The China Economic Challenge:
Strength, Fragility, and the Limits of Isolation

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If I had to reduce the current debate about China's economic rise to one phrase, it would be "technology trumps tariffs." While much of our energy is consumed by familiar debates over trade wars, the deeper forces reshaping the global economy are technological change, demographic shifts, and capital flows.

We are entering a period where the certainties of the past no longer hold. In such a world, humility is essential as we confront novel and contentious questions about China, technology gaps, and economic security.

I offer not prescriptions but four observations on U.S.-China economic relations, each reflecting skepticism about elements of conventional wisdom in today's strategic debates.

First, the widely accepted "China Shock" narrative is substantially exaggerated when thinking about the evolution of the U.S. economy. That account, while capturing real regional pain, misstates the aggregate economics. Feenstra, Ma, and Sasahara (2018) show that when one includes offsetting effects—the employment generated by export expansion, the gains from lower input and consumer prices, and macroeconomic adjustments such as interest-rate and exchange-rate responses—the total U.S. employment impact of Chinese trade is close to zero. The national story is one of reallocation, not collapse.

If there were a policy failure, it lay less in trade than in the failure to support domestic adjustment. Some regions and workers bore disproportionate costs without adequate support. The remedy lies not in reversing globalization but in strengthening the social contract: wage insurance, retraining, and mobility assistance for those affected.

Second, paradoxically, China's challenge to the world may arise less from its strength than from its fragility. It is entirely possible for a society to experience extraordinary technological advance yet weak or unstable economic performance. The United States itself offers the cautionary precedent.

The 1920s were a decade of dazzling technological breakthroughs in mass electrification and the spread of the automobile, radio, motion pictures, and synthetic chemistry. Productivity growth was rapid, innovation relentless, and optimism boundless. Yet that very economy entered the Great Depression, the deepest collapse in modern history, within a decade. The lesson is sobering: great technological progress does not immunize a nation against economic crisis. Innovation can race ahead of institutions' capacity to sustain financial stability, aggregate demand, and social cohesion.

Moreover, history shows the limits of these so-called two-track economies. Russia built one around space. Japan built one around electronics while its housing sector languished. Neither path ended well. As a general rule, when the children of a country's elite begin studying foreign languages in large numbers, that country is in trouble. I suspect history will record Russia, Japan, and China as repeating this pattern in roughly thirty-year gaps.

China today faces its own version of this paradox. Its advances in artificial intelligence, green manufacturing, and telecommunications are remarkable. But these coexist with worrying fundamentals:

- Demographic contraction: births have fallen by roughly half since 2016, and the working-age population is shrinking.
- Capital flight: private wealth is leaving the country at a scale rarely seen outside systemic crises—a traditional marker of fading confidence.
- Productivity stagnation: total factor productivity growth has slowed to near zero, suggesting diminishing returns to state-directed investment.

- Debt and real-estate excesses: household wealth remains trapped in an overbuilt property sector and highly leveraged local government balance sheets.

This combination—technological vigor amid structural fragility—may define the Chinese economy for the next decade. A China that is advanced but anxious could prove more unpredictable than a uniformly ascendant one.

Third, there is growing talk in U.S. and European policy circles about "total resilience"—the ability to sever dependence on China in critical technologies, minerals, and components. While prudence in sensitive sectors is justified, the pursuit of absolute insulation from trade cutoffs is both infeasible and counterproductive.

In no other domain of national policy do we demand perfection. We do not design our defense posture for total invulnerability to nuclear attack; we rely on deterrence, redundancy, and response capacity. As in the nuclear arena, stability comes from reciprocity: if we depend on them, they depend on us. Deterrence works not by removing vulnerability but by balancing it. In finance, we manage risk through insurance and capital buffers, not by eliminating exposure. In engineering, we design for fault tolerance, not impossibility of failure. The challenge in economics is to build mutual dependence that deters recklessness without allowing exploitation.

To attempt the equivalent of "nuclear-proofing" the economy—total elimination of risk from foreign supply—would impose enormous costs on efficiency, innovation, and diplomacy. It would also appear profoundly threatening to any rival, signaling that the United States seeks not stability but dominance. History suggests that such perceived encirclement can become self-fulfilling: measures intended as protection are interpreted as provocation.

The goal should therefore be resilient interdependence, not autarky: diversified supply chains, transparent partnerships, and credible emergency capacity without dismembering the global production system that underwrites prosperity.

Fourth, a confident and growing China has room to accommodate others; a cornered China does not. The most dangerous moments in world history arise when major powers feel their opportunities slipping away. During a recent trip to Japan, I visited a World War II museum in Tokyo. Its depiction of the road to Pearl Harbor emphasizes economic containment as a driving force—actions carried out by those who believed they were doing something just but which Japan saw as strangulation.

The analogy is imperfect but cautionary. The United States is right to control exports of the most sensitive dual-use technologies. Yet declaring AI the defining technology of the twenty-first century while simultaneously excluding China from it risks feeding a sense of existential isolation. A Beijing that believes its modernization is being deliberately suppressed might act from insecurity rather than ambition—and that might prove a more volatile impulse.

The China challenge is not a binary choice of toughness versus weakness or engagement versus decoupling. It is a test of balance and humility: protecting national interests without mistaking complexity for weakness, competing vigorously without foreclosing cooperation.

The enduring lessons are threefold:

- Technology, not tariffs, will shape the future of power.
- Interdependence, prudently managed, is a stabilizing force.
- Fragility in China may be as dangerous as strength.

Our task is not to contain China's growth but to manage its turbulence—to ensure that its transformation, whatever direction it takes, occurs within an international order capable of absorbing shocks rather than amplifying them.

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