The Economic Consequences of Sino-US Trade Conflict: Reasons, Growth and Finance

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Abstract: From 2018, as the US trade imbalance with China has grown, the US has slapped tariffs and high-tech export sanctions on China, and China has retaliated. This led to the beginning of a war between China and the United States over trade. This article will analyze the deeper reasons why the United States wants to use a war over trade to against China from the historical and current macro level and analyze the economic impact of the trade war on the two countries from three aspects: stock market, business, and currency. And compare the trade war's consequences with the goals that the United States hopes to achieve through the trade war to analyze whether this war has achieved good results for the United States. The research in this paper finds that the trade war has not brought the United States the results it sought to achieve. The trade war has influenced many industries, and it has caused the economies of the two countries to regress to varying degrees. This article hopes to give the reasons why the trade war is meaningless through research.

Keywords: trade conflict, finance, market

1. Introduction

On March 22, 2018, the U.S. President claimed China is stealing U.S. intellectual property and starting to raise tariffs on Chinese goods. The entire value of the commodities involved is estimated to be $60 billion. The Chinese government immediately reacted to this surprise by raising tariffs by 25% on part of the U.S. imports to China, which are worth $34 billion, as a response to the U.S.. This is the beginning of the trade war between the U.S. and China. China and the U.S. have had a lot of disputes over tariffs due to the large trade balance between the two sides in the past few years. And this series of disputes is known as the " Sino-US Trade Conflict". Because the United States and China are the first and second largest economies in the world, and both sides occupy an important position in each other's foreign trade, this trade war will undoubtedly have a huge impact on the economies of both sides.

All wars are waged for self-interest reasons. This article wants to analyze the reasons for the Sino-US trade war from two dimensions: history and present. And study whether the United States achieved its original goal through the trade war, and whether China was affected by the trade war.

The remaining sections of this paper will be organized as follows: Section 2 introduces the past position of China and the United States in international trade and how these historical reasons affect future decisions made by these two countries. These reasons are combined to analyze why a trade war would occur; Section 3 will analyze the impact of the trade war on the economic situation of both countries from three perspectives: stock market, corporate, and currency market. Section 4 is the conclusion.

2. Reasons for This Trade Conflict

Because of the robust industrial system and the sale of weaponry, the United States become the world's most powerful country after World War II, and the world's gold flowed to America. Through the Bretton Woods system, the United States gave the U.S. dollar a dominant position in the international monetary system and acted like a hegemon in the world financial system. Even after the U.S. dismantled the Bretton Woods system in the 1960s and signed the Jamaica Accord in 1976, the U.S. dollar's international standing still did not receive much impact [1]. Since the U.S. dollar has an unassailable position in the international monetary system, MacKinnon referred to the Jamaican system as the "floating-rate dollar standard."[2]. However, with one financial crisis after another, and under the influence of the globalized free market, with the shift of manufacturing center of gravity. The U.S. hegemony is gradually shaken. So, the United States needed to take a series of measures to re-consolidate its financial hegemony. For example, Japan in the 1980s, and the United States through various means to force the yen to appreciate against the U.S. dollar, the yen's substantial appreciation led to the rapid accumulation of Japan's domestic economic bubble eventually collapsed in the 1990s, into more than 10 years of economic downturn, meanwhile, the U.S. economy ushered in a new rapid development [3]. The United States also relied on this direct confrontation with the country that threatened it the most to consolidate its financial hegemony again and again. Secondly, due to the high level of U.S. imports, the U.S. foreign trade situation is characterized by a large trade deficit

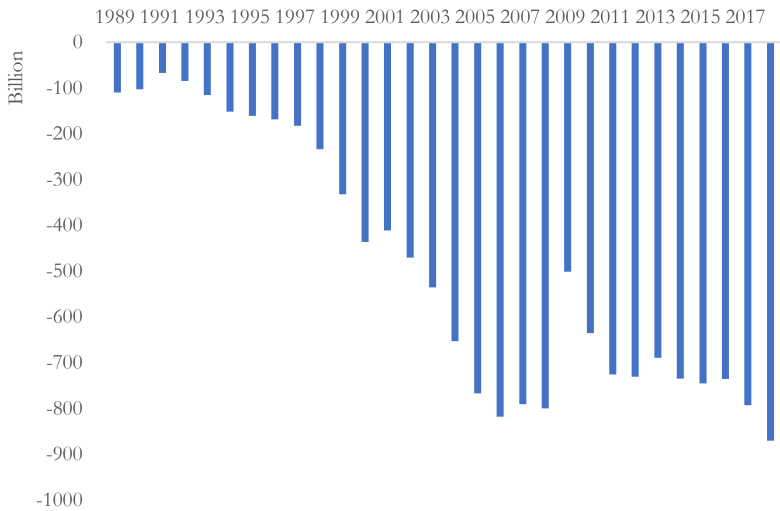

Figure 1: Total Exports FAS - General Imports Customs Val. TOTAL.
Data source: https://zh.tradingeconomics.com/united-states/balance-of-trade.
Photo credit: Original

China has been the most populous country in the world for the past few decades, and its cheap labor has brought a lot of low-cost manufactured goods to the world. This in turn has generated a lot of foreign exchange for China. After 2001, when China joined the WTO, China's foreign exports increased significantly from $266 billion to $2.592 trillion by 2020 (please see Figure 1) [4]. This has also led to a significant increase in China's financial status, which, combined with China's low labor costs, has attracted a large number of companies to build factories in China. China has become the

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country with the most purchasing power in the world, as well as the largest producer, dealer, and holder of foreign exchange reserves. However, as China's economic system has matured, the growth of China's GDP has begun to decelerate, in 2007 is 14.2%, but in 2018, it became 6.6% [5]. Moreover, as labor costs rise, the original advantage of lower labor costs and resource prices begins to diminish. The Chinese government has also begun to seek a transformation of its economic development from low-yield manufacturing processing to high-yield high-technology.

According to DataWeb, from 2008 to 2018, China's exports to the US climbed from $102.3 billion to $539.2 billion, whereas US exports to China increased only from $19.2 billion to $120.2 billion over the same period [6]. However, after 2001, the U.S. trade deficit with China grew by an average of 11.2 percent per year, to $20 billion. Even though exports have grown faster than imports. This is because the base is so tiny. The U.S.-China trade relations have also become very unbalanced because of these figures. The sharp rise in U.S. unemployment is a further problem created by the trade deficit.

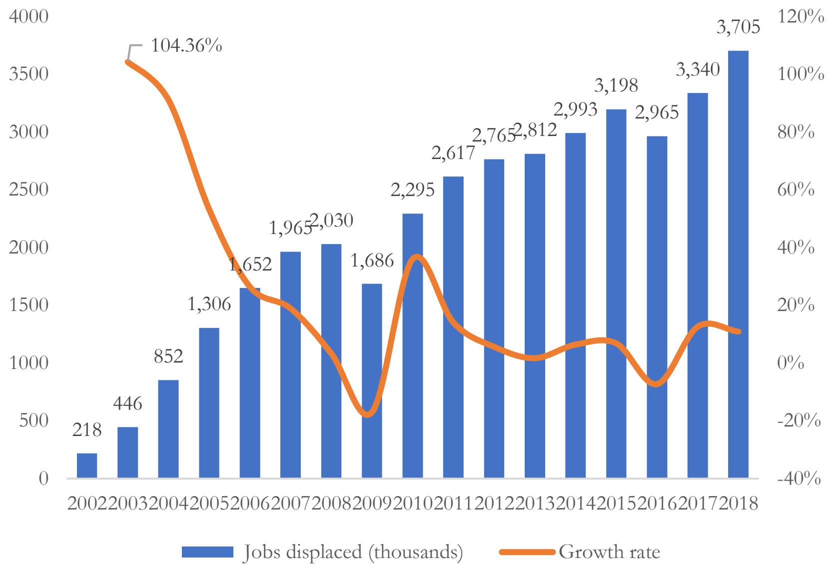

Figure 2: Amount of U.S. job losses due to merchandise trade deficit since 2001 (in thousands of jobs).
Data source: https://www.epi.org/publication/growing-china-trade-deficits-costs-us-jobs/
Photo credit: Original

Figure 2 shows a graph of the trade deficit and the number of jobs lost from 2002 to 2018. As we can see from the Figure 2, the number of unemployed people in the United States due to China has been increasing every year since China joined the WTO in 2001. According to Robert E. Scott's model, the number of unemployed people caused by the trade deficit can be estimated by replacing the number of workers needed to produce (work) for exports with the number of workers when imports replace domestic output [7]. From Robert E. Scott's research, we can find that in 2001, U.S. exports supported 175,800 jobs, but imports displaced 1,132,500 jobs. In 2001, trade conflict is only $83 billion and cost 956,700 jobs that year. But until 2018, that number had risen to 4,661,400. That's a growth rate of about 9.8% per year. This shows that the U.S. desperately needs to address the domestic employment problem by raising tariffs.

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3. The Economic Impact

After the Trump administration took office, its conservatism allowed it to seek this trade deficit down. China, on the other hand, has exported a lot of handicraft products to the world and reaped a lot of trade by providing manufacturing services, thanks to its low labor costs after joining the WTO. On the other hand, the United States is one of the countries with the largest trade deficit. And China also relied on foreign trade and its growing strength to begin to have a voice in international financial markets. So whether to reduce the trade deficit or to defend its financial hegemony, The U.S. needs a battle with China.

3.1. Economic Growth

The trade war has disrupted global supply chains and created uncertainty in international trade, most notably, as trade between the two countries has decreased due to tariffs added to each other The U.S. government increased tariff rates on more than $300 billion of Chinese goods from 2.7 percent to 17.5 percent at the beginning of 2018. The Chinese government started changing the average tariff on U.S. exports to 20.4%, 14.7% higher than it was, as a counter to the U.S. government [8]. From Table 1, it can be found that in 2019 US exports to China fell by 11.4% because of the trade war. And during the same period, China's exports to the United States fell by 16.60%, while exports to other regions of the world increased by only 5.5% [6]. This indicates that the increase in tariffs led to a significant decline in export trade between the two countries and each other. However, through several other important trading partners of the United States (United Kingdom, Canada, Japan, Mexico), it can be found that exports to the rest of the world also declined to varying degrees, and the total export volume was a decrease of 1.19%. In terms of imports, there was a small increase to these countries, but overall, there was a decrease of 1.75 percent. So, it can be seen that the United States failed to make up for this shortfall by trading with other countries.

Table 1: Total export.

Country	2018	2019	Change
China	120,281,213,791	106,481,217,316	-11.47%
United Kingdom	66,503,855,791	69,079,944,687	3.87%
Canada	299,731,711,825	292,820,257,565	-2.31%
Japan	75,163,791,885	74,479,657,382	-0.91%
Mexico	265,968,016,784	256,676,487,323	-3.49%
All	1,665,786,886,956	1,645,940,338,649	-1.19%

Source：https://dataweb.usitc.gov/

And by examining the monthly statistics of China's total imports and exports to the U.S., in 2018, China's cumulative export growth rate and cumulative import growth rate to the U.S. declined year-on-year and started to become negative in 2019 (please see Figure 3). But for China, it does not seem to cause too obvious problems in terms of total imports and exports. But according to macrotrends China's GDP growth rate in 2019 was down 0.8% from 2018. while the U.S. GDP growth rate is down 0.65% from 2018 [9]. So the decrease in trade between the two sides has somewhat contributed to the slowdown in economic growth in both countries.

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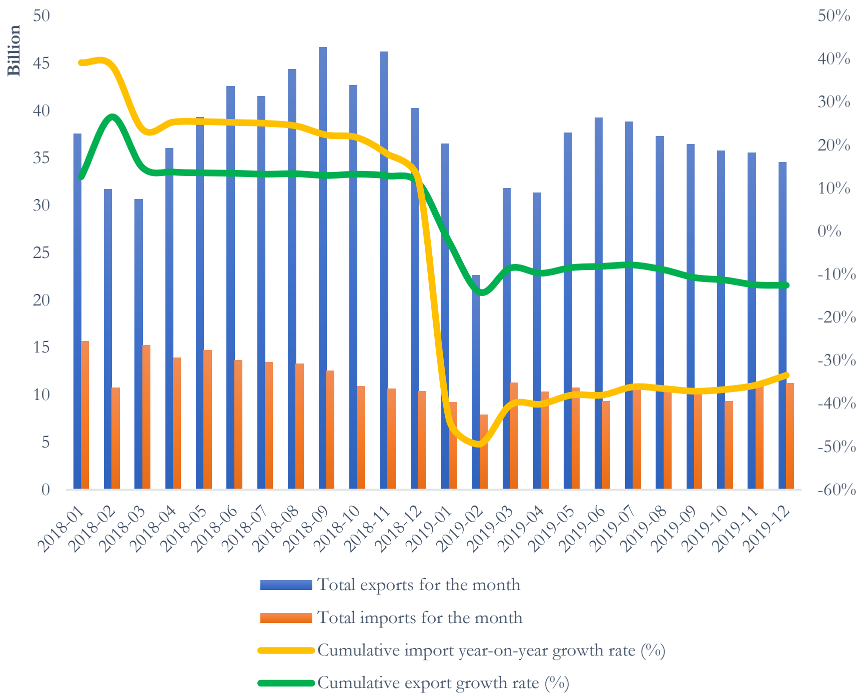

Figure 3: Monthly total import and export statistics between China and the United States.
Data source: http://cn.gtadata.com.hn.guangjie568.com
Photo credit: Original

In addition, because higher tariffs lead to higher production costs for businesses, this could lead to lower profits, less investment and possibly layoffs by multinational companies. According to a study by Liberty Street Economics, U.S. investment growth will be 0.3 percentage points lower at the end of 2019 because of the trade war [10]. And according to a September 2019 study by Moody's Analytics, there were 300,000 jobs lost due to the trade war, estimated at 0.3% of real GDP [11]. Continued uncertainty over trade policy and the potential for further escalation of the conflict has created a more cautious and investment-unfriendly business environment. This could lead to slower economic growth and lower investor confidence.

3.2. Stock Market

For equity markets, firstly, there will be increased volatility, which could lead to increased volatility in financial markets, including equity markets, due to the ongoing uncertainty and changing trade policies associated with trade wars. Secondly for certain sectors, such as technology and manufacturing, affected by the trade conflict, stock prices may fall as a result. Thirdly changes in interest rates, such as those implemented by the Federal Reserve, could also affect the stock market. If the trade war leads to lower economic growth and inflation, the Federal Reserve may respond by lowering interest rates, which may boost the stock market. Trade conflicts may also affect investor sentiment, as investors become more cautious in the face of uncertainty. This can result in fewer stock market investments. The stock market may suffer if the trade conflict causes weaker growth in the United States and China, as slower growth typically leads to lower corporate earnings and lower investor confidence.

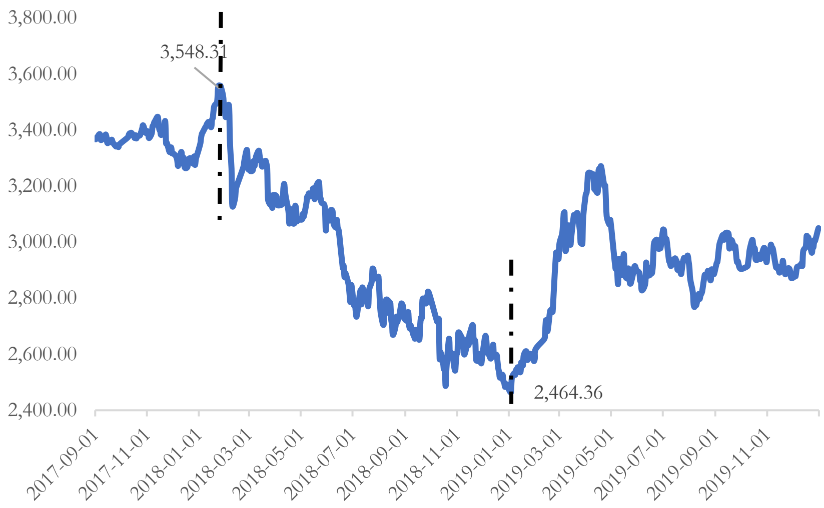

Figure 4: SSEC.
Data source: Investing
Photo credit: Original

First, as shown in Figure 4, U.S.-China trade frictions have decreased by 27.27% since March 2018, and the CSI Index has only gained from July 12 to August 1, with a range of 1.55%. The biggest drops were seen in the third and fifth phases. In the third phase, after the imposition of tariffs on $50 billion worth of Chinese products and the announcement of tariffs on $200 billion worth of products, this led to a drop of almost 5% in the CSI Index on the next Monday. In the fifth stage, after announcing an increase in the tariff rate from 10% to 25% on $200 billion of products, on the same day, the CSI All Share Index fell 1.92%. Nonetheless, the effect on the sectors did not differ much from the market average. From the pair CSI All Share Index, investor confidence was greatly affected at the beginning of the trade war., although there were several volatile rises in between, but these were due to some specific reasons, such as the rise in 2019. According to the CNBC article, the majority of the stock market's gains in 2019 may be credited to the Federal Reserve's major policy move. In 2018 the Fed made four rate hikes, including one in December 2018 that raised its key rate to 2.5%. But by 2019, the Fed changed its previous approach and cut rates three times [12]. Since investors will seek higher returns through the stock or bond market in a low interest rate environment. Therefore, this stock market rebound cannot be accounted for as a gain from the trade war.

Although the trade war did cause a lot of volatility to China's stock market, because the impact of the trade war is global, the U.S. stock market has also received a lot of impacts. From Fed’s research, it can be found that due to the tariffs added by the U.S. on Chinese imports, the stock prices of American companies have lost at least 1.7 trillion US dollars, and it may also affect the growth rate of investment. By the end of 2020, it will be reduced by 1.9 percentage points. The trade war has made capital bearish on the market. At present, it seems that the part of the United States trying to recover the trade deficit through the trade war may still lose money in the stock market.

3.3. Related Industries

Three major industries - agriculture, technology and automobiles - are particularly affected by the trade war when it begins, leading to job losses and lower profits for companies in these industries. And business costs will increase, with tariffs imposed by both countries increasing costs for companies that rely on imported goods, leading to higher prices for consumers and potentially lower profits for companies. Chip makers and electronics manufacturers in the technology industry that rely on Chinese sales are particularly hard hit. In a report reported on CNBC, Needham's senior semiconductor analyst Quinn Bolton argued that semiconductor suppliers' relatively high exposure to China's 'ship-to' revenue is leading to greater risk for the semiconductor industry in an escalating U.S.-China trade war.[13] In agriculture, it led to a decrease of about 8.6 % in U.S. agricultural exports and a decrease of about 17 % in China. [14]. Since China is the main market for U.S. agricultural exports, China’s countermeasures against U.S. agriculture have brought uncertainty and instability to farmers and herdsmen who rely on international trade.

Since China and the U.S. are major technology, and manufacturing nations, respectively, many companies would choose to locate their R&D departments in the U.S. and their component assembly in China, but due to the trade war companies have begun to move production to countries outside these two countries to avoid tariffs and the effects of the trade war.

3.4. Foreign Exchange Market

In terms of the exchange rate it mainly shows a weaker RMB: the ongoing trade conflict has led to increased market uncertainty and reduced investor confidence in the Chinese economy. A stronger USD: The USD has been seen as a safe-haven currency in times of uncertainty and the ongoing trade conflict has led to increased demand for the USD. However, overall, the RMB is still volatile against the USD due to increased market volatility from the trade conflict. Just by and large the RMB has depreciated against the USD.

But when a country's currency is devalued, the goods it exports become cheaper, thereby causing sales to rise, which in turn reduces its trade deficit. The goods it imports become more expensive, and thus their sales fall, favoring domestic products. But China has always been a profitable party in U.S. and China trade, and the devaluation of the dollar is more favorable to the export of Chinese goods. So even though the US has claims that the Chinese government is deliberately manipulating the exchange rate, the attractiveness of Chinese goods in the international market has not been affected too much.

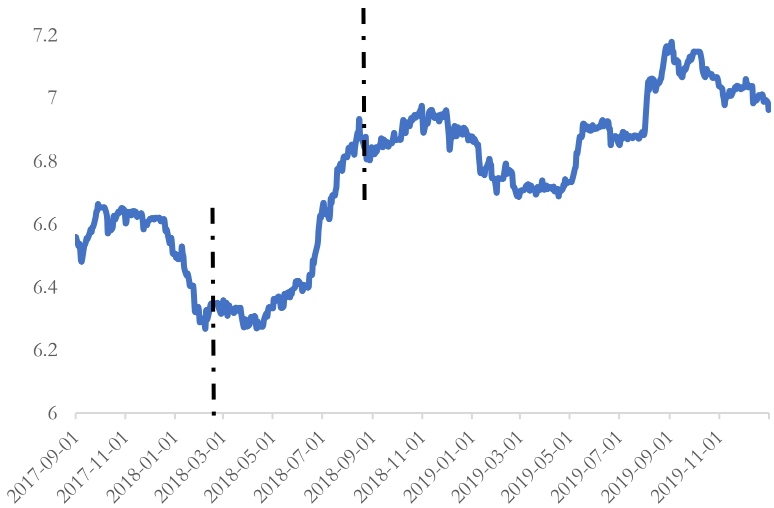

Figure 5: Exchange rate, USD to RMB.
Data source: Investing
Photo credit: Original

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4. Conclusion

The Sino-US Trade Conflict that began in 2018 is the biggest battle over international trade in recent years. In most of the world's two largest economic systems, any little change in policy between these two countries will cause changes in the global economic system, and this trade war is also a huge impact on the global economy. By analyzing the commerce between China and the United States following China's WTO membership in 2001, this article discusses why the United States started a trade war against China. It also analyzes what the U.S. gained in economic development, stock market and foreign exchange market after launching the trade war to compare the results the U.S. hopes to gain from the trade war. It was found that while China's GDP growth declined sequentially in 2018 as well, so did it in 2019. A series of U.S. crackdowns on Chinese technology also took a heavy toll on Chinese high-tech companies. However, while some of these actions have improved the U.S. position in trade with China, they have not ultimately lowered the overall U.S. trade deficit. With covid-19 on the horizon in 2020, China and the U.S. economic system are being hit even harder. It is hard to argue that the United States has gained anything from the Ming trade war. This paper hopes that the results of the study will allow the leaders of both countries to understand that trade wars will do more harm than good.

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