Research on the Impact of the US China Trade War on the Economy of Other Regions of the World

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Abstract. In recent years, China's economy has developed rapidly, and the technology industry has made significant progress. The US launched a tariff-fueled trade war with China in 2018. The ongoing economic dispute, characterized by a series of tariffs, trade restrictions, and negotiations, not only affect themselves but also deeply on the rest of the world. This article is going to discuss how the trade dispute affects the global economy and the influences on each separate country. While some countries experienced benefits from the trade war, these advantages were often offset by broader economic uncertainties and disruptions caused by the trade tensions. The overall global economic impact of the trade war is negative and the benefits to certain countries are limited and temporary. Overall, the whole world's economy has benefited very little but has mostly been negatively affected by the trade tensions and trade war dynamics between the US and China.

Keywords: US-China trade war; Globalization; US; China; World economy.

1. Introduction

1.1. History background

The trade between the US and China has grown enormously and has huge impacts on both countries ever since China has joined the World Trade Organization (WTO) twenty years ago. However, in August 2017, the United States Trade Representative (USTR) initiated a "Section 301" investigation which was conducted under the Trade Act of 1974, giving the US government authority to take action against countries engaging in unfair trade practices.

Then in 2018, Donald Trump, the president of the US, started a tariff-fueled trade war with China by placing 25% duties on about $34 billion of steel, aluminum and other imports from China. In return, China fought back by imposing a 25% tariff as well on some American products.

So far, the trade battle didn't come to an end, it escalated instead. Despite several attempts at negotiations and ongoing conversations, little progress has been made to resolve the trade dispute. Instead, tension between the two countries seems to be increasing in the subsequent months and years.

1.2. Effects on US and China

Due to the huge current account deficit causing a huge leakage from the US economy, the US aimed to reduce the deficit and protect domestic industries from China by imposing tariffs on Chinese goods. The protectionism approach didn't go as well as expected, instead, it increased the US's current account deficit and reached $1.18 trillion. What's more, it caused a loss of $51 billion annually for the US, since the consumers and firms needed to buy imported goods and raw materials at a higher price [1].

The reason many economists claimed that protectionism could only put the burden on domestic producers and consumers is that the trade war shifted the deficit from China to other countries [2]. Through the trade war US only reduced the account deficit between China, but couldn't solve the nature of the trade problem. The lost share of the account deficit from China was transferred to other countries. What's more, importing goods from other countries instead of China only costs more, since China is a relatively low-cost producer, and all of these extra costs have been borne by domestic producers and consumers.

China was also seriously affected due to its heavy reliance on exports to the United States. Since China is one of the world's largest exporters, and the United States is one of its most significant trading partners. The trade war led to a decline in Chinese exports, which affected various industries, including electronics, machinery and textiles. Chinese exports to the U.S. decreased significantly, impacting many different manufacturers and industries which contributed to a slowdown in China's economic growth. In 2019, China's economy grew at its slowest rate in nearly 30 years.

1.3. How it affects the rest of the world

The U.S. trade war with China, which escalated significantly, and continued to have global implications, has had a complex and far-reaching impact on the world economy. Apart from the US-China trade war, the US also engaged in trade disputes with other countries, which also affected various industries. And some countries benefited from the shift in trade patterns as companies looked for alternatives to Chinese manufacturing. While this trade war had negative consequences for the global economy as a whole, some countries and regions did experience certain benefits or opportunities as a result of the trade tensions.

2. Global aspect

2.1. Global supply chain disruption

Supply chains are intricate networks of organizations, resources, and activities involved in producing and distributing goods and services. The worldwide disruption of global supply chains can lead to delays in production, shortages of goods and increased costs that extend far beyond the initial point of disruption.

Many multinational companies rely on complex global supply chains that include Chinese components or manufacturing. The trade war disrupted these supply chains and forced businesses to face the increasing costs due to tariffs and to adapt to the changing trade environment.

Especially for electronic products, clothing, and automotive components, international companies had to relocate production or find alternative suppliers, which led to uncertainty and inefficiencies in global production networks.

2.2. Commodity and raw material prices

The trade tensions also had an impact on global commodity markets. Tariffs and trade restrictions affected the prices of raw materials and agricultural products, leading to volatility in commodity markets. Since the 2018 Sino-U.S. trade dispute, China has imposed restrictions on soybean imports to the United States. Throughout 2018, the export volume of US soybeans to China sharply decreased to 16.64 million tons, a year-on-year decrease of 48% compared to 32 million tons in 2017.

Soybeans, coffee and cotton are three of the most affected agricultural products, which exhibit the highest level of responsiveness to the trade tension between the US and China. Agricultural commodities are the most extensively impacted by the trade war rather than other financial crises, including the recession and COVID-19. [3] Since the trade war specifically focused on commodities, the impact on the dynamics of agricultural products is huge.

The reduction of soybean imports from America led to a global increase in demand for Brazilian soybeans. High soybean demand incentivized Brazil to expand the supply of soybeans which led to large deforestation. Extra profits and market power exceeded the process of deforesting, and the lack of government supervision and regulation, and reduced budgets escalated the land-clearing process.[4] Even though the deforestation rate could be temporary, it still hugely affected Brazil’s environment and caused huge negative externalities.

2.3. Global growth slows down

The ongoing trade dispute has created uncertainty in the global business environment. While it's challenging to isolate the trade war as the sole cause of the global economic slowdown, it certainly played a role in exacerbating existing economic uncertainties. This uncertainty can lead to reduced investment and slower economic growth in many countries, as businesses hesitate to make long-term commitments in the face of unpredictable trade policies. Especially in the field of technology and manufacturing, trade disputes affect the investment and supplier choices of global companies, and the cost increase caused by it cannot be avoided. Financial markets also experienced increased volatility due to uncertainty surrounding the trade war. Stock prices fluctuated in response to developments and statements from both sides, impacting the whole world's economy.

The International Monetary Fund (IMF) and other organizations revised their global growth forecasts in response to the trade tensions. Global growth forecast for 2019 is at 3.0 percent, which is the lowest ever since 2008. And after April 2019, the IMF downgraded another 0.3 percent of the global growth forecast [5]. Although other factors, such as the COVID-19 pandemic, influenced the global economic slowdown during the same period, the trade war overall contributed to global economic uncertainties and disruptions, with consequences that extended beyond the US and China to affect many parts of the world.

2.4. Currency fluctuations

The trade war not only affected the real economy severely, it's impact also resulted in the fluctuations of currency. Currency exchange rates between the U.S. dollar and the Chinese yuan fluctuated in response to trade war developments. These fluctuations impact international trade competitiveness and financial markets.

The Chinese government allowed the Chinese Yuan (Renminbi, RMB) to depreciate against the US dollar in response to the trade war. This move aimed to counteract the impact of US tariffs on Chinese exports by making Chinese goods relatively cheaper and have more competitiveness. The yuan went from about 6.4 RMB per US dollar in early 2018 to around 7 RMB per US dollar by August 2019. Several other countries intervened in currency markets to mitigate the impact of the trade war. Most of the currencies of the major trade partners of China were affected by the trade war, including Australia, Europe, Japan, Korea, and Congo, all against the US currency [6]. As they were concerned about their export competitiveness, they all intervened to prevent their currencies from appreciating too rapidly.

Trade tensions can also lead to other countries adjusting their exchange rates in response to trade policy changes. These fluctuations can affect the competitiveness of exports and imports, making it more challenging for businesses to plan and invest. For example, sharp currency depreciations can trigger concerns about financial stability, leading to capital outflows. For investors holding assets denominated in foreign currencies, changes in exchange rates can affect the value of their investments, causing an outflow on foreign investments. Thus, countries, central banks, and monetary authorities intervened in currency markets to manage exchange rates and mitigate extreme fluctuations.

2.5. Global policy response

Many countries responded to the trade war by implementing their own trade policies in order to mitigate the trade war's effects and safeguard their economic interests. Some imposed retaliatory tariffs on U.S. goods, while others sought to negotiate new trade agreements to mitigate the impact of the trade war. For example, the US repeatedly increased tariffs on European goods, and European countries also responded to retaliatory tariffs.

Many countries sought to diversify their trade relationships by exploring new markets and reducing their reliance on the two economic giants US and China. This involved forging new trade agreements and strengthening existing ones with other nations. For example, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) was signed by 11 countries after the US withdrew from the Trans-Pacific Partnership (TPP). Bilateral trade agreements and regional trade initiatives also gained prominence and secured favorable trade terms from tariffs. Such agreements were pursued to protect key industries and maintain market access.

Other countries that were less affected by the trade war looked to capitalize on the situation by promoting their exports, particularly to markets left underserved due to tariffs, which can boost economic growth and trade tariffs. Investment strategies and subsidies were also adjusted. Investors and multinational corporations adjusted their investment strategies, and subsidies were provided to mitigate the impacts of the trade war. Companies that were heavily reliant on China as a manufacturing base started diversifying their supply chains by relocating production to other countries, driving foreign direct investment into new regions.

The diversification of trade partners helped reduce the concentration of trade with the US and China, potentially reducing vulnerability to their trade disputes. Also, bilateral agreements and negotiations led to enhanced trade relations with the US and China for some countries, providing them with preferential terms and exemptions from tariffs. The frequent policy changes and shifting trade alliances aimed to reduce the impact of the trade dispute but also contributed to trade policy uncertainty, which can inhibit long-term investments and impact economic stability.

3. Regional impact

Some regions were more directly affected than others, and the economic impact of the trade war varied from country to country, depending on the level of dependence on the two superpowers of trade, their role in the global supply chains, and the measures they took to adapt to the changing trade dynamics. Countries in East Asia that are part of China's supply chain saw significant disruptions. European countries, too, faced challenges as they were caught in a trade dispute and had to navigate their economic relationships with both the U.S. and China.

3.1. Positively impacted

Vietnam was one of the countries that benefited from the trade war, as businesses relocated their manufacturing operations to Vietnam to avoid US tariffs on Chinese goods. Vietnam has undertaken some of China's production capacity to export to the US. Vietnam imports intermediate goods from China, processes them and exports them to the US. This led to a surge in exports, particularly in the electronics and textiles industries. [7] In 2019, Vietnam’s exports to the US increased by around 29% compared to the previous year. [8]

Mexico was another beneficiary of the trade war, as it became an attractive destination for companies looking to manufacture goods for the US market due to its proximity. As a result, Mexico’s exports to the US also increased significantly in 2019. [9] Mexico's manufacturing industry benefited as companies sought to relocate production closer to the US, and Mexico remained a key link in North American supply chains.

3.2. Negatively impacted

Europe Union (EU) faced challenges due to reduced global trade, as it is closely integrated into global supply chains. Germany, as an export-oriented economy, was negatively impacted by the trade war due to less interest in Chinese companies investing in Europe instead of America.[10] Also, as trade tensions between the US and China created uncertainty in global markets, it had a chilling effect on business investment and trade, and negatively affected the EU's economic growth. France was also adversely affected by the trade war, as a country with a significant steel and aluminum industry. The whole EU faced trade tensions with the United States related to issues like steel and aluminum tariffs. Regions with companies exporting products like steel, automakers and aluminum were strongly affected.

3.3. Mixed impacted

The trade war had mixed effects on Japan. While Japanese firms that exported to China faced challenges, Japan also benefited as some companies relocated their production back to Japan or expanded their facilities there [11]. Japanese businesses increased investments in the United States during the trade war.

Australia's economy also faced mixed effects, as it had strong trade links with China. Exports of commodities like iron ore remained robust, but sectors such as education and tourism were affected.

4. Conclusion

The trade war only encourages inefficiency and trade is an engine of growth. Trade can stimulate economic growth by expanding the domestic markets into the international markets. The reduction of national trade leads to higher prices and a decrease in welfare for people around the world. Nonetheless, under the whole economic background of globalization, international trade is the future's major trend.

The article mainly discussed how the global economy was negatively affected by the trade tensions between the US and China in several aspects: global supply chain disruption, commodity and raw material prices increase, global growth slow down, currency fluctuate, and numerous policy responses according to the dynamics of the trade war.

Even though plenty of countries experienced potential benefits of the trade war, the threats and negative consequences of the US and China trade war have been proven by numerous facts and data. The minority-beneficial countries did benefit from the trade war but also had its side effects, or the benefits could be temporary. The world's economy benefited very little from the trade deficit but experienced more uncertainty and disruption. The trade war between the US and China overall negatively affected the whole world's economy.

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