SOCIAL SCIENCE AND HUMANITIES

Manuscript info:
Received November 4, 2018., Accepted November 17, 2018., Published November 30, 2018.

US-CHINA TRADE DISPUTE AND ITS IMPLICATIONS

Syed Haider Ali Zaidi[1]; Xin-Yu Wang[1]; Muhammad Sajid[2],
1. School of Management, China University of Mining & Technology, Xuzhou, Jiangsu, 221116, China
2. Institute of Business Management Sc iences, University of Agriculture, Faisalabad, 38000, Pakistan

http://dx.doi.org/10.26739/2573-5616-2018-12-3

Abstract: The US-China trade dispute or Trump War started between the United States of America and Peoples Republic of China during 2018 after the administration of US administration imposed heavy tariff on Chinese imports. US President Trump reiterated US has no intentions of starting a trade war with China, however, this initiative has been taken to counter China's historical unfair and illegal trade practices. Currently, the US has a yearly trade deficit of $500 bn and an additional intellectual property theft of $300 bn which can only be narrowed down through imposition of trade tariffs. Accordingly, the United States Trade Representatives (USTR) Office carried out investigation under Section 301 of the United States Trade Act 1974 and determined that China's constant and unfair practices for gaining access to US intellectual property have severely affected thousands of American industries and rendered millions unemployed. Eventually, as per President Trump announcement, USTR recommended imposition of tariff on Chinese imports to the extent of $50 bn to counter the negative impact of China's so called illegal trade practices. China retaliated by imposing similar tariffs on US imports thus escalating the trade dispute. and prompted the US President to instruct USTR to identify products upon which additional tariffs of $100 bn could be imposed under the Section 301. Trump encouraged the world trade community to reduce the trade barriers to facilitate global economic growth while simultaneously allowing the American companies and personnel with equal opportunities for fair competition and discouraging unfair trade practices which threaten to undermine American interests.

Key words: US-China trade dispute; trade deficit; intellectual property rights; United States Trade Representative; US Trade Act 1974 Section 301.

Recommended citation: Syed Haider Ali Zaidi, Xin-Yu Wang, Muhammad Sajid. US-China trade dispute and its implications. 11-12. American Journal of Research P. 32-54 (2018).

1. Introduction

During his presidential campaign, Donald Trump stated that China had been exploiting the loop holes in international trading system to carry out unfair trade practices which adversely affect the US economy and people and promised that he would take stringent actions to end this impasse. He further said that all the countries unilaterally impose trade tariffs on exports/imports hence it is perfectly legitimate for US to impose trade tariffs likewise. Resultantly, in 2018 a trade dispute started between US and China (USA Today, 2018) (Reuters, 2018). In April 2018, the US government imposed tariffs on import of aluminum and steel from China, Canada and several EU countries which were followed by imposition of additional tariffs of 25% on Chinese goods worth $34 billion as per Trump's tariff policy. China retaliated by imposing similar tariffs on US imports. In wake of Trump orders, USTR office published a list of Chinese products amounting to $ 200 billion subjected to a 10% tariff (proposed but not implemented) which were deemed irrational and rejected by China (Caixin Global, 2018). The US administration point-of-view was that imposition of such tariffs is crucial to US national security; safeguarding intellectual property rights of U.S. business ventures; and narrowing down the US- China trade deficit (White House, 2018) (CNN News, 2018).

Between May 15 and 19, 2018 Liu He (Chinese Deputy Prime Minister and Chief economic advisor to President Xi Jin Ping) visited Washington to conduct trade talks in order to resolve this matter which resulted in a joint declaration that China would significantly increase purchase of US goods for trade deficit reduction (Caixin Global, 2018). However this arrangement was threatened, when on May 29 White House announced imposition of a 25% trade tariff on Chinese products using significant industrial technology. Furthermore, it was proposed to place restrictions on Chinese individuals and organizations from acquiring US technology and investing in US infrastructure (National Public Radio, 2018). In response, China threatened to discontinue trade negotiations with the US in event of imposition of aforementioned sanctions (BBC News, 2018).

In order to counter China's alleged illegal trade practices and pilfering of intellectual property, the Trump administration is relying partially on US Trade Act 1974 - Section 301 (Fortune, 2018) (Bloomberg, 2018) which give absolute authority to the US President to unilaterally impose penalties and tariffs on a trading partner if its activities are found to be conflicting with American business interests (ABC News, 2018). In August 2017, President Trump had initiated a probe into theft of intellectual property of the U.S. and its allies amounting to $225-600 billion a year (New York Times, 2018) (CNN Money, 2018).

1.1 The tariffs timeline

January 23, 2018: US president imposed a 30% tariff on import of solar panels to be reduced to 15% after four years (The Time, 2018) (CNBC, 2018). China strongly protested against these tariffs since it is the lead manufacturer/exporter of solar panels (CNN Money, 2018). Simultaneously, an additional tariff of 20% was imposed on washing machine units imported during the year. During 2016, industrial washing machines worth $ 425 million were imported by the US from China (USITC, 2018) (USTR, 2018).

March 22, 2018: The USTR, as the instructed by US President prepared a feasibility report on 1,300 categories of Chinese good, which included weapons, satellites, medical devices, flat panel television sets, batteries and aircraft parts etc, worth $ 60 billion (CNN News, 2018) (Caixin Global, 2018) for imposition of tariffs (USTR, 2018) (New York Times, 2018).

April 2, 2018: China imposed 25% tariff on several goods viz: aluminum, airplanes, cars, pork, and soybeans and an additional 15% tariff on fruit, nuts, and steel piping (Washington Post, 2018) (Tridge, 2018). This retaliation prompted the US President and he announced intentions of enforcing special tariffs on several Chinese goods worth $ 100 billion (Caixin Global, 2018). Furthermore, China lodged a complaint with the World Trade Organization (WTO) protesting against new tariffs imposed by the United States (Caixin Global, 2018).

April 18, 2018: China enforced preliminary antidumping tariffs of 178.6% on sorghum, a crop which is a major ingredient used in production of alcohol and bio-fuels.

June 15, 2018: The US President announced imposition of 25% tariff upon $ 50 billion worth of imports which was to be executed in two phases viz: (i) effective July 6, tariffs would be imposed on $ 34 billion worth of goods; (ii) cut-off date for imposing of tariffs on remaining $16 bn worth of imports was to be announced later (CNN Money, 2018) (Caixin Global, 2018). China accused US of initiating a trade war and warned of severe repercussions for both countries as well as global economy (Washington Post, 2018)

June 18, 2018: White House warned that in event of China retaliating against the aforementioned tariffs, a further 10% tariff would be enforced on Chinese imports worth $ 200 billion w.e.f. September 11, 2018 (USTR, 2018) (Caixin Global, 2018). This announcement prompted China to enforce tariffs on $ 50 billion worth of American goods. The global trade markets feared disruption of global supply chain due to this trade war, which would have devastating impact on global economy (CNN, 2018)

August 8, 2018: USTR announced that effective August 23, 2018, 280 imports items worth $16 billion would be subjected to a 25% tariff. Accordingly, China enforced similar tariffs on American items w.e.f. August 23, 2018 (Caixin Global, 2018) (USTR, 2018).

August 14, 2018: China lodged a complaint with the World Trade Organization (WTO) stating that the imposition of trade tariff on solar panels by the US is severe infringement of the WTO rules which has led to destabilization of the international market and has adversely affected China's legitimate trade interests.

August 22, 2018: David Malpass, Under Secretary of US Treasury and Wang Shou Wen, China's Deputy Minister of Commerce met in Washington to initiate a dialogue to come up with a solution to reduce the intensity of the trade war however no consensus was reached between the two parties.

August 23, 2018: According to a USTR announcement made on August 8, the US imposed a further tariff of 25% on imports worth $ 16 billion and a similar action was taken by China. Furthermore, in response to this tariff escalation, China also lodged a complaint against US with the WTO (China Briefing, 2018)

1.2 Rationales given for the tariffs

During his presidential campaign, Donald Trump had promised that in order to ensure America's economic well being, he would not hesitate to international free trade agreements contest China's unfair economic practices (New York Times, 2016). Furthermore, in January 2018, he said that he is a ardent supporter of good diplomatic relations with China however China should treat the US fairly (CNBC, 2018). While delivering his State of the Union Address he said that finally America is not going to tolerate unfair trade agreements which, over the years, have had a detrimental effect on the US companies, employment and national wealth and that from here on there would be no economic surrender. He further stated that the US government would renegotiate unfair trade agreements, negotiate new ones and would strive to ensure the protection of American workers as well as US intellectual property by ensuring apt enforcement of US trade rules (White House, 2018).

Mixed reactions have been given by government and industrial professionals regarding the appropriateness and future implications of these import tariffs some of which are discussed below:

i) John Ferriola, CEO and President of Nucor: The imports tariffs imposed by the US government are completely just and fair and are supposed to balance demographics of global trade. Furthermore, he quoted the example of the European Union where a 25% value added tax (VAT) is imposed on the US imports. Likewise, imposition of 25% tariff by US on goods imported from EU is absolutely fair (CNBC, 2018). NUCOR is US largest producer of steel as well as biggest metal recycler

ii) Zachary Karabell, Analyst with Wired: The idea of replacing the long standing trade consensus with a nationalist approach, introduced by the US administration has very little chance of success. He further stated that the imposition of such trade tariffs would not undo what has already been done and couldn't possibly challenge China which is not a manufacturing novice anymore (Wired, 2018).

iii) Peter Navarro, Director of White House Office of Trade and Manufacturing Policy: This initiative is defensive measure taken by the US government to protect the lives and interests of the American people (Fox Business, 2018). He also claimed that due to these trade deficits trillions of dollars are transferred to other countries which are then utilized for acquiring American assets instead of investing in them to ensure economic well being and prosperity of American people (CNBC, 2018).

iv) Richard Trumka, President of the AFL-CIO: China is responsible for theft of intellectual property (IP) as well as acquisition of US critical technological advances worth trillions of dollars. He further stated that these tariffs would exterminate unfair trade practices which have been draining American jobs and reducing earnings of an average American worker (AFL-CIO, 2018).

v) Robert Lighthizer, USTR representative: Launched a probe into alleged IP and forced technological transfer from US companies and after seven months of investigation deduced an estimate of actual economic damage caused to the American economy and recommended imposition of import tariffs (Washington Post, 2018).

Several other experts have focused on the China's IP theft amounting to billions of dollars. The primary issue is that before getting access to the China's market, foreign firms and investors have to transfer trade secrets and confidential technology to their Chinese partners. Since, WTO rules strictly prohibit such transfers therefore negotiations are always kept secret to evade penalties (Market Watch, 2018) a concern which was also voiced by the American and European Chambers of Commerce in China (DW, 2018). In response, China promised that it would take steps to protect the rights of foreign investors and would strike down laws which prevent the global automakers and ship builders from operating independently in Chinese markets and require them to operate in collaboration with the SOEs. The same pledges were also reiterated by Chinese President, Xi Jin Ping (New York Times, 2018).

The imposition of tariffs and the possibility of trade war also had a negative impact on the stock markets of two countries inflicting significant losses on the investors. Resultantly, till June 2018, the cumulative stocks' value had decreased by 20% as compared to the value at the beginning of the year (Reuters, 2018). Simultaneously Nikkei, the Japanese stock market, also endured a three-week retraction (Investors' Business Daily, 2018). Moreover, following formal enforcement of tariffs on July 6, the markets recovered and rallied because of encouraging employment reports from the US, finally closing on a favorable note. The Associated Press stated that another reason for this uplift was that the imposition of tariffs ended any speculations and uncertainty (Los Angeles Times, 2018). Simultaneously, the tariffs were severely criticized by representatives of several major American industries fearing adverse effect of tariffs and the ensuing trade war on businesses. Some of them included American Soybean Association (ASA), National Pork Producers Council (NPPC), and Retail Industry Leaders Association (RILA) etc since china is one of the biggest importers of soya bean and pork (New York Times, 2018).

This topic is diverse and multi dimensional with a wide range of anomalies and implications which are difficult to cover in the scope of this article. Hence, for the sake of simplicity the article would be divided into three sections. Section 1 gives a brief but compact introduction of the topic background and current scenario. Section 2 reviews the repercussions for China, United States and the global economy followed by conclusion and recommendations in section 3.

2. Ramifications of China-US trade war

In this section we would discuss the consequences of trade war on China, United States and the global economy.

2.1 Ramifications for China

2.1.1 China's $14 trillion debt-ridden economy and shadow banking sector

In this scenario, a trade war with the U.S. would have a significant negative impact on China's economic growth. Interestingly, over the last few years, China's had experienced an inward economic shift which saw its increased dependence on its citizens for growth generation therefore it could fare better in the event of trade war. However, China's exports still make a significant contribution to the economy. In 2017, China's exports to the United States were estimated at a robust $ 506 billion whereas imports from the United States amounted to a meager $ 130 bn. International Monetary Fund (IMF) had warned that a trade war would cause China GDP growth to diminish by 0.5% or even more. Here it is worth mentioning that China's debt-to-GDP has seen an unprecedented increase from 160% to 300% during the last decade or so which, according to the experts, could cause a massive financial crisis.

David Dollar, senior fellow at Brookings Institute said that recently a rapid increase has been noticed in classic economic indicators e.g. corporate debt-to-GDP and debt-to-GDP which are early indicators of a financial crisis. After the 2008 global recession, China invested trillions with both regulated and shadows banks and extended massive loans to enterprises for financing infrastructure projects which although generated considerable economic growth but also increased the volume of non-performing loans (NPLs) which is expected to reach an alarming $ 476 trillion till 2020.

Simultaneously, China's banking system is also underdeveloped which along with an increasing volume of NPLs is a formidable challenge faced by the China's government. Another financial dilemma faced by the government is the almost impossible regulation of country's $ 20 trillion shadow banking industry which is more critical than the sub-prime mortgage meltdown which caused the US financial crisis. Several of these shadow banks have used a plethora of bizarre financial instruments to finance risky infrastructure projects e.g. coal and copper mines and poorly constructed buildings. Furthermore, to safeguard against losses due to NPLs, several of the regulated banks have sold them to these shadow institutions; that embedded them in their financial products and sold to normal consumers as well as other banks. These unregulated wealth management products worth trillions pose severe economic risk. Additionally, non-payment of loans on a massive scale could cause banks to default complicating problems for local governments and other corporations who have benefited from these loans. In fact, China would end up paying a huge cost for this post-recession infrastructure development.

Chinese government has taken concrete steps to counter the escalating volume of NPLs e.g. establishment of a financial stability and development committee entrusted with designing and implementation of stringent banking regulations and coordination of financial reforms. The government has also directed the banks to discontinue guaranteed investments holders of which have to be bailed-out by the government in case of non fulfillment. The government is also trying to bring the off-balance debts into the balance sheets. In fact, China's four major banks account for 70% of total banking operations and their prudent operations render them impervious to these financial repercussions.

Even if China could avert a financial crisis, its being overleveraged could threaten economic growth. It had been observed that high debt loads tend to considerably decrease growth rates. A trade war could cause an accelerated decrease in China's GDP. China is not heavily reliant on exports and if the US government continues to levy tariffs on Chinese imports, China could avoid them by shifting its trade focus to other countries in the region. Nonetheless, if the US decides to impose tariffs on all Chinese imports (estimated at $ 500 billion) it could substantially affect economic growth which in the long run could cause decline in economic expansion and generate unemployment. Several steps could be taken to avert this scenario e.g. (i) opening of economy to foreign investors and corporations; (ii) mitigation of financial risks; and (iii) establishing a market oriented economy. In any case, an economic slowdown would be worrisome for the investors' confidence, which is an unfavorable prospect for any economy. It could be said that China is facing stern financial and economic challenges and the prospective trade war further complicates the situation (CNBC News, 2018).

2.1.2 Implications for the technological sector

Previously, several American and European ventures had shifted moved their manufacturing hubs to China due to cheap manufacturing cost and extensive market access e.g. Apple, Volkswagen and IBM etc. Since President Trump decided to impose tariffs on Chinese goods, these companies have been under massive pressure from the US government to shift their operations stateside to alleviate domestic employment generation for citizens' benefit. Therefore, experts have been saying that repercussions in the technological sector could be potentially more harmful for China. The products that had been subjected to the tariffs include products utilized in aerospace, communication and information technology. Some of the economic experts say that these areas would greatly benefit from China's plans for industrial up gradation. A common example is of Apple whose manufacturing operations are based in China. The technological giant sources parts, used in its iPhone devices, from several other companies like Samsung and SK Hynix (South Korea) which are assembled by Foxconn (Taiwan). According to a report from China Daily, approx. 50% iPhones are manufactured at Foxconn's plant in Zhengzhou, Central China. This plant has 94 iPhone production lines and a labor force of 350,000 workers. Therefore, Apple and Foxconn decision to shift their operations stateside would definitely cause loss of employment in Zhengzhou. Same scenario goes for other industrial concerns operations in the country.

In January, Apple had announced investing approx. $ 350 billion in U.S. operations; generation of 20,000 jobs over a five years period and providing innovation support to domestic manufacturers. Additionally, to generate and boost economic growth the US government offered tax concessions and other incentives for US firms if they move their operations stateside. In fact, value-added jobs catered by the US firms are of utmost importance to China since they boost middle class's purchasing power parity growth. These circumstances coupled with the tariffs would pressurize China and provide some leverage to the U.S. during trade negotiations. In this respect, Reuters learned that USTR had been employed a computer algorithm to single out products for tariffs imposition which would affect the Chinese exporters and have minimal impact on general population of the US. Resultantly, majority of goods (communication and information technology) exported by China to the US, which comprise of consumer electronics and relatively low value-added computers have not been subjected to any tariffs but significant tariffs have been imposed on technological parts and components e.g. printed circuit assemblies, semiconductor devices and transistors used as raw material to produce finished goods e.g. cell phones and computers.

In spite all these events leading to trade war, eventually China and US would have to undertake negotiations for conflict resolution due to impending consequences. Especially, in the technological field, market operations of China and US are incredibly entangled which should be analyzed before making any decision. Global economic experts have also held China responsible for current scenario since it favored the domestic enterprises over foreign ones thus abusing the privilege of being a WTO member while simultaneously criticizing Trump's idea of imposing import tariffs while debating their historically proven ineffectiveness and saying that these tariffs would also affect the American public. Resultantly, this approach would severely impact trade interests of China and the US and other global markets unless all stakeholders negotiate to resolve this issue amicably (CNBC News, 2018).

2.1.3 Impact on soybeans trade and associated costs

The US government announced imposition of import tariffs on Chinese goods due to its unfair trade policies and involvement in a massive intellectual property and technological theft. China immediately retaliated by imposing tariffs on 106 American imports including soybeans of which US is a major producer and China a major consumer. Actually, of US total soybeans production, 60% is exported to China. In 2016, United States soybeans export to China amounted to $ 14.2 billion. Given this interdependence, experts contemplate whether China could afford the cost of this decision. Soybeans are dominantly cultivated in US's Midwest region states especially Indiana, Ohio and Michigan. Hence imposition of tariffs on soybeans would also cause a decline in the US exports while greatly affecting the soybeans farmers who would need compensation from the government. Moreover, this would also have implications for the China. In fact, China's annual soybeans consumption is estimated at a robust 10 million tons of which almost 90% is imported. Additionally, China has also imposed tariffs on American corn; however, since China is largely self-sufficient in corn production it would not have widespread repercussions.

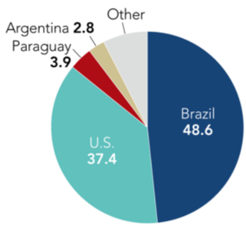

Figure 1: Share of global soybean exports (Source: US Department of Agriculture)

Brazil and United States dominate the global soybeans trade since they account for approx. 150 million tons (80%) of total soybeans production. Brazil is the largest exporter of soybeans to China followed by the US. Likewise, China dominates the global soybeans import accounting for approx. 60% of total imports worldwide. China is heavily dependent on soybeans for satisfying its various nutritional needs. Soybean is primarily converted to soybean oil and byproduct is converted to soy meal which is used as livestock feed especially for pigs. In fact, meat consumption has been increasing in China since late 90's and as of now has reached approx 70 million tons annually. Pork is widely used as a staple food by the Chinese and soybeans is an important element for fulfilling demand for pork meat. Therefore, higher tariffs on soybeans would accordingly increase the production cost and hence the prices of pork for general public. Additionally, the government would have to give subsidies to the pork producers/ feed makers to negate price alleviation. In the aftermath of announcement of tariffs, the soybeans futures on the U.S. Chicago Mercantile Exchange declined sharply before attaining stability. Market experts believe that both countries should realize that this decision and the incumbent costs would have severe repercussions for soybeans trade which should be avoided. Presently, the economies of both countries are much more entwined as compared to the past and the implications to soybean market is a perfect example of this dilemma (Nikkei Asian Review, 2018)

2.2 Ramifications for United States

2.2.1 China holding of US treasury bonds worth $1.2 trillion

Currently, China is holder of US treasury bonds amounting to $ 1.2 trillion and there is a serious possibility that if trade war escalates, China could reduce these holdings as a financial weapon against the United States and other nations could also follow suit hence causing a massive decline in dollar's price. As a matter of fact, few days ago, China already sold $ 3 billion worth of these bonds hence unveiling its future intent If this happens at a time when America is increasing the treasuries' market supply then there would be a rout of dollar in the bond market. Experts believe that China's partial sale of US treasury bonds would be a worst case scenario for US since, China had accumulated U.S. bonds worth $ 1 trillion both as a safe investment option collecting interest payments. China reduced some of the holdings during 2016-2017 to compensate an increase in Chinese Yuan but had repurchased almost all of it.

Supposedly, China decides to sell its holding of the U.S. bonds it would cause a mayhem in international financial markets affecting bond prices and interest rates while increasing the US bond supply and hence causing fixed income prices to decrease and increase in yields ultimately increasing the borrowing cost for both businesses and consumers. Simultaneously, it would also increase government cost of issuing debt due to payment of higher rates to investors. It would also depreciate the value of treasury bonds worth $ 15 trillion which are held by the US government and domestic investors hence causing an economic slowdown.

On the other hand, this decision could also have totally opposite consequences. If the other countries panicked and sold the treasuries while the prices are falling then China would have to sale some of its holding at loss thus inflicting a capital loss of billions and hence severely affecting its financial affairs. Economists debate that the interest rate would remain steady if bonds sold by China are purchased by other countries. Generally, US bonds are considered safe investment option and increasing interest rate would render them more attractive. U.S. is also reducing its quantitative easing-related bond purchases, China could stop purchasing new bonds while maturing the old ones which would cause a slow increase in the market supply of bonds thus increasing interest rates and rest of the scenario would follow as explained above, ultimately causing a decline in Dollar price. China could also (i) devalue Chinese Yuan which would increase the attractiveness of Chinese exports while simultaneously increasing the US trade deficit. (ii) Adoption of strict visa/work permit policy for U.S. citizens to get work visas and take official positions in the country. These actions will make doing business in China almost impossible (CNBC News, 2018).

2.2.2 A trade war would be detrimental for American people

Trump had vowed to safeguard interests of people who have not benefitted from past several decades of free trade. In this context, Nobel Prize winning economist, Christopher Pissarides said that casualties of this trade war would be the same people Trump pledges to protect. Despite of substantial economic growth, the living standards of certain groups of people had failed to alleviate and they could all mutually benefit if the government could address their grievances in a beneficial manner, something that earlier government had failed to achieve. He further explained that US would be severely affected if the countries phase out open trade. Trump had also promised renegotiation/eradication of bad trade agreements and detesting China for its unfair trade policies. Trump also imposed tariffs on all aluminum and steel imports except Canada and Mexico and EU was put on temporary hold.

Pissarides stated that said Trump's recent actions affirm his pre-election vows of revival of national manufacturing industry and employment generation. However, he warned that a trade war would actually hurt the American agricultural and manufacturing workers who are heavily reliant on foreign investment and trade especially from China and Japan However, economists say that primarily Trump should have focused on technological frontier since US is the world's most technologically advanced country (CNBC News, 2018).

2.2.3 Repercussions for US and its allies

Presently, majority of global trade is conducted through global value/ supply chains that traverse single and at times multiple sovereign borders. Resultantly, a certain Chinese product undergoes value-addition in several ways e.g. American firms operating in China, suppliers of spare parts from Japan, South Korea and Taiwan, before the finished product is finally delivered to the US. Therefore, a trade war between China and America would inflict collateral damage on the third countries as well. US had accused China of unfair trade policies, especially intellectual property theft and forced technological transfer from China based U.S. companies to their Chinese partners. Apparently, targeting beneficiaries of the said technological transfer would be reasonable. However, US faces a severe quandary i.e. majority of exports that reach the US have minute value addition (sometimes less than 10%) from the Chinese and rest from other countries which are US's allies. In this respect, a major example could be of computers and electronic appliances which are manufactured primarily by those multinational corporations (MNCs) operating in China, whose operations are considered domestic but resulting profit benefits the foreign owners and ultimately the US.

More often, China's industrial policies aim at alleviation of its state-owned enterprises (SOEs). Previously, until 1995, SOEs accounted for approx. 50% of Chinese exports but the arrival of western corporations has declined their export volume. Currently, traditional industrial sectors are the only ones producing exports with domestic value-addition e.g. textiles with approx. 75% domestic value addition; therefore they could be targeted to minimize collateral damage on U.S. firms and allied countries. Globally, almost 37% of Chinese exports to the US are intermediate goods utilized by US firms for competitive advantage and pricing which have been subjected to the import tariff s by the US.

China is major exporter of consumer goods e.g. dishwashers, washing machines and televisions to the US. The tariffs would cause an increase in prices of several consumer goods which would affect both the consumers, who would have to pay higher prices; and producers, whose production costs would increase and profit margin would decline. China had published a list of US goods it intends to penalize, the most notable ones being aircraft exports and soybeans. As discussed above, production costs and prices of soybeans and pork would significantly increase. Similarly, the inability to procure

American aircraft would render Chinese airlines far less efficient and productive. Simultaneously, majority of U.S. exports contain domestic content so the tariffs would negatively influence the US producers as well (Brookings Institution, 2018).

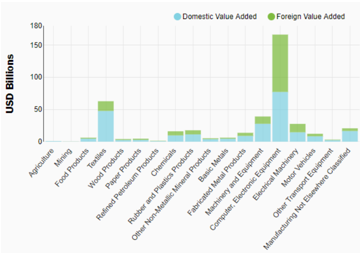

Figure 2: Value-added structure of U.S. imports from China, in billions of U.S. dollars, 2014

2.2.4 U.S. could be plunged into recession as a result of trade war with China

Economists and investors fear that a trade war between China and US which would have widespread anomalies for the United States e.g. recession, rise in unemployment, decline in GDP growth and ultimate economic slowdown. Experts at Macquarie Investment Bank said that trade war could render up to 6 million people unemployed. Experts at the Macquarie predicted that a full fledge trade war with China could plunge US into recession by 2019 and double the current unemployment levels. Simultaneously, rising import prices could also correspondingly increase the inflation rate hence prompting the Federal Reserve to increase interest rates. The economic uncertainty surrounding the dilemma could increase spread and cost of capital thus influencing consumption and investment. Moreover, eradication of trade war threat would still have negative consequences with greater magnitude e.g. GDP growth rate could decline by 1.2% in 2018 and the unemployment could increase to 6% in 2019.

Keeping in view all the pros and cons, trade war scenario is increasingly becoming realistic. Reportedly, China is set to impose 15-25% import tariffs on several items e.g. ethanol, pork, recycled aluminum, soybeans and steel. China reiterated its resolve stating that it doesn't have any intention of a trade war however it would not abstain from one and would fight till the end using all means necessary to safeguard its legitimate interests (Business Insider, 2018).

2.2.5 Why America would lose a trade war with China?

Earlier this year President Trump imposed import tariffs on Chinese goods in pressurize China into negotiating its trade balance with the US which is a robust $ 500 billion. Until now Trump intentions towards executing his plans and the impending consequences are uncertain. However, US abandonment of Trans Pacific Partnership (TPP) clearly indicates that Trump is not backing off from his campaign commitments. Experts say that America exit from TPP would act as a catalyst to accelerate

China's approach as the world leading economic power.

Presently, China is waiting for US to make the first move. Reason being a trade war would affect not only China and US but also their trade partners in South East Asia. But ultimately consequences would not be so disastrous for China due to US overdependence on China in various fields. Furthermore, China is much more developed and self sufficient then China of the old which was underdeveloped and needed the Western technology and manufacturing techniques for its advancement. Since then, flourishing supply chain and global trade has rendered China fully capable of fulfilling its needs and in the event of imposition of trade restrictions could easily shift its focus to other emerging markets e.g. India, Latin America and Africa. On the contrary, China's massive 1.5 billion population could also be very attractive for foreign investors. Statistical comparison of the sales of e.g. iPhones in China and U.S. reveals that till the end of 2015, Chinese consumers purchased 131 million iPhones while US consumers purchased 110 million. Another example is of Boeing, which has a work force of 150,000 in the US. Boeing estimates that China would procure approx. 7,000 airplanes worth $ 1 trillion over the next 2 decades.

The occurrence of the trade war would also have widespread repercussions to international companies like Wal-Mart whose imports from China amount to billions of dollars. These tariffs would increase the prices of these goods manifold which would pose problems for domestic households finally leading to a war of attrition in which the odds are heavily against United States and in favor of China e.g. (i) Presently, China's foreign exchange reserves are a robust $ 3 trillion as compared to US's $120 billion; (ii) These import tariffs would lead to imposition of penalties on US in the WTO which could result in collapse of WTO and imposition of even higher tariffs on US exports. Globally, the consequences would be catastrophic for American businesses and employment which might end United States 150 years rein as global economic super power and ascension of China as new global economic power.

As a matter of fact, several competitors are already challenging the US firms in China. Apple is already facing tough competition from local Chinese cell phone manufacturers like Xiaomi, Huawei, and Oppo etc. Similarly, Airbus, a European firm, is building an assembly plant in China where large, twin-aisle jets would be assembled and could increase China's inclination towards shifting their future aircraft purchases, worth trillions, from Boeing to Airbus. Likewise, majority of Chinese prefer German and Japanese automobiles e.g. BMW and Mercedes instead US ones Lexus or Ford. In spite of all the rhetoric surrounding the trade war, economic experts believe that US system has appropriate checks and balances to prevent any such catastrophe (Forbes, 2018)

2.3 Ramifications for global economy

2.3.1 The global implications of trade war

In order to reprimand China for its years of unfair trade practices and policies, US president Trump invoked Section 301 of the Trade Act of 1974 and Section 232 of the Trade Expansion Act of 1962 and imposed import duties on Chinese imports to the US. Similarly, Trump has been acting to restrict China from procuring US national assets, most recent being China's attempt to purchase a US semiconductor concern which was stopped by the regulators. The American intelligence community had specifically called for an import ban on Chinese cell phone company Huawei in order to send a strong message regarding future of Chinese investment attempts in US's critical economic sectors.

Roberto Azevedo, Director General (WTO) cautioned that consequences of this trade war would be catastrophic and could also stir a full0-scale global depression. Later on, United States exempted most of its trade partners e.g. Argentina, Australia, Brazil, Canada, European Union, Mexico and South Korea from the import tariffs to avert adiplomatic meltdown while alienating two key allies, Japan and Turkey and escalating trade tensions with two key rivals China and Russia. As of now, China has threatened to (i) Reduce purchasing of US treasury bonds; (ii) Cancelling key trade deals e.g. procurement of Boeing aircraft and instead shifting focus to Airbus; (iii) Placing restrictions on US automobile and electronics investors and (iv) Imposing a long term ban on Silicon Valley's technological companies from entering China's internet market. In its National Security Strategy (NSS), the US government pledged that it would persuade the Committee on Foreign Investment and its Congressional support to tackle current/future national security risks and support government resolve to defend the National Security and Innovation Base (NSIB) which represents network of competency, knowledge and people which undergird U.S. technological superiority.

Christine Lagarde, Director of International Monetary Fund (IMF) stated that the world trade order is in danger of being torn apart due to prospective trade war between China and US. All this economic turmoil is due to Trump's zero-sum approach towards global trade. He had severely criticized the trade irregularities and US external deficit Later on, he abandoned the Trans Pacific Partnership (TPP) membership; ceased trade negotiations with Asia and Europe; threatened to abandon the North America Free Trade Agreement (NAFTA) and severely criticized WTO and its policies. While imposing the tariffs Trump had primarily focused on steel and other heavy industrial goods and targeting those high tech industries where the China intends to attain global supremacy. Economists and critics around the world have stated that tariffs won't be able to regenerate employment due to complex trade relations and massive incumbent costs of relocation of manufacturing operations from China to the US hence making it impossible for US to reduce its trade deficit with China. Moreover, reduction of China's trade deficit and import barriers make it attractive for overseas investors and companies. Hitherto policymakers have evaded the protectionist rejoinder witnessed during the Great Depression of 1930s. However, since the Global Financial Crisis (GFC) 2008 increasing protectionist measures have lead to decline of the international trading system. Till now, the measures and countermeasures taken by U.S. and China are just to determine initial bargaining positions and gaining public confidence. However, if the trade war escalates, it would have severe repercussions for global economy (Eye Witness News, 2018).

Additionally, in order to further reduce and prevent transfer of intellectual property to competitors by non-traditional intelligence collectors e.g. foreign students, government is also considering review of visa procedures for students of specific countries. According to experts, this initiative is solely aimed at forcing China to eradicate restrictions on American companies from entering China's automobile, electronics and financial markets. Nevertheless, this hardball strategy could also incite China into unleashing a beggar-thy-neighbor dynamic against the US. More recently, Chinese Prime Minister Li Ke Qiang had ensured to take practical steps to facilitate the US investors; reinforce restrictions on intellectual property; and discourage demand of technology transfer from foreign enterprises to their Chinese partners. Whether these initiatives would satisfy the Americans is yet to be seen, but currently both economic powers are locked in a fight which ensures mutual and global financial annihilation. Finally, all these initiative could seriously impact those trade accords which ensure global commerce between the nations (Al-Jazeera, 2018).

2.3.2 Implications for UK's free trade and Brexit

This dilemma would also be detrimental have severe repercussions for United Kingdom and would severely dent its hopes of free trade Brexit. United Kingdom is a relatively open economy and has been striving hard for establishment of an open global trade order since attrition of a world trade system based on rules would severely threaten UK's prosperity. Furthermore, a fragmented and protectionist trade order would complicate the challenges for post Brexit UK. Notably, Britain has serious considerable potential in the services arena, but its expansion is obstructed by the high global barriers. Meanwhile, WTO's global negotiations to liberalize services trade have been stagnant for a considerable period of time. Simultaneously, European Union (EU) and United Kingdom have been trying to establish a preferential trading agreement focusing primarily on goods rather than services as a part of post Brexit negotiations. Furthermore, there had been several rumors of a lucrative trade deal between UK and US. Presently, US is the world's lead services exporter and the competitive advantage enables it to take a tough stance in the trade negotiations. Trade negotiations, especially in the services arena, have become increasingly intricate, and focus on uniform rules and standards than just reducing tariffs. Additionally, free trade in services would also bring competition from private competitors against public services. Since UK is medium sized economy it would have a weaker standpoint while negotiating favorable trade in a fragmenting world trade order. At the same time, its government is proclaiming capability to negotiate favorable deals and expand trade with countries beyond the purview of European Union (Eye Witness News, 2018).

2.3.3 Implications for consumer markets

With Donald Trump becoming the US President, dawning of a regressive era of trade protectionism was imminent which was confirmed by e.g. US pulling out of TPP; imposing import tariffs on China etc. Additionally, to the chagrin of Canada and Mexico, the US government has plans to renegotiate North American Free Trade Agreement (NAFTA). An executive order was signed by the president to strengthen upon the "Buy American" preferences in government funded infrastructure ventures. The US administration signals that trade dispute patience with China could be a part of a broader political strategy to pressurize it into allegiance against the North Korean stand-off. However, the spectre of the trade war could broaden in view of several recent developments e.g. the Korean peninsula, the South China Sea issue and pressure from trade giants in Washington.

Economists believe that the trade war would affect an increase in prices of consumer goods and components thus causing a sharp rise in inflation. According to an estimate resulting inflation would be 0.9% higher (2017) and 1.5% higher (2018) then the actual baseline forecasted figure which would cause a decline in private consumption growth till 202. Currently, every average retail store contains goods of everyday life imported from China therefore rising inflation would definitely cause inconvenience to American consumer while the Chinese consumers would be largely unaffected. Reason being that (i) Chinese imports are well distributed globally which decreases their dependency on US for fulfilling their needs; (ii) China's private consumption growth is already declining, and consumer sentiment resulting from a trade war would not have that accelerating effect. Simultaneously, in the event of a trade war, China could also explore other emerging markets for finding substitutes for the affected imports e.g. importing soybeans and other agricultural products from Latin America. On the Other hand, it could be very difficult for American retailers to find new and abundant sources of low-cost consumer goods for replacing the Chinese goods. With the passage of time, the American companies relocating their operations stateside could fill the void but at an increased production cost ad price.

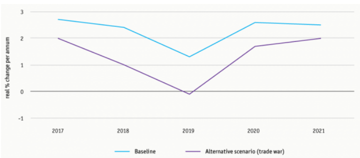

Figure 3: US private consumption growth 2017-2021: baseline and alternative (trade war) scenarios

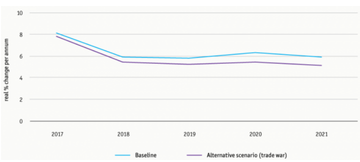

Figure 4: China private consumption growth 2017-2021: baseline and alternative (trade war) scenarios

Eventually, if NAFTA negotiations don't pan out as expected then the Canadian and Mexican producers/consumer would also face similar repercussions while the Asian supply chains would also be disrupted. As of now, the system of global supply and value chains, which supply components, sub-components and raw material into the Chinese manufacturing and assembly base, is so extensive that retaliatory tariffs would have widely distributed ramifications which is also reciprocated for many US companies since they have many Chinese and several other Asian manufacturers implanted in their supply chains. Since Trump is highly critical of US-China trade surplus and NAFTA and his attitude reflects cynicism towards international trade accords, therefore a possibility of a trade war escalation could not be ruled out. This situation would put the supporters of Pro-globalization in a defensive stance for the anticipated future. In this regard, adoption of moderate and symbolic protectionist approach towards China and US's other trade partners is highly probable since the domestic economic connotations dictate prudence (The Economist, 2018).

3. Conclusion and recommendations

Hence, it could be said that the retaliatory tariffs imposed by China and the US on each other imports could possibly escalate into a trade war which would have pervasive global economic anomalies. If things escalate America could also restrict Chinese investment in American infrastructure and similar retaliation is expected from China as well which could disturb global distribution and supply chains hence affecting world trade and causing long-lasting repercussions e.g. relocation of manufacturing concerns and distribution centers by the manufacturers. Furthermore, investment decisions directly affect employment and taxes with widespread implications. This trade war escalation would be exceedingly damaging for the American and Chinese economies since majority of MNCs e.g. Apple, IBM, Ford, etc invest in infrastructure development and manufacturing in both countries. Simultaneously, it would also affect American, Chinese and global businesses and consumers since majority of goods and intermediates manufactured by China-based foreign enterprises which facilitate pricing control.

As mentioned earlier, US is targeting high-tech manufacturers to upset China's flagship industrial strategy "Made in China 2025", which aims to increase global competitiveness of Chinese industry through introduction of artificial intelligence and automation which heavily depends on access to modern Western technology. The primary reason behind imposition of these tariffs is the problem of the intellectual property theft since China requires companies intending to invest in its infrastructure to transfer technology to their Chinese partners. However, this is a known fact that these measures won't result in better protection of American technology nor would facilitate access to Chinese markets. A grievance constantly reiterated by China is that its firms are barred from investing in American infrastructure especially the technological sector which is vital to its economic growth.

Nevertheless, China is reluctant in giving open market access to foreign competitors since it believes that its underdeveloped domestic industry needs protection from foreign dominance. However, China also has firms like Alibaba, Huawei, and Tencent which ranked among largest global enterprises. Additionally, entering of foreign competition would also enhance China's growth prospects, efficiency and productivity, especially for less developed and less efficient SOEs. But there is a possibility that instead of carrying out effective trade negotiations, additional imports tariffs could be mutually imposed by the two countries hence causing further economic damage. However, all this could be averted if both economic powerhouses take the route of negotiation and agree to open up their markets not only for wellbeing of their people but for the global economy as a whole since the economies of both countries are significant interdependent on each other.

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