This material is neither intended to be distributed to Mainland China investors nor to provide securities investment consultancy services within the territory of Mainland China. This material or any portion hereof may not be reprinted, sold or redistributed without the written consent of J.P. Morgan.

China Equity Strategy

Seven questions on bridging China's innovation-to-returns gap

With stubbornly sluggish macro and ongoing headwinds for a variety of 'old economy' sectors and headline indices, China's equity debate has shifted towards innovation – and whether that innovation can translate into durable earnings growth, stronger margins and better shareholder returns. We think the answer depends on how quickly three gaps can narrow: **the demand gap**, as export resilience has yet to translate into a broader recovery in household income and consumption; **the value-capture gap**, as intense competition and excess capacity still limit the margin benefit from innovation; and **the market-access gap**, as China's most competitive industries face a more complex global trade environment. This report addresses seven questions that sit behind these gaps (pages 6-31), from how far exports can drive earnings and what could trigger a stronger policy response, to when AI can broaden from infrastructure strength into internet-stock re-rating, which sectors are benefiting from anti-involution, and what could unlock household deposits into equities. For now, **our analysis of the past 20 years suggests that sectors aligned with policy priorities, funding support and earnings momentum, as well as those with strong entrepreneurial spirit, can still generate meaningful alpha, even in slower-growth environments (Figure 7).** Investor conviction on China could strengthen further if progress becomes more visible in narrowing these gaps, through stronger domestic demand, a more stable property and local-government financing backdrop, better pricing discipline, more durable overseas access, and deeper capital-market reform.

- **China has become an innovation powerhouse, but equity returns have yet to fully reflect that progress.** China's strengths now span electric vehicles, batteries, solar, shipbuilding, industrial robotics, AI and biotech. The country accounts for roughly 30% of global manufacturing value added and around 15% of global merchandise exports. Yet equity market performance has lagged this industrial and technological progress. Despite a strong 2025, Chinese equities pulled back in 2026, particularly in 3Q26. Since the start of 2025, MSCI China and the CSI 300 have returned 9% and 6%, respectively, underperforming the MSCI ACWI at 35% and the MSCI EM at 49%. For global investors, the key question is no longer whether China can innovate, but how that innovation will translate into sustained earnings growth and shareholder returns. **We think the link between innovation and earnings is still being built, with three gaps explaining the delay.**

China & HK Equity and Thematic Strategy

Chloe Liu, CFA AC
(852) 2800-0853
chloe.x.liu@jpmorgan.com
J.P. Morgan Securities (Asia Pacific) Limited

Tim Huang AC
(852) 2800-4323
tim.huang@jpmorgan.com
J.P. Morgan Securities (Asia Pacific) Limited/ J.P. Morgan Broking (Hong Kong) Limited

China A-share Equity and Thematic Strategy

Erin Zhang, CFA
(86-21) 6106 6328
erin.zhang@jpmorgan.com
SAC Registration Number: S1730521090002
J.P. Morgan Securities (China) Company Limited

Asia Equity and Thematic Strategy

Rajiv Batra
(65) 6882-8151
rajiv.j.batra@jpmorgan.com
J.P. Morgan Securities Singapore Private Limited

Mixo Das
(852) 2800-0511
mixo.das@jpmorgan.com
J.P. Morgan Securities (Asia Pacific) Limited/ J.P. Morgan Broking (Hong Kong) Limited

See page 32 for analyst certification and important disclosures, including non-US analyst disclosures.

- **The demand gap remains a key constraint: exporters are resilient, but domestic demand still drives most index earnings.** China's exports have remained strong, rising 19% y-y in USD terms in 8M26, while the domestic economy remains weak, with retail sales up only 1% y-y, new home sales value down 13% y-y, and secondary home prices across 70 cities down 2.6% y-y (Figure 1). Strong exports have not spilled over into broad consumption or household income recovery, as today's export growth is more capital-intensive than labor-intensive. At the index level, overseas revenue accounts for around 18% of MSCI China revenue, and the remaining 82% still depends on the domestic economy. Recent property measures to phase out pre-sales should help stabilize prices in tier-1 and leading tier-2 cities by reducing medium-term supply, but a broader recovery in consumption and property will require more widespread property price stabilization beyond Shanghai and greater household confidence in income growth. On policy, with exports and inflation stronger than in 'Sep 24' (Figure 2), JPM's China Macro team expects policy support to remain incremental and targeted rather than a 'bazooka', mainly through faster fiscal execution. A more decisive policy step-up is more likely if slower exports begin to weigh on employment.

- **The value-capture gap shows that China's innovation is strong, but the next step is converting it into sustainable margins.** China's manufacturing upgrade is evident in rising R&D intensity, an improving product mix, growing global market share, and higher representation in Chinese indices, with the high-end manufacturing weight in the CSI 300 rising from 42% in 2021 to 49% in 2026 (Figure 4). However, rapid capacity growth and weak domestic demand have intensified price competition, so much of the innovation benefit has been passed to customers through lower prices and margins. The government's 'anti-involution' initiative is designed to address this, with results more visible where supply discipline has improved, including logistics, chemicals, and lithium, while sectors such as solar and autos are struggling more (Figure 32). Implementation may take time, given the dominance of private companies in overcapacity sectors, current demand conditions, and local governments' fiscal considerations.

- **The market-access gap reflects China's need to adapt to a more complex global trade environment.** China's most competitive sectors are also among the most exposed to trade measures from major partners, including batteries, EVs, wind projects, and power systems. Listed exporters' share-price performance increasingly depends on RMB stability and the direction of US/EU trade policy. China is responding constructively, companies are localizing production overseas, while export VAT rebates are being phased out gradually – for solar in Apr 2026, batteries from Jan 2027, and EVs from Apr 2027. We believe the trade tensions may persist for some time, although selective trade negotiations and gradual localization could help reduce near-term disruption risks.

- **Even with China facing these structural challenges, we believe there will remain meaningful opportunities for sector alpha in areas supported by policy priorities and entrepreneurial innovation**. The macro backdrop may remain constrained by fragile domestic demand, demographics, geopolitical and trade friction, but equity performance is unlikely to be uniform across sectors. Policy-supported sectors with government priorities, funding, and earnings momentum can still outperform. At the same time, sectors with strong entrepreneurial spirit, innovation intensity, and global competitiveness, such as biotech, and AI applications, may also generate alpha in a slower-growth macro environment. Our analysis of China's past 20 years of development and policy stimulus shows that sectors with strong policy support – including telecom, property, mobile internet, NEVs, renewables and AI – generally saw leading listed companies deliver strong revenue/profit growth and five-year returns (Figure 7). AI is one of the clearest illustrations of this policy-supported opportunity set: infrastructure and localization remain supported by a clear policy agenda, with domestic chips expected to rise from 40% of AI infrastructure demand in 2025 to around 80% by 2028. At the same time, China's model and application layers are gaining global relevance through open models and strong value-for-money propositions, while monetization is still developing. As AI adoption broadens and platform-based monetization becomes more visible, internet companies could see meaningful re-rating opportunities.

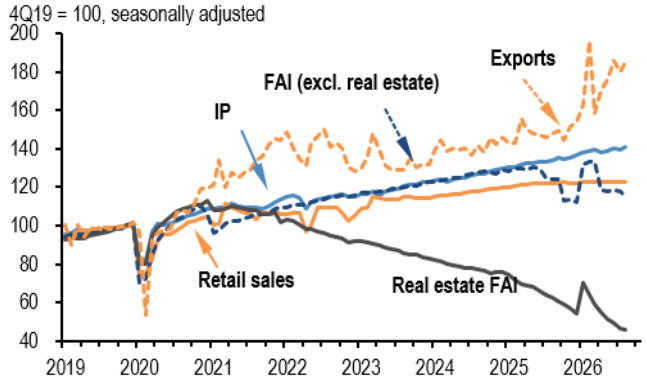
- **Investors' conviction on China could strengthen further if progress becomes more visible across five areas that help translate innovation into earnings growth and shareholder returns**: 1) Stronger domestic demand, greater support for social security, pensions, and household income could give consumers more confidence and allow consumption to play a larger role in growth, 2) a more stable property and local-government financing backdrop, alongside a larger role for central fiscal resources, could help reduce the drag from housing-related wealth effects, 3) further progress on the anti-involution agenda, tighter financing for oversupplied sectors, more disciplined capacity expansion, and more rational pricing behavior could allow innovation to be better rewarded through higher margins, 4) continued production localization and broader export-market diversification could help companies manage geopolitical and trade uncertainties, and 5) deeper ongoing capital-market reform, substantial higher shareholder returns and a larger base of long-term institutional capital could help reduce equity-market volatility and improve investor confidence over time.

We will continue to roll out further aspects of our China Equity Strategy views in upcoming reports, and we look forward to engaging with you on these critical China debates and market opportunities.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

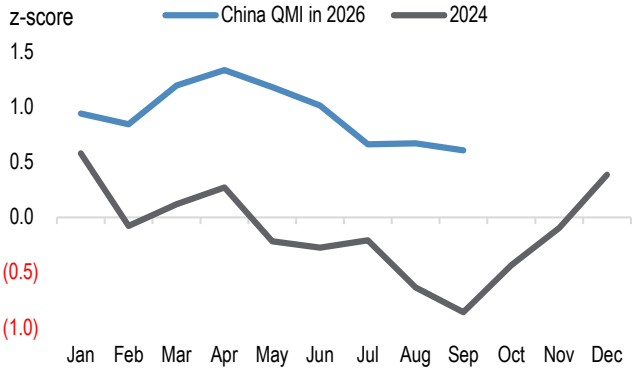
Key Charts in Focus

Figure 1: China's two speed economy – strong export growth, but weak domestic demand



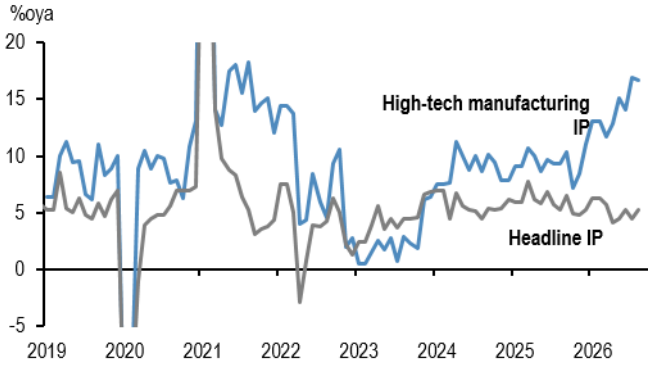
Source: China Customs, J.P. Morgan.

Figure 2: China's quantitative macro indicator (QMI) is higher in 2026 vs 2024



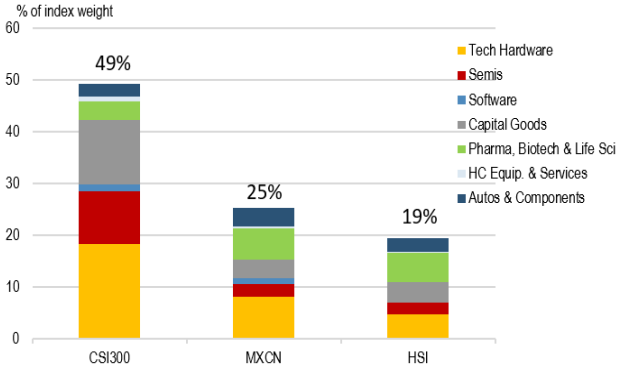
Source: J.P. Morgan.

Figure 3: High-tech production remains a bright spot



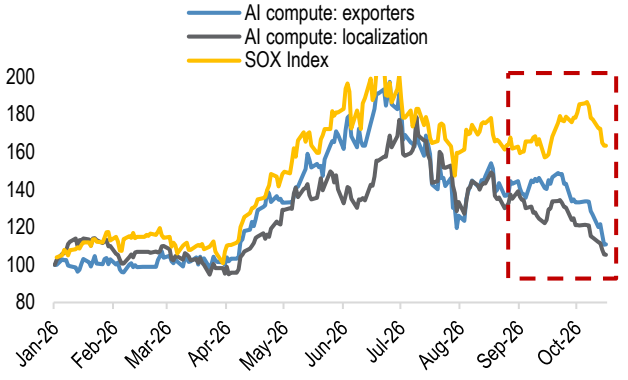
Source: Wind, J.P. Morgan.

Figure 4:CSI300 leads in high-end manufacturing exposure



Source: Wind, J.P. Morgan.

Figure 5: China AI lagged the global AI rally in September, but follows the dips in October



Source: Wind, J.P. Morgan.

Figure 6: China households are structurally under-invested in financial assets

	Cash	Deposits	WMP	Stocks	Fund products	Insurance	Bonds	Loans	Housing	TOTAL
2010	2.7%	22.9%	2.1%	7.5%	2.1%	2.3%	0.9%	0.1%	59.4%	100%
2011	2.7%	22.5%	2.9%	4.9%	1.8%	2.4%	0.7%	0.3%	61.7%	100%
2012	2.6%	23.5%	4.1%	3.2%	2.2%	2.6%	0.8%	0.3%	60.7%	100%
2013	2.4%	23.2%	5.1%	3.6%	2.3%	2.7%	0.9%	0.4%	59.3%	100%
2014	2.2%	22.4%	6.6%	5.5%	3.1%	2.9%	0.8%	0.4%	55.8%	100%
2015	1.9%	20.0%	8.5%	9.2%	4.4%	2.8%	0.9%	0.5%	51.8%	100%
2016	1.8%	19.4%	9.3%	8.1%	4.5%	3.0%	0.8%	0.5%	52.5%	100%
2017	1.7%	19.4%	8.8%	8.4%	5.1%	3.1%	0.7%	0.6%	52.1%	100%
2018	1.7%	20.3%	6.2%	3.5%	5.0%	3.2%	0.7%	0.5%	58.9%	100%
2019	1.6%	20.8%	5.9%	3.7%	4.9%	3.3%	0.7%	0.4%	58.8%	100%
2020	1.5%	20.9%	5.8%	6.7%	4.5%	2.6%	0.6%	0.2%	57.2%	100%
2021	1.4%	20.5%	5.8%	8.8%	4.7%	2.6%	0.6%	0.1%	55.5%	100%
2022	1.5%	24.2%	5.5%	5.4%	4.4%	2.9%	0.6%	0.0%	55.5%	100%
2023	1.6%	26.8%	5.2%	5.2%	4.3%	2.9%	0.6%	0.0%	53.5%	100%
2024	1.7%	29.8%	5.9%	4.1%	4.5%	3.1%	0.6%	0.0%	50.5%	100%
2025	1.7%	31.6%	6.3%	5.1%	4.7%	3.1%	0.6%	0.0%	46.8%	100%
2026E	1.7%	32.6%	6.6%	5.6%	5.1%	3.2%	0.6%	0.0%	44.5%	100%

Source: Wind, J.P. Morgan.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

J.P.Morgan

Figure 7: Key industrial policy initiatives and impacts on growth and share price returns

Industry	Landmark Policy Event	Date	Policy Significance	Top 3 listcos	5Y backtest date	5Y revenue growth	5Y profit growth	Avg. 5Y return
Telecom	Telecom restructuring and the creation of a multi-operator market	2001-2002 restructuring	Promoted full-service competition, network investment and wider mobile adoption.	China Mobile (0941 HK), China Telecom (0728 HK), China Unicom (0762 HK)	2002-2007	158%	122%	470%
Property	State Council Notice on Promoting the Sustainable and Healthy Development of the Property Market (State Council Document No. 18 [2003])	12 August 2003	Defined property as a pillar industry and supported housing marketisation, home purchases and mortgage credit.	Vanke (00002 CH), Gemdale (600383 CH), China Resource Land (1109 HK)	2003-2008	508%	689%	526%
Infrastructure / High-speed Rail / Construction Machinery	Ten measures to expand domestic demand and the approximately RMB4tn stimulus plan	9 November 2008	Prioritized railways, roads, airports, water conservancy and urban grids, creating a direct infrastructure demand shock.	CRRC (601766 CH), China Railway Group (601390 CH), SANY Heavy Industry (600031 CH)	2008-2013	145%	340%	37%
Mobile Internet	Issuance of 4G licences; Broadband China Strategy and Implementation Plan	4 December 2013	4G supported networks, smartphones and mobile applications; broadband was designated strategic public infrastructure.	Tencent (0700 HK), Alibaba (BABA US), JD.com (JD US)	2013-2018	524%	485%	89%
New-energy Vehicles / Power Batteries	Energy-saving and New-energy Vehicle Industry Development Plan (2012–2020)	28 June 2012	Established electric drive as the main strategic direction and supported vehicles, batteries, motors, control systems and charging infrastructure.	BYD (002594 CH), Ganfeng Lithium (002460 CH), EVE Energy (300014 CH)	2013-2018	155%	481%	199%
5G / Telecom Equipment	MIIT issued commercial 5G licences	6 June 2019	Marked the start of commercial 5G deployment and supported investment in base stations, optical modules, RF, network equipment and devices.	China Unicom (600050 CH), ZTE (000063 CH), Accelink Tech (002281 CH)	2019-2024	34%	73%	37%
Renewables (Solar, Wind, Energy Storage)	China announced carbon peaking before 2030 and carbon neutrality before 2060	22 September 2020	Elevated renewable energy into a long-term national strategy, followed by wind, solar and new power-system targets.	Sungrow (300274 CH), LONGi Green (601012 CH), CATL (300750 CH)	2020-2025	370%	392%	104%
AI / Computing Power / Smart Devices	AI Plus was included in the Government Work Report for the first time	5 March 2024	Shifted policy focus from AI R&D towards scaled integration with industry, consumption, smart devices and public services.	Cambricon (688256 CH), Hygon (688041 CH), Zhongji Innolight (300308 CH)	2023-now	239%	495%	625%
Humanoid Robots	MIIT published the Guiding Opinions on the Innovation and Development of Humanoid Robots	2 November 2023	China's first dedicated national-level humanoid-robot policy. It targeted breakthroughs in robot "brains," "cerebellums," limbs, core components and operating systems, alongside initial mass production by 2025.	UBTECH (9880 HK), Estun (002747 CH), Inovance (300124 CH)	2023-now	44%	21%	-3%

Source: State Council, MIIT, NBS, NDRC, J.P. Morgan. Note: the avg. 5Y return and aggregated 5Y revenue/profit growth refer to the top 3 listcos per sector.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

1.China's two-speed economy – is the export engine enough for earnings?

GDP growth has held up, but on one engine: China's GDP grew 4.7% YoY in 1H26 (1Q 5.0%, 2Q 4.3%), within the 2026 target of 4.5-5.0%. Its composition, however, has become increasingly K-shaped. In the first eight months, exports rose 14.6% YoY in RMB terms, while retail sales grew only 1.1% and fixed-asset investment fell 7.2% (Figure 8). The gap has widened since 2025, when exports rose 6.1%, retail sales grew 3.7% and fixed-asset investment fell 3.8%.

Export growth is strong but narrow, and the external cushion is becoming less reliable. Exports rose 19.3%YoY in USD terms in 8M26, led by high-tech products: integrated circuits (mainly memory chips) almost doubled, while ADP equipment, the 'new three', autos and ships all grew 35-55% (Figure 9). Lower-end consumer goods, by contrast, barely grew. This supports China's industrial upgrading but leaves exports increasingly dependent on the global technology cycle, and price-led tech exports do less for jobs and incomes than broad volume growth would. The main risk is rising trade barriers: the US has expanded tariffs and technology controls, the EU is stepping up trade-defense actions, and shipments to the EU have already declined for two months.

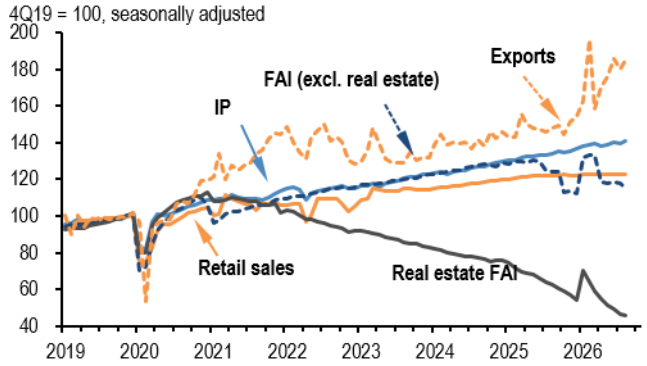
Domestic demand remains the weak leg. Consumption weakness is concentrated in autos, household appliances and electronics, and building and decoration materials. These categories face a high base after the 2025 trade-in program, soft consumer confidence and a negative wealth effect from housing. Investment is weaker still. Property development investment fell 20% YoY in 8M26, about RMB1.2tn below the same period last year and on track for a full-year decline of ~RMB1.6tn (Figure 11). Despite the strong policy push, AI capex cannot fill that gap. Per JPM estimates, China's major platforms are expected to spend ~RMB670bn in 2026E and ~RMB940bn in 2027E – much of it already counted within manufacturing and infrastructure investment.

Turning the macro into index earnings: overseas sales are only 18% of MSCI China revenue, leaving the other 82% exposed to weak domestic demand. Overseas revenue accounted for 18% of MSCI China revenue in 1H26, up from 15% in 2024, reflecting the index's growing external exposure. That exposure is concentrated: overseas revenue accounted for 56% in IT, 21% in materials and industrials, but only 6% in financials and 4% in staples (Figure 15). With more than 80% of revenue still domestic, domestic demand remains the binding constraint on earnings (Figure 13).

MSCI China consensus earnings growth expectations of 14% in both 2026E and 2027E appear somewhat aggressive. Assuming the overseas business (18% of revenue, estimated 25% of earnings) grows 20% and the domestic business (82%, estimated 75% of earnings) grows 5%, index earnings would rise ~8%, below consensus of 14% in 2026E, reflecting lingering weakness in consumption and property (Figure 14, Figure 16). Every 1pp of domestic growth moves index EPS ~4.5x as much as 1pp of overseas growth, simply because 82% of revenue is domestic. Consensus implies domestic earnings growth of close to 10%, which we see as too optimistic with retail sales growing ~1% and CPI near zero in 8M26.

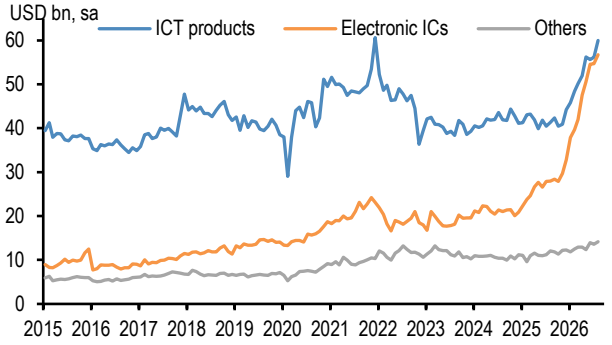
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 8: China's two speed economy



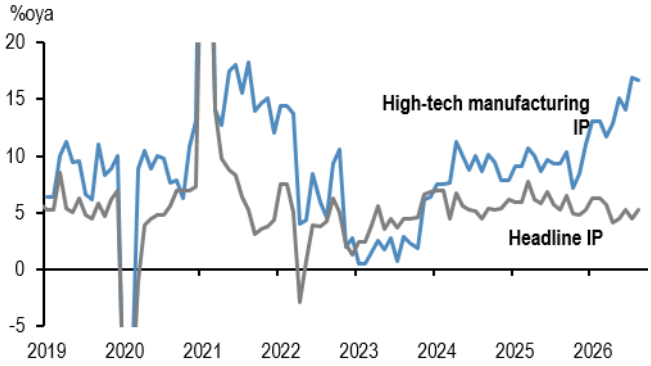
Source: China Customs, J.P. Morgan.

Figure 9: Technology products have become the key export engine



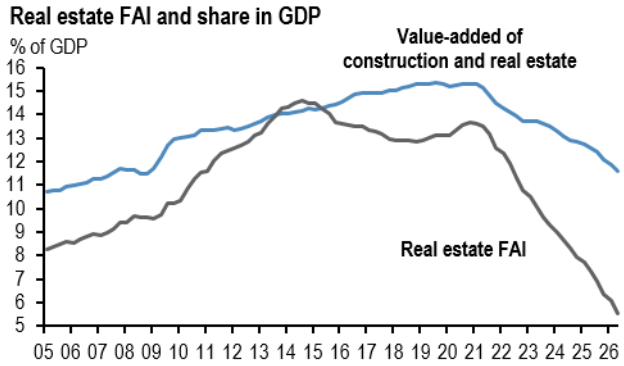
Source: Wind, J.P. Morgan.

Figure 10: Tech production remains a bright spot



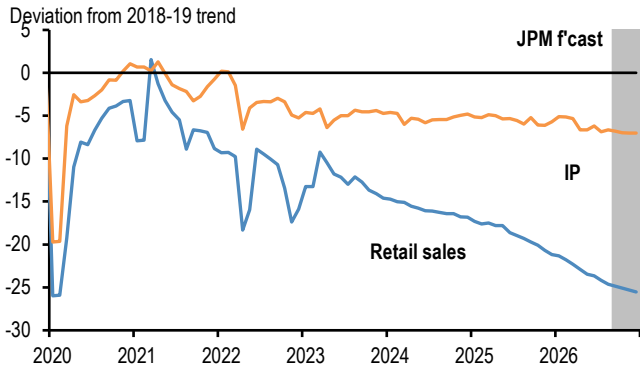
Source: Wind, J.P. Morgan.

Figure 11: A smaller contribution from real estate FAI



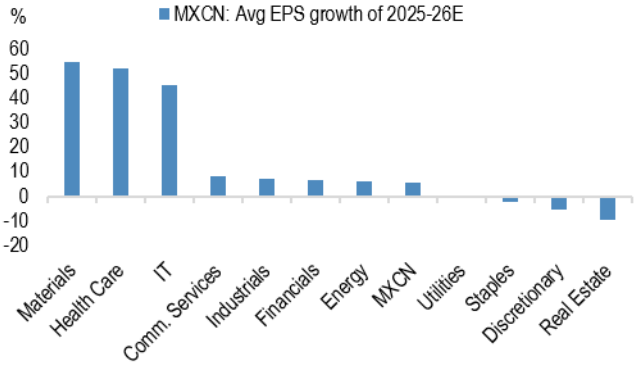
Source: Wind, J.P. Morgan.

Figure 12: Supply-demand imbalance



Source: Wind, J.P. Morgan.

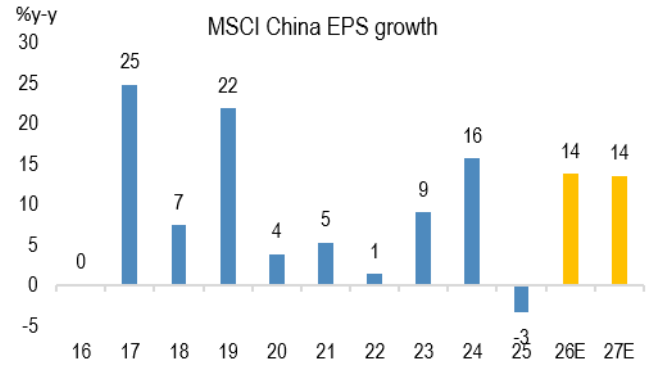
Figure 13: MXCN EPS growth: high-end manufacturing led, consumption proxies lagged



Source: IBES, J.P. Morgan.

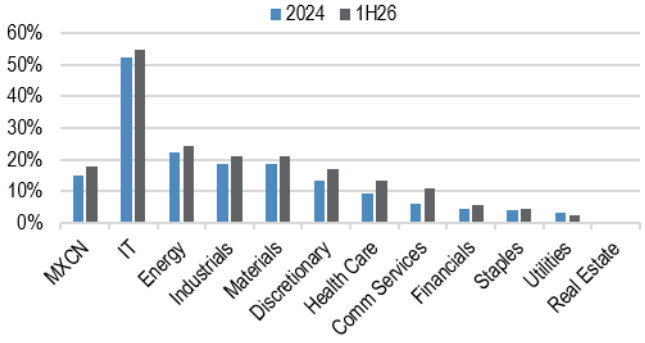
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 14: MSCI China EPS growth



Source: IBES

Figure 15: MXCN overseas revenue exposure



Source: Wind

Figure 16: Sensitivity of MXCN EPS growth to domestic and overseas growth

Domestic growth ↓ / Overseas growth →	15%	20%	25%
3%	6.0%	7.3%	8.5%
5%	7.5%	8.8%	10.0%
8%	9.8%	11.0%	12.3%

Source: J.P. Morgan.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

2. Waiting for the next 'Sep 24' moment: What would force a bigger policy response?

September 2024 was a policy pivot, driven by broad domestic weakness: soft demand, persistent deflation and a depressed stock market. In September 2024, PPI had been falling for two years, property and consumption remained very weak, and the CSI 300 was near a five-year low. With the full-year growth target at risk, Beijing changed course within days. The PBOC cut rates and launched dedicated facilities to support the stock market, and the Politburo then pledged to stabilize property and step up fiscal support. The CSI 300 rallied more than 25% in just over a week. What forced the pivot was not external demand, since exports were holding up reasonably well, but the simultaneous failure of domestic demand, prices and market confidence.

Today, the domestic triggers that forced the 2024 pivot have largely eased, with consumption and property the clear exceptions. The JPM Quantitative macro indicator (QMI) is higher in 2026 vs 2024 (Figure 20), PPI has swung from -1.8% to +3.8%, the equity market has held up despite the recent pullback and exports, already a cushion in 2024, are growing at about 15% in 8M26 (Figure 18, Figure 21). Only domestic demand is clearly weaker: retail sales grew just 0.4% y-y in August, household loans are shrinking, and there has been a protracted downturn for property price in 70 cities (Figure 22, Figure 23). With 1H26 GDP growth at 4.7%, the GDP growth target of 4.5-5% is not at risk. Policymakers can, therefore, tolerate a two-speed economy, and they are prioritizing supply-side reform and technology, through anti-involution and AI, over demand-side stimulus.

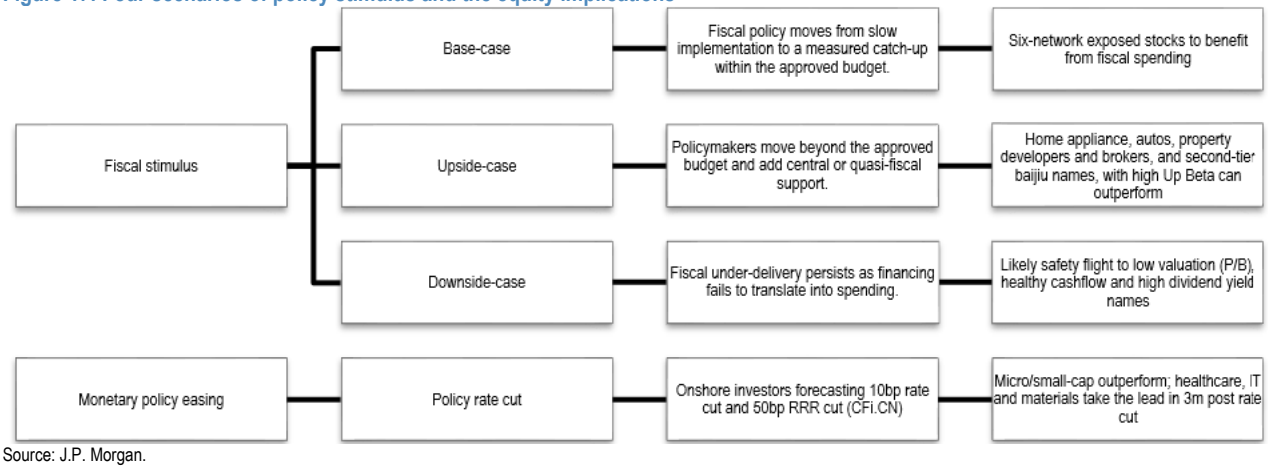
For now, policy is incremental and targeted, not a bazooka. The September mortgage subsidy is a gesture rather than a game changer, costing only about Rmb30bn a year. Fiscal policy is catching up within the approved budget rather than expanding it, centered on the 'Six Networks', with more than Rmb7tn of investment planned for 2026. At its late-September meeting, the State Council pledged to study measures to stabilize property and support employment and income. JPM China macro team's base case is fiscal execution improves from slow to measured, with faster government-bond issuance, fiscal-deposit drawdown and policy-bank funding directed at infrastructure, urban renewal, project completion and strategic investment; the impulse is supportive rather than expansionary. Over the next six months, we believe speculation will center on three events: 1) the 5th Plenum in late October, which is likely to focus mainly on Party matters; 2) the Central Economic Work Conference in December; and 3) the Two Sessions in March 2027.

We believe the most likely trigger is an export slowdown that exposes the weakness of domestic demand and shows up first in jobs. Export growth slowing to mid-single digits may serve as the precondition for a major response. We see three potential risks: 1) **Higher US rates.** The Fed's hike – US team expects one more hike in Dec is likely to weigh on US and global demand; 2) **Trade barriers.** EU safeguards and US equipment bans are reaching the sectors where China's exports have been strongest; and 3) **Export Payback.** Front-loaded exports are likely to moderate after the battery export VAT rebate is removed in January 2027.

Position for the base case, but keep cheap optionality on an upside surprise. In our base case of fiscal catch-up within budget, we stay with the Six Networks and AI infrastructure, where policy turns into orders and earnings over the next two to three quarters. In the bull case of a September 2024-style package, it may trigger a rally for domestic cyclicals, as they are under-owned with inexpensive valuations – we believe likely leaders would be home appliances, autos, property developers and brokers, and second-tier liquor names (Figure 17).

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

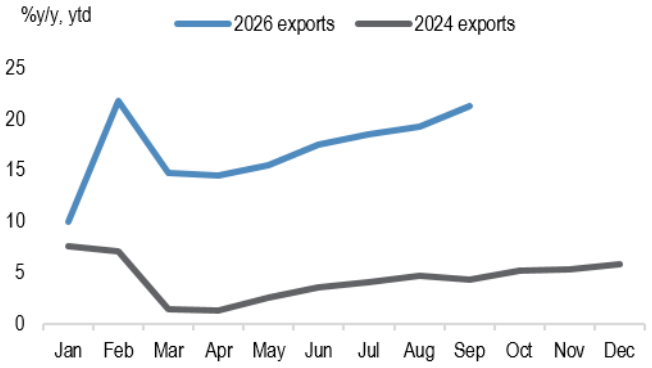
Figure 17: Four scenarios of policy stimulus and the equity implications



Source: J.P. Morgan.

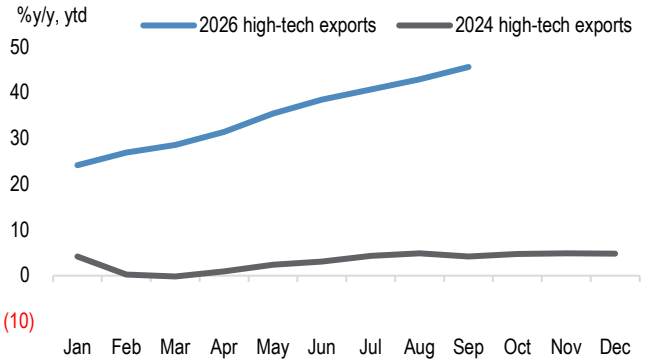
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 18: The next 'Sep 24' moment could potentially emerge if export momentum fades



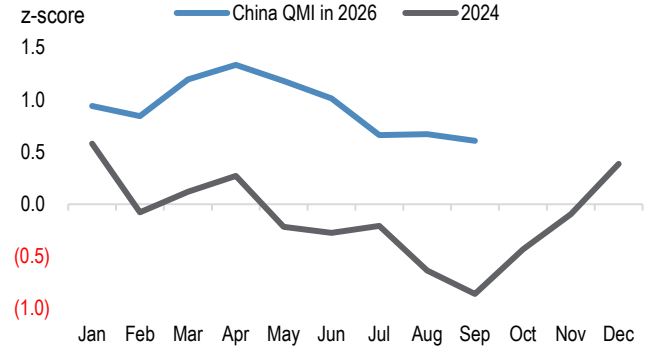
Source: China Custom, J.P. Morgan.

Figure 19: High-tech exports remain the bright spot in 2026 exports



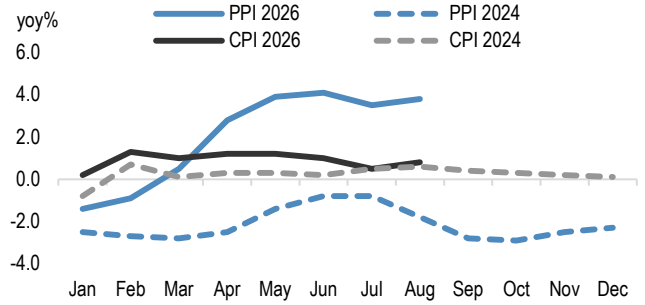
Source: Wind, J.P. Morgan.

Figure 20: China's quantitative macro indicator (QMI) is higher in 2026 vs 2024



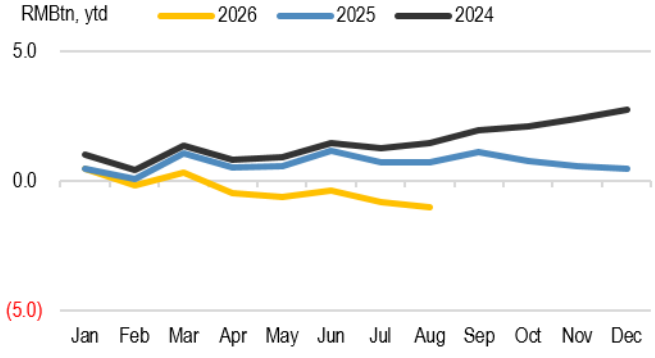
Source: J.P. Morgan.

Figure 21: PPI recovered from disinflation, although mostly driven by input cost hikes while outputs remain under pressure



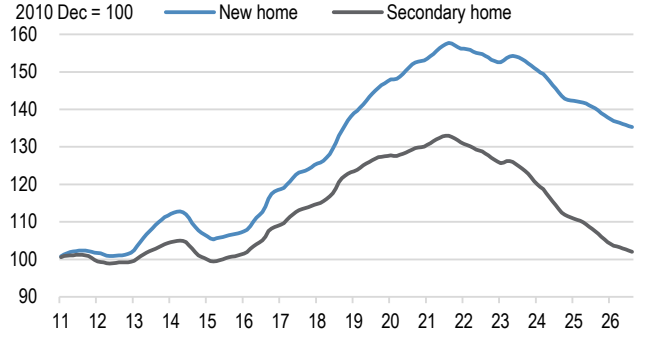
Source: Wind

Figure 22: Household new loan creation has turned negative in 2026



Source: Wind.

Figure 23: A protracted downturn of 70 cities' housing price



Source: Wind.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

J.P.Morgan

3. China's AI ecosystem: From infrastructure to applications, when will internet stocks become AI stocks?

China's AI cycle can be read as a single chain of capital: policy-anchored capex funds compute, compute is increasingly supplied by domestic chips, models turn that compute into tokens, and applications turn tokens into revenue. Right now the chain is uneven. Returns are strongest in the infrastructure layer, where demand is visible and localization is policy-driven. The model layer is growing fast but competes on price. The application layer, where Internet platforms sit, is still investing ahead of monetization. This sequencing drives our allocation: **we own infrastructure and localization as the core, select model names on pricing power, and treat Internet platforms as optionality that turns into a re-rating once AI revenue can be attributed without diluting cash flow.**

Capex: China spends about one-tenth of the US, but its spending is faster-growing, policy-anchored and less exposed to the global tech cycle. Per JPM estimates, US hyperscaler capex is expected to reach roughly US$900bn in 2026 (+93% y-y) and US$1.5tn (+70% y-y) in 2027, against about US$100bn and US$140bn for China's hyperscalers, respectively. Under China's 15th Five-Year Plan and its flagship 'AI Plus' initiative, Beijing is seeding a RMB100bn state-backed fund-of-funds to mobilize up to RMB1tn of long-term 'patient capital', and it targets more than 70% AI-agent penetration by 2027 and more than 90% by 2030, so demand is anchored by an explicit diffusion agenda aimed at the real economy. Usage is already running ahead of spend. Daily AI token consumption rose from about 100tn at end-2025 to more than 140tn by March 2026. JPM's China Internet team expects token consumption to grow about 60x over 2026-30E (Figure 27), and the JPM China Technology team expects domestic compute demand to grow at about an 80% CAGR through 2030. The gap reflects efficiency gains per unit of compute: falling cost per token expands usage, so price competition at the model layer ultimately supports infrastructure volumes.

Localization: We believe local chips can meet 80% of AI infrastructure demand by 2028, up from 40% in 2025 (Figure 25)**, and the bottleneck is shifting from chip design to foundry and HBM.** Localization is the core growth driver of the chain. With policy support, JPM expects domestic AI chip shipments to rise from about 1mn units in 2025 to more than 5mn in 2028E, led by Huawei Ascend and Cambricon. The constraint is now manufacturing rather than design. Local foundries are likely to add 150-200k wpm of advanced logic capacity over the next two to three years, but yield challenges and technology migration will slow the ramp, and the move to local HBM3/3E production is constrained by qualification timelines and access to equipment. We expect the demand-supply gap to close only gradually, and Chinese vendors to bridge it through system design rather than single-chip performance: chiplet-based, multi-die designs, which domestic packaging and test providers (OSATs) can already deliver as CoWoS-S-like solutions, and supernode solutions such as CloudMatrix384 that raise scale-up density**. That shifts value towards advanced packaging and server ODMs and OEMs, and beyond semiconductors into power, cooling, energy storage and data centers. We expect the main beneficiaries to be domestic AI chip vendors with secure foundry capacity and inventory, and the leading domestic wafer-fab equipment vendors.**

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Models: Chinese LLMs are a step behind the US frontier but cost 10% to 20% as much, and that cost-performance is winning them global share. Chinese foundation models are now in the global top tier and lead the open-weight segment. On independent benchmarks such as Artificial Analysis and LMArena, several Chinese models rank close behind the US leaders, and their strength is concentrated in coding – the use case with the highest willingness to pay and the heaviest usage (

Figure 26). Chinese Models deliver roughly 90% of the capability of the leading US models at only 10-20% of the price. Usage is following price. On global developer platforms such as OpenRouter, Chinese models together now account for a larger share of token volume than any single US lab, driven mainly by coding agents in production workflows. MiniMax already earns most of its revenue outside China, and Zhipu is scaling its API with global developers. Chinese models already lead the commoditised tier on cost and are now moving into the premium tier, where reliability and tool use matter most and where we believe the margin opportunity lies.

The model and application layer turns profitable around 2028E, but the market still prices today's revenue mix, not tomorrow's profit mix. The JPM China Internet team expects model and application operating profit to turn positive in 2028E. The layer turns profitable not because training spend falls, but because revenue outgrows a training bill that stays roughly stable. Timing, not direction, is where company outcomes diverge: labs that lead on capability and paid API growth break even earlier than peers, so the ability to fund operations through 2028E is a selection criterion. Models and applications account for about 14% of China-AI-attributable listed market value, broadly in line with their c.12% share of 2026E value-chain revenue. JPM's China Internet team expects that revenue share to rise to c.49% by 2030E, with the layer contributing about 64% of the sector's profit growth. We would pay a premium only for labs that show four things: a sustained top-tier ranking, pricing resilience through rounds of price cuts, a rising overseas revenue mix together with adoption of their own agent tools, and funding through 2028E. The JPM China Internet team's top picks are Zhipu, Alibaba and Tencent. Zhipu is the preferred exposure to differentiated model capability. Alibaba offers integrated exposure across silicon, cloud and models (Qwen). Tencent holds scarce distribution and application assets, which we believe are largely unpriced and become more valuable as model costs fall.

China Internet: Platforms are the main vehicle for AI monetization, but share prices need consumption to recover and AI profit to show up in reported earnings. China's AI economy is profitable today, but only at the bottom of the stack. Hardware captures about 93% of 2026E industry operating profit. US AI, by contrast, already earns across the full stack: cloud, APIs, enterprise and consumer subscriptions, and advertising. The JPM China Internet team expects models and applications to reach about 54% of total AI profit by 2030E. We believe China will not monetize mainly through standalone subscriptions. It will monetize through platforms and usage-based pricing, benchmarked against the labor AI replaces rather than IT budgets. The JPM China Internet team estimates a c.US$250bn B2B opportunity in China, alongside c.US$100bn of consumer demand. That makes the large Internet platforms the main vehicle for AI monetization in China. Yet China Internet stocks have underperformed YTD despite their AI exposure. The market still prices them on core businesses tied to a weak domestic consumer, and it treats AI spending as a cost until returns are visible. We believe **two catalysts could turn sentiment: 1) a recovery in China's macro and consumption, and 2) clear proof of AI monetization: attributable revenue and rising gross profit after inference costs**, before depreciation and operating costs dilute free cash flow and buybacks. Alibaba is further along on the second catalyst but more exposed to the first. Tencent's core business is more resilient, but its AI proof points are still ahead.

Our top picks in AI localization include:

- **Core: infrastructure and localization offer the highest earnings visibility.** Capex is policy-anchored and the localization ratio is rising from 40% to 80%, which gives these names the clearest earnings path in the chain. JPM Asia Tech teams' top picks in semiconductor localization are Iluvatar CoreX (AI chips), NAURA and AMEC (wafer-fab equipment), JCET (advanced packaging) and V-Test (testing). In the broader AI infrastructure build-out, their picks are Huaqin (servers), VNET (data centres), and Sungrow, CATL and TGOOD (power and energy storage). The catalysts to watch are hyperscaler capex guidance, domestic chip shipments, and foundry and HBM capacity additions.
- **Selective: in models, pay only for demonstrated pricing power.** Zhipu is our preferred exposure to differentiated model capability. The catalysts to watch are paid API growth, a rising overseas revenue mix, and gross profit sufficient to fund continued model development.
- **Optionality: Internet platforms are an accumulation opportunity ahead of the monetization proof.** We prefer Alibaba over the next three to six months, as its cloud margin and ARR are already proving the AI thesis. We see Tencent as a 12- to 18-month accumulation, with the catalysts being a broader AI rollout, specifically Xiaowei agent in Weixin. We believe both stocks would benefit further if consumption recovers.

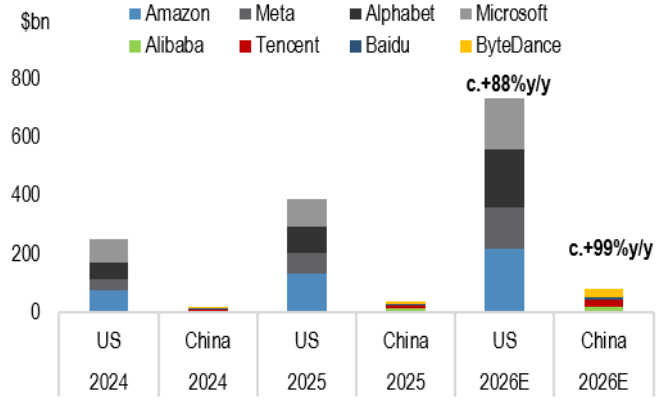
Positioning favours adding platforms at the margin. After the 1H26 deleveraging, AI hardware and localization remain crowded trades, while Internet platforms are under-owned following domestic fund selling. Adding platform exposure diversifies AI risk while keeping the upside if monetization is proven.

China AI-related stocks lagged the recent global recovery, while the US SOX Index rebounded back towards its August level. The underperformance appears to reflect investor concerns around: 1) potential US FCC restrictions on China optical modules, even though these were not included in the September round of measures, and 2) weaker-than-expected delivery momentum in AI localization due to constraints in foundry capacity and HBM supply. Within China AI, however, exporters have performed relatively better than the localization line, suggesting the market is differentiating between companies with stronger external demand exposure and those more exposed to domestic supply-chain bottlenecks.

Fundamentals appear more supportive for AI exporters with more EPS upward revisions and more reasonable valuations, but the AI localization theme remains intact in the medium term. 64% of AI export companies have seen FY1 consensus EPS upgrades since August, compared with only 28% for AI localization names. Average FY1 EPS revisions were also positive for exporters at +10%, versus -2% for the localization cohort. At the same time, exporters are trading at a lower median forward P/E of 24x (vs 56x for AI localization), while delivering a higher median ROE of 21% (vs 9% for AI localization), suggesting a more attractive combination of earnings momentum, profitability, and valuation. That said, the medium-term case for AI localization remains intact, in our view, supported by policy tailwinds and the expected rise in China's AI chip localization ratio to 80% by 2028. If foundry and HBM supply constraints ease, localization names could see stronger delivery momentum and potentially improved share-price performance.

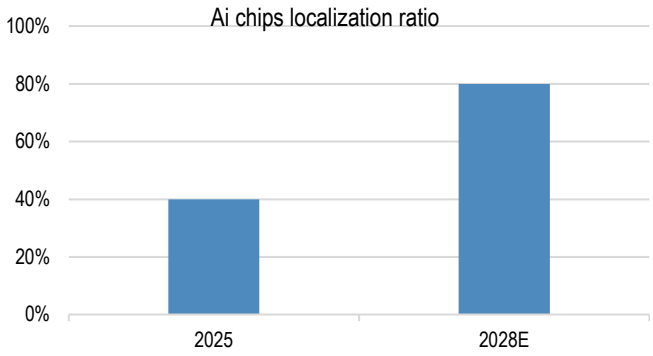
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 24: US/China hyperscalers' AI capex



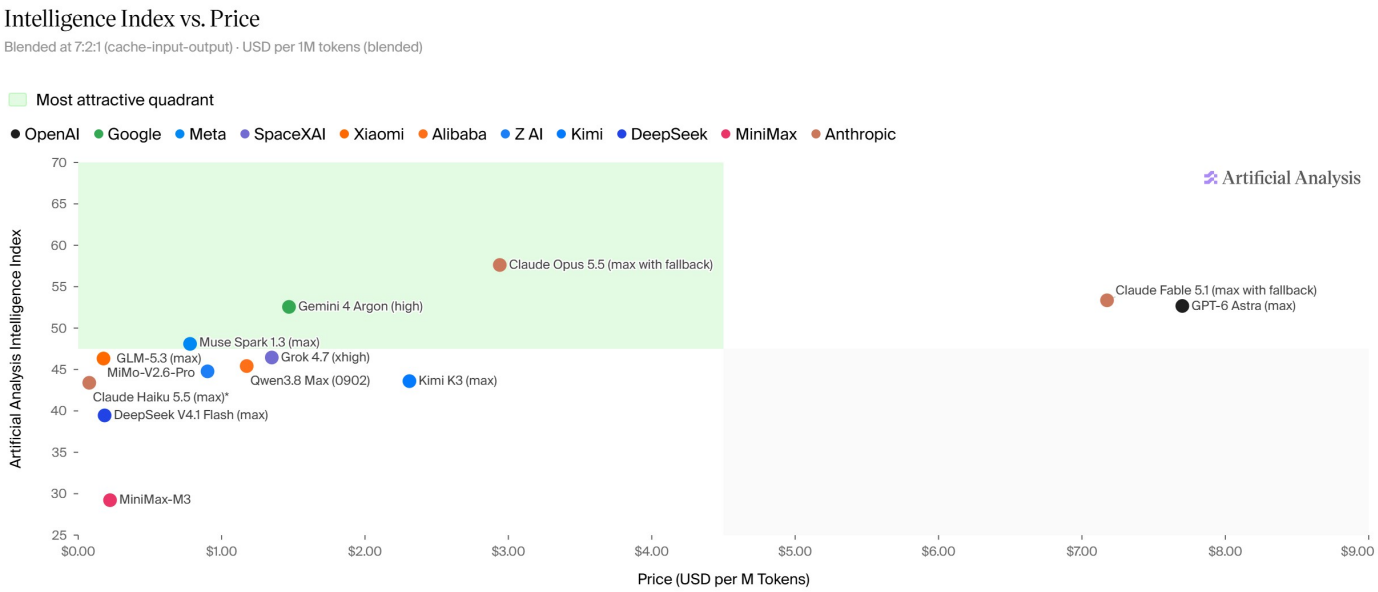
Source: J.P. Morgan estimates, company report

Figure 25: JPM forecasts China can support 80% of its AI infra demand with local chips by 2028, up from 40% in 2025



Source: J.P. Morgan estimates.

Figure 26: LLM intelligence level vs Price

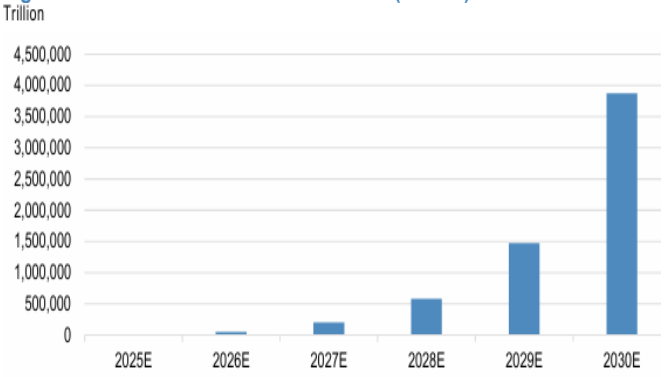


Source: Artificial Analysis

.

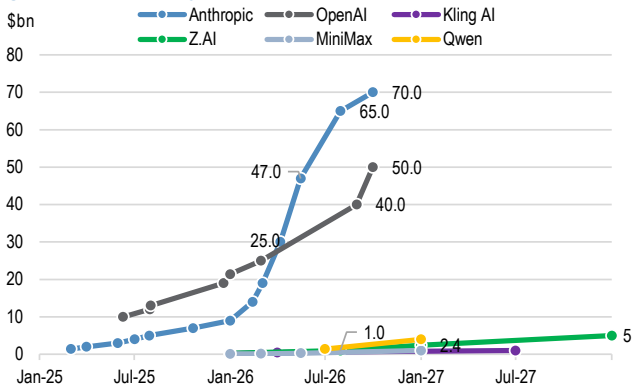
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 27: China inference token demand (annual)



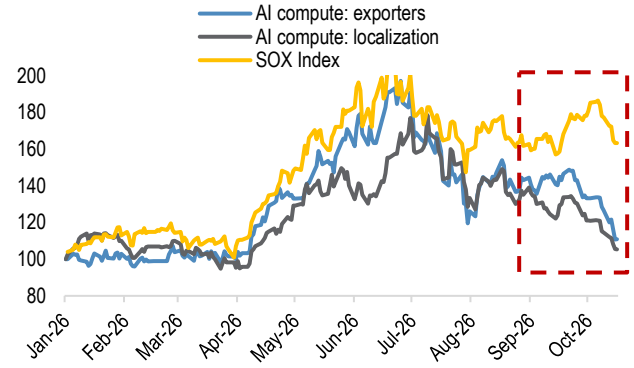
Source: J.P. Morgan estimates.

Figure 28: ARR of major LLMs



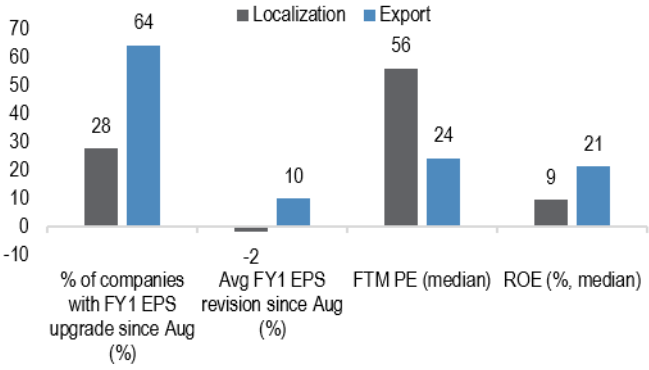
Source: J.P. Morgan estimates.

Figure 29: China AI lagged the global AI rally in September; exporters outperformed localization line



Source: Wind.

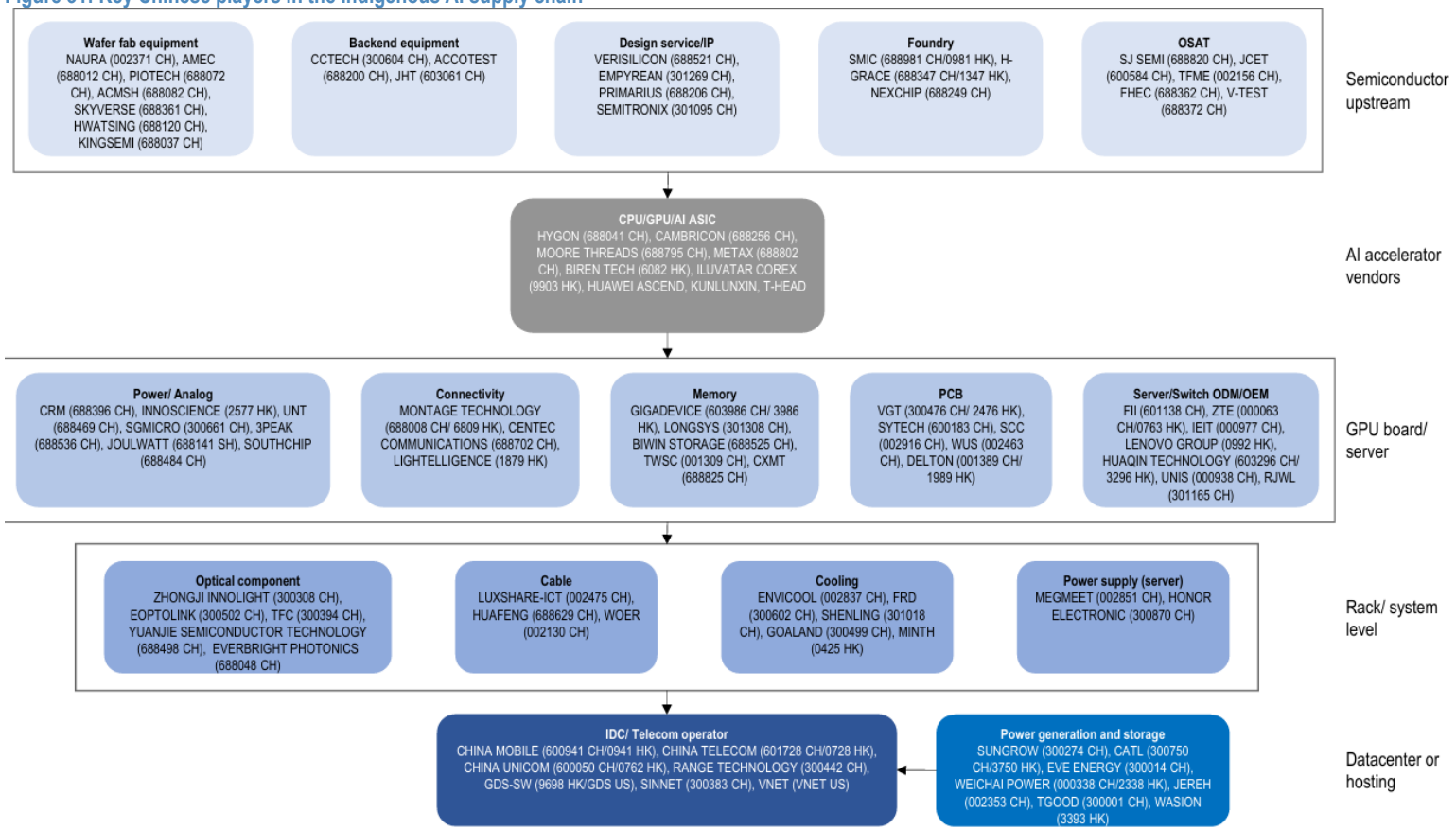
Figure 30: AI Export vs localization lines: Exporters offer stronger EPS revision and profitability at a lower valuation



Source: IBES.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 31: Key Chinese players in the indigenous AI supply chain



Source: J.P. Morgan Technology Research.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

4. Anti-involution: Which sectors are finally regaining pricing power?

After over one year of anti-involution as a top-level mandate in the Central Financial and Economic Affairs Commission, it has made uneven progress across sectors. We track 12 over-capacity industries in sequence: supply discipline first (capex and inventory days), then pricing (revenue), then earnings (net margin), to gauge the anti-involution leaders and laggers (Figure 32-Figure 33).

Leaders: logistics, chemicals and lithium have cleared all three steps, with net margins up 550-2,600 bpsYoY

Logistics is the leading sector. It was the first sector to enter the 'capex up + destocking' quadrant, in 3Q25, because pricing was coordinated directly. Yiwu raised its parcel floor price from Rmb1.1 to Rmb1.2, Guangdong pushed average prices above Rmb1.4, and 22 provinces followed with self-discipline rules. Stable prices first lifted revenue, which has grown 7-11% YoY for five straight quarters.

Chemicals reached the same outcome by a different route. The driver was spreads, not administrative pricing. Geopolitics and supply repair widened refining and petrochemical margins, while Europe's structural exit removed a marginal competitor: about 9% of its chemical capacity was shut in 2022-25 because of higher energy costs. Net margin rose ~550 bps YoY in 2Q26, to ~400bp above its ten-year average. Revenue growth recovered from -7% in 2Q 2025 to +12% in 2Q 2026, led by Rongsheng (1H26 profit +749%), Wanhua (+64%) and Baofeng (+70%). Utilization, however, is still about three standard deviations below history. The recovery has been price-led so far. That leaves volume as a possible second leg, but it also leaves earnings exposed if spreads normalize.

Lithium made the deepest supply cut and has the strongest rebound. Capex fell 63% and inventory days 30% y-y in 2Q 2026. Revenue then rose 207% and net margin expanded ~2,600bps, driven by the strong energy storage demand, and strong EV exports. Energy storage has become the largest source of incremental demand: storage batteries accounted for 34% of total battery sales. EVs added to demand through exports and larger battery packs rather than domestic volume, with battery exports up 88% y-y and average battery capacity per vehicle up 28% to 69kWh. Because the upside came mainly from price, earnings are highly sensitive to the supply-demand balance. Lithium carbonate has already fallen ~22% since end-August to about Rmb122,000/t as output resumed after summer maintenance, so sustaining the margin gains will depend on continued supply discipline.

Laggards: solar, autos and liquor are stuck at the first step, in 'capex down + restocking'

The laggards have cut capex but inventory is still building, so price competition still sets earnings. Solar is the clearest case. Supply is more than twice demand and utilization is below 40%. Inventory days rose ~65% YoY in 2Q26 despite a ~40% capex cut, and net margin is ~2,100bp below its 10-year average. Removing the export VAT rebate in April has also dampened the overseas outlet.

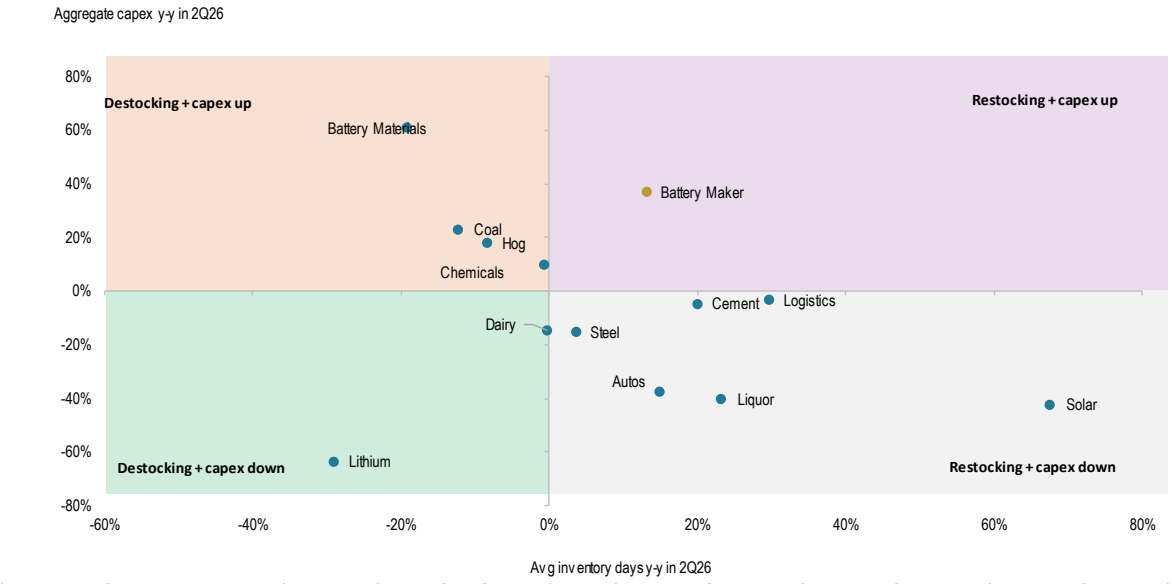
Autos face the same squeeze at home, where profit per vehicle is Rmb3,000. Automakers are offsetting weak domestic margins over earned 69% of its 1H26 revenue abroad, and BYD's overseas revenu domestic for the first time, at 53% of the total. Overseas growth, ho fully offset the domestic squeeze. BYD's group revenue fell 7% and The exit route itself is increasingly exposed to trade policy.



Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

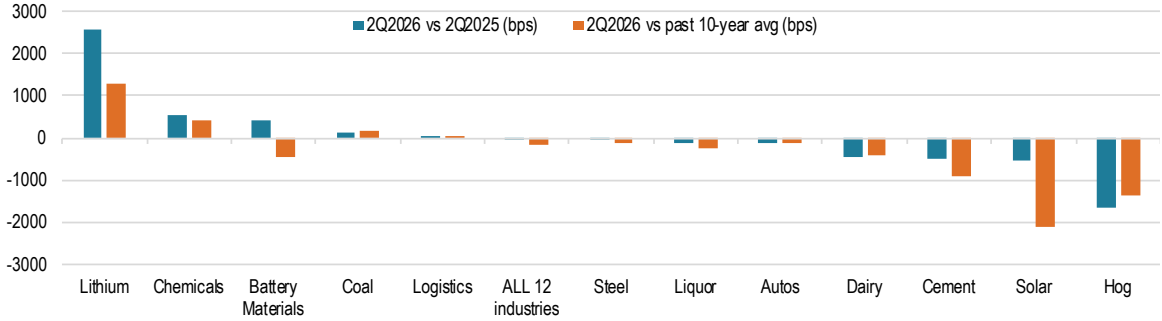
Liquor's problem is different. Inventory days are still up 23% YoY, although that is slower than the 35-45% of 2025, and revenue fell 16%. The constraint is demand, which supply policy cannot fix.

Figure 32: Anti-involution quarterly assessment on capex and inventory days



Source: Wind

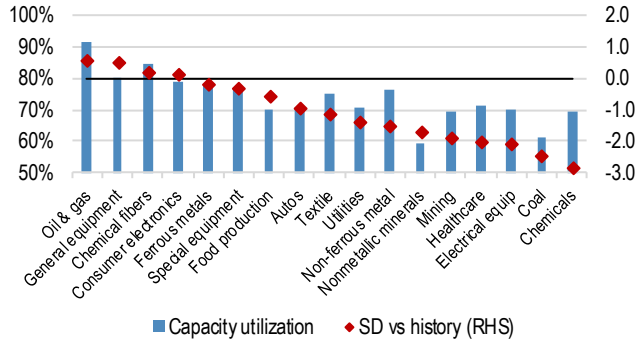
Figure 33: Anti-involution quarterly assessment on NPM



Source: Wind

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 34: Capacity utilization



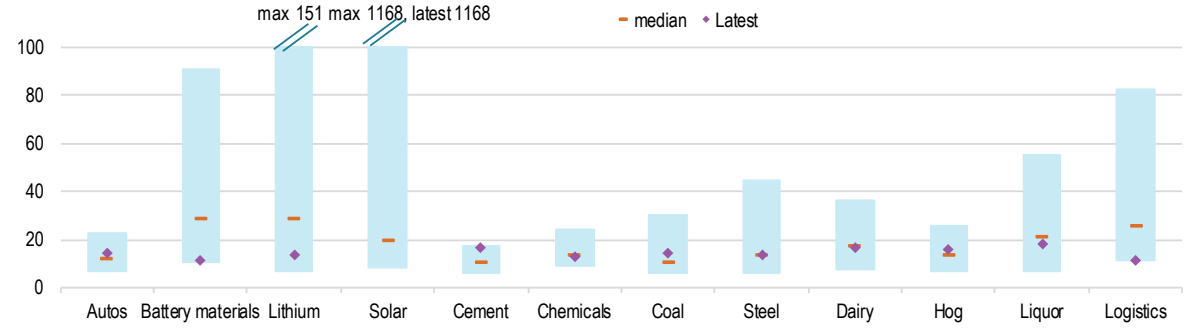
Source: Wind

Figure 35: Revenue y-y of anti-involution industries

Industry	2Q2025	3Q2025	4Q2025	1Q2026	2Q2026
Autos	11%	9%	-3%	-3%	-4%
Battery Materials	11%	30%	53%	69%	97%
Lithium	-18%	10%	43%	125%	207%
Solar	-7%	-2%	-18%	-21%	-13%
Cement	-10%	-15%	-21%	-8%	-15%
Chemicals	-7%	-3%	7%	-3%	12%
Coal	-16%	-6%	-12%	0%	37%
Steel	-7%	0%	0%	0%	1%
Dairy	5%	-1%	-3%	5%	2%
Hog	15%	-4%	-8%	-2%	-12%
Liquor	-14%	-15%	-29%	3%	-16%
Logistics	11%	8%	7%	9%	9%

Source: Wind

Figure 36: Anti-involution FTM P/E by sector



Source: Wind

5. China's manufacturing upgrade: Stronger products, better profits – but when do equities benefit?

China's manufacturing upgrade can be read as one chain, running from R&D to product mix, from product mix to margins, and from margins to index weight. High-tech output is growing nearly three times as fast as industry overall, and profits are shifting faster than output with margin expansion. Yet the upgrade has not translated into equity returns for exporters. Exporter share prices have lagged since 1Q26, held back by RMB appreciation and rising trade barriers in the EU and US.

R&D intensity reached 2.8% of GDP in 2025, above the OECD average for the first time: China's R&D spending rose 8.1% to Rmb3.93tn in 2025, and R&D intensity rose 0.11pp to 2.80%, exceeding the OECD average of about 2.7%. Basic research, long the weak spot, grew faster than the total, rising 11.1% to Rmb278bn. Its share of R&D reached a record 7.08%, although that is still well below the roughly 15% typical of advanced economies. China's R&D is predominantly applied and corporate-led, so it feeds quickly into products, cost curves and market share.

High-tech output is growing nearly three times as fast as industry, and exports are moving from labour-intensive goods to machinery and electronics. The Machinery and transport share in export has increased from 50.7% in Jan 2016 to 56.8% in July 2026, while the labor-intensive textiles, footwear and furniture share in export has declined from 25% in Jan 2016 to 16% in July 2026 (Figure 37).

In 8M26, industrial value-added grew 5.3%.

- High-tech manufacturing grew 14.2%. Within it, computers, communication and other electronic equipment grew 15.7% and railway, shipbuilding and aerospace equipment grew 12.8% y-y.

On the export side, total exports rose 14.6% in 8M26.

- Mechanical and electrical products, 64% of exports, grew 21.9%, and high-tech products, 28% of exports, grew 37.1%, led by integrated circuits (+95.4%) and computers and components (+43.3%).
- The same shift is visible in other mid- to high-end categories: autos (+47.1%), ships (+29.8%), lithium batteries (+34.4%), wind power equipment (+29.5%) and industrial robots (+13%).
- Labour-intensive exports, by contrast, were essentially flat (-0.6%).
- Export growth is, therefore, increasingly driven by higher-value goods rather than volume in low-end categories.

Profits are growing faster than output – the clearest evidence that the upgrade is about value, not volume. Industrial profits rose 15.7% to Rmb5.27tn in 8M26, while revenue grew 6.6%, lifting the revenue margin 0.44pp to 5.66%.

- High-tech manufacturing profits rose 54.7%, 39pp faster than industry overall.
- Electronics profits more than doubled (+110%) and contributed 62% of the increase in industrial profits.
- AI hardware is where the gains are steepest, profits rose 530% in optical fibre, 390% in computers, 230% in electronic materials and 100% in optical fibre cable.

Index composition is following earnings, and high-end manufacturing now carries a much larger weight. In 2021, Financials, Consumer Staples, and Industrials were the three largest sectors in the CSI 300, collectively accounting for approximately 57% of the index. By October 2026, Information Technology had become the largest sector, followed by Financials and Industrials; together, these three sectors represented around 58% of the index.

This shift reflects the growing importance of high-end manufacturing within the CSI 300. The combined weight of high-end manufacturing sectors increased from 42% in 2021 to 49% in 2026. By comparison, the equivalent weight in MSCI China rose only modestly, from 24% in 2021 to 25% in 2026, while the Hang Seng Index remained lower at 19% in 2026 (Figure 40,Figure 41).

A higher allocation to globally competitive manufacturers supports stronger structural earnings growth for the China market. At the same time, it increases the index's sensitivity to the global technology cycle and trade policy developments.

Despite strong exports, exporters' share prices have been lackluster in 2026, peaking in 1Q26 after a strong 2025 (Figure 43**). We attribute this to two main factors.**

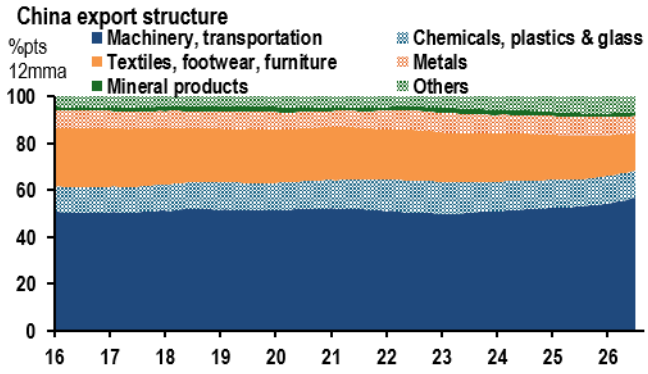
- **RMB appreciation.** The RMB has appreciated by about 4% against the USD since the end of 2025, and by about 5% against the CFETS basket. With hedging coverage low across the sector, this has fed directly into FX losses and turned strong USD revenue growth into much weaker RMB earnings growth. Market expectations of further appreciation are also weighing on sentiment towards exporters.

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

- **Tightening of trade policy in the EU and US, aimed at the very sectors where China's upgrade is most advanced.** These measures have raised concerns about the durability of export growth in the affected products, and shipments to the EU have softened since July (Figure 44).

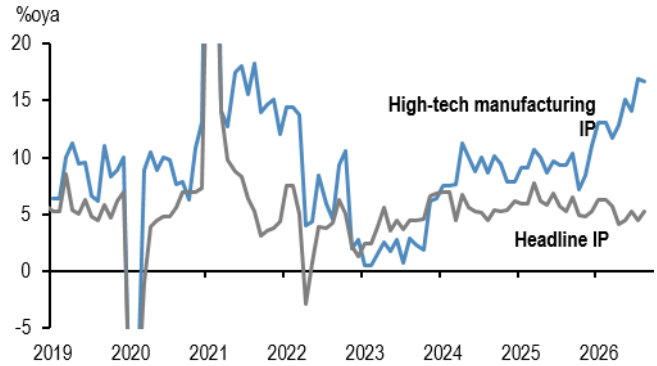
The upgrade is intact, but exporters need a catalyst from the currency or trade policy. We expect China's exports to keep growing strongly, supported by competitive products, pricing and supply chains. Share price performance, however, now depends more on two external factors: the RMB trajectory and the direction of EU and US trade policy toward China. An improvement on either would be the main catalyst for a re-rating of China's manufacturers and exporters. Over the longer term, a shift from exporting products to exporting the manufacturing system itself, through localized overseas production, would reduce both FX and trade-policy exposure. That transition will take time, but it is the structural solution to both headwinds.

Figure 37: China export structure



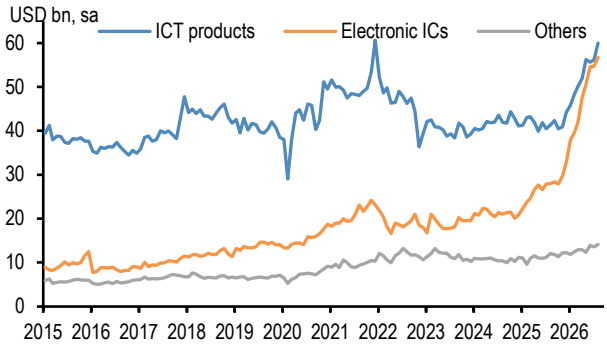
Source: China Custom, J.P. Morgan.

Figure 38: High-tech manufacturing remains a bright spot



Source: J.P. Morgan.

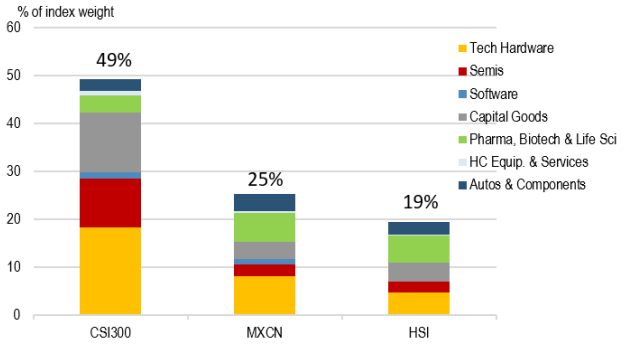
Figure 39: Technology products become the key export engine



Source: J.P. Morgan.

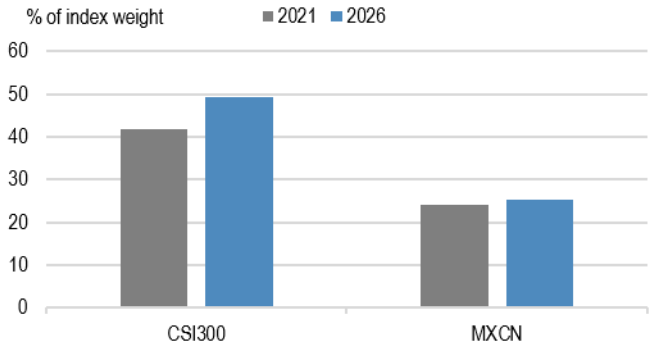
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 40:CSI300 leads in high-end manufacturing exposure



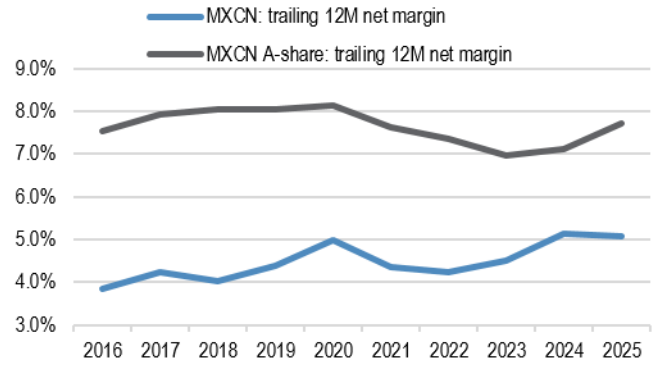
Source: J.P. Morgan.

Figure 41: A steady rise in exposure to high-end manufacturing



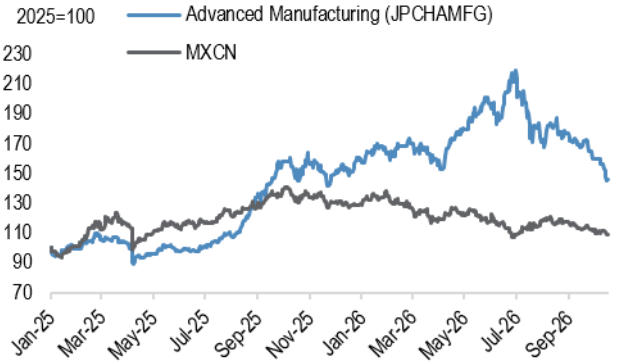
Source: J.P. Morgan. Note: High-end manufacturing sectors include Tech Hardware, Semis, Software, Capital Goods, Biotch & Life Sci, Healthcare Equipment and Auto

Figure 42: Higher exposure to advanced manufacturing does not translate to higher margin



Source: IBES.

Figure 43: JPM's China advanced manufacturing index has outperformed MXCN since mid-2026, but pulled back since Jul 2026



Source: IBES, Wind

Figure 44: Major EU and US trade policy on China

Date	Jurisdiction	Measure	Implication
Feb 2026	EU	In-depth Foreign Subsidies Regulation investigation into Goldwind, opened on the Commission's own initiative	Precedent-setting FSR case against a Chinese wind OEM; sets a precedent for wind
Mar 2026	EU	Industrial Accelerator Act proposal: "Made in EU" requirements for publicly funded solar, battery, EV etc.; Investments >€100mn from >40% capacity jurisdictions must meet 4 of 6 conditions (≤49% ownership, JV with technology transfer etc.)	Limits both exports and greenfield FDI; still in legislative process
28 Jul 2026	US (FCC)	Foreign-produced connected power inverters and advanced robotic devices added to the Covered List	New models barred from import and sale; existing authorizations unaffected
26 Aug 2026	US	Executive Order 14421: authorizes DOE to restrict imports, purchases, transfers or installations of bulk-power system equipment from covered foreign entities, including China	DOE rules due within 120 days; DOE may require removal of installed equipment
11 Sep 2026	US (FCC)	The final rule neither names nor designates optical transceivers as covered equipment	Partial reprieve for optical modules
Oct 2026 (TBC)	EU	Deadline for rebalancing EU–China trade	Sector-specific safeguards expected on EVs, solar and batteries

Source: European Commission, US FCC, The White House, J.P. Morgan.

6. Muddling through: What to do with property, consumption and other macro-proxy sectors?

The property downturn has entered its fifth year – construction, land sales and prices outside the top cities all point to a sector that remains a major drag on growth, household wealth and local government finances. In 8M26, real estate investment fell 19.9% y-y to Rmb4.8tn. new starts dropped 24.8% and new home sales value fell 13.0%. Unsold inventory remains at about 750mn sqm, barely below last year's level. Land sales revenue fell 28.6% to Rmb1.38tn, adding to the strain on local government finances. Prices are still declining outside the top cities: in August, new home prices in tier-3 cities were down 4.1%, while tier-1 cities property prices turned more stabilized since 2Q 2026.

Against this backdrop, two headline policies announced in quick succession have materially reshaped the sector landscape.

1) The '828' policy phases out pre-sales in substance. By changing the economics of property development, cutting project returns and raising up-front capital needs, it will reduce new supply. On 28 August 2026, MOHURD, the PBOC/NFRA and the CSRC jointly released a coordinated package.

- Pre-sale launches are pushed back by 3-12 months. Pre-sales are still permitted, but a project now qualifies only once its main structure has topped out. The first launch, therefore, moves from about 3-6 months after land acquisition to about 6-18 months.
- Pre-sale proceeds stay in escrow until completion. Developers previously drew on escrowed funds in stages as construction progressed. Under the new rules, the full amount stays locked until the project is completed. Construction will have to be funded mainly by bank development loans and developers' own equity, which requires substantially more internal capital.
- Mortgage proceeds are paid out only on completion. Mortgages usually account for 50-80% of pre-sale receipts and are now disbursed only on completion, typically more than two years after land acquisition. Together with the escrow rule, this delays most of a developer's sales cash by one to two years. To protect liquidity, developers will have to slow the pace of land acquisition.

2) The '929' mortgage subsidy points in the right direction but is not a game changer. Any support to sales will be concentrated in tier-3/4 cities. On 29 September, the Ministry of Finance, the PBOC and the NFRA jointly announced a nationwide mortgage interest subsidy.

- From 1 October 2026, eligible buyers receive a 100bp subsidy on their mortgage rate for five years, lowering the effective rate from 3.05% to 2.05%. To qualify, a purchase must meet all three of the following criteria:1) it is a first home; 2) the unit is under 120 sqm; and 3) the price is below Rmb1.5mn.

The subsidized loan amount is capped at Rmb1mn, so the maximum benefit per buyer is about Rmb50K over the full five years.

Limited reach. The size and price limits exclude most homes in higher-tier cities, so eligible transactions will be concentrated in tier-3/4 cities. The subsidy may lift sales volumes there at the margin. With inventory in tier3/4 cities still above 35 months levels, we do not expect a visible effect on home price stabilization in the near term.

Slower land acquisition will hit land sales and add to pressure on local government revenue. It will also drag on new starts and property investment over the next 12-18 months. The upside is that longer cash collection cycles will restrain land purchases and, with them, future housing supply, which could bring forward price stabilization in tier-1 and tier-2 cities. Shanghai has already stabilized in 2026, and JPM's China Property team expect more tier-1 cities to follow in 2027, although this has yet to be proven.

A broader consumption recovery may take time amid moderate income growth and continued pressure on household wealth. Retail sales grew only 1.1% y-y in 8M26, down from 3.7% in 2025, and slowed to just 0.4% in August (Figure 46). The weakness is structural rather than cyclical. Per-capita disposable income grew 5.2% nominal in 1H26, but urban median income rose only 4.0% (Figure 45). The wealth effect is the main reason. Home prices are still falling y-y in most cities, by 2.7% for new homes and 4.9% for secondary homes in tier-2 cities, and housing makes up the bulk of household wealth. Until prices stabilize more broadly, we believe households will keep prioritizing saving over spending.

Strong exports have yet to translate into a broad improvement in employment, wages and household spending, because today's export growth is capital-intensive rather than labour-intensive. The sectors driving exports, such as electronics, semiconductors, power equipment, autos and ships, generate high profits per worker but relatively few jobs and modest wage gains. The labour-intensive categories that employ far more people, such as apparel, furniture and toys, saw exports fall 0.6% in 8M26. As a result, the export boom has lifted corporate profits and index earnings much more than household incomes. That is why record exports and soft consumption can coexist, and why we do not expect the external cushion to translate into a broad consumer recovery.

Evolving policy and regulatory considerations may add to the near-term challenges facing the consumer. The market is focused on three concerns:

- Social security back payments. Stricter collection would raise labour costs, particularly for SMEs and labour-intensive businesses, which could squeeze profitability and hiring.
- Preferential tax rates. A potential tightening would reduce after-tax earnings for companies that currently benefit from them.
- Offshore trusts. Increased personal income tax scrutiny of offshore trusts could prompt founders and major shareholders to sell shares to fund tax liabilities, adding to supply in consumer stocks.

Each of these could weigh on business profitability, employment and household spending at a time when the consumer is already fragile.

It is too early to position for a broad recovery in property or domestic demand, but light positioning and low valuations create selective, asymmetric opportunities. With household income growth subdued and the wealth effect still negative, we do not expect a broad-based recovery in property or consumption in the near term. That said, positioning in both sectors is light, expectations and valuations are low. The bar for positive surprises is therefore low, and we believe selected names offer an attractive risk-reward skew as well as diversification away from the crowded AI and export trades. We would focus on two groups:

1. Leading SOE developers and property agents. Leading SOE developers' stronger funding access position them to gain share as the 'post pre-sales' regime accelerates industry consolidation, and property agents benefit from the growing secondary transaction market share.

2. Consumer names with company-specific stories. These are category leaders with resilient earnings, high-dividend names, and companies with clear alpha drivers, such as turnaround stories or overseas expansion.

What would make us more constructive on the bottom half of the K?

- **First, property price stabilization broadening beyond Shanghai.** Consecutive month-on-month gains in secondary home prices across more tier-1 and top tier-2 cities would show that stabilization has moved from a single-city story to a broader market trend (Figure 47).
- **Second, an end to seller capitulation in the secondary property market.** Falling listing volumes and a smaller share of listings with price cuts would show that distressed supply is being absorbed.
- **Third, rental yield moving above mortgage rates.** Once effective mortgage rates (currently at 3.1%) fall below average rental yields, currently about 2.3%, households have a clear financial case for owning rather than renting, which would support genuine end-user demand (Figure 48).
- **Fourth, a household-focused stimulus at scale.** Direct consumption subsidies, childcare and pension top-ups, or a central-government-funded programmed to absorb housing inventory.

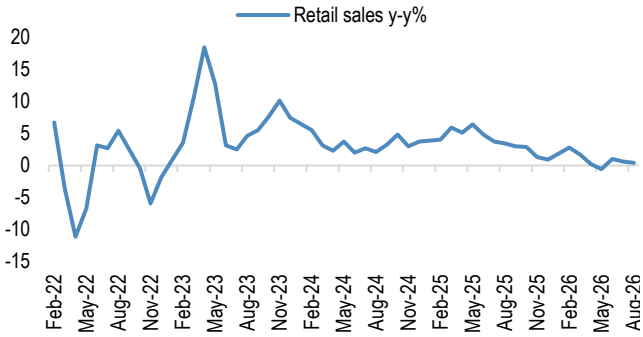
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 45: Disposable income growth at only +4%yoy



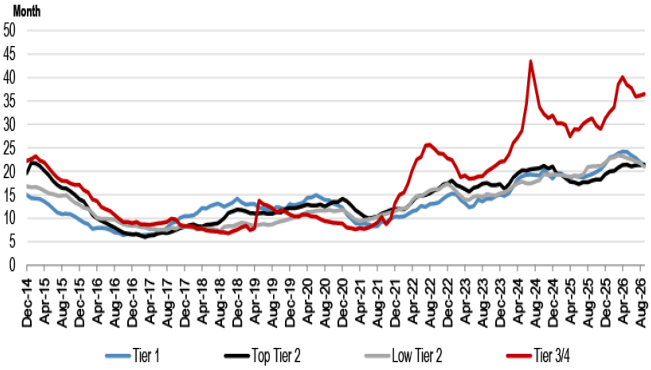
Source: Wind

Figure 46: China retail sales



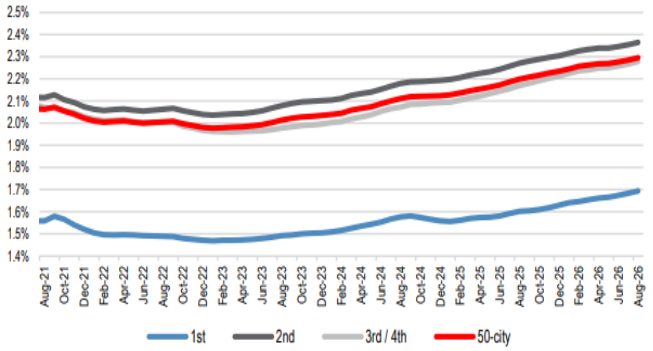
Source: Wind

Figure 47: Primary homes - inventory month by tier



Source: CREIS, J.P. Morgan China Property Research

Figure 48: Rental yield by tier



Source: CREIS, J.P. Morgan China Property Research

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

J.P.Morgan

7. China's Liquidity Cycle: What could turn household savings into a market tailwind?

Households are in the early to middle stage of a multi-year shift from deposits into financial assets. The direction is structural, but the pace is pro-cyclical and tracks market return closely. Three forces keep the direction in place: 1) real deposit rates are close to 0%; 2) households hold an unusually low share of their wealth in financial assets; and 3) policy is pushing savings towards capital markets.

Excess deposit accumulated during the COVID period are gradually shifting into financial markets, with the balance declining from RMB9.1tn in 2023 to RMB6.0bn in June 2026. Household deposit growth has slowed from a peak of 19% y-y in February 2023 to about 8%, below the 11% average of 2010-19. The JPM Financials team estimates excess household deposits, measured against the pre-Covid trend, peaked at Rmb9.1tn in 2023 and had fallen to Rmb6.0tn by June 2026 (Figure 51). At the same time, there has been a sharp bounce in the growth of deposits from non-bank financial institutions (NBFI), which include deposits from brokers and insurance companies (Figure 49, Figure 50).

One of the key drivers of the shift in household asset allocation is the sharp decline in time deposit rates. The 3Y time deposit rate has contracted by ~135bps since 2023. In an environment of low inflationary pressure, a continued shift from direct to indirect financing, low loan demand from private and retail segments and the lack of RMB depreciation pressure, we believe the risk of a deposit rate hike is low. On the other hand, the 1Y time deposits rate (0.95%), is close to the August CPI of 0.8%, real interest rate is close to zero, supporting continued household asset allocation from deposits to financial products.

Chinese households remain structurally under-invested in financial assets, while property is increasingly unable to serve as the default store of value. We estimate that Chinese households' allocation to property has declined from 56% in 2021 to 45% in 2026. Despite this decline, property exposure remains significantly above the US level of 23%. By contrast, allocation to financial assets, specifically equities and fund products, remains low. We estimate that these assets accounted for 11% of Chinese household wealth in 2026, recovering from 9% in 2024 but still below the 14% level reached during the 2021 bull market (Figure 54). With China's property market now in its fifth year of decline and deposit rates remaining low, we believe there is further room for household allocation to shift toward equities. However, the pace and scale of this reallocation will likely depend heavily on stock market performance and investor confidence. **We estimate that every 1 percentage point increase in household allocation to the equity market could generate approximately RMB5.3tn of inflows, equivalent to around 10% upside to the current level of household equity market allocation.**

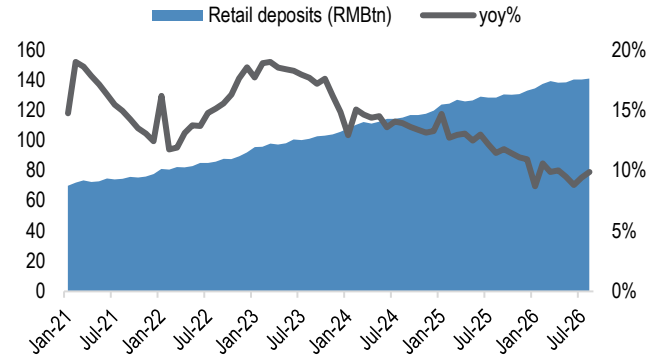
Onshore equity funds, particularly private funds, have seen a sharp 63% increase in AUM since mid-2025, although they have experienced some recent pullback: Onshore private funds (mainly targeting high net worth individuals) AUM saw a sharp jump of 63% from Jun-2025 to Rmb9tn in Aug-2026 (Figure 55), indicating the high net worth individual's strong interest to participate in market. Hybrid funds AUM saw a 46% jump from Jun-2025 to Rmb4.7tn in Aug-2026 (Figure 56).

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Policy appears to favor a 'slow bull' market rather than a sharp, momentum-driven rally, with the national team increasingly acting to smooth market volatility in both directions. When the market showed signs of overheating in January, we estimate that national team were net sellers, with outflows of around RMB700bn from January 2026 to early July, using CSI 300 ETF flows as a proxy. Since mid-July, the national team appears to have stepped back in to support the market as sentiment weakened, but the scale of intervention has remained measured rather than aggressive, with estimated net inflows of around RMB50bn (Figure 52). This suggests policymakers are not aiming to push the market sharply higher, but rather to reduce downside volatility, prevent disorderly corrections and maintain a more sustainable upward trend.

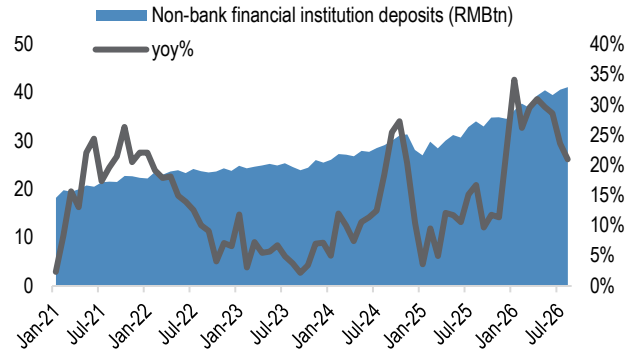
Sustained inflows will ultimately depend on earnings, not just low rates. Low deposit rates push money out of the banks, but returns decide where it goes. We expect it would first into low-volatility wealth-management, insurance and 'fixed-income-plus' products, and then to equity markets gradually, hinging on the performance. The allocation to equity markets would accelerate if earnings growth takes over from re-rating as the driver of returns and volatility stays contained.

Figure 49: Retail deposit growth has moderated



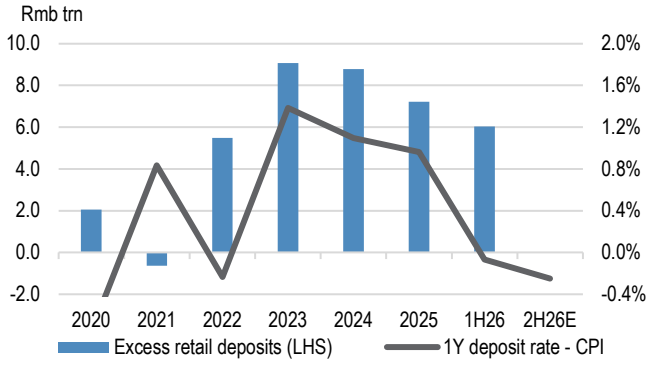
Source: Wind

Figure 50: Non-bank FI deposits growth has accelerated



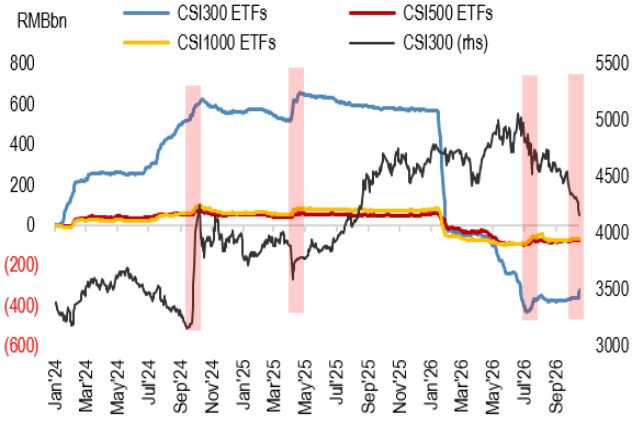
Source: Wind

Figure 51: JPM financial research estimates Rmb6tn excess deposit in 1H16, down from Rmb9tn in 2023



Source: Wind, J.P. Morgan estimates

Figure 52: Cumulative ETF net flows by indices, national team's flows shows signs of uptick



Source: Wind

Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 53: JPM estimates on Chinese household asset allocation in monetary value

(Rmb trn)	Cash	Deposits	WMP	Stocks	Fund products	Insurance	Bonds	Loans	Housing	TOTAL
2010	3.7	31.2	2.8	10.2	2.9	3.2	1.2	0.2	80.9	136.3
2011	4.2	35.2	4.6	7.7	2.8	3.8	1.1	0.4	96.3	156.1
2012	4.5	41.0	7.1	5.5	3.9	4.6	1.4	0.6	105.8	174.4
2013	4.9	46.5	10.2	7.2	4.7	5.4	1.8	0.8	118.8	200.4
2014	5.0	50.7	15.0	12.4	7.1	6.5	1.9	1.0	126.2	226.0
2015	5.2	55.2	23.5	25.4	12.1	7.8	2.4	1.3	143.2	276.2
2016	5.6	60.7	29.1	25.3	14.1	9.4	2.5	1.6	164.0	312.2
2017	5.8	65.2	29.5	28.4	17.2	10.4	2.5	2.0	175.5	336.6
2018	6.1	72.4	22.0	12.3	17.9	11.5	2.6	1.7	209.7	356.3
2019	6.4	82.1	23.4	14.5	19.2	13.0	2.7	1.4	232.5	395.2
2020	6.6	93.4	25.9	29.9	20.1	11.8	2.8	0.7	255.1	446.3
2021	7.0	103.3	29.0	44.3	23.7	13.3	2.9	0.4	279.1	503.0
2022	7.6	121.2	27.7	27.1	22.0	14.3	3.0	0.0	278.1	501.0
2023	8.1	137.9	26.8	26.9	21.9	15.0	3.1	0.0	275.4	515.1
2024	8.6	152.3	30.0	20.7	22.8	15.7	3.2	0.0	257.7	510.8
2025	9.0	167.0	33.3	27.1	24.8	16.3	3.3	0.0	246.9	527.7
2026E	9.2	173.7	35.0	29.7	27.2	16.9	3.4	0.0	237.0	532.2

Source: Wind, J.P. Morgan.

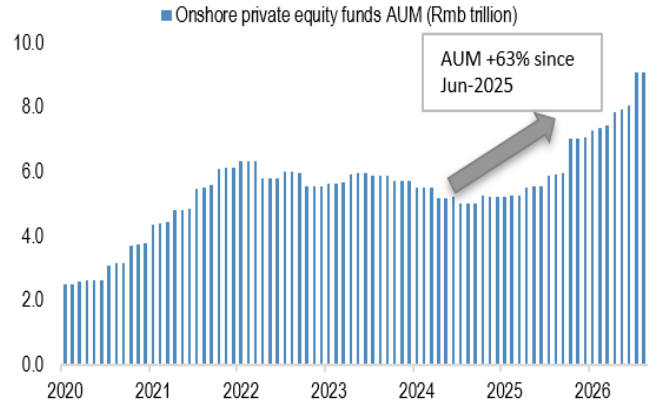
Figure 54: JPM estimates on Chinese household asset allocation breakdown

	Cash	Deposits	WMP	Stocks	Fund products	Insurance	Bonds	Loans	Housing	TOTAL
2010	2.7%	22.9%	2.1%	7.5%	2.1%	2.3%	0.9%	0.1%	59.4%	100%
2011	2.7%	22.5%	2.9%	4.9%	1.8%	2.4%	0.7%	0.3%	61.7%	100%
2012	2.6%	23.5%	4.1%	3.2%	2.2%	2.6%	0.8%	0.3%	60.7%	100%
2013	2.4%	23.2%	5.1%	3.6%	2.3%	2.7%	0.9%	0.4%	59.3%	100%
2014	2.2%	22.4%	6.6%	5.5%	3.1%	2.9%	0.8%	0.4%	55.8%	100%
2015	1.9%	20.0%	8.5%	9.2%	4.4%	2.8%	0.9%	0.5%	51.8%	100%
2016	1.8%	19.4%	9.3%	8.1%	4.5%	3.0%	0.8%	0.5%	52.5%	100%
2017	1.7%	19.4%	8.8%	8.4%	5.1%	3.1%	0.7%	0.6%	52.1%	100%
2018	1.7%	20.3%	6.2%	3.5%	5.0%	3.2%	0.7%	0.5%	58.9%	100%
2019	1.6%	20.8%	5.9%	3.7%	4.9%	3.3%	0.7%	0.4%	58.8%	100%
2020	1.5%	20.9%	5.8%	6.7%	4.5%	2.6%	0.6%	0.2%	57.2%	100%
2021	1.4%	20.5%	5.8%	8.8%	4.7%	2.6%	0.6%	0.1%	55.5%	100%
2022	1.5%	24.2%	5.5%	5.4%	4.4%	2.9%	0.6%	0.0%	55.5%	100%
2023	1.6%	26.8%	5.2%	5.2%	4.3%	2.9%	0.6%	0.0%	53.5%	100%
2024	1.7%	29.8%	5.9%	4.1%	4.5%	3.1%	0.6%	0.0%	50.5%	100%
2025	1.7%	31.6%	6.3%	5.1%	4.7%	3.1%	0.6%	0.0%	46.8%	100%
2026E	1.7%	32.6%	6.6%	5.6%	5.1%	3.2%	0.6%	0.0%	44.5%	100%

Source: Wind, J.P. Morgan.

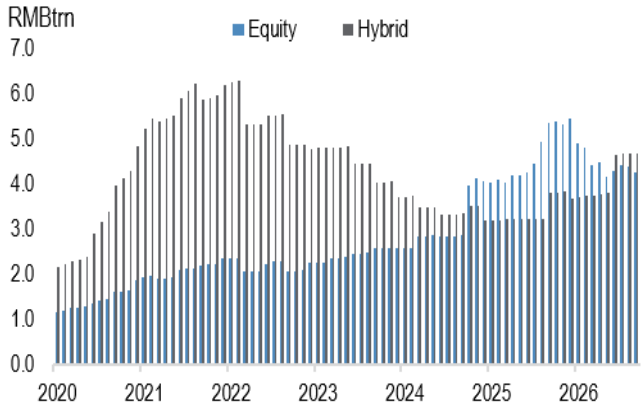
Chloe Liu, CFA
(852) 2800-0853
chloe.x.liu@jpmorgan.com

Figure 55: Onshore private equity funds AUM recorded 63% growth since Jun-2025



Source: Wind

Figure 56: Onshore equity and hybrid mutual funds AUM – Hybrid mutual funds AUM recorded 46% growth since Jun-2025



Source: Wind