Opinion **US-China trade dispute**

China is well positioned to weather Trump's trade war

Five years of export controls have helped it get very good at making things without American technology

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China may be losing demand from the US, but this can be replaced by domestic consumer demand © Jessica Lee/EPA/Shutterstock

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A week of tariff trauma has left the world economy not much worse off than it was on President Donald Trump's "liberation day". Trump climbed down from his most extreme reciprocal tariff threats, but we are still left with a 10 per cent minimum levy on almost all US imports, 25 per cent duties on steel, aluminium and cars, and an outlandish 145 per cent tariff on China.

The president's team is scrambling to rationalise the chaos as a master plan to build a coalition to defeat Chinese mercantilism. But any such plan is doomed to fail. To understand why, we first need to get at what Trump really wants from tariffs. The usual claims — that he wants to crack down on unfair trade practices, eliminate trade deficits, reindustrialise America, confront China — do not hold up. Trump often invokes these goals. But these stated aims often contradict each other, are contradicted by other policies or are obviously unachievable.

A better explanation is that Trump is motivated mainly by a desire to accumulate and exercise power, and tariffs are the best instrument of that power. The purpose of his general trade war is to remove the constraints imposed by the global economic order on the unilateral exercise of US power, and in particular the exercise of power by the president.

Tariffs are the preferred tool for two reasons. First, Trump has believed for decades that the rest of the world will pay any price to gain access to the US market. Second, and perhaps more important, until Congress chooses to stop him, Trump has unlimited personal authority to impose (or withdraw) tariffs on any country, at any time, for any reason.

What Trump wants above all is to display dominance and extract submission. Countries that did not actively resist his tariffs were graciously granted reprieves from the higher rates. The country that dared to defy him was savagely punished.

Most countries now understand that the various economic rationales offered by Trump's advisers are just window-dressing. So long as Trump is in charge, the US is unreliable and no sane leader will join him in a crusade against China.

A second reason why Trump's trade war on China will fail: last Wednesday's ignominious retreat from "reciprocal" tariffs showed that the bond market sets the size of his tariff stick, and it is much smaller than he thought it was. Trump had to back off from high tariffs after an adverse market reaction.

So Trump has lost his leverage in trade negotiations. He cannot raise tariffs again, because the Treasury market will revolt again. The incentive for most global leaders will be to cut quick deals where tariffs are lowered in exchange for cosmetic concessions and tokens of deference. These will not include promises to blow up their trading relations with China.

The third reason why the China trade war will fail is China itself. At first glance China seems worse off now than the US: it has lost access to one of its biggest export markets, and seems diplomatically isolated. But in fact, it is well prepared to fight a war of economic attrition against the US.

China may be losing demand from the US, but this can be replaced by domestic consumer demand, which has been abnormally weak thanks to overly tight monetary policy, and an obsession with pouring state resources into manufacturing. Xi Jinping has reversed course and is now serious about boosting domestic demand.

China can also get along fine without imports from the US. Five years of export controls have helped it get very good at making things without American technology.

Despite some market fears, China can stabilise without a major currency depreciation. Beijing has slightly relaxed its controls on the renminbi to absorb some of the tariff pressure, and might let it fall another per cent or two. But a convincing move to demand stimulus will bring in fresh capital flows, supporting the exchange rate.

Meanwhile the US faces much higher inflation thanks to its tax on Chinese consumer goods. Its reliance on Chinese industrial inputs is three times that of China's reliance on US components. Higher input prices are already hurting business investment. China has a demand problem that it can solve with better macro policy. The US faces a supply shock and possible stagflation, which can only be solved by economic regime change.

If the aim of Trump's new trade war with China is to get Beijing to bend the knee before US power, the result will only be frustration and disappointment.

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