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Morning Briefing

Does China Need The US?

Check out the accompanying [chart collection](#).

Executive Summary: In setting cartoonishly large tariffs on China, Trump assumes the US has the upper hand. But does China really need America as much as Trump thinks? President Xi hasn't come crawling to Trump, pleading for softer terms; he's been working out new trade deals with other Asian nations. Today, Contributing Editor William Pesek exposes the Trump administration's potential miscalculations regarding China. China has been diversifying its export markets ever since Trump 1.0 in anticipation of just such a trade war, and it no longer needs the US consumer to meet its GDP growth goals. Moreover, China has a higher pain threshold than Americans can fathom (*"chiku"*) as well as unused stimulus options in its arsenal.

Weekly Webcast. If you missed Monday's live webcast, you can view a replay [here](#).

YRI Bulletin Board. We asked William Pesek, our new Contributing Editor, to analyze whether China is as dependent on the US consumer as the Trump administration seems to believe. It is essential reading.

William is an award-winning Tokyo-based journalist and author of [Japanization: What the World Can Learn from Japan's Lost Decades](#). He [won](#) the 2018 prize for excellence in opinion writing by the Society of Publishers in Asia for his work for the *Nikkei Asian Review*. He is a former columnist at *Barron's* and *Bloomberg*.

China I: Dragons vs Tigers. We now know what happens when an unstoppable force like Donald Trump meets an immovable economic object like Xi Jinping's China. In the case of the US President, it's blinking on tariffs in ways to which Trump World isn't accustomed.

China's intransigence clearly caught the Trump White House off guard. Since February 1, Trump has been raising China's tariff rate like a manic auctioneer: First 10%, then 20% on up to 54%, 104%, 125%, and at last look a cartoonishly large 145%. Team Trump assumed that sticker shock would have Xi calling the White House switchboard in a panic to make a deal. Yet no call came to Washington. Instead, Team Xi called Japan and South Korea

about a free-trade deal. It called officials across Southeast Asia. It called Europe.

China surely will be hurt by losing the US market, but Xi's Communist Party is betting that Trump's America will be hurt more. Trump effectively confirmed Beijing's suspicions when he exempted smartphones, laptops, and other key electronics categories from most China tariffs, raising the question for Team Trump: What's the point of a trade war if everyone gets a carve-out? Then again, tariffs on these items are still being considered.

And just like that, Trump's efforts to make China heel suddenly resemble the very "[Swiss cheese approach](#)" that US Trade Representative Jamieson Greer told Congress earlier this month the administration wanted to avoid, an outcome sure to "undermine" the impact of tariffs.

Yet the biggest miscalculation by Trump 2.0 may be taking China's secret weapon for granted: an economy that's been relying less and less on the US consumer to reach its 5% annual real GDP growth targets. And, probably, even less going forward.

China didn't enter 2025 firing on all cylinders. Asia's biggest economy faces a giant property crisis that's generating deflation ([Fig. 1](#) and [Fig. 2](#)). Local government finances are in disarray. Youth unemployment is [near record highs](#). Chinese households are more enthusiastic savers than spenders. These are the pre-existing conditions Xi carries into Trump's one-man tariff arms race.

The [5.4%](#) y/y real GDP growth rate that China produced in Q1-2025 was clearly boosted by exporters frontloading shipments to beat Trump's tariffs ([Fig. 3](#)). Going forward, though, China has many tools in its arsenal to fight back. It can always raise its [125% tariff](#) rate on the US to a Trump-matching 145%. It could squeeze American farmers, particularly those in red states. It could dump its [\\$760 billion](#) of US Treasuries ([Fig. 4](#)). It could also tax made-in-China goods and devalue the yuan. It could even confiscate manufacturing facilities.

China II: Chiku vs Cheek. Here we explore a number of reasons why China might not need the US consumer to thrive nowadays.

One ace up Xi's sleeve is a pain threshold that would be unthinkable in the US. Mainlanders call it "*chiku*," a Mao Zedong era ethos that means to "eat bitterness." In authoritarian China, Xi doesn't need to stand for elections. Credible opinion polls encapsulating the views of his 1.4 billion subjects aren't really a thing.

This is a big reason why China feels little urgency, if any, to come to the negotiating table. *Chiku* was largely how Beijing got away with its draconian Covid-19 lockdowns. And now, it's helping Xi rally public support, as Trump makes it all too easy for the party to paint China as a victim of US aggression.

This dynamic is as asymmetrical as they come. How much bitterness are Americans ready to eat?

At the same time, China's been preparing for this trade war for a long time. That includes diversifying its trade away from US households. In 2018, the last time Xi's economy dealt with "Tariff Man," Chinese exports to the US accounted for about 19.2% of the total, according to China's National Bureau of Statistics. At the end of 2024, that stat had [fallen to 14.7%](#).

As Matthews Asia points out, [only 29%](#) of Chinese exports now go to the Group of Seven countries, compared to 48% in 2000. By the end of 2023, China was the biggest [trading partner](#) of 60 countries, roughly twice as many as the US, according to the Lowy Institute ([Fig. 5](#) and [Fig. 6](#)).

That's because China has been actively diversifying its overseas shipments, sending more to Southeast Asian and so-called "Global South" nations.

Today, China's main customer is the bloc of 10 countries in the Association of Southeast Asian Nations (ASEAN), followed by the European Union. In 2024, China's trade with ASEAN [grew 7.1%](#) y/y to \$234 billion, according to China's General Administration of Customs. The US is now only China's No. 3 market. Sure, Trump can make life harder for Xi's nation; but now Washington lacks the direct leverage to alter China's behavior that it had and exerted in 2018.

In the West, we follow the money. In the East, it's wise to follow Xi's travel itinerary. This month, he visited Cambodia, Vietnam, and Malaysia, three key Asian economies unhappy about being targeted by Trump's reciprocal tariffs. That wasn't a coincidence. With Phnom Penh, Hanoi, and Putrajaya facing direct tariffs of [49%](#), [46%](#), and [24%](#), respectively, Xi enjoyed what Chinese state media called "all-around cooperation" on his whistle-stop tour.

China III: China's Bazookas. Manufacturing, Trump World seems to think, has been a bright spot in China's economy, as China's property sector has sputtered and deflation deepened in recent years. Goldman Sachs, after all, [thinks](#) between 10 million and 20

million Chinese workers rely on US-bound export businesses. If that fact doesn't move Xi to capitulate, Trump reckoned, what will? Xi, though, has the scope needed to continue to offset lost business from anxious American consumers.

One way is via large-scale reductions in official interest rates and reserve-bank ratios. The People's Bank of China's (PBOC) one-year loan prime rate is currently [set](#) at 3.1%, while the five-year rate is 3.6% ([Fig. 7](#)).

Until now, the PBOC has been reluctant to ease too assertively. For one thing, it worries about the yuan weakening. A yuan-dollar exchange rate lower than the [current 7.29](#) might increase default risks among property developers with heavy dollar-denominated debt loads ([Fig. 8](#)). And it might enrage Trump's Treasury Department, which is hypersensitive to China's supporting its exporters at America's expense.

But China's deflation risks mean that the PBOC always has the option of trying quantitative easing (QE) with Chinese characteristics. Chinese QE could help alleviate pressure on local government finances hit hard by China's property crisis—and now Trump's tariffs. It's no coincidence that on [November 8](#), a few days after Trump's re-election shocked China, Team Xi moved to let municipalities expand their debt financing via the issuance of \$1.4 trillion of long-term bonds to replace short-term debt.

Though the father of monetarism Milton Friedman would object, Xi wants local governments to use some of the proceeds to buy up unsold or unfinished residential buildings around the nation. Beijing has been prodding state-owned non-bank institutions to buy back shares and hang on to them indefinitely. And a government not wedded to the normal laws of financial gravity has multiple ways to support consumer demand if cornered: For example, Xi has the scope to direct the PBOC to make electronic payments directly into household bank accounts. That's just one option for providing broad income assistance.

The fact that Beijing hasn't yet deployed its stimulus "bazooka" suggests that Team Xi isn't panicking. Zhang Di, analyst at China Galaxy Securities, thinks Beijing might announce a stimulus jolt of as much as 2 trillion yuan (\$274 billion).

But there's renewed focus on increasing pension payments and building more robust national safety nets. This would pivot China once and for all toward domestic-demand-driven growth and away from exports.

Part of the challenge is reforming China's "*hukou*" household registration system, one that

long has limited the ability of rural Chinese to seek employment in booming urban centers ([Fig. 9](#)). The resulting higher wages—and yes, government transfers—would increase household purchasing power on everything from consumer goods to education and training to healthcare to financial services.

The wisdom—and inherent moral hazards—of such tactics might make Adam Smith turn over in his grave. But Trump World is learning the hard way that China has a deep well of strategies it can use to wait out the trade war.

China IV: Trump 1.0 Prepared China for Trump 2.0. The irony is that Trump 1.0 made China markedly more resilient to shocks. Team Xi prioritized building more dynamic supply chains. The Trump 1.0 trade war saw Beijing prodding state-owned enterprises to diversify income streams globally as a matter of course, in case another US trade war came around. It was a savvy bet.

China also pumped untold billions into supersizing its controversial Belt and Road initiative to sell more to Southeast Asia, Latin America, Africa, and beyond.

Soybeans tell the [story](#). In 2017, American farmers produced about 40% of China's soybeans imports. Now it's around 20% thanks to China pivoting to Global South nations like Brazil instead. The South American economic power is now China's top supplier. It's an example of how Trump's tariffs can backfire on Trump country as American farmers pay the price.

Asymmetric warfare is China's friend. Xi's people know it's virtually impossible for the US to replace in short order what its economy gains from trade with China. With tariffs around 145%, Julian Evans-Pritchard, head of China economics at Capital Economics, estimates that Mainland shipments to the US will plunge by 80% over the next two years.

China's next bet is that it needs America's business less than America needs China's goods, industrial inputs, and minerals. In 2024, imports from China rose 2.8% to [\\$438.95 billion](#), according to US Census Bureau [data](#) ([Fig. 10](#)). And America's extreme reliance on China can obscure the ways in which Mainland goods are increasingly rerouted. Vietnam is a big [beneficiary](#) of this dynamic. Between 2019 and 2024, US imports from Vietnam more than doubled.

It's an example of how, even as direct US imports from China are declining, Chinese-made components and raw materials are still pivotal to goods imported from emerging market

economies.

China is banking, too, on its ability to weaponize America's access to rare earth minerals, which are essential to making artificial intelligence chips, among other things. China is home to roughly 61% of rare earths production and 92% of related refining, according to the [International Energy Agency](#). The question of whether Australia, Japan, Vietnam, and others can fill the void could take years to answer.

Pini Althaus, CEO of Cove Capital, told [The Washington Post](#) that it could take 10-15 years to devise a resilient China-free supply chain for minerals critical to making everything from smartphones to automobiles to jet engines to MRI machines to big-ticket weapons. "The writing has been on the wall for a long time," Althaus explained.

This 10- to 15-year window is worth exploring further. There are myriad reasons to criticize Xi's reign that began in 2012. He's been slow to build a thriving private sector to grab control from inefficient state-owned enterprises dominating his nearly [\\$18 trillion economy](#). Beijing still must craft more resilient and transparent capital markets and make the yuan fully convertible. It also must build social safety nets to encourage greater domestic demand.

But this year's "DeepSeek shock" was a wake-up call that Silicon Valley didn't see coming. China is showing it's got some serious AI game. For Xi, it was a sign that his "Made in China 2025" enterprise is putting some wins on the scoreboard.

Back in 2015, when Trump was famously descending an escalator in New York, Xi put in motion a 10-year plan to dominate the future of batteries, electric vehicles, renewable energy, aerospace, computing, biotechnology, green infrastructure, robotics, and AI.

Ask Elon Musk how all this is working out for Tesla. At a moment when the Warren Buffett-backed BYD, China's largest EV maker, is shocking the industry with an ultrafast battery charging system, Trump World is debating whether EVs are too woke for America.

As an economic thinker, Xi is no more omniscient than he is omnipotent. It's entirely possible that posterity will be harsh on his strategy for navigating around Trump's Tariff Turmoil. We don't mean to suggest it will succeed. Our point is simply that Trump's confidence that he can drive China's economy off the road with something as unoriginal as import taxes is in for a crashing reality check.

Calendars

US: Tues: Consumer Confidence; JOLTS Job Openings 5.7m; Wholesale Inventories 0.7%; S&P Case Shiller Home Price Indices 4.8% y/y. **Wed:** Real GDP & GDP Price Index 0.4% & 4.1%; Personal Income & Spending 0.4% & 0.6%; PCE 0.0% m/m, 2.2% y/y; ADP Employment Change 108k; Employment Cost index 0.0%; MBA Mortgage Applications; Chicago PMI 45.9; Pending Home Sales -0.3%. (FXStreet estimates)

Global: Tues: Eurozone Economic Sentiment Indicator 94.5; Germany GfK Consumer Confidence -26; Spain GDP 0.7%; Spain CPI; Japan Industrial Production -0.4%; Japan Retail Sales 3.5% y/y; Cipollone. **Wed:** Eurozone GDP 0.2% q/q, 1.0% y/y; Germany GDP 0.2% q/q, -0.2% y/y; Germany 6.3%; GDP Retail Sales -0.4%; Germany Import Prices -0.7%; France CPI 0.3% m/m, 0.8% y/y; France GDP 0.2%; Italy GDP 0.2% q/q, 1.0% y/y; Italy CPI 0.2% m/m, 2.3% y/y; China NBS M-MI & NM-PMI 49.9 & 50.7; Montagner. (FXStreet estimates)

Strategy Indicators

S&P 500/400/600 Forward Earnings ([link](#)): During the April 25 week, forward earnings fell for all of these three indexes simultaneously for a third week. LargeCap's forward earnings fell 0.4% w/w to 0.9% below its record high during the April 4 week. MidCap's dropped 0.3% to 1.2% below its record high, also during the April 4 week. SmallCap's fell 0.7% w/w to 13.6% below its June 2022 record. LargeCap's forward earnings remains 22.4% above its 54-week low during the week of February 1, 2023; MidCap's is 7.8% above its 55-week low during the week of March 10, 2023; and SmallCap's is now even with its 72-week low during the March 17, 2023 week. These three indexes' forward earnings downtrend from mid-2022 to early 2023 was relatively modest compared to their deep double-digit percentage declines during the Great Virus Crisis and the Great Financial Crisis. Here are the latest consensus earnings growth rates for 2024, 2025, and 2026: LargeCap (9.7%, 8.8%, 14.4%), MidCap (0.4, 6.9, 15.8), and SmallCap (-10.2, 5.2, 19.6).

S&P 500/400/600 Valuation ([link](#)): Valuations rose to four-week highs last week for all three of these indexes. LargeCap's forward P/E rose 1.0pt w/w to 20.0. It's now 2.3pts below its 43-month high of 22.3 during the December 6 week and 3.0pts above the seven-month low of 17.0 during the October 27, 2023 week. That compares to a 30-month low of 15.1 at the end of September 2022 and an 11-year low of 11.1 during March 2020.

MidCap's forward P/E rose 0.5pt w/w to 14.3. It's now 2.8pts below its 40-month high of 17.1 during the November 29 week and 2.1pts above the 12-month low of 12.2 in October 2023. That compares to a record high of 22.9 in June 2020 when forward earnings was depressed, and an 11-year low of 10.7 in March 2020. SmallCap's forward P/E rose 0.6pt w/w to 13.8 and is just 0.9pt above its 17-month low of 12.9 during the April 4 week. It's now 3.3pts below its 41-month high of 17.1 during the November 29 week and 3.2pts above its 14-year low of 10.6 in September 2022. That compares to a record high of 26.7 in early June 2020 when forward earnings was depressed, and a record low of 10.2 in November 2009 during the Great Financial Crisis. The forward P/Es for the SMidCaps have been mostly below LargeCap's since August 2018. MidCap's P/E is at 28% discount to LargeCap's P/E, not much above its 25-year-low 29% discount during the July 5, 2024 week. That compares to a 19% discount during the March 2, 2023 week, which matched its best reading since October 14, 2021. SmallCap's P/E is now at a nine-month-low 31% discount to LargeCap's P/E, which compares to a 23% discount during the November 29 week, which was its best reading since the March 2, 2023 week. It's 3pts above its 24-year-low 34% discount during the July 5, 2024 week. SmallCap's P/E was steady at a 4% discount to MidCap's, but that remains among the smallest since July 2021. Prior to that, from 2003 to 2018, SmallCap's P/E had been mostly above MidCap's, and both were above LargeCap's.

US Economic Indicators

Regional M-PMIs ([link](#)): Five regional Fed banks have reported on manufacturing activity for April, and there was weakness across the board. April's reading of the average of the five districts sank to -17.5—the weakest since May 2020. Here's a look by district: The Philadelphia region contracted sharply in April, with its composite index sinking 38.9 points (to -26.4 from 12.5), to its lowest reading since April 2023, with both the new orders (-34.2 from 8.7) and shipments (-9.1 from 2.0) components swinging from expansion to contraction; the new orders' decline was its weakest performance since April 2020. The employment measure dropped 19.5 points (0.2 from 19.7), just shy of the breakeven point between expansion and contraction, while the average workweek (-12.7 from 8.7) fell sharply. Manufacturing activity in the Richmond region deteriorated, with its composite (-13 from -4) index in contraction territory for the second month, after being above zero in February (at 6). Both the new orders (-15 from -4) and shipments (-17 from -7) measures sank deeper into negative territory, while employment (-5 from -1) fell slightly. The New York region showed a modest decline in April after dropping sharply in March. Its general business conditions measure improved 11.9 points (to -8.1 from -20.0), declining at a much

slower pace than last month; both the new orders (-8.8 from -14.9) and shipments (-2.9 from -8.5) measures contracted at a slower pace, with the latter nearing the breakeven point of zero. Meanwhile, employment (-2.6 from -4.1) was little changed, while the average workweek (-9.1 from -2.5) moved lower. The Kansas City region also showed a modest decline in the composite index, slipping to -4 this month from -2 in March. The production (to -5 from 1) measure slipped back into contraction territory, while the new orders (-11 from -12) gauge was little changed from March. The employment (-11 from -4) gauge shows manufacturers continued to cut payrolls, while the average workweek (-6 from 6) turned negative. Meanwhile, supplier deliveries (13 from -1) was a positive contributor in April. Activity in the Dallas region continued to rise in April, though the production index (to 5.1 from 6.0)—a key measure of state manufacturing conditions—was little changed. Meanwhile, the new orders (to -20.0 from -0.1) measure deteriorated dramatically this month, while shipments (-5.5 from 6.1) fell into negative territory for the first time this year. The labor market saw a slight decrease in head counts, with the employment measure holding steady at -3.9, while hours worked (-6.4 from -2.9) fell. Turning to pricing, both of the New York region's price indexes climbed for a fourth successive month to their highest levels in two years; both were up six points in April, with prices-paid at 50.8 and prices-received at 28.7. Philadelphia's price-paid (51.0 from 48.3) measure posted its highest reading since July 2022, while prices received (30.7 from 29.8) ticked slightly higher during the month. In the Kansas City region, price-paid was unchanged at 47, while prices-received (29 from 15) continued to accelerate. The Dallas region saw an acceleration in both prices-paid (48.4 from 37.7) and prices received (14.9 from 6.3). Meanwhile, both of the Richmond price measures, which are measured as percentage changes over the last 12 months, continued to accelerate in April: Prices paid rose to 5.37% from 3.75%, and prices received to 2.65% from 2.34%.

Contact us by [email](#) or call 480-664-1333.

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-241-6502
Melissa Tagg, Senior Global Investment Strategist, 516-782-9967
Mali Quintana, Senior Economist, 480-664-1333
Jackie Doherty, Contributing Editor, 917-328-6848
Valerie de la Rue, Director of Institutional Sales, 516-277-2432
Mary Fanslau, Manager of Client Services, 480-664-1333
Sandy Cohan, Senior Editor, 570-228-9102

