Opinion **Global trade**

China is smarter about subsidies than everybody else

Beijing is stealing a march on its competitors by targeting strategic sectors

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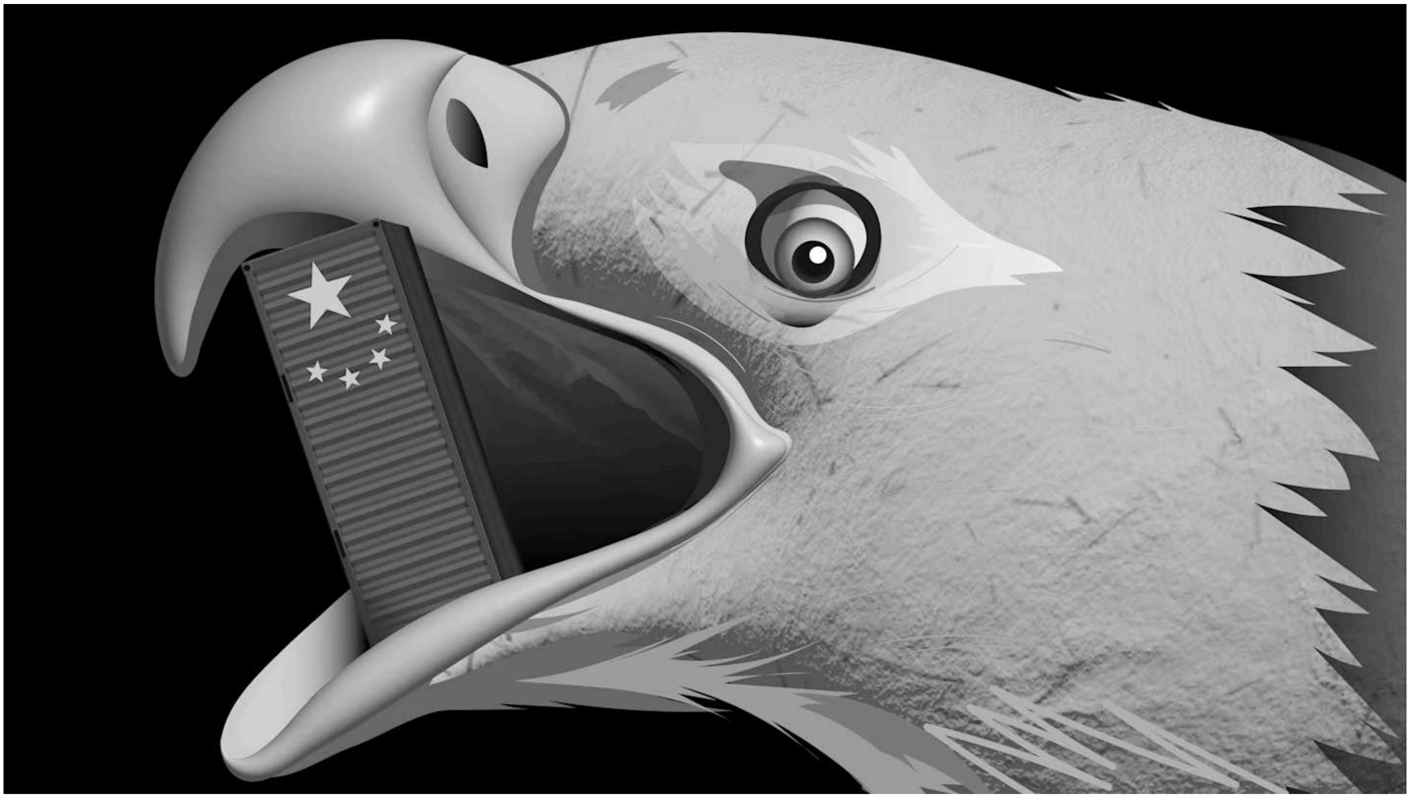

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What is driving the explosion of Chinese exports, which hit almost $4tn last year? That question is creating deep angst among non-Chinese policymakers amid fears of a second "China shock".

It is an issue I have been considering myself recently, having just crossed China in an electric vehicle Silk Road convoy, where I saw up close the startling quality of its EVs, green tech and artificial intelligence. Witnessing all that, it is hard not to worry about how others will compete.

And now a row about this has erupted between some Chinese economists and the OECD. Last month the Paris-based organisation reported that China's subsidies were three to eight times higher than its rich-world rivals in 2024, accounting for up to 60 per cent of its global market share gains between 2005 and 2023. This echoes repeated American and European complaints that China is using "unfair" tactics to undercut rivals.

But Chinese economists such as Kai Guo argue that "subsidies are no longer the most convincing explanation for Chinese firms' growing competitiveness". They accuse the OECD of miscalculating how cheap loans work — a point echoed by a paper from the World Economic Forum that finds little evidence of "broad, systematic below-market finance".

No doubt this debate will run and run. However, last week a thought-provoking perspective emerged in a much delayed paper from the IMF.

This notes, correctly, that measuring subsidy levels is very hard, since data is poor and definitions vary. Thus, while OECD calculations include cheap loans, the IMF ones do not, instead "just" focusing on direct grants and aid.

The paper makes three crucial points. First, even on a narrow definition, Chinese subsidies accounted for more than 2.5 per cent of value added in 2023, up from 1 per cent in 2015, or an average of around 1.8 per cent in this period. (This small number matters enormously when set against slim business margins.)

Second, China is not alone in such government meddling. Far from it. In the US, government subsidies were 1.3 per cent of value added in this period, and 1 and 0.6 per cent respectively in Canada and the EU. Complaints from Washington about "unfair" Chinese state meddling thus look somewhat hypocritical.

Third, not all subsidies are the same. Chinese subsidies were 3 per cent of value added in strategic industries such as semiconductors and tech hardware, helping that export boom, the IMF says. However, they were just 1 per cent of value added in non-strategic sectors like agriculture.

But in the US, subsidies were 2 per cent of value added in non-strategic sectors, and just 0.5 per cent in strategic ones. In the EU the ratio was 1 and 0.2 per cent. So China is backing strategic businesses, like green tech, while the west props up old sectors with political clout, like agriculture.

US techies might retort that they do better without state help. Maybe so. But there is another key issue the IMF paper does not cover: policy integration. When countries like China (or Singapore) subsidise strategic industries, as other IMF economists have noted, they often implement complementary measures, such as worker training or the installation of high-speed electricity transmission lines to support green tech.

But America is less holistic. It is now implementing tariffs and backing strategic groups like chipmakers. However, as the economists Marc Fasteau and Ian Fletcher have noted, this is piecemeal. Worker training is limited, there are attacks on green energy (which is insane), and failure to install transmission lines. Hence China is leaping ahead with power generation, which matters for AI.

So how should governments respond? In an ideal world, they would all immediately stop this mercantilist meddling, which is undermining global growth. Kristalina Georgieva, the head of the IMF, has begged China to slow its export flood by stimulating domestic demand.

“If it doesn’t happen it could ironically be China, not the US, that destroys the rules-based trading system because . . . countries will be left with no option but to put tariffs on Chinese goods,” she told me in Saudi Arabia earlier this year.

Emerging markets are suffering too. “China is one of the biggest risks to our external imbalance [and] we are trying to talk to our Chinese friends about how to fix this,” Mehmet Şimşek, Turkish finance minister, told me.

But in the real world, Beijing is unlikely to change policy and the US equally unlikely to drop its tariffs. After all, the IMF calculates that if the 2015-2023 Chinese subsidy trends continue, “China’s electronics exports increase by around 20 per cent over the long term”. We are in a brutally mercantilist age.

So what EU governments, and others, must do is not just contemplate tariffs, but the nature of their industrial policies too. Supporting farmers while cutting funding for science, say, is mad. So is failing to invest in a joined-up electricity grid or worker training. Let us hope that Donald Trump and his British and EU counterparts understand this. Sadly, I doubt they do.

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