

China's investment slump and the geometry of power

This article is authored by Sriparna Pathak.

Published on: Sep 19, 2026

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Great-power competition is often narrated in the language of fleets, chips, and alliances. It is still, more prosaically, a contest over who can generate surplus, absorb shocks, and convert growth into usable capacity. In that arithmetic, a multi-year compression of capital formation in the world's second-largest economy is not a domestic footnote. It is a revision of the material base on which influence is supposed to rest.



Chinese flag (Photo for representation.) (AFP)

China's first-half 2026 figures make the revision visible. Fixed-asset investment excluding rural households fell 5.7%. Strip out property development and the decline was still 2.7%. Real-estate development investment itself contracted by 18%. By August the headline figure had worsened to a 7.2% year-on-year drop, with property down nearly 20%. Headline GDP grew 4.7% in the first half, then slowed to 4.3% in the second quarter, inside the official 4.5-5% band, yet revealing a familiar imbalance: Factories still produce, households and private firms hesitate to spend.

That pattern is not an accident of weather or a single bad quarter. It is the delayed consequence of a development strategy that, for two decades, treated urbanisation, land finance, and ever-rising capital formation as near-substitutes for productivity and household demand. The three red lines of 2020 were an attempt to restrain developer leverage after the fact. They precipitated a liquidity crisis rather than a tidy deleveraging. Subsequent policy has oscillated between whitelist financing, destocking through state purchases, urban-village renovation, and, in August 2026, a shift away from the presale model toward completed-home sales. Each step is internally coherent. Together they concede that the old engine cannot be restarted at previous scale without recreating the risks it produced.

The official narrative is high-quality development: Intellectual-property investment rising, high-tech outperforming, equipment purchases holding up while construction-and-installation spending collapses. Those compositional shifts are real. They are also, so far, too small to replace the demand that property and conventional infrastructure once supplied. Private investment remains weaker than state-led spending. Local governments, long dependent on land-sale revenue, have less fiscal room. Housing still accounts for a dominant share of household wealth; when prices and transactions sag, consumption follows. The result is the supply-demand mismatch officials themselves now name: strong production, weak absorption.

An investment share of GDP that stayed near 40% for years was not a law of nature. It was a political choice that postponed the harder work of raising household income, social insurance, and the returns to private capital. When that choice collides with demographics, excess housing stock, and local-government debt, growth does not vanish; it becomes thinner, more export-dependent, and more reliant on a handful of advanced manufacturing niches. Quality can improve even as the volume of capital formation falls. Whether that is enough depends on whether one measures success by steel poured or by living standards that do not require another construction boom—and, in an age of strategic rivalry, by whether growth still compounds the resources states actually deploy.

China remains large enough that a multi-year compression of construction demand is a global event. Commodity exporters that priced in perpetual Chinese steel, copper, and iron-ore intensity will face a structurally lower baseline, even if green-tech metals offset some of the loss. Manufacturers elsewhere will confront continued Chinese export strength in batteries, machinery, electronics, and intermediate goods, the counterpart of weak domestic absorption. That is not dumping in every case; it is what an economy does when investment and consumption at home cannot clear the output of a still-formidable industrial base. Trade partners will feel the pressure as surplus capacity seeks markets. Financial markets will keep pricing the difference between official growth targets and the demand that actually appears in import orders and commodity volumes.

If Beijing continues to prefer targeted industrial policy and urban renewal over a broad household-transfer stimulus, the world will import Chinese goods more readily than Chinese demand. Supply-chain diversification, already underway since the late 2010s, will look less like a hedge against geopolitics alone and more like a hedge against a demand shortfall that lasts longer than a cycle. Power calculations shift with that mix. A China that invests less in buildings and more in selected high-tech industries will still project industrial and technological weight. It will find it harder to underwrite the same pace of external economic statecraft if domestic demand remains the weak link and local finances stay constrained. Rivals and partners alike should update not a caricature of decline, but a more precise map: Ample production, thinner absorption, and a growth rate that no longer automatically enlarges every instrument of influence.

Other countries should not confuse a high investment ratio with a durable growth model. Credit-fuelled construction can raise measured GDP and urban skylines for a generation and still leave an overhang of empty floor space, strained local balance sheets, and households whose wealth is concentrated in a single, illiquid asset. Several emerging economies have flirted with variants of the same formula. The Chinese case is a reminder

that the exit is slower and politically harder than the entry. The composition of investment matters as much as its level. Rising spending on equipment, computing infrastructure, and high-tech manufacturing can be genuine upgrading. It does not automatically restore domestic demand if property, local public works, and private confidence remain depressed. Export success in a few sectors can mask a hollowed-out household sector. Solvency risk and demand risk are not the same thing. China has so far avoided a systemic banking collapse of the 2008 variety. That is not the same as restoring animal spirits. Japan's post-bubble experience showed that investment and consumption can stay weak for years without a classic banking crisis. Wealth effects, unfinished projects, and pessimistic expectations are enough. Policymakers who treat the absence of a financial meltdown as proof that the problem is solved will misread the lag. Nor should surplus capacity be treated as a permanent gift. Cheap capital goods and intermediate inputs lower costs. They also concentrate industrial employment and political grievance in the importing country. The appropriate response is not autarky; it is realism about how long an external surplus can substitute for missing domestic demand in the source country.

How China manages the new model of housing-completed sales, destocking, affordable units, urban renewal rather than endless greenfield expansion-will decide how long this adjustment lasts. If that transition stabilises prices and finishes projects without reigniting leverage, it will be a genuine institutional achievement. If it merely relocates the overhang onto the state and stretches the correction across a decade, the global economy will live with a large producer that invests less in buildings and more in factories whose output must be sold abroad. The first-half figures do not announce collapse. They announce a slower, more lopsided equilibrium.

For China, the test is whether new drivers can carry a larger share of employment and income before confidence erodes further. For everyone else, the test is whether policy and firms plan for a world in which Chinese construction is no longer the swing factor it was in the 2000s and 2010s, and in which Chinese factories, for that very reason, remain very much in the market. In contemporary power politics, growth is not the only currency. It is still the one that makes the others spendable.

(The views expressed are personal)

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