of the 15th FYP rests not only on the development of frontier technological capabilities but also on the commercialization of key technologies at the near-frontier level across various applications. As documented in the plan, Beijing treats these technologies as general-purpose capabilities that create compounding advantages and drive broader innovation. The worrisome implication is that the United States could win the frontier AI capabilities race but still lose the broader technology competition if China succeeds in scaling low-cost adoption of AI, robotics, and biopharmaceuticals across its economy. Beijing is also playing defense: tightening state control over key components of its tech ecosystem and restricting overseas transfers of technology, talent, and capital while boosting state-backed financing.

China's "New Frontier" for Science and Technology Gets More Specific, More Ambitious, and More AI

Among frontier technologies prioritized in the 15th FYP, AI occupies a uniquely prominent position. The plan presents AI as a foundational strategic capability for advancing China's security, political, and economic objectives.[248] AI receives more mentions than any other emerging technology in the plan, reflecting its central role in Beijing's development agenda.[249] Its prominence has also increased dramatically over successive planning cycles. The term "artificial intelligence" appeared four times in the 13th FYP, rising to six mentions in the 14th FYP and 52 in the 15th.*[250] Chinese leadership further reinforced its emphasis on AI at the 2026 World Artificial Intelligence Conference (WAIC) in Shanghai, where Xi Jin-

*Although the Chinese term for "artificial intelligence" (人工智能) only appeared in the 13th FYP four times, the term "intelligentization," or "intelligentize" (智能化), appeared seven times in the plan. In the 14th FYP, the word appeared 11 times. One could argue that these words represent an earlier interpretation of China's aim to encourage the adoption of AI throughout the Chinese economy and military domain.

ping delivered a keynote address portraying China as a champion of international AI cooperation, safety, and "open" development, with "openness" likely referring to the broad diffusion of AI throughout Chinese industry and the wider economy rather than an explicit commitment to unrestricted open-weight models.[251] Xi also paired the release of new frontier AI models with new international AI governance initiatives, underscoring China's effort to advance domestic technological leadership while shaping global AI standards and positioning Chinese AI as an alternative to U.S. systems.[252]

The 15th FYP also promotes AI as an enabler of breakthroughs in other key technologies and critical sectors. From its initial efforts to drive China's AI development, Beijing has long viewed AI as a general-purpose technology that drives innovation elsewhere: for example, the Chinese government has promoted AI for science, encouraging research institutions to explore ways to use AI to enhance scientific discovery.[253] The 2025 AI+ Initiative and the subsequently released 15th FYP reinforce the concept of AI convergence with scientific research into a cohesive national-level, state-driven strategy.[254] The plan specifically envisions AI converging with other technologies such as quantum, life sciences, new materials, new energy, and 6G, leveraging technical advances in one sector to catalyze breakthroughs in another.[255] Beyond scientific discovery, the plan also emphasizes the practical application of AI technologies and their widespread adoption across critical sectors, including manufacturing, finance, healthcare, agriculture, and logistics.[256] Essentially, China is seeking to lead in global adoption and reap the benefits of AI across diverse sectors by focusing on deploying the technology throughout society rather than focusing exclusively on reaching the AI frontier.

Moving into the 15th FYP era, China has also articulated more specialized and operational objectives for other frontier technologies. In the 14th FYP, deep-sea and deep-space exploration were grouped together under the broad goal of advancing frontier scientific research and exploration capabilities. In contrast, the 15th FYP pulls deep-space exploration into a separate domain, with specific objectives including planetary exploration and the advancement of China's lunar program and launch vehicles, while deep-sea exploration remains grouped with other technology frontiers like deep-earth and polar exploration.[257] Whereas the 14th FYP emphasized advancing quantum information science broadly, the 15th FYP expands these ambitions to include building an integrated space-ground quantum communication network; developing fault-tolerant, general-purpose, and scalable specialized quantum computers; and achieving breakthroughs in high-precision quantum sensing.[258]

China's 31 provincial governments submitted new provincial-level FYPs in June 2026 that build on the central government's technology focus. The provincial plans show unity on several technology-related priorities: all 31 name new energy, biopharma, new materials, and AI as key sectors; 28 highlight aerospace and semiconductors; and 27 emphasize robotics, even as provinces pitch different approaches to upgrading these industries.[259] For example, Guizhou is positioning itself as a low-cost compute hub, Anhui is targeting memory and advanced packaging for semiconductors, and resource-rich provinces

such as Sichuan and Hunan are focusing on scaling up China's raw materials and rare earths.[260]

China's Trajectory in Key Areas of U.S.-China Technology Competition

As previously mentioned, Chinese labs, firms, and policymakers are not simply racing to match the United States in its drive toward frontier capabilities—they are also pursuing widespread AI adoption and deployment both domestically and globally. Beijing believes this dual approach offers parallel and mutually reinforcing pathways to leadership across multiple technology sectors. Chinese AI labs are flooding the global market with increasingly capable open-weight models that are quickly becoming the default choice for developers worldwide, including in the United States. Chinese robotics firms are enhancing capabilities, scaling production, and reducing prices, while Chinese biopharmaceutical companies are offering faster, cheaper drug development that is drawing Western pharmaceutical firms into deepening licensing relationships, presenting China with another potential point of supply chain leverage.[261]

China Improves Frontier AI Capabilities While Making Its Open Models the Default

From the perspective of Beijing and Chinese AI labs, AI competition with the United States is no longer solely about the race to the frontier. Rather, Beijing believes leadership in AI is contingent upon a country's ability to increase widespread adoption of AI across its own economy and around the world.[262] As the Commission found in a March 2026 paper examining China's AI development, Chinese AI labs are pursuing multiple pathways to compete with U.S. frontier labs as they grapple with compute constraints imposed by U.S. export controls. (For more, see Ngor Luong, "Two Loops: How China's Open AI Policy Reinforces Its Industrial Dominance," *U.S.-China Economic and Security Review Commission*, March 23, 2026.) These labs are simultaneously striving to achieve frontier model capabilities* while deploying open-weight models (i.e., models that release the learned numerical values that determine how AI processes inputs and generates outputs) globally and at scale.† China's open model strategy serves as a means for Chinese AI labs to increase their user base, innovate, tailor their models for specific industries and use cases, and obtain access to specialized data.‡[263]

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*Frontier AI models are the most capable models at a given time, representing the most cutting-edge technology based on performance benchmarks and capabilities that are regularly evolving. "What Is a Frontier Model?" *IBM*.

†Open-weight models also have varying degrees of licensing permissions, which may allow developers to independently understand, audit, recreate, and build upon the model, unlike closed or proprietary models. U.S.-China Economic and Security Review Commission, *AI Technology Stack Glossary*, June 25, 2026.

‡U.S. frontier AI labs, including OpenAI, Anthropic, and Google DeepMind, have accused Chinese labs such as DeepSeek, Moonshot, Minimax, and Alibaba of using fraudulent proxy accounts to harvest outputs from U.S. models at scale to generate synthetic training data—an attack U.S. labs called adversarial distillation—allowing them to build near-peer models cheaply. The U.S. National Security Agency, U.S. Cybersecurity and Infrastructure Agency, and U.S. Department of Justice published a joint cybersecurity advisory in September 2026, noting that DeepSeek, Moonshot AI, StepFun, and other Chinese AI labs had used adversarial distillation of U.S. models to reduce their training costs. (For more on adversarial distillation attack and synthetic data, see Chapter 8, "Silicon to Sovereignty: China's Bid to Control the AI Stack from Wafer to Weights, Part One.") National Security Agency, Cybersecurity and Infrastructure Security Agency, and De-

China's strategy to widely deploy open-weight models across key sectors such as manufacturing, robotics, and scientific research creates a feedback loop where deployment generates domain-specific data, these data refine models, and the refined models enable more advanced deployment.[264] (For more on China's "data flywheel" strategy for AI, see Chapter 7, "Collect, Steal, Buy, Fuse, Monetize: How China Is Turning Data into Assets and Ammunition.")

In 2026, Chinese open-weight models have gained significant traction among AI developers worldwide, including those in the United States.[265] By June 2026, Chinese models accounted for around 60 percent of all open model downloads on Hugging Face—a global open-source platform—surpassing U.S. models.[266] With their increased popularity, Chinese open models are now embedded in some U.S. businesses. Major U.S. companies—including Airbnb, DoorDash, Amazon, and Microsoft—have reportedly adopted, considered adopting, or have integrated into their products Chinese models.[267] U.S. startups such as Cursor, Lindy AI, and Perplexity also rely on them; Lindy and Perplexity cited their cost efficiency while delivering competitive performance.[268] (For more on China's open-weight models in the AI tech stack, see Chapter 8, "Silicon to Sovereignty: China's Bid to Control the AI Stack from Wafer to Weights, Part One.")

China continues to face constraints in frontier AI development due to export controls the United States and its allies have placed on its AI and semiconductor manufacturing equipment industries. Leadership in advanced semiconductor manufacturing depends on a small number of highly specialized firms concentrated in the United States and other allied countries and partners, and these jurisdictions have worked to establish controls targeting multiple chokepoints across the supply chain. Nvidia designs the most advanced AI chips, which are manufactured at or below 7 nanometer nodes. Since 2022, U.S. export controls have kept Chinese AI labs such as DeepSeek behind U.S. frontier labs by restricting their access to these chips and hampering Chinese firms' ability to manufacture them domestically.[269] Chip design also relies on electronic design automation (EDA) software dominated by U.S.-based Synopsys and Cadence and Germany-based Siemens, while high-end AI chip manufacturing is nearly monopolized by Taiwan Semiconductor Manufacturing Company, which currently depends on Netherlands-based ASML's extreme ultraviolet lithography equipment.[270] Advanced AI systems also require high-bandwidth memory, manufacture of which is controlled largely by South Korea-based SK Hynix and Samsung, and U.S.-based Micron, with Chinese competitor CXMT lagging by at least two generations.[271] (For more on China's challenges and progress in indigenizing its advanced semiconductor industry, see Chapter 8, "Silicon to Sovereignty: China's Bid to Control the AI Stack from Wafer to Weights, Part One.")

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partment of Justice, *China-Based Artificial Intelligence Companies Conducting Industrial-Scale Distillation Campaigns Against U.S. AI Companies,* September 8, 2026, 3–5.

Threat From China's Foundational Semiconductors Sector Begins to Take Shape in 2026

Chinese producers of foundational semiconductors are becoming more competitive in the global market, driven by China's massive subsidies in recent years to expand capacity.* As the Commission reported in its 2025 Annual Report to Congress, once planned investments come online, they are projected to push China's share of global production of foundational semiconductors from 34 percent in 2024 to 47 percent by 2027, exceeding Taiwan's share as the leading producer.[272] China's capacity buildout, supported by both industrial policy programs and investments to localize supply chains, has started to translate into export growth. In the first half of 2026, China's integrated circuit exports—which include memory, microcontrollers, and other foundational semiconductors—already nearly doubled from a year earlier, totaling $177.28 billion across 179.44 billion units.†[273]

China's capacity buildup creates conditions for intensified competition with market-based producers. According to microelectronics industry association SEMI, China's 12-inch wafer fabs are projected to account for 25 percent of global capacity this year, surpassing South Korea (23 percent) and Taiwan (21 percent).[274] Backed by a decade of Made in China 2025 industrial policy and more recent urgency following the 2022 and 2023 U.S. export controls, China's capacity expansion is already reshaping the competitive landscape for foundational semiconductor manufacturing, previously dominated by market-based players.[275] In the wafer manufacturing segment, for example, Taiwan market research firm TrendForce reported a 40 percent price drop of six-inch silicon carbide wafers (from $1,000 to $600) in 2024, with Chinese firms offering record-low prices of $400 per wafer.[276] In response to China's nonmarket practices in the foundational semiconductor sector, the Office of the U.S. Trade Representative concluded a Section 301 investigation in December 2025, finding China's semiconductor practices unreasonable and burdensome to U.S. commerce and imposing a tariff action that holds at 0 percent until it rises to an as-yet-to-be-determined rate, scheduled to be announced on June 23, 2027.[277]

AI Accelerates Other Strategic Technologies

For China, AI integration has the potential to accelerate breakthroughs in biotechnology, including synthetic biology, which applies engineering principles to design or modify biological systems for specific purposes.[278] Developments in AI have already dramatically sped up how fast and widely these advances are developed and deployed, and this trend is likely to continue.[279] Against this backdrop, a number of Chinese companies are attempting to replicate, match, or surpass Google DeepMind's AlphaFold's protein-folding capability,

*Foundational chips are sometimes called legacy chips or mature nodes because they are produced on long-established process nodes with older-generation equipment. Bryon Moyer, "Legacy Process Nodes Going Strong," *Semiconductor Engineering*, July 23, 2024.

†The export growth is partly driven by the rise in memory chip prices. Graham Ayres et al., "China Bulletin," *U.S.-China Economic and Security Review Commission*, July 23, 2026.

often positioning their domestic models as commercial competitors. For example, Baidu-backed Biomap claims its xTrimo model is more accurate than AlphaFold in testing ways that 70 antibodies and 44 single-domain antibodies each bind to their target molecules.[280] ByteDance claims its open-weight SeedFold model outperforms AlphaFold3 on protein-related tasks such as predicting how proteins bind to RNA and how two proteins bind to each other.[281]

AI is also a force multiplier for the robotics sector. As China climbs the value chain, it is leveraging AI to move from conventional automation to embodied AI—systems that can perceive, interact with, and act in a physical world, adapting to tasks and environments for which they were not explicitly programmed.[282] Yao Maoqing, a partner at China's embodied AI company Agibot, explained, "Industrial robots do not have intelligence. Embodied intelligence uses large models to form abilities… to perform tasks in relevant environments and adaptively adjust according to environmental changes."[283] The convergence of AI and robotics will be critical for China to maintain its dominant position in the sector. (For more on China's use of data to improve embodied AI, see Chapter 7, "Collect, Steal, Buy, Fuse, Monetize: How China Is Turning Data into Assets and Ammunition.")

China Deploys More Humanoid Robots and Drives Down Prices

The year began with humanoid robots* taking the center stage at China's New Year celebration and performing coordinated martial arts moves and flips—a visible marker of China's growing competitiveness.[284] According to the Commission's 2025 Annual Report, China's lead in manufacturing has driven rapid industrial robot deployment, and this year the advantage has extended to humanoid robots, which have demonstrated growing capabilities alongside falling prices.[285] In 2025, Chinese humanoid robotics companies such as Agibot, Unitree, and UBTech accounted for nearly 70 percent of the global humanoid market share.[286] Morgan Stanley projects China's humanoid robots sales will more than quadruple to 50,000 units in 2026, with input costs dropping 16 percent.[287] Unitree's initial public offering (IPO) filing points to scale as a driver of falling prices, noting that "large-scale production has further strengthened our bargaining power with upstream suppliers, creating a sustained cost advantage."[288] Longer-term forecasts point to a much wider gap, where Chinese humanoid robot companies are expected to sell 263,000 units by 2030, nearly eight times the projected U.S. total.[289] China's push for faster robotics deployment and lower pricing may also reflect a deliberate strategy. Faced with compute and data constraints, Chinese firms may be attempting to generate a positive feedback loop of real-world data needed to improve the software systems that run their robots.[290]

The United States has taken several notable steps in response to China's robotics surge. On June 8, 2026, DOD released an updated Section 1260H list identifying "Chinese military companies" oper-

*Humanoid robots combine humanlike form, mobility, dexterity, and embodied intelligence. Not all humanoid robots guarantee advanced embodied intelligence, as some perform fixed, tightly programmed motions with limited perception and in a structured environment. U.S.-China Economic and Security Review Commission, *Humanoid Robots*, October 10, 2024.

ating in the United States, adding Unitree and RoboSense.*[291] On July 27, 2026, a White House-convened interagency body issued a National Security Determination stating that all foreign-made advanced robots—including those from China—pose national security and safety risks.[292] Afterwards, the FCC added these devices to its Covered List, which means covered entities cannot obtain new equipment authorizations to import, market, and sell in the United States.†[293] Separately, on June 23, 2026, *Politico* reported that Department of Commerce Secretary Howard Lutnick said the department is reviewing Chinese state-subsidized robotics imports to the United States, signaling potential trade-related policies.[294]

China's Biopharmaceutical Rise Reshapes U.S. Drug Development

In March 2026, Pfizer CEO Albert Bourla warned that "for the first time in history or in recent decades… U.S. dominance in biotech technology is [being] challenged by a competitor, and that's China."[295] China is gaining a competitive advantage in biopharmaceuticals, which rely on biological processes rather than standardized chemical synthesis and could uncover novel new treatments. Due to the growing innovative capacity of Chinese biopharma companies, Western firms are increasingly paying large upfront licensing fees for global rights to China-origin biologics and next-generation candidates.[296] As shown in Figure 7, China's outbound licensing deals (i.e., agreements that grant non-Chinese companies the right to develop and commercialize a Chinese company's innovative products for upfront payments) hit a record $130 billion in 2025, a 150 percent increase from 2024.[297] The year 2026 was on pace to set a new record, with $110 billion in licensing value across 81 deals already in the first half of the year.[298] Chinese biotech firms have had particular success in developing potential oncology (cancer) biologics.[299] (For more on China's strategy to leverage data for advances in clinical trials and drug discovery, see Chapter 7, "Collect, Steal, Buy, Fuse, Monetize: How China Is Turning Data into Assets and Ammunition.")

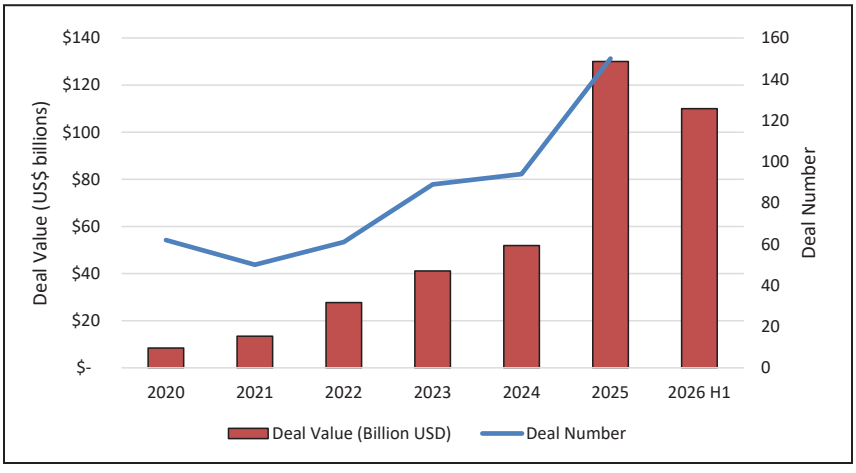
Since the launch of its Made in China 2025 industrial policy program in 2015, China surpassed its drug approval targets, boosted by streamlined regulations, cheap access to drug ingredients, strong oncology demand, and a well-developed biotechnology intermediate production infrastructure.[300] (For more on China's use of industrial policy to grow its biotechnology sector, see U.S.-China Economic and Security Review Commission, Chapter 6, "Interlocking Innovation Flywheels," in *2025 Annual Report to Congress*, November 2025, 313–357.) In addition, clinical trials in China are now 30 percent cheaper and 20 to 40 percent shorter than they were in the past.[301]

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*While Section 1260H of the Fiscal Year 2021 National Defense Authorization Act itself does not impose sanctions, provisions that took effect this year restrict DOD from contracting with listed entities. U.S. Department of Defense, *Department of War Launches New Website to Help Industry Partners Navigate Section 805 Supply Chain Requirements*, June 30, 2026.

†Unlike the 1260H listing, which only constrains DOD's own procurement, the Covered List reaches the broader consumer market, effectively banning the sale of Chinese robots in the United States by requiring online marketplaces to prevent sales of unauthorized covered equipment. U.S. Federal Communications Commission, *Covered List FAQs: UAS and UAS Critical Components*, July 21, 2026.

Figure 7: China's Outbound Licensing Pharmaceutical Deals Growth, 2020–2026*



Note: *2026 is as of June.
Source: Various.[302]

In response to China's growing advantages in biotechnology, the United States has attempted to curb U.S. dependence on Chinese companies for intermediate steps in the biopharmaceutical supply chain. The BIOSECURE Act, enacted December 18, 2025, as part of the Fiscal Year (FY) 2026 National Defense Authorization Act (NDAA), establishes a framework under which certain entities can be designated "biotechnology companies of concern (BCCs)," prompting federal contracting and funding restrictions.[303] While the Act doesn't name specific BCCs, it treats any companies on DOD's Section 1260H list as "Chinese military companies" and therefore subject to the same restrictions as designated BCCs.[304] On June 8, 2026, DOD updated the list to include WuXi AppTec.[305] In August, a federal district court blocked enforcement of the designation based on a legal challenge by WuXi.[306] WuXi AppTec and other Chinese contract development and manufacturing organizations are deeply embedded in U.S. supply chains. In 2024, experts estimated U.S. companies will need roughly eight years to disentangle themselves and shift to alternative providers.[307] The full list of BCCs is scheduled to be published by December 18, 2026.[308]

China Aims to Sustain and Expand U.S. Dependency on Its Pharmaceutical Ingredients

The United States is heavily dependent on China for raw pharmaceutical ingredients—particularly active pharmaceutical ingredients (APIs) and key starting materials (KSMs)—used in generic drugs, which make up 90 percent of U.S. prescriptions.[309] In its 2025 Annual Report to Congress, the Commission noted that while the precise nature and degree of U.S. dependence is unclear, nearly a quarter of APIs used in U.S. generic drugs come from China.[310] The Commission further estimated that anywhere

China Aims to Sustain and Expand U.S. Dependency on Its Pharmaceutical Ingredients—*Continued*

between 24 and 46.8 percent of generic daily doses distributed in the United States that use APIs from India depend on upstream Chinese inputs.[311] In addition to high average dependencies, certain KSMs are sole-sourced from China. One US Pharmacopeia study found that 12 percent of a sample of almost 2,000 APIs rely solely on China for their KSMs.[312] Drugs with high U.S. reliance on Chinese inputs include those with few immediate substitutes, including the blood thinner heparin, the immunosuppressant mycophenolate, and other hospital antibiotics.[313] China is taking actions to consolidate and grow this dependency. In September 2025, Chinese producers flooded the global market with below-cost APIs and KSMs to undercut India's attempts to stand up alternate supply.[314] In 2026, the 15th FYP called for cultivating new capabilities in biomanufacturing, including novel cell and gene therapy drugs and emergency vaccine and drug development.[315] And, in September, China's Ministry of Industry and Information Technology released a new FYP for the pharmaceutical industry to enhance innovation-driven drug development and strengthen supply chains alongside indicative 2030 targets, including to have at least five drugs reach global annual sales exceeding $1 billion.[316] (For more on India's reliance on China for pharmaceutical ingredients, see Chapter 3, "China's Other Front: India and the Future of U.S. Strategy in the Indo-Pacific.")

U.S. reliance on China for APIs and KSMs poses national security, economic, and public health risks to the United States, as some medical drugs—including certain anticoagulants, antibiotics, and cancer treatments—appear wholly sourced from China.[317] As the critical minerals example has demonstrated, reliance on Beijing for inputs in sensitive sectors creates significant risks, exacerbated given the immediate threat to many Americans' health if China caused shortages or disruptions to U.S. access.[318]

China Strengthens Control over Technology and Capital

China Updates Its Regulatory Toolkits to Protect Domestic Technology Ecosystem

As China seeks to maintain critical capabilities in AI and other advanced technologies, it is tightening its legal authorities to regulate the transfer of commercially valuable technology, data, and expertise. Beijing seeks to retain control over strategically valuable technology, capital, and talent while expanding tools to deter, penalize, or retaliate against firms that hinder China's technological advancement.

China's weak private investment climate, slowing economic growth, and constrained access to capital have incentivized some Chinese AI companies to seek overseas financing or relocate abroad.[319] As a result, Beijing has turned to more aggressive regulatory measures to retain technology, talent, and investment within China. On April 17, 2026, the State Council adopted a new outbound investment regula-

tion preventing investors from exporting restricted technology, know-how, data, or other goods and services under the guise of outbound investment.[320] The regulations were published and made effective on June 1, 2026, but even before the regulations became public, the NDRC had already begun taking steps to discourage AI firms from relocating overseas or accepting Western capital. On April 27, 2026, the NDRC blocked Meta's proposed $2 billion acquisition of Chinese AI startup Manus (headquartered in Singapore) after a months-long review of the company and its owners.[321] The companies have since complied with the decision and returned to operating as independent entities.*[322] The CCP's concerns even extend to foreign capital invested into China's AI sector—Beijing reportedly instructed several firms, including ByteDance, Moonshot AI, and StepFun to reject investment of U.S. origin unless explicitly approved.[323]

Reflecting its view of technology as a strategic national asset, the Chinese government has also expanded its oversight beyond companies to include AI talent. In 2026, authorities reportedly prevented employees at frontier AI firms, including Alibaba and DeepSeek, from leaving China without government approval, barring the founders of Manus from departing the country during the government's review of Meta's proposed acquisition of the company.[324] These efforts will likely make it harder for Chinese firms to tap private capital from more capital-rich global investors and will force entrepreneurs to choose whether to build their companies in China, Singapore, or the West.

In June 2026, SAMR introduced the Regulations on Trade Secret Protection (Order No. 126), expanding China's trade secrets regime to explicitly cover data, algorithms, and other digital assets.[325] The regulations introduce several legal authorities that allow Beijing to scrutinize and penalize cross-border business activity relating to AI, such as sharing internal business data with foreign affiliates or hiring foreign technical staff who may have access to proprietary information. Additionally, they significantly increase administrative penalties for trade secret theft and strengthen enforcement tools against employees and firms that misappropriate proprietary data, algorithms, and code.[326] While the United States provides trade secret treatment in appropriate circumstances for AI algorithms, knowhow, and data, the new decree coincides with China's recent push to control commercial decisions made by its firms and tech talent to move abroad or to make deals with foreign firms.

State Role in Financing Technology Sector Has Grown, Increasing Importance of Hong Kong

Reflective of Xi Jinping's effort to further centralize technology development, state-backed capital now dominates China's venture capital (VC) ecosystem.[327] China has emphasized the use of state-backed equity funding to provide companies "patient capital"—long-term capital for technology research and commercialization.[328] According to China-based independent research group Zero2IPO, the share of state-backed funds serving as limited partners in Chi-

*Given the steps taken by the Chinese government in 2026, it seems likely that so-called "Singapore-washing," a corporate strategy in which Chinese-founded companies relocate or restructure operations through Singapore to obscure their Chinese identity, is no longer an option without severing operational ties to China.

na's VC fundraising rose from 65 percent in 2019 to 81 percent in 2025.[329] As of February 2026, the ten largest VC investors in China were all state-backed entities and had committed RMB 33 billion ($4.87 billion), accounting for half of total contributions.[330]

VC investments have focused on supporting Beijing's technology goals. Investments in China's information technology sector in particular rose 53 percent from 2024 to 2025—with a large share of investments going to AI, embodied AI, and autonomous driving.[331] Many of these technology-related VC investments are also backed directly by the state. Chinese AI lab MiniMax, for example, raised a $300 million funding round from investors, including the State-Owned Assets Supervision and Administration Commission of the Shanghai Municipal Government.[332] China's AI chip startup MetaX Integrated Circuits has also raised VC funding from Shanghai Science and Technology Innovation Fund and the Pudong District Fund.[333]

As Chinese tech companies mature, Hong Kong serves as an important gateway to global financial markets, allowing them to access foreign capital to advance China's technology ambitions.[334] The Hong Kong stock exchange led the world's capital market in 2025, raising approximately $36.4 billion from 119 new listings.[335] In the first half of 2026, 83 companies listed on the exchange, raising $26.4 billion and making it the second-largest IPO market after U.S.-based Nasdaq.[336] MiniMax, for example, raised $619 million in January.[337] AI lab Z.ai also raised $4 billion on the Hong Kong stock exchange in July 2026.*[338] In addition, China hosted two of its biggest tech IPOs on the Shanghai STAR market: China's leading memory chip production company CXMT in July and leading robot company Unitree in August. CXMT, which is profitable, raised almost $10 billion to fund domestic expansion and briefly surpassed Tencent to become China's most valuable company.[339] Unitree intends to use a portion of its IPO proceeds to fund research and development and manufacturing expansion.[340] While sector champions like CXMT and Unitree both chose Shanghai for their IPOs in August 2026, first-day trading pops of over 400 percent for each of them reflect the difficulties Chinese underwriters have in assigning accurate valuations in an environment where retail investors lack many attractive investment opportunities.[341] Mainland regulators also discourage assigning ultra-high valuations in scenarios that lack publicly listed comparable firms to protect retail investors from potential losses.[342] (For more information on Hong Kong as a financial and tech hub and China's use of the Hong Kong stock exchange versus the STAR market, see Chapter 10, "Hong Kong: Enabler of China's Global Finance and Technology Ambitions.")

*Z.ai (formerly Zhipu AI), listed under its legal name Beijing Zhipu Huazhang Technology Co., Ltd., was added to the Department of Commerce's Entity List on January 16, 2025. See U.S. Department of Commerce, Bureau of Industry and Security, "Addition of Entities to and Revision of Entry on the Entity List," 90 Fed. Reg. 10 (January 16, 2025): 4617–4620.

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