

Insulate, Then Press

A Sequencing Framework for U.S. Policy Toward a Structurally Declining China

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ABSTRACT

China's economic difficulty is best understood as chronic structural decline rather than imminent collapse: a demand-deficient, deflation-prone, demographically contracting economy whose leadership recognizes the diagnosis but declines the rebalancing that would resolve it, because the required measures shift income and authority toward households. This diagnosis is now well established in the peak-China literature. Its policy implications are not. This paper argues that because the decline is substantially endogenous, it cannot be triggered externally, and coercion aimed at rupture tends to consolidate the regime while imposing disproportionate cost on the initiator. It develops a single organizing contribution — a *sequencing framework* governed by an operationalized stability constraint. The framework holds that the United States must reduce its exposure to China's one instrument of real, currently unhedged coercive force against it, critical-minerals processing, before applying most forms of pressure, with technology denial as an argued exception that races a faster-closing window. The paper confronts the two strongest objections to its decline premise — overcapacity as durable strategic strength, and the preventive-war risk of a pressured peaking power — and specifies indicators that would falsify the assessment.

KEYWORDS

China; economic statecraft; export controls; critical minerals; peak China; deterrence; sanctions.

METHOD

Structured qualitative assessment: a decision framework specified in advance and applied to cases, rather than a formal model or statistical estimation. Sources are ranked in a deliberate hierarchy — primary releases and institutional data for empirical magnitudes, peer-reviewed and think-tank analysis for framing, and contemporaneous press only for the characterization of events, not for the underlying figures.

GOVERNING JUDGMENT

China's decline is endogenous and cannot be triggered externally. The United States must reduce its exposure to Chinese critical-minerals processing before applying most categories of pressure, with technology denial as a reasoned exception that races a faster-closing window. Every measure is disciplined by a lexicographic stability constraint with a veto on severe, durable U.S.-side damage.

FALSIFICATION

Eight indicators are specified in Section 8 — five that would disconfirm the decline diagnosis, three that would defeat the sequencing strategy on its own terms independent of the diagnosis.

IF YOU READ NOTHING ELSE

The claim	Ordering is decisive, not incidental. The United States holds one unhedged exposure to Chinese coercion — critical-minerals processing, where China refines nineteen of twenty strategic minerals and holds a near-monopoly on heavy rare-earth separation. Pressure applied before that exposure is hedged converts sound instruments into self-harm.
The exception	Technology denial does not wait. The frontier window closes faster than the minerals exposure can be hedged, so semiconductor controls proceed in Phase 1 while the insulation is built. Trade remedies and financial measures do wait.
What the rule condemns	The constraint draws blood from live policy rather than ratifying it: secondary banking sanctions and the 2025–26 unilateral tariff program both fail, the first on financial-market and alliance damage, the second on alliance damage alone.

1 Introduction and Claim

The debate over China's economic trajectory has substantially shifted toward the structuralists, though it is not settled. The catastrophist prediction of financial rupture has been wrong for a decade, and the triumphalist projection of smooth ascent is inconsistent with the arithmetic of demography and the persistence of a demand deficit that Beijing has not corrected. The prevailing synthesis — associated with Pettis on the demand side and with Posen and the peak-China literature on the strategic side — holds that China faces prolonged stagnation rather than either collapse or continued convergence.¹

What remains unsettled is the policy question that follows. If the decline is real but slow and largely self-inflicted, what should the United States do about it, and in what order? Much of the competitive-strategy literature treats the answer as self-evident: apply pressure across technology, trade, and capital, and let the contradictions compound. This paper argues that the ordering is not incidental but decisive, and that getting it wrong converts sound instruments into self-harm.

The claim is threefold. First, because China's decline is endogenous, external coercion cannot cause it and, when legible as an attempt to do so, tends to strengthen the regime by supplying a nationalist substitute for the household prosperity it will not deliver. Second, the United States is presently exposed to a single instrument of real, currently unhedged coercive force against it — Chinese dominance of critical-minerals processing — and must reduce that exposure before applying most categories of pressure; this is the *sequencing* argument, and it is the paper's primary contribution. Third, the framework requires an explicit evaluative criterion — a *stability constraint* — that this paper operationalizes rather

1. Michael Pettis and Matthew C. Klein, *Trade Wars Are Class Wars: How Rising Inequality Distorts the Global Economy and Threatens International Peace* (Yale University Press, 2020); Adam S. Posen, “The End of China's Economic Miracle,” *Foreign Affairs*, Aug. 2, 2023. The pessimist reading is contested; for the sustained counter-position that China pessimism is overdrawn and the productivity case underrated, see Nicholas R. Lardy, *The State Strikes Back: The End of Economic Reform in China?* (Peterson Institute for International Economics, 2019), and Lardy's subsequent commentary.

than asserts, and applies transparently to the hard cases of secondary financial sanctions and capital-market decoupling.

The paper does not claim novelty for its underlying diagnosis, which it draws from and cites throughout. Its contribution is the sequencing rule, the operationalized constraint that governs it, and the treatment of technology denial as a reasoned exception rather than an unexamined inclusion. Section 2 states the decline mechanism and its limits, incorporating the mid-2026 inflection in Chinese price data. Section 3 confronts the strongest counterargument, that overcapacity is strategic strength. Section 4 builds the stability constraint. Section 5 develops the sequencing framework and resolves the technology-denial exception. Section 6 addresses the preventive-war feedback that a pressured peaking power presents. Section 7 treats the domestic preconditions for the strategy as boundary conditions. Section 8 states the indicators that would falsify the assessment.

The method is structured qualitative assessment: a decision framework specified in advance and then applied to cases, rather than a formal model or statistical estimation. The stability constraint of Section 4 supplies the decision rule; Sections 5 through 7 apply it. Sources are ranked in a deliberate hierarchy — primary releases and institutional data for empirical magnitudes, peer-reviewed and think-tank analysis for framing, and contemporaneous press only for the characterization of events, not for the underlying figures. Where the load-bearing evidence is disputed, as with the effectiveness of export controls, both sides are cited and the argument is made against the stronger version of the objection.

2 The Endogenous Decline and Its Limits

Four structural forces drive the decline. None is a reversible policy error; each is entangled with the political economy of one-party rule.

2.1 The demand deficit

The core defect is a household-consumption share far below international norms. Household final consumption stood at roughly 40 percent of GDP in 2023 against a world average near 64 percent; even on the broader measure that includes government, total consumption was about 56 percent against a global figure near 76 percent.² The gap is absorbed by investment, now past its productive frontier, and by exports. Closing it would require sustained transfers to households, a genuine social safety net, hukou liberalization, and a higher wage share — measures that redistribute income and authority away from the state. The binding constraint is therefore political, not technical, a point developed in Section 2.5.

2.2 Price weakness and its mid-2026 inflection

China recorded twelve consecutive quarters of a negative GDP deflator through the first quarter of 2026, on the standard analyst reading the longest such run since the market-transition era; consumer inflation

2. World Bank, World Development Indicators, “Households and NPISHs final consumption expenditure (% of GDP),” China (39.6% in 2023; world 63.6%). Broader consumption figures per Michael Pettis, “The Impact of Household Consumption Growth on China’s GDP Growth,” Carnegie Endowment, Mar. 2025.

averaged zero in 2025 against a two-percent target, and producer prices were negative for over three years.³ The deflator turned positive in the second quarter of 2026, at 1.6 percent, formally ending the run. This inflection matters for intellectual honesty and for the static-Beijing objection (Section 2.5): the assessment must account for it. It does not, however, disturb the structural diagnosis, because the recovery was driven by global energy costs rather than by a revival of domestic demand, and nominal growth rather than real household consumption led the rebound.⁴ The distinction between a price-level recovery and a demand recovery is the entire point; the former can occur while the demand deficit persists.

2.3 The property unwind and its fiscal transmission

Real estate and its linkages represented roughly 25 to 29 percent of GDP at peak and held the majority of household wealth.⁵ Existing-home prices had fallen more than twenty percent from their 2021 peak by early 2026, with transaction volumes down by roughly half over five years.⁶ The second-order damage runs through public finance: local governments financed themselves through land sales, that revenue is structurally impaired, and the center has not recentralized fiscal responsibility at the required scale, managing the resulting local-government solvency problem through forbearance.

2.4 Demography

The one irreversible force is demographic. The workforce is already contracting and total population is declining; the 2040 labor force is already born, so no natalist policy alters it. This is the categorical difference from prior collapse forecasts: demographic decline is immune to policy competence and removes the labor-force growth that historically offset China's low productivity growth.

2.5 Why this is decline, not collapse — and the static-Beijing caveat

China retains capital controls, a state-directed banking system, and the capacity to socialize losses. These tools prevent a market-clearing rupture, but they also prevent the clearing that would end the malaise; the resulting condition is prolonged stagnation on the Japanese template, with worse demographics and a larger external sector, partially offset by an advanced-manufacturing and artificial-intelligence push Japan lacked. The comparative claim is developed, not merely asserted, in Section 3.

The analysis rests on an assumption that must be stated: that the political constraint on rebalancing binds. The evidence is suggestive rather than dispositive. Xi Jinping has explicitly warned against

3. Consecutive-quarter count per National Bureau of Statistics quarterly GDP releases (deflator negative Q2 2023 through Q1 2026); see also China.org.cn, “GDP deflator likely to turn positive in Q2,” Jul. 13, 2026. Consumer price index and the 2 percent target per NBS Consumer Price Index monthly releases and the 2025 and 2026 Government Work Reports respectively.

4. Bloomberg, “China's GDP Price Gauge Turns Positive After Years of Deflation,” Jul. 15, 2026 (deflator +1.6% in Q2 2026, attributed to energy costs rather than domestic demand recovery).

5. Kenneth Rogoff and Yuan Chen Yang, “Peak China Housing,” NBER Working Paper No. 27697 (2020), estimating real estate and linked activity at roughly 29% of GDP.

6. National Bureau of Statistics, 70-City Sale Prices of Residential Buildings series: existing-home prices down 22.5 percent from the 2021 peak as of April 2026, new-home prices down 13.2 percent, transaction volumes off 53.8 percent over five years. Forward projection per S&P Global Ratings, *China Real Estate Outlook* (2026), estimating further primary-home price declines of 1.5–2.5 percent.

“welfarism” that breeds indolence, and Beijing's chosen response to weak demand has been state-directed investment in high-technology manufacturing rather than transfers to households.⁷ But Beijing is not static. It executed policy pivots in 2015–16 and again in 2024–25, and the March 2026 Government Work Report, while retaining the familiar “around 2 percent” consumer-price target, reframed it as a floor to be lifted rather than a ceiling to be held — an explicitly anti-deflationary posture that treats subdued prices as the problem to be solved.⁸ The honest form of the assumption is therefore conditional: if Beijing executes a genuine consumption pivot — real transfers, hukou reform, a rising consumption share — the decline thesis weakens and the strategy in Section 5 should shift toward managed coexistence. Section 8 specifies the observable thresholds that would trigger that revision.

3 The Strongest Objection: Overcapacity as Strategic Strength

The most serious challenge to the decline premise is not that China will collapse less than expected but that what reads as pathology is in fact successful restructuring. On this account — the “second China shock” — scale economies, learning-curve dominance, and price leadership in electric vehicles, batteries, solar, legacy semiconductors, and shipbuilding are durable strategic gains that convert domestic price weakness into global market share and coercive leverage. The record 2025 goods-trade surplus of \$1.189 trillion, built on \$3.8 trillion of exports rising 5.5 percent while imports were flat, is on this reading not a symptom of weakness but evidence of a completed transition from a property-led to a manufacturing-export-led model; integrated-circuit exports alone rose 26.8 percent.⁹ A country capturing dominant share of the growth industries of the next two decades, the objection runs, should be modeled as ascending in the sectors that matter, not declining.

The objection has real force and cannot be dismissed. Three responses bound it without denying it. First, the two framings are not mutually exclusive across time: export dominance can be genuine while the model that produces it remains demand-deficient and deflation-prone, because the surplus is the mechanism by which domestic overcapacity is exported rather than resolved. The surplus and the deflation are one phenomenon observed from two sides. Second, the strategy in this paper does not depend on China failing in advanced manufacturing; it depends on China being unable to escape the demand trap, which the export success does not address and arguably deepens by absorbing capital that household rebalancing would otherwise claim. Third, the sectoral strength is precisely why Section 5 treats technology denial as the one form of pressure that cannot wait — if the second-China-shock thesis

7. Xi Jinping, “扎实推动共同富裕” [“Making Solid Progress Toward Common Prosperity”], *Qiushi*, Oct. 15, 2021, cautioning against welfarism (福利主义) that would “encourage laziness”; on the investment-over-transfers policy choice, see Rhodium Group analysis summarized in Pettis, Carnegie, Mar. 2025.

8. Li Qiang, *Report on the Work of the Government* (2026), delivered to the Fourth Session of the 14th National People's Congress, March 5, 2026 (full text released by China.org.cn), framing the price objective in support of “a modest rebound in prices and a virtuous economic cycle.” The “around 2 percent” consumer-price target itself is long-standing (it appears in the 2025 report and earlier); the novelty is the inversion from ceiling to floor, not the target's existence.

9. U.S.-China Economic and Security Review Commission, *China Bulletin*, Feb. 4, 2026 (2025 goods surplus \$1.189 trillion; exports \$3.8 trillion, +5.5%; imports flat; integrated-circuit exports +26.8%). Full-year 2025 exports to the United States down roughly 20 percent per the General Administration of Customs of the PRC (2025 full-year trade data, released Jan. 14, 2026); the –28.6 percent figure sometimes cited was the November 2025 monthly print.

is correct, the frontier is where the contest is decided, and ceding time there is the costliest error available.

The residual disagreement is empirical and resolves over five to ten years: whether manufacturing-productivity gains can offset demographic contraction and the demand deficit, or whether they compound the overcapacity that generates the deflation. This paper takes the second position while conceding the first is live; Section 8's indicators are designed to adjudicate between them as data accrue.

4 Operationalizing the Stability Constraint

Any prescription of pressure requires a criterion for which measures are worth their cost. A bare injunction that pressure “must not damage U.S. stability more than China's” does no analytic work; it licenses the author's priors. This section specifies the constraint so that it can adjudicate cases rather than decorate conclusions.

The constraint operates over five dimensions of stability, each assessed for both parties: price level (consumer-inflation impact), fiscal (debt service and deficit path), financial-market (integrity of and access to the dollar system for the United States; capital-account and banking stress for China), alliance (partner defection or hedging), and domestic-political (legitimacy and coalition durability). Each party's damage on each dimension is characterized ordinally by severity (severe, moderate, low) and by reversibility (durable, reversible). The dimensions are not commensurable — there is no exchange rate between basis points of consumer inflation and increments of allied hedging — so the rule is deliberately not an aggregation across weighted scores. It is lexicographic with a veto:

A measure fails if it inflicts severe, durable damage on the United States on any single dimension, irrespective of the cost it imposes on China. Among measures that survive that veto, the rule prefers those imposing greater and less reversible damage on China.

Two features carry the analytic load that fiat carried in the prior formulation: the reversibility distinction (a cost China can unwind through alternative arrangements is worth less than a permanent structural loss, and symmetrically for U.S. costs) and the veto on U.S.-side severe-durable damage, which encodes the finding of Section 5 and Section 7 that instruments eroding the financial system or alliance reliability are strictly self-defeating because most of the toolkit is weaker without those assets. This rule is executable without inventing weights, and it is what the case reasoning below actually performs.

Worked application — secondary sanctions on China's core banking system. The ordinal scoring for both parties:

Dimension	U.S. damage	China damage	Note
Price level	Low	Moderate	Limited direct consumer-price effect either side.
Fiscal	Low	Low	Not a primary channel.
Financial-market	Severe, durable	Severe, reversible	U.S.: dollar-system fragmentation and third-country hedging, hard to reverse. China: acute bank stress, but partially unwound via alternative rails over time.
Alliance	Severe, durable	Low	U.S.: coercing partners into extraterritorial enforcement drives durable hedging away from U.S. jurisdiction. China: few alliance equities to damage.
Domestic-political	Low	Low	For China, arguably negative: the measure supplies a nationalist narrative rather than imposing durable legitimacy cost.

The measure fails at the financial-market and alliance dimensions on the veto alone: both show severe, durable U.S.-side damage. That the Chinese financial-market damage is also severe is irrelevant under the rule, because it is reversible while the U.S. damage is not. The verdict does not depend on how the dimensions are weighted, which is the point of the lexicographic construction. Reversibility is judged here over a roughly ten-year horizon — long enough that alternative-payment-rail construction counts as a Chinese recovery path, which is what makes the Chinese financial-market damage reversible and the U.S. dollar-system fragmentation durable. The remaining cases are stated in summary; each could be scored identically.

Summary of the hard cases.

Measure	Result	Reasoning under the constraint
Secondary sanctions on China's core banking system	Fails	Severe U.S. financial-market and alliance damage (fragmentation of the dollar system; third-country hedging), much of it durable; Chinese cost real but partially reversible via alternative rails. Restraint here is analytically forced, which is why enforcement against Chinese banks has been withheld even where Iranian-oil evasion is documented.
Comprehensive capital-market decoupling	Fails	Destroys U.S. investor value and cedes the depth-and-rule-of-law premium that is a genuine asymmetric U.S. advantage; accelerates the alternative-rail project. Chinese cost is real but the measure is self-harm on the financial dimension.

Measure	Result	Reasoning under the constraint
The 2025–26 unilateral tariff program (as implemented)	Fails	Fails on the alliance dimension, where the damage is severe and durable: tariffs applied to partners alongside adversaries drive hedging away from U.S. arrangements that does not unwind on repeal. The price-level damage is real but reversible, so the veto rests on alliance, not price. The tariffs imposed genuine bilateral cost on China — full-year 2025 exports to the United States fell roughly 20 percent — but China substantially offset it by diversifying to other markets, producing a record 2025 surplus, while the U.S.-side alliance and price damage accrued in full. The failure is the asymmetry, not the absence of Chinese cost.
Rules-of-origin / transshipment enforcement	Passes	Low U.S. damage on every dimension; targets the specific leakage — Chinese content routed through third countries — that makes nominal diversification cosmetic; coalition-compatible.
Allied-coordinated semiconductor controls	Passes, with a timing caveat	Imposes durable, hard-to-reverse cost on the Chinese technology frontier; U.S. damage manageable if coordinated. The caveat is exposure timing, resolved in Section 5.

The framework is meant to constrain real policy, not only to adjudicate hypotheticals. Applied to the current period, it condemns two measures actually pursued or seriously proposed: the unilateral tariff program of 2025–26, which fails on the alliance dimension, and the recurrent proposal for secondary banking sanctions. That the constraint draws blood from live policy — rather than blessing whatever the United States already does — is the test of whether it is analysis or decoration. It is also the strongest reply to the suspicion that a framework of this kind is reverse-engineered to endorse the author's prior preferences.

On the Iran case specifically, the constraint explains observed U.S. restraint. Washington's August 2026 sanctions expansion targeted dozens of entities but again stopped short of major Chinese banks, and analysts noted that without such measures China could sustain Iranian-oil imports with little disruption.¹⁰ The restraint is not timidity; it is recognition that the banking measure fails the financial-market and alliance dimensions against a target holding the manufacturing midstream.

5 The Sequencing Framework: Insulate, Then Press

The framework's organizing rule is that exposure reduction precedes pressure, because China's one instrument of real, currently unhedged coercive force against the United States is critical-minerals processing. Its potency and the paper's response to the natural objection — that minerals can simply be bought elsewhere — are established first, after which the rule and its single exception are stated.

¹⁰. Designations per U.S. Department of the Treasury, “Operation Economic Outcast,” OFAC action of August 24, 2026 (Press Release sb0613; remarks sb0614), designating roughly sixty entities, individuals, and vessels across the UAE, Hong Kong, China, Singapore, and Switzerland and issuing five sectoral determinations under Executive Order 13902 — Chinese entities designated but no major Chinese banks. For the characterization that the action again stopped short of Iran's Chinese financial enablers and the estimated 48 percent decline in Iranian shipments, see *The National* (UAE), “US sanctions threaten China's Iranian oil lifeline as Hormuz blockade cuts imports 48%,” Aug. 25, 2026; on the limited oil-security impact of a full halt, Rystad Energy analyst commentary in CNN, Aug. 25, 2026.

5.1 The binding constraint: processing, not mining

The claim is deliberately narrow, and the narrowing matters. China possesses other coercive instruments in general — most visibly the denial of market access, which it has deployed against South Korea over THAAD in 2016–17, against Australia in 2020, and against Lithuania in 2021.¹¹ But market-access denial is structurally weak against the United States for the reason Section 3 already establishes: China runs a large and growing surplus, so closing its market to the economy absorbing its overcapacity exports is a form of self-punishment. That is why Beijing's actual retaliation against U.S. pressure in 2023–25 took the form of mineral export controls rather than market closure. Market-access coercion is also hedgeable after the fact, as Australia's post-2020 diversification demonstrates, whereas the minerals chokepoint, as the remainder of this section shows, is not. The instrument that is both potent against the United States specifically and not yet hedged is minerals processing alone — which is what the sequencing rule is built to address.

Chinese leverage lies in refining and separation, not extraction. The International Energy Agency finds China the leading refiner for nineteen of twenty strategic minerals, at roughly seventy percent average share; for rare earths the figure was ninety-one percent in 2024, and China holds a near-monopoly on the separation of dysprosium and terbium, the heavy rare earths essential to high-temperature permanent magnets in defense systems.¹² The decisive point for policy is that buying ore elsewhere does not escape this: most non-Chinese ore is refined in China and repurchased as finished material, so mining diversification shifts dependence down the value chain rather than removing it.¹³ China has demonstrated the leverage through a widening sequence of controls: gallium and germanium licensing from July 2023, graphite from October 2023, a ban on rare-earth extraction, separation, and smelting technology in December 2023, an in-principle cutoff of gallium, germanium, antimony, and superhard materials to the United States in December 2024, and — the action that bit hardest — the April 2025 licensing regime on seven medium and heavy rare earths and the permanent magnets containing them, which disrupted Western automakers and defense suppliers dependent on Chinese-monopoly dysprosium and terbium.¹⁴

11. On Chinese market-access coercion against these three states, see Fergus Hunter et al., “Countering China's Coercive Diplomacy: Prioritising Economic Security, Sovereignty and the Rules-Based Order,” Australian Strategic Policy Institute, Policy Brief Report No. 68/2023 (Feb. 22, 2023), which provides in-depth case studies of the Republic of Korea (THAAD, 2016–17), Australia (2020), and Lithuania (2021); and Matthew Reynolds and Matthew P. Goodman, “Deny, Deflect, Deter: Countering China's Economic Coercion,” Center for Strategic and International Studies (Mar. 2023). On Lithuania specifically, the European Union's WTO challenge, *China — Measures Concerning Trade in Goods* (DS610, 2022), is the authoritative anchor. These episodes targeted smaller, asymmetrically dependent economies; the ASPI report's economic modeling further finds that flexible economies recover from such coercion, the ex post hedgeability noted above.

12. International Energy Agency, *Global Critical Minerals Outlook 2025 and 2026* (nineteen of twenty minerals; ~70% average refining share; rare-earth refining 91% in 2024; graphite ~94%, cobalt ~76%, lithium ~74%, gallium ~99%); on the dysprosium/terbium separation near-monopoly, IEA, *Global Critical Minerals Outlook 2025* (rare-earth value-chain analysis).

13. Bank of Finland Institute for Emerging Economies (BOFIT), “China retains dominance of critical raw material production,” 2026, summarizing IEA: diversification focused solely on mining shifts dependence down the value chain.

14. Chronology per MOFCOM announcements and Global Trade Alert, “A Short History of Chinese Export Controls on Critical Raw Materials,” Oct. 2025: gallium/germanium licensing announced Jul. 3, 2023 (effective Aug. 1, 2023); graphite Oct. 2023; rare-earth processing-technology ban Dec. 21, 2023; gallium/germanium/antimony/superhard cutoff to the U.S. Dec. 3, 2024; medium- and heavy-rare-earth and magnet licensing (MOFCOM Announcement No. 18) Apr. 4, 2025. On the disproportionate impact of the April 2025 rare-earth measures relative to the earlier metals controls, see Center for Strategic and International Studies, “The Consequences of China's New Rare Earths Export Restrictions,” Apr. 2025; on the dysprosium/terbium monopoly, IEA, *Global Critical Minerals Outlook 2025*.

The constraint on any pressure-first strategy is that ex-China refined supply does not exist at volume today. Rare-earth refining outside China rose only enough to ease Chinese share from about ninety-one to about eighty-five percent between 2023 and 2025, as U.S. and Malaysian plants came online; heavy-rare-earth separation and battery-grade graphite remain overwhelmingly Chinese.¹⁵ Meaningful substitution in narrow chains is an early-2030s prospect contingent on sustained subsidy, permitting reform, and price-floor protection against Chinese market-flooding, the tactic that contributed to Molycorp's 2015 bankruptcy alongside post-2011 price normalization and leverage.¹⁶

5.2 The rule and its single exception

The exposure asymmetry yields the sequencing rule: measures whose costs the United States cannot yet absorb must wait until insulation matures, while insulation is built. The apparent counterexample — that technology controls are themselves pressure and have already drawn minerals retaliation — is not an inconsistency but the location of the framework's one reasoned exception, and it must be argued rather than asserted.

The distinction is between pressure that races a closing window and pressure that can wait. Trade remedies against overcapacity impose costs that do not grow if deferred; the overcapacity persists and the case for action is as strong in 2030 as in 2026, so these measures wait until minerals insulation reduces retaliatory exposure. Technology denial is different: the frontier gap in advanced semiconductors compounds, and a generation ceded is difficult to recover, so the cost of waiting is itself irreversible. If the second-China-shock thesis (Section 3) has merit, the frontier is where the contest is decided, and deferring denial to await minerals insulation would trade a recoverable exposure for an unrecoverable one. The exception is therefore principled: contest the faster-closing window now, accept the residual minerals-retaliation risk in the interim, and mitigate that risk through the stockpiling and offtake measures below rather than by delaying the controls.

The sequencing rule is not “no pressure before insulation” but “defer pressure whose exposure the United States cannot absorb, unless the pressure races a window that closes faster than the exposure can be hedged.”

Semiconductor controls meet the exception; trade remedies do not.

The exception rests on a premise that must be defended rather than assumed, because Section 3 subjected the decline thesis to its strongest objection and consistency demands the same here. The premise is that controls actually hold China back at the frontier. The skeptic case is serious: controls leak

15. IEA, *Global Critical Minerals Outlook 2026* (Chinese rare-earth refining share easing from >90% to ~85%, 2023–2025, on new U.S. and Malaysian capacity).

16. Molycorp's June 2015 Chapter 11 filing reflected multiple causes, not Chinese price suppression alone: the post-2011 collapse of rare-earth prices after the 2010–11 export-restriction spike drew a supply surge from reopened and new mines and prompted end-user substitution; the firm carried roughly \$1.7 billion in debt following its leveraged 2012 acquisition of Neo Material Technologies; and a 2014 WTO ruling against China's export limits pushed Chinese export volumes, and prices, back down. See *High Country News*, “The U.S.'s only rare-earth mine files for bankruptcy,” Jun. 2015; Reuters, “U.S. bankruptcy judge refuses Molycorp request for loan,” Jun. 26, 2015; Molycorp SEC filings, 2011–2015.

through third-country intermediation and mislabeled equipment sales, and they accelerate an indigenization drive Washington can no longer monitor. SMIC produced 7-nanometer logic without extreme-ultraviolet lithography as early as 2022, and Huawei's 2023 Mate 60 launch was read in Washington as evidence the controls had failed.¹⁷

The stronger evidence, however, favors partial effectiveness, which is all the exception requires. SMIC's 7-nanometer output has been constrained to the low tens of thousands of wafers monthly rather than the planned hundreds of thousands; yields on that node have reportedly been poor; the path beyond 5 nanometers without EUV lithography is unclear and uneconomic; and by 2025 the frontier had visibly stalled, with Huawei's own published roadmap showing a next-generation chip less capable than its current best.¹⁸ The exception does not require permanent denial, which is likely unattainable; it requires that controls impose delay and cost at the frontier during the demographic window in which China's structural position deteriorates. Time-buying against eventual indigenization has value precisely because the competitor's underlying trajectory is adverse. On the evidence, controls purchase that time, and the residual minerals-retaliation risk accepted in the interim is bounded by the stockpiling and offtake measures below. If the skeptics prove right and controls demonstrably cease to impose a frontier gap, the exception collapses and technology denial should be treated like any other deferrable instrument — a contingency the falsification indicators in Section 8 are written to detect.

One seam with Section 6 must be closed explicitly. Section 6's de-escalation branch eases punishment-oriented measures when mobilization indicators fire, while holding denial-oriented ones. Semiconductor controls are experienced by Beijing as punishment, so the two sections appear to give conflicting instructions when those indicators fire. They do not, once the instrument is distinguished from the posture. The controls are retained through a mobilization scare because their object is denial of a specific military-relevant capability rather than generalized economic pressure, and abandoning them under coercive signaling would both surrender the capability and reward the signaling. What the de-escalation branch eases is the broad-based punitive layer — tariffs, financial measures, anything whose function is aggregate cost rather than capability denial. The technology-denial exception therefore survives a firing of the Section 6 indicators; the punitive measures do not.

5.3 The phased program, gated by conditions

The sequencing logic requires transitions triggered by an observable state of the world, not by elapsed time. Gating the phases by calendar would reintroduce the arbitrariness the framework exists to remove: Phase 2 should begin when insulation conditions are met, whenever that is. The phases below are therefore defined by entry conditions, with indicative horizons shown only to convey expected pace. The

¹⁷. On the skeptic case, see MERICS, “Export control breach reveals China's continuing struggle to produce high-end semiconductors” (2024); and the indigenization-acceleration argument in International Center for Law & Economics, “US Export Controls on AI and Semiconductors: Two Divergent Visions,” Mar. 24, 2025. On SMIC's 7nm production without EUV, Gregory C. Allen, as quoted in the ICLE analysis: SMIC was producing and selling 7nm chips no later than July 2022.

¹⁸. Center for Strategic and International Studies, “In Chip Race, China Gives Huawei the Steering Wheel” (2024) (7nm output constrained to the low tens of thousands of wafers monthly; no clear path beyond 5nm without EUV); Council on Foreign Relations, “China's AI Chip Deficit: Why Huawei Can't Catch Nvidia,” Dec. 15, 2025 (SMIC stuck at 7nm; Huawei's 2026 roadmap chip less powerful than its current best); on constrained scaling, International Center for Law & Economics, Mar. 24, 2025.

thresholds are drawn from the same IEA data the paper cites and are stated as targets to be revised against the annual *Global Critical Minerals Outlook*.

Phase	Entry condition (not calendar)	Principal actions
Phase 1: Insulate INDICATIVE: NEAR-TERM	Entry: now. Exit to Phase 2 when all three legs are met — (i) ex-China rare-earth separation share above 30 percent, roughly double the ~15 percent of 2025, sufficient that a Chinese cutoff no longer controls majority supply; (ii) defense stockpiles at the months-of-consumption floor set inside government for named materials (heavy rare earths, gallium, germanium, battery-grade graphite); and (iii) price-floor plus offtake arrangements covering at least half of projected allied demand for those materials. The separation-share and offtake legs are public and revisable against the annual IEA <i>Global Critical Minerals Outlook</i> ; the stockpile leg is necessarily set inside government, because National Defense Stockpile quantities and requirements are largely classified.	Fund allied refining and separation (not mining) with Defense Production Act Title III support, price floors, and guaranteed offtake; build defense stockpiles to the floor; enforce rules of origin against transshipment; proceed with allied-coordinated semiconductor controls under the Section 5.2 exception, which is not gated because it races a faster-closing window.
Phase 2: Press INDICATIVE: MEDIUM-TERM	Entry: Phase 1 exit conditions met — that is, retaliatory minerals exposure hedged to the defined thresholds — not a fixed year.	Multilateral anti-dumping against overcapacity; sustained technology-frontier denial; outbound-investment screening and audit-transparency enforcement; deepen minilateral security architecture.
Phase 3: Outlast INDICATIVE: LONG-TERM	Entry: escape routes durably closed and allied coordination institutionalized enough to survive administration changes.	Maintain denial-oriented deterrence (Section 6); preserve capital-market and reserve-currency advantages; sustain the technology lead through the demographic window; avoid measures legible as rupture attempts.

Two features of the gating deserve emphasis. First, the technology-denial exception is explicitly exempt from the gate, for the reason argued in Section 5.2: it races a window that closes faster than the minerals exposure can be hedged, so it proceeds in Phase 1 despite constituting pressure. Second, the two public legs — separation share and offtake coverage — are observable and published, which is what makes the sequence auditable: an analyst can determine from the IEA's annual data and public offtake announcements whether those conditions are met, rather than deferring to a policymaker's assertion that the time is right. The stockpile leg is verifiable only inside government, a limitation the paper states rather than obscures.

The escape routes the program targets — external demand, the technology frontier, capital and confidence, and a benign security environment — are the only exits from a demand trap that is otherwise

self-perpetuating. The design principle is denial of exits, not the manufacture of rupture, for the reason developed next.

6 The Preventive-War Feedback and the De-escalation Branch

The decline thesis imports a hazard that the competitive-strategy literature has made central: declining powers facing closing windows are the ones most prone to preventive aggression.¹⁹ This is not a marginal caveat to be relegated to a closing paragraph; it is a feedback loop that bears directly on the deterrence measures in Phase 3. Sustained deterrence that sharpens Beijing's guns-versus-butter bind, applied to a regime that substitutes nationalism for the household prosperity it withholds, can produce the diversionary escalation the strategy most needs to avoid. A strategy that denies economic exits while also foreclosing a face-saving external posture raises, not lowers, the probability of a manufactured crisis.

Two design choices contain the hazard. First, deterrence is specified as denial rather than cost-imposition: its object is to make the military option appear unwinnable, not to starve the regime, because the former defers a timeline while the latter shortens it. The distinction is operational — denial-oriented posture emphasizes the defender's ability to defeat an attack, whereas punishment-oriented posture emphasizes the aggressor's economic vulnerability, and the latter is precisely what feeds the siege narrative. Second, the strategy carries an explicit de-escalation branch: pressure is calibrated to deny options, and is eased on the specific dimension that is producing mobilization rather than internal compounding.

The branch requires indicators that distinguish pressure working as intended (internal contradictions compounding) from pressure producing external adventurism, each stated against a baseline so that a change is measurable rather than impressionistic. Three suffice. First, a shift from episodic gray-zone probing to sustained force-posture change around Taiwan — measured as a step-change in the tempo and duration of major exercises and standing deployments relative to the preceding several years' average, not any single incident. Second, a rise in the frequency and severity of coercive incidents against neighbors — measured against the running annual rate of such incidents recorded by the standard maritime-incident trackers. Third, a turn in authoritative domestic messaging from a prosperity frame to a mobilization frame, measured as a sustained shift in Party organs rather than a transient propaganda cycle. The joint appearance of these signals is the trigger to ease punishment-oriented measures while holding denial-oriented ones, on the logic that the objective is a declining China that stagnates rather than one that gambles.

7 Domestic Preconditions as Boundary Conditions

The external strategy depends on four U.S. advantages that are domestic in origin: reserve-currency status and capital-market depth, demographic optionality through immigration, the alliance network, and institutional self-correction. These are not a competing thesis that displaces the China analysis; they are *boundary conditions* on it. Each is a necessary input to measures in Sections 5 and 6, and degradation of

19. Hal Brands and Michael Beckley, *Danger Zone: The Coming Conflict with China* (W. W. Norton, 2022).

any raises the cost or lowers the probability of success of the external program rather than substituting for it. The claim is not that the domestic front outweighs the external program — that comparison is unmeasurable — but the narrower and defensible one that the external measures are conditional on the domestic inputs, and fail without them.

The dependence is specific. Allied-coordinated controls and friend-shored refining (Section 5) require partner reliability; unilateralism renders both strictly weaker, sometimes to the point of futility, because controls leak when allied producers see no reason to absorb the cost and refining capacity is not built for an unreliable customer. Reserve-currency depth (the financial dimension of Section 4) is what makes the banking-sanction restraint a choice rather than a necessity and what underwrites sanctions reach; its erosion advances the alternative-rail project the constraint is designed to avoid feeding. Demographic optionality is the one advantage structurally unavailable to China, whose 2040 workforce is fixed, and it directly supplies the frontier talent on which the technology-denial exception depends. Institutional self-correction is the capacity to reverse a failing policy without systemic rupture, which is the precise faculty China's political economy lacks; its degradation would import China's core disability without China's compensating state capacity.

The remedies for these conditions — fiscal credibility, expanded high-skill immigration, predictable alliance management, protection of institutional independence — lie largely outside the scope of a paper on China policy, and are noted here as inputs the external strategy assumes rather than as prescriptions this paper defends. Their honest status is that of stated dependencies: the external program is viable only to the extent they hold.

One qualification bounds the boundary-conditions move so that it does not become an evasion. Treating these inputs as exogenous is defensible only while they hold approximately steady. If any is actively deteriorating — if reserve-currency credibility is being spent down, if high-skill immigration is being curtailed, if alliance reliability is falling — then it is not a background condition but the binding variable, and the correct object of analysis shifts from China policy to the failing input, because a strategy whose necessary inputs are eroding is inoperative regardless of how well its external moves are sequenced. A specific instance of this tension sits inside the framework itself: Phase 3 assumes a sustained conventional-deterrence build-out in the Indo-Pacific, while Section 7 makes fiscal credibility a boundary condition, and the two compete for the same constrained resources. The paper does not resolve that competition; it flags that the deterrence posture's fiscal and industrial cost is a real claim on the very credibility the strategy elsewhere depends on, and that assuming both can be satisfied simultaneously is an assumption, not a finding.

8 What Would Falsify This Assessment

An assessment that cannot be wrong is not analysis. Two distinct classes of claim can fail: the decline diagnosis, and the sequencing strategy itself. Both are specified, observed as sustained trends rather than single prints.

The diagnosis would be substantially disconfirmed by:

1. Real household-consumption growth durably above five percent — a threshold chosen because it exceeds the 3–4 percent ceiling that Rhodium and Pettis estimate as the model's medium-term limit absent structural reform, so a durable breach would evidence the reform rather than the trend.²⁰
2. The household-consumption share of GDP rising past the mid-forties — a threshold set roughly ten points above the ~40 percent household share of the early 2020s, the order of shift observed in genuine consumption transitions rather than cyclical noise.
3. Consumer inflation durably above two percent driven by domestic demand rather than energy costs, distinguishing a demand recovery from the 2026 deflator inflection.
4. Local-government debt resolution at scale without a growth collapse, removing the fiscal transmission of the property unwind.
5. A reacceleration of total-factor-productivity growth sufficient to offset demographic contraction, which would vindicate the second-China-shock thesis over the demand-trap thesis.

The strategy would fail on its own terms — independent of the diagnosis — if any of the following obtained:

1. Allied coordination collapses, so that controls and friend-shored refining cannot be sustained multilaterally; the Section 5 measures are strictly weaker unilaterally, to the point of futility, so their coordination is a precondition rather than a convenience.
2. The minerals build-out stalls past the early-2030s horizon — ex-China separation share failing to clear the Phase 1 thresholds — leaving the United States in indefinite unhedged exposure and the sequence stuck in Phase 1.
3. Export controls demonstrably cease to impose a frontier gap — Chinese indigenization reaching commercial scale at the leading edge — which would collapse the Section 5.2 exception and reclassify technology denial as a deferrable instrument.

The diagnosis failures would, under Section 2.5's conditional assumption, warrant a shift from sequencing-and-outlast toward managed coexistence, because a China that rebalances is neither declining in the relevant sense nor susceptible to the exit-denial logic. The strategy failures would instead call for a different instrument set — burden-shifting to allies, accelerated stockpiling, or a shift from denial to resilience — without necessarily disturbing the diagnosis. Conversely, the continuation of a demand deficit alongside energy-driven price recovery, the mid-2026 pattern, is consistent with both the diagnosis and the strategy and disturbs neither.

²⁰. Logan Wright et al., Rhodium Group, on long-term consumption growth of 3–4 percent real absent significant fiscal reform (2024), as discussed in Michael Pettis, “The Impact of Household Consumption Growth on China's GDP Growth,” Carnegie Endowment, Mar. 2025.

9 Conclusion

China's decline is chronic, self-inflicted, and largely beyond the reach of external inducement; it can be neither caused nor prevented from Washington, only accelerated or retarded at the margin. The policy question is consequently one of ordering. The United States is exposed to a single instrument of real, currently unhedged coercive force against it, and must reduce that exposure before applying most categories of pressure, contesting only the technology frontier immediately because its window closes faster than the exposure can be hedged. Every measure is disciplined by a stability constraint that penalizes irreversible self-harm and the erosion of alliance reliability, which is why secondary financial sanctions and capital-market decoupling fail while transshipment enforcement and coordinated technology controls pass. The deterrent posture that sustains the strategy must be denial-oriented and paired with a de-escalation branch, because a pressured peaking power is a dangerous one.

The strategy's viability rests on domestic preconditions the paper does not defend but must name: a China policy is only as sound as the fiscal, demographic, alliance, and institutional inputs it assumes. Within those bounds, the contribution is deliberately narrow: not a new diagnosis of Chinese decline, which is by now well established, but a defensible and auditable rule for the sequence in which the United States should act on it, together with a decision criterion that condemns live policy rather than ratifying it.

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