

# Is China's Economic Policy Too Cautious?

*Resilience is not the same as momentum.*

BY JONG-WHA LEE

**I**n the Chinese zodiac, 2026 is the Year of the Fire Horse. Pairing the powerful and lively horse with the element of fire yields a symbol of intensity, vitality, and forward momentum. But, the wisdom goes, the fire horse must not allow its determination to give way to recklessness. Likewise, the tension between balance and dynamism will define Chinese economic policy in the year ahead.

By conventional measures, China's performance exceeded expectations in 2025. Manufacturing output held firm and exports expanded, despite renewed trade tensions with the United States. China also avoided financial instability, even as the property downturn persisted for a fifth year. GDP growth is projected to have reached 5 percent for the year.

These indicators highlight the Chinese economy's enduring resilience, which is underpinned by deep-rooted structural strengths. China accounts for roughly 30 percent of global manufacturing value-added, and its firms dominate supply chains in electric vehicles, batteries, solar panels, and a range of advanced industrial inputs. China's adaptability also helps: When the United States hiked tariffs and tightened export restrictions, Chinese exporters redirected shipments toward Europe, Southeast Asia, and the Global South, often overcoming complex logistical challenges.

But resilience is not the same as momentum, and China remains beset by acute imbalances that are constraining economic growth. While China's trade surplus—which now exceeds \$1 trillion—may look like something to boast about, it underscores the economy's enduring dependence on external demand to offset weak domestic consumption.

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Persistent deflationary pressures reinforce this imbalance. Producer prices have been falling for more than three years, owing to chronic excess capacity—a symptom of the demand shortfall at home. Deflation enhances the competi-

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tiveness of Chinese exports but erodes corporate profitability and increases debt burdens.

China's leaders are well aware of these dynamics. That is why they indicated at last month's Central Economic Work Conference that they plan to emphasize caution over ambition in 2026. According to the Fifteenth Five-Year Plan (2026–2030), “high-quality development,” stability, and risk management will take precedence over headline growth targets.

Boosting domestic consumption will be a top priority, but it will be pursued in a measured way, using tools like targeted subsidies and service-sector expansion. Likewise, rather than devising radical strategies to reverse the property-market downturn, the authorities will seek to manage it by absorbing inventory and offering selective financial support.

China's macro stance will remain expansionary in form, but conservative in intent, aimed at stemming the decline in growth, rather than igniting a new growth cycle. Fiscal and monetary expansion will occur within strict boundaries, resulting in policy-supported (not self-sustaining) GDP growth of around 4.5 percent this year.

China's leaders also recognize the deeper structural constraints on the economy, though these will be more difficult to address. Consider overcapacity. The government has highlighted the dangers of “involution”—competition so fierce that it often comes at the expense of profits—but decisive consolidation would entail bankruptcies and job losses, raising the risk of a social and political backlash.

The demographic challenge is even more intractable. After decades of strict family-planning rules, China's population is shrinking fast, and the government's embrace of pronatalist policies has done little to reverse this trend. Given high barriers to increased fertility, China's demographic profile may well amount to a binding constraint on long-term growth.

Geopolitics complicates matters further. In fact, China's export strength has become something of a strategic

liability, as indicated by growing friction with Europe and other advanced economies. While tensions with the United States have been “managed,” they are far from resolved, and U.S. President Donald Trump's positions can change on a dime. As shown by the Trump administration's attack on Venezuela—whose ties with China included preferential oil access—even actions that are not directed at China can have major economic effects, and China's capacity to protect its partners from U.S. aggression is limited.

With the United States retaining considerable influence over China's strategic environment, China's geopolitical room for maneuver is narrower than its apparent economic leverage might seem to indicate. While unification with Taiwan remains a key goal of Chinese President Xi Jinping, any military escalation would entail very high costs.

Even Xi's goal of making China a “moderately developed” economy by 2035 might be out of reach, as this would require sustained GDP growth per capita that is rarely achieved at China's current income level. Countries that have made it to the top of the development ladder, such as Japan and the Asian Tigers (South Korea, Taiwan, Hong Kong, and Singapore), did so under very different demographic and geopolitical conditions. China's shift from rigid numerical targets to more qualitative objectives suggests that this, too, is clear to its leaders. The old growth model has largely run its course.

China's leaders are right to pursue a measured strategy, based on realistic expectations. But they must not be so cautious that they entrench the imbalances that will

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limit long-term growth for the sake of short-term stability. They must make the most of the economy's considerable strength to address the challenges ahead with shrewdness, boldness, and flexibility. The balance they strike between consumption and exports, state control and market discipline, and power projection and peaceful coexistence will be decisive.

Resilience has bought China time. What it does with that time will determine whether 2026 marks the beginning of a durable transition or a process of economic erosion, with today's pressures hardening into permanent constraints on China's future prospects. ◆