

## How To Respond To Chinese Imports

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*China's export machine demands the attention of economic policymakers everywhere. But erecting trade barriers is the wrong response and distracts from the need for more targeted measures to address the risks to national security, innovation, and jobs.*

CAMBRIDGE – As China's trade surplus grows, with its manufacturing exports increasingly dominating global markets, the rest of the world is grappling with how to respond. Should countries erect trade barriers against China? Try to decouple from China by reshoring manufacturing and building national supply chains? Emulate its strategy of boosting manufacturing through industrial policies?

Policymakers must begin by asking why China's exports are a problem in the first place. After all, cheap imports epitomize the gains from trade. In important areas such as renewables, Chinese innovation and manufacturing prowess have produced significant climate benefits – a global public good. Moreover, bilateral trade deficits on their own are of little concern. Large overall trade imbalances can be a problem, but these are better handled with macroeconomic policies than with sectoral strategies aimed at China.

Still, there are three sensible arguments for why China's exports are problematic. These center on national-security considerations, the impact on innovation, and job losses. Each of these motives calls for a separate strategy. But because current policymakers too often conflate them, we have gotten bad policy outcomes instead.

Start with national security. Leaders in the United States and Europe increasingly view China as an adversary and a geopolitical threat. Hence, there is a valid justification for trade and industrial policies that protect strategic and defense interests, such as by reducing dependence on critical military supplies and safeguarding sensitive technologies. When such measures are deployed, governments have an obligation to show citizens – as well as China, lest international tensions be magnified – that their policies are appropriately

targeted at national security-related goods, services, and technologies, and that they are well-calibrated to avoid exceeding their objective.

Here the “small yard, high fence” strategy that Jake Sullivan, President Joe Biden’s national security adviser, articulated remains the correct approach. Applied in earnest, this doctrine would ensure discipline in the use of trade measures for national-security purposes. It would also encourage a mutual exchange of explanations and dialogue, thus preventing harmful escalation.

Next, consider innovation. The concern here is that China’s exports could undermine innovative capabilities in importing countries, reducing the prospects for future prosperity. Although manufacturing employs an ever-smaller share of advanced economies’ labor force, it remains a disproportionately large source of R&D and innovation spillovers. When those activities are crowded out by Chinese imports, the gains from trade are reduced or even transformed into losses.

But addressing this problem also requires a calibrated and differentiated response. Policies must focus on the more advanced segments of manufacturing, where the prospects for new technologies and innovation externalities are greatest. It makes little sense to protect consumer goods or established industries that use standard technologies. In autos, for example, the US and Germany should focus on the next generation of electric vehicles, rather than on the mass-market EVs that China has become so good at producing.

The right way to counter Chinese imports in technologically sophisticated areas is to deploy modern industrial policies that directly encourage investment and innovation through the provision of public inputs, coordination, and subsidies where necessary. In effect, other countries should emulate China’s own industrial policies, though with appropriate adaptation to local economic, political, and institutional contexts. Import protection is at best a temporary shield behind which such policies can produce their fruits over time.

Finally, consider jobs. There is a legitimate concern that Chinese imports produce adverse effects on employment, particularly in lagging regions where competing industries are concentrated (the so-called China shock). This concern goes beyond traditional equity considerations. Localities that experience job losses tend also to exhibit social and political dysfunction: rising rates of crime, family breakdown, opioid addiction, mortality, and support for authoritarian populism.

A focus on jobs, however, does not justify support for manufacturing and import protection. In fact, it is difficult to see how the jobs lost in manufacturing can be replaced, no matter how much reshoring is accomplished. For nearly a decade,

the US has pursued a manufacturing revival, variably through import tariffs (during President Donald Trump's first and current terms in office) and industrial policies (under Biden). Yet manufacturing's share in employment has continued to decline. European countries have experienced similar trends, though from different starting points.

A critic might argue that a more aggressive stance toward Chinese imports could reverse this trend. But such optimism is undercut by the fact that China itself has been losing tens of millions of manufacturing jobs even as it continues to dominate global manufacturing. More aggressive policies may bring some manufacturing back, but few jobs will be created as a result. Automation in manufacturing can no longer be undone.

Good jobs are essential to restore the health of our middle class. A good-jobs strategy must necessarily focus on services such as care, retail, hospitality, and gig work, since these will continue to absorb the bulk of future employment. As I argue in my new book, this can be accomplished through a combination of regional development initiatives based on partnerships between government agencies and business, and additional investment in labor-friendly technologies that augment and expand the range of tasks performed by workers without a college education. Both legs of this strategy require government action, but of a very different kind than protecting domestic manufacturing.

China's export machine is a wake-up call for economic policymakers everywhere. But import barriers are the wrong response and distract from the real priorities. Policy should be driven by clearly articulated economic, social, and national-security objectives. These typically call for targeted responses focusing on relatively narrow segments of manufacturing. And in the case of jobs, they require a reconsideration of manufacturing's role in generating economic prosperity.

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