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There Are Dangers to Overestimating China

It is time to ask if policies intended to shut out China are actually leading to innovation, jobs, security, and a stronger United States.

Critics of U.S. engagement with China emphasize the dangers of underestimating that nation's capabilities and its leaders' malign intentions. Yet too many steps to limit U.S.-China economic interactions overestimate the power of China's party-state and its control over Chinese firms. Rhetorically, U.S. policymakers are imitating China's leaders by pursuing a "**securitization of everything**," whether or not a particular Chinese action actually poses much of a threat.

Even more problematic, U.S. policy reflects little awareness—or evaluation—of the costs of overestimating China. These costs include: misallocating economic and political resources, embarking on potentially ineffective policies, and ignoring second-order consequences (see also the Nahm memo elsewhere in this report). To address ongoing missteps, the new administration must ask: Is shutting out Chinese firms and beefing up U.S. protectionism actually leading to innovation, jobs, security, and a stronger United States?

FIRM GROUND

Building effective policy approaches to China, as anywhere, requires an informed perspective of its intentions and capabilities. Intentions are notoriously hard to parse in the context of a great power competition characterized by mixed signals of reassurance and aggression. Still, Xi's overall direction is clear.

Few can doubt that Xi Jinping seeks to build a strong economy that can resist threatening actions by the United States. His goal is "rejuvenation" of the Chinese economy that combines both mercantilism and globalization. This philosophy goes back at least to Hu Jintao's policy of indigenous innovation. **Xi's triumphalist tone**, now bolstered by policies to develop cutting edge technology in "**new quality productive forces**," shows he aims to develop China into a technological powerhouse.

Xi also has sought to enhance the party's tools to monitor and influence firms, as my work with **Meg Rithmire and Kellee Tsai** has shown. These tools include: mandating party cells in all firms; blurring the lines between state and private companies; and passing new laws over national security and state secrets. Such moves have alarmed U.S. policymakers and U.S. companies, as they put teeth into the previously vague risks associated with Chinese firms.

Nevertheless, perceived intent does not equal capabilities or outcomes. That China's party-state continues to have **difficulty controlling and incentivizing** its firms is unambiguous. China's government has long produced plans that offer rough guidance, often with subsidies. But Beijing's restraints on companies fail to rein in problematic behavior; firms often overreact or go their own direction. The plights of the **real estate sector** and of **non-performing loans** are only the most recent examples.

Firms, even state-owned ones, often are more dedicated to making money than to following a party line. There is, as yet, little evidence that the party presence in firms has altered how they operate. To depict successful Chinese firms as mere agents of an all-controlling party is naïve, distorts perceptions, and thereby distorts U.S. policy.

Thus, although Chinese economic policy has helped produce major achievements, it often overshoots or even fails. U.S. policy should account for both. It is no secret that China has sought to bolster sensitive industries through **policies and subsidies**. U.S. vigilance in promoting some domestic industries at home, notably semiconductors that are core to national security and technology, is therefore appropriate.

Elsewhere, however, China's efforts to build competitive industries are not directed at competing with or weakening U.S. national security, as is often **depicted**. China's policy toward electric vehicles, for example, is focused on stimulating a domestic market—an effort characterized by much **clumsy and wasteful industrial policy**. Even though a handful of competitive Chinese firms are thriving, over 150 have stuck their toes in the market, with many failing. Moreover, it is uncertain how much of these flourishing firms' success is due to **subsidies**. Given China's extremely competitive automobile landscape, it is plausible that its healthy EV firms would have succeeded with minimal funding.

In short, the context of economic competition with China matters for U.S. policy.

THREE WAYS FORWARD

U.S. policy can get China more right in three ways. First, it can better differentiate between low-level and high-level threats to economic prosperity as well as to national security. What belongs in these 'threat buckets' should be discussed and debated, following a principled risk-based approach (see also the Farrell and Triolo memos elsewhere in this report). At present, nearly all sectors in the China-U.S. economic relationship are deemed high-level threats.

Where the administration can readily agree on high-level security concerns, such as for advanced semiconductors, policy responses might include outright bans and restrictions on a Chinese presence, or a rapid build out of U.S.-secured alternatives. In contrast, low-level threats should not be met with overreactions of the sort seen in outright bans by states on **land sales** to Chinese individuals or companies (see also the Gorski & Toomey memo elsewhere in this report). The 25% tariffs on **facemasks** and **regressive rules** on **low-value sales** from Chinese online retailers such as Shein are other examples. In the green technology space, Chinese advancements in carbon capture do not rise to the level of a security threat, although battery technology may.

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Second, U.S. policy should acknowledge the substantial costs to U.S. consumers and businesses of a securitization of everything. Numerous analyses emphasize the inflationary and job-destroying **impact of tariffs** that have already been imposed and of even more expansive measures—notably **the possible revocation** of China's Permanent Normal Trade Relations (PNTR) status **threatened by the Trump administration**. Particularly when such tariffs are imposed on low-threat items, which many Chinese imports are, the costs—especially to U.S. consumers—are unwarranted. While our own industrial policies may bolster important sectors of the U.S. economy on some dimensions, **job creation** thus far has been disappointing (see also the Gallagher memo elsewhere in this report).

Third, U.S. policy should correct weaknesses in many tools currently proposed or used to address concerns over threats from China. Tools cannot be effective if they lack carefully drawn goals and metrics—outcomes and timeframes—with which to monitor progress. When policies to catch up with China are unequal to the task, they should be abandoned. For example, the United States is already far behind China in solar technology and production capacity, with Chinese panels 44% cheaper according to a ***Wall Street Journal*** analysis.

Seeking to catch up is unnecessary and misguided. Building U.S. capacity for EVs behind a protectionist wall of tariffs and industrial policy may be a reasonable, if costly, economic decision, but only if the federal government has the follow-through and levers with industry to make it successful. Fundamentally, policymakers should ask: Is it worth the significant expense to catch up for products that are relatively low-threat?

ANSWER TOUGH QUESTIONS

An even more difficult issue concerns the very capacity of U.S. agencies to oversee the myriad initiatives underway. Bold measures such as the Inflation Reduction Act and controls on exports and outbound investment require that the government extensively monitor firms—not just from China but from the United States and its allies and partners—for supply chain actions and policy violations. This is a tall order. It is not clear the United States has the personnel or, normatively, that it should want to further build out this bureaucratic capacity. Expansive government monitoring of firms would take the United States in a new direction toward a much larger state presence in directing economic goals.

Lack of bipartisan consensus on many of these actions also hinders the long-term focus needed for industrial policy to succeed. Ironically, the Trump administration's stated **commitment to cut costs and bureaucracy** contradicts the idea that the United States needs to use state tools to counter China's threat.

Charles Darwin, among others, wrote of two types of scientists: "lumpers," who create broad categories for analysis; and "splitters," who attend to the nuances within categories. U.S. worries about China's firms and the threats they pose to national security veer too much toward lumping. When there is so much uncertainty about China's capabilities—and about America's—policymakers need to become more like splitters and make sober assessments of costs and benefits. Instead of treating every action by Chinese firms as a security threat, the government would do well to consider the costs of self-inflicted damage to the U.S. economy.

FURTHER READING

Pearson, Margaret M., Meg Rithmire, and Kellee S. Tsai. "China's Party-State Capitalism and International Backlash: From Interdependence to Insecurity." *International Security* 47, no. 2 (2022): 135–76. **https://doi.org/10.1162/isec_a_00447**.

Davidson, Michael R., Valerie J. Karplus, Joanna I. Lewis, Jonas Nahm, and Alex Wang. "Risks of Decoupling from China on Low-Carbon Technologies." *Science* 377, no. 6612 (2022): 1266–69. **https://doi.org/10.1126/science.abq5446**.

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